

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES

AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL

AREA DE ARCHIVO DIGITAL

MUNICIPIO DE TOA BAJA

AUDITORIA 2005-2006

30 DE JUNIO DE 2006

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MUNICIPALES

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA**

**BASIC FINANCIAL STATEMENT AND
SUPPLEMENTAL SCHEDULE**

With Independent Auditor's Report Thereon
JUNE 30, 2006

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA**

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INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
Municipal Legislature Body
Municipality of Toa Baja
Toa Baja, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Toa Baja of the Commonwealth of Puerto Rico (the "Municipality"), as of and for the year ended June 30, 2006, which collectively comprise the Municipality's basic financial statements as listed in the accompanying table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

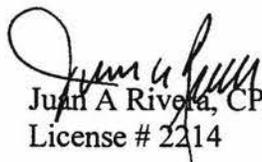
As more fully described in Note 6 to the financial statements, the Municipality has properties and equipments tat has not been valued. The amount of capital asset investment represents 65% of the assets on the statement of net assets. The effects on the financial statements of the preceding practiced are not reasonably determinable.

In our opinion, except for the effects on the matters discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Toa Baja of the Commonwealth of Puerto Rico, as of June 30, 2006, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Audit Standards, we have also issued our report dated December 28, 2006 on our consideration of the Government's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Audit Standards and should be read in conjunction with this reporting in considering the results of our audit.

Our audit was performed for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The accompanying schedule of expenditure of federal awards is presented for purpose of additional analysis as required by US Office of Management and Budget Circular A- 133, Audit of States, Local Governments, and Non- Profit Organizations, and is not required part of the general purpose financial statements. Such information has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the general purpose financial statements taken as a whole.

The accompanying Management's Discussion and Analysis and the Budgetary Comparison Schedule are not required parts of the basic financial statements referred to above, but are supplementary information required by GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.


Juan A Rivera, CPA
License # 2214

Toa Baja, Puerto Rico
December 28, 2006



NOTE: Stamp No.25195608 of the Puerto Rico State Society of Certified Public Accountants was affixed to the original report.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2006

Management of the Municipality of Toa Baja (the "Municipality") provides this Management's Discussion and Analysis of the Municipality's basic financial statements as an overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2006. We encourage readers to consider the information presented here in conjunction with the additional information that we have furnished in the accompanying basic financial statements.

USING THIS ANNUAL REPORT

This annual report consists of a series of new financial statements with a change in the focus from previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

FINANCIAL HIGHLIGHTS

- The Municipality net assets decreased by \$12,557,325, including prior period adjustment of \$(80,553).
- In the Governmental financial statements, general fund balance decreased by \$4,123,978, including prior period adjustment of \$41,977.
- Capital expenditures amounted to \$5,050,239.

GOVERNMENT-WIDE-FINANCIAL STATEMENT

The government-wide financial statements are designed to provide readers with a broad overview of the Municipality's operations and finance as a whole in a manner similar to private-sector business. 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 the end of the fiscal year. These financial statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means that these financial statements follow methods that are similar to those used by most businesses. They take into account all revenues and expenses connected with the fiscal year ended June 30, 2006 even if cash involved have not been received or paid. The government-wide financial statements include: (1) the statements of net assets and (2) the statement of activities.

Statement of Net Assets

The statement of net assets presents all of the Municipality's assets and liabilities, with the difference between these two items reported as "net assets" (equity). Over time, increases or decreases in the net assets may serve as a useful indicator of whether the financial position of the Municipality is either improving or deteriorating.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2006

Statement of Activities

The statement of activities presents information showing how the Municipality's net assets changed during the fiscal year ended June 30, 2006. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as uncollected taxes and earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenues for each function of the Municipality.

Both of the abovementioned financial statements present all the governmental activities of the Municipality, which consist mostly by taxes and intergovernmental revenues (such as federal grants). Most services provided by the Municipality fall into this category, including culture and education, general government, health and sanitation, public safety, public housing and welfare, etc.

Fund Financial Statements

The Fund Financial Statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only one kind of fund which is the governmental fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government Wide Financial Statements. However, unlike the Government Wide Financial Statements, Government Fund Financial Statements focus on near term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2006

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

As noted earlier, net assets may serve over time as a useful indicator of the Municipality's financial position. In the case of the Municipality liabilities exceeded assets by \$18,006,781 at June 30, 2006.

As previously discussed, by far the largest portion of the Municipality's net assets reflect its investment in capital assets (e.g., land, buildings, machinery, equipment and all other property), less any related debt used to acquire those assets that is still outstanding. The Municipality uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. The following is a condensed presentation of the Municipality's financial position and results of operations, as reported in the government-wide financial statements:

Municipality of Toa Baja
Condensed Statement of Net Assets
June 30, 2006 and 2005

	2006	2005
Current assets	\$ 51,893,880	\$ 40,751,135
Capital assets	94,592,320	92,062,815
Total assets	146,486,200	132,813,950
Current liabilities	40,081,269	15,018,194
Noncurrent liabilities	88,398,150	87,231,647
Total liabilities	128,479,419	102,249,841
Invested in capital assets, net of related debt	60,792,905	40,601,190
Restricted	24,573,579	8,234,158
Unrestricted	(67,359,703)	(18,271,242)
Total net assets	\$ 18,006,781	\$ 30,564,106

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2006

Changes in Net Assets

The Municipality's net assets decreased by \$12,557,325. Approximately 32 percent of the Municipality's total revenue came from grants and contributions, including federal aid, while 45 percent resulted from taxes. The Municipality's expenses cover a range of services. The largest expenses were for general government and public works. In future years, when prior-year information is available, a comparative analysis of government-wide data will be presented.

Municipality of Toa Baja
Condensed Statement of Activities
June 30, 2006 and 2005

	2006	2005
General revenues		
Property taxes	22,640,396	16,678,811
Municipal license tax	10,668,526	9,526,980
Grants and contributions restricted to specific programs	23,369,244	21,499,147
Rent and Landfill Services	11,369,108	10,636,383
License, Permits, Fines and Forfeitures	1,628,092	1,041,262
Miscellaneous	3,271,130	3,285,570
	<u>72,946,496</u>	<u>62,668,153</u>
Expenses		
General government	27,507,292	17,046,515
Public safety	6,388,157	9,184,310
Culture	4,483,047	2,355,717
Health and sanitation	12,834,659	11,000,431
Public housing and welfare	22,061,825	22,654,992
Urban and economic development	8,866,806	638,487
Interest on long-term debt	3,281,482	4,264,934
Other	273,703	273,703
	<u>85,423,268</u>	<u>67,419,089</u>
Change in net assets	(12,476,772)	(4,750,936)
Net assets, beginning of year (restated)	<u>30,483,553</u>	<u>35,315,042</u>
Net assets, end of year	<u>\$ 18,006,781</u>	<u>\$ 30,564,106</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2006

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

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

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$24,573,579, a decrease of \$1,159,359, including prior year adjustment of \$(2,786,829), in comparison with the prior year.

The general fund is included within the governmental funds; it is the operating fund of the Municipality. As of June 30, 2005, the general fund had a fund balance of \$4,271,667, adjusted. An operational deficiency of \$ 4,165,955 during fiscal year 2006, left a fund balance, reserved for encumbrance, of \$105,712.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2006, amounts to \$124.3 million, net of accumulated depreciation of \$29.7 million, leaving a net book value of \$94.6 million. This investment in capital assets includes land, buildings, improvements, equipment construction in progress.

The total net increase in the Municipality's investment in capital assets for the current fiscal year was about .26% in terms of net book value. Actual expenditures to purchase or construct capital assets were \$7.4 million for the year. Depreciation charges for the year totaled \$2.5 million.

The Municipality finances a significant portion of its construction activities through bond issuances. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayers, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer at P. O. Box 2359, Toa Baja, Puerto Rico 00951.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Statement of Net Assets
June 30, 2006

Assets	<u>Governmental activities</u>
Current assets:	
Account receivables:	
Taxes:	
Property taxes	\$ 327,262
Excise taxes	84
Municipal license taxes	46,886
Landfill and property rents	3,582,880
Grants and contributions	6,889,349
Accrued interest on deposits	171,259
 Restricted assets:	
Cash in commercial banks	10,835,370
Cash in fiscal agent	30,040,790
Total current assets	<u>51,893,880</u>
 Noncurrent assets:	
Capital assets:	
Capital assets	124,352,007
Accumulated depreciation and amortization	<u>(29,759,687)</u>
Capital assets, net of accumulated depreciation	<u>94,592,320</u>
Total noncurrent assets	<u>94,592,320</u>
Total assets	<u><u>\$ 146,486,200</u></u>

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Statement of Net Assets (concluded)
June 30, 2006

Liabilities and net assets	Governmental activities
Current liabilities (due within one year):	
Accounts payable	\$ 5,911,871
Intergovernmental payables	5,079,263
Legal claim payable	585,592
Accrued employees christmas bonus	3,137,713
Accrued interest payable on long-term debt	1,769,190
Unearned revenues	9,642,461
Current portion of long-term obligations:	
General obligation bond payable	\$ 7,824,178
Special obligation bond payable	1,964,000
Note payable	190,517
Federal cost disallowance	39,000
Compensated absences	3,937,484
Total current portion of long-term obligations	13,955,179
Total current liabilities	40,081,269
Noncurrent liabilities, excluding current portion (due in more than one year):	
General obligation bond payable	46,371,645
Special obligation bond payable	8,705,000
Note payable	5,267,460
Federal cost disallowance	44,100
Compensated absences	3,186,478
Landfill closure accrued liabilities	24,823,467
Total noncurrent liabilities	88,398,150
Total liabilities	128,479,419
Net assets (deficit):	
Invested in capital assets, net of related debt	60,792,905
Restricted for:	
Encumbrances	105,712
Debt service	\$ 3,258,704
Other specified purposes	21,209,163
Total restricted net assets	24,467,867
Unrestricted deficit	(67,253,991)
Total net assets	\$ 18,006,781

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Statement of Activities
Fiscal Year Ended June 30, 2006

Functions/Programs	Expenses	Program Revenues			Net (Expenses) Revenues and Changes in Net Assets Governmental
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
General government and administration	\$ 27,507,292		\$ 970,993		\$ (26,536,299)
Urban and economic development	8,866,806		203,279	\$ 565,170	(8,098,357)
Health and sanitation	12,834,659	\$ 13,745	2,042	-	(12,818,872)
Public housing and welfare	22,061,825		12,218,684	3,298,517	(6,544,624)
Culture, recreation and education	4,483,047	133,332	1,858,733	-	(2,490,982)
Public safety	6,388,157		594,478	-	(5,793,679)
Interest on long term debt	3,281,482	-	-	-	(3,281,482)
Total governmental activities	\$ 85,423,268	\$ 147,077	\$ 15,848,209	\$ 3,863,687	\$ (65,564,295)
General revenues:					
Property taxes					\$ 22,640,396
Volume of business tax					10,668,526
Licenses, permits, fines and forfeitures					1,628,092
Grants and contributions not restricted					3,657,348
Rent and landfill services					11,369,108
Special item					685,031
Miscellaneous					2,439,022
Total general revenues					53,087,523
Change in net assets					(12,476,772)
Net assets at beginning of year					30,564,585
Prior period adjustment					(81,032)
Restated net assets at beginning of year					30,483,553
Net assets at end of year					\$ 18,006,781

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Balance Sheet – Governmental Funds
June 30, 2006

	<u>General Fund</u>	<u>Debt Service</u>	<u>Head Start</u>	<u>\$12,065,000 Loan</u>	<u>Other Funds</u>	<u>Total Governmental Funds</u>
<u>Assets</u>						
Account receivable, net of allowance of uncollectible accounts						
Taxes:						
Property tax	\$ 202,997	\$ 124,265				\$ 327,262
Municipal licence tax	46,886					46,886
Construction excise tax	84					84
Landfill	964,544					964,544
Accrued interest on deposits	869	27,431				28,300
Grants and contributions	2,332,739		\$ 1,736,942		\$ 1,993,374	6,063,055
Due from other funds	3,635,007					3,635,007
Restricted assets:						-
Cash in commercial banks	7,927,123		169,993		2,738,254	10,835,370
Cash in fiscal agent		9,772,671		\$ 11,811,119	8,457,000	30,040,790
Total assets	<u>\$ 15,110,249</u>	<u>\$ 9,924,367</u>	<u>\$ 1,906,935</u>	<u>\$ 11,811,119</u>	<u>\$ 13,188,628</u>	<u>\$ 51,941,298</u>
<u>Liabilities</u>						
Accounts payable and accrued liabilities	\$ 2,150,482		\$ 182,473	\$ 60,490	\$ 1,275,332	\$ 3,668,777
Intergovernmental payable	3,008,597					3,008,597
Due to other fund		\$ 86,881	839,715		2,708,411	3,635,007
Advance to other fund						-
Deferred revenues	9,845,458				631,098	10,476,556
Mature bonds ue and payable (Int. Incl.)		6,578,782				6,578,782
Total liabilities	<u>15,004,537</u>	<u>6,665,663</u>	<u>1,022,188</u>	<u>60,490</u>	<u>4,614,841</u>	<u>27,367,719</u>
<u>Fund Balances</u>						
Reserved for:						
Encumbrances	105,712					105,712
Debt service		3,258,704				3,258,704
Other specified purpose			884,747	11,750,629	8,573,787	21,209,163
Unreserved						-
Total fund balances	<u>105,712</u>	<u>3,258,704</u>	<u>884,747</u>	<u>11,750,629</u>	<u>8,573,787</u>	<u>24,573,579</u>
Total liabilities and fund balances	<u>\$ 15,110,249</u>	<u>\$ 9,924,367</u>	<u>\$ 1,906,935</u>	<u>\$ 11,811,119</u>	<u>\$ 13,188,628</u>	<u>\$ 51,941,298</u>

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Reconciliation of the Balance Sheet – Governmental Funds
to the Statement of Net Assets
June 30, 2006

The amounts of governmental activities reported in the statement of net assets and the balance sheet – governmental funds, are different for the following reasons:

Total fund balance reported in the balance sheet – governmental funds	\$ 24,573,579
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Add (Deduct):

Capital assets used in governmental activities are not considered available financial resources at fiscal year-end, therefore, are not reported in the governmental funds.	94,592,320
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Receivables that are unavailable to be recorded in the governmental funds but are recorded in the statement of activities.	2,761,295
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Christmas bonus receivable in the statement of activities that are not recorded in the governmental funds.	826,294
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Deferred (unavailable) revenues in the governmental funds that are recorded as revenues in the statement of activities.	834,095
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The following liabilities are not due (mature) in the current fiscal year, therefore are not reported in the governmental funds at June 30, 2006:

General obligations bonds	(50,344,231)
Special obligation bonds	(9,711,000)
Notes payable	(5,457,977)
Reserve for federal cost disallowance	(83,100)
Compensated absences	(7,123,962)
Landfill closure and postclosure care costs	(24,823,467)
Account payables	(3,729,804)
Intergovernmental payable	(583,956)
Legal claim payable	(585,592)
Accrued employees' Christmas bonus	(3,137,713)

Net assets – governmental activities, as reported in the statement of net assets	\$ 18,006,781
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The accompanying notes to the basic financial statement are an integral part of this statement. See Auditor's reports.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Statement of Revenues, Expenditures and
Changes in Fund Balances – Governmental Funds
Fiscal Year Ended June 30, 2006

	<u>General Fund</u>	<u>Debt Service</u>	<u>Head Start</u>	<u>\$12,065,000 Loan</u>	<u>Other Funds</u>	<u>Total Governmental Funds</u>
Revenues						
Taxes:						
Property taxes	\$ 14,516,176	\$ 7,921,223				\$ 22,437,399
Municipal licence tax	10,153,290				\$ 515,236	10,668,526
Landfill and rent	8,750,772					8,750,772
Licenses and permits	1,481,015				147,077	1,628,092
Grants and contributions	2,707,448		\$ 9,555,873		10,400,784	22,664,105
Interest on deposits	644,832			\$ 315,668	375,510	1,336,010
Special item					685,031	685,031
Other	886,533				220,597	1,107,130
Total Revenues	39,140,066	7,921,223	9,555,873	315,668	12,344,235	69,277,065
Expenditures						
Current:						
Municipal Legistadure	816,455					816,455
Mayor's Office	2,629,780					2,629,780
General Government	16,096,353				6,310,656	22,407,009
Urban and economic development	5,776,800			60,490	1,570,223	7,407,513
Public Safety	5,562,921				595,974	6,158,895
Health and sanitation	7,367,537				31,660	7,399,197
Culture, recreation and education	2,252,949				1,829,894	4,082,843
Public Housing and welfare	4,029,240		9,147,078		7,794,141	20,970,459
Debt service:						
Principal		4,915,723				4,915,723
Interests		3,281,482				3,281,482
Capital outlays	259,707			253,881	4,536,651	5,050,239
Total expenditures	44,791,742	8,197,205	9,147,078	314,371	22,669,199	85,119,595
Excess (Deficiency) of revenues over (under) over (under) expenditures:	(5,651,676)	(275,982)	408,795	1,297	(10,324,964)	(15,842,530)
Other financing sources (uses)						
Transfer-in from other fund	3,040,261	1,554,540			178,500	4,773,301
Transfer-out to other fund	(1,554,540)	(1,804,522)		(315,668)	(1,098,571)	(4,773,301)
Proceed from issuance of bonds				12,065,000	5,405,000	17,470,000
Total other financial source (use):	1,485,721	(249,982)	-	11,749,332	4,484,929	17,470,000
Net changes in fund balances	(4,165,955)	(525,964)	408,795	11,750,629	(5,840,035)	1,627,470
Fund balance at beginning of year	4,229,690	6,613,953	475,952		14,413,343	25,732,938
Prior period adjustments	41,977	(2,829,285)			479	(2,786,829)
Fund balances at beginning of year, adjusted	4,271,667	3,784,668	475,952		14,413,822	22,946,109
Fund balances at end of year	<u>\$ 105,712</u>	<u>\$ 3,258,704</u>	<u>\$ 884,747</u>	<u>\$ 11,750,629</u>	<u>\$ 8,573,787</u>	<u>\$ 24,573,579</u>

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

D. Lopez
15/03/2007
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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
 Reconciliation of Statement of Revenues, Expenditures and Changes
 in Fund Balances - Governmental Funds to the Statement of Activities
 Fiscal Year ended June 30, 2006

The amounts of governmental activities reported in the statement of activities and the statement of revenues, expenditures and changes in fund balances are different for the following reasons:

Excess of revenues and other financing sources over expenditures and other uses reported in the statement of revenues, expenditures and changes in fund balances – governmental funds	\$ 1,627,470
 Add (Deduct):	
Governmental funds report capital outlays as expenditures. However, in the accompanying statement of activities, the cost of those assets is allocated over their estimated useful life as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	2,529,505
Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the governmental fund financial statements.	3,669,431
Proceeds on issuance of bonds and bonds anticipation notes, are recorded as other financing sources in the fund financial statements, but the issuances increases long-term liabilities in the statement of net assets.	(17,470,000)
Repayment of bonds and notes principal is recorded as expenditures in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.	6,209,240
The landfill closure and post closures care costs do not require the use of current financial resources and therefore are not reported as expenditure in the governmental fund financial statements.	(2,878,936)
Some expenses reported in the statement of activities do not require the use of current financial resources and are not reported as expenditures in governmental funds.	<u>(6,163,482)</u>
 Net change in net assets as reported in the accompanying statement of activities	 <u>\$ (12,476,772)</u>

The accompanying notes to the basic financial statement are an integral part of this statement. See Auditor's report.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

1. Summary of Significant Accounting Policies

The Municipality of Toa Baja of the Commonwealth of Puerto Rico (the "Municipality") is a local government with full legislative, fiscal and administrative powers to operate as a government under Law No. 81 of August 30, 1991, as amended, known as the *Autonomous Municipalities Act of the Commonwealth of Puerto Rico (Law No. 81)*.

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

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

a) New Financial Reporting Model

The accompanying basic financial statements present the financial position and the results of operations of the Municipality as a whole, and its various governmental funds as of and for the year ended June 30, 2006, in conformity with accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (GASB).

In June 1999, GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB No. 34). This statement established new financial reporting requirements for state and local governments. On July 1, 2003, the Municipality adopted the provisions of GASB No. 34 as well as other statements referred to below. These statements require the reporting of new financial information and restructured much of the information that governments have reported prior to this implementation.

According to the financial reporting model established by GASB No. 34, the minimum required financial statement presentation applicable to the Municipality is composed of the following elements: (1) government-wide financial statements (GWFS), (2) governmental fund financial statements (GFFS), (3) notes to basic financial statements, and (4) required supplementary information (RSI).

The RSI, which consists of a management discussion and analysis (MD&A) and budgetary comparison schedule - General Fund that are information presented along with, but separate from, the Municipality's basic financial statements. The MD&A is a narrative report that introduces the accompanying basic financial statements and provides

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

a) *New Financial Reporting Model (Cont.)*

an analytical overview of the Municipality's financial activities for the year ended June 30, 2006, 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.

As previously mentioned a series of statements and interpretations were also adopted in conjunction and simultaneously with GASB No. 34. Those statements and interpretations are: (1) GASB Statement No. 33 – *Accounting and Financial Reporting for Nonexchange Transactions*, (2) GASB Statement No. 37 – *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, (3) GASB Statement No. 38 – *Certain Financial Statement Note Disclosures* and (4) GASB Interpretation No. 6 – *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

GASB No. 34 also required that the accounting for all governmental activities reported in the GWFS be based on applicable pronouncements issued by the Financial Accounting Standards Board (FASB) and its predecessor bodies, such as the Accounting Principles Board (APB), issued on or before November 30, 1989, provided those pronouncements do not conflict with or contradict GASB pronouncements. Accordingly, in conjunction and simultaneously with the adoption of GASB No. 34, the Municipality also adopted the following pronouncements: (1) APB Opinion No. 20 – *Accounting Changes*, (2) APB Opinion No. 21 – *Interest on Receivables and Payables*, (3) FASB Statement No. 5 - *Accounting for Contingencies* and (4) FASB Statement No. 16 – *Prior Period Adjustments*. The Municipality has elected to not apply all statements and interpretations issued by FASB after November 30, 1989.

b) *Financial Reporting Entity*

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

The Municipality adopted the provisions of GASB Statement No. 40, *Deposit and Investment Risk Disclosures* – an amendment of GASB Statement No. 3. The new standard enhances the deposit and investment risk disclosures by updating the custodial credit risk disclosure requirements of GASB No. 3 and addressing other common risk, including concentrations of credit risk. The changes are reflected in Note 2.

c) *Government-wide Financial Statements*

The accompanying GWFS are composed of: (1) the statement of net assets and (2) the statement of activities. These financial statements do not report fund information but rather report information of all of the Municipality's governmental activities. These

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

c) Government-wide Financial Statements(Cont.)

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

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

c) *Government-wide Financial Statements(Cont.)*

The classification of restricted net assets 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 assets. These designations consist of management's plans for the use of resources, which are subject to change at the discretion of the Municipal Legislature.

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

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

The accompanying statement of activities presents the results of the Municipality's operations by showing how the Municipality's net assets changed during the year ended June 30, 2005, 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) Municipal Legislature, (2) Mayor's office, (3) general government, (4) urban and economic development, (5) public safety, (6) health and sanitation, (7) culture, recreation and education and (8) public housing and welfare. 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 two broad categories: (1) program revenues and (2) general revenues.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

c) Government-wide Financial Statements(Cont.)

revenues reduce the costs (expenses) of the function/program to arrive at the net cost of the function/program that must be financed from the Municipality's general revenues. The accompanying statement of activities separately reports the following categories of program revenues:

- **Charges for services** – These 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 include fees charged for specific services, charges for licenses and permits, and fines and forfeitures, among others.
- **Program-specific capital and operating grants and contributions** – These consist of transactions that are either mandatory or voluntary nonexchange transactions with other governments, organizations, or individuals that restrict the resources for use in a particular program. Capital grants and contributions consist of capital assets or resources that are restricted for capital purposes – to purchase, construct or renovate capital assets associated with a specific 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. Restricted capital and operating 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 and construction excise taxes are reported as general revenues. All other nontax revenues (including unrestricted investment earnings, 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 overhead expenses of the Municipality's other functions/programs. Even though some of these costs have been charged to other funds in the governmental fund financial statements as indirect cost allocations permitted under some federal programs, the Municipality has reported these indirect expenses as direct expenses of the general government function. Accordingly, the Municipality does not allocate general government (indirect) expenses to other functions.

COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

c) Government-wide Financial Statements(Cont.)

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

The Municipality classifies all of its activities as governmental activities in the accompanying GWFS. These are activities generally financed through taxes, intergovernmental revenues and other nonexchange revenues that can be used to support the Municipality's programs or services. These governmental activities are also generally reported in the governmental fund financial statements.

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

d) Governmental Fund Financial Statements

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

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

- ***General fund*** – The general fund is the Municipality's main operating and major fund, as defined below, used to account for all financial resources and governmental activities, except for financial resources required to be accounted for in another fund. It is presumed that the Municipality's governmental activities have been reported in

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

General fund (Cont.)

the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) GAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund.

- ***Special revenue funds*** – The special revenue funds are nonmajor funds, as defined below, used by the Municipality to account for revenues derived from grants or other revenue sources (other than major capital projects) that are either self-restricted by the Municipality or legally restricted by outside parties for use in specific purposes. 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 fund, as defined below, used by the Municipality to account for the accumulation of resources for, and the payment of, principal and interest for: (1) bonds and notes for which debt service payments are legally mandated to be accounted for in a debt service fund and/or (2) 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. Principal and accrued interest due on July 1 of the following fiscal year related to long-term debt for which debt service payments are accounted for in the debt service fund, are recorded as debt service fund's liabilities at June 30, if resources are available at June 30 for its payment.

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

- ***Capital projects funds*** – Capital projects funds are major and nonmajor funds, as defined below, used to account for the financial resources used in the acquisition or construction of major capital facilities, other assets and permanent improvements. Significant capital outlays financed from general obligation bond proceeds are accounted for also in the capital projects funds.

The use of the capital projects funds has been reserved for major capital acquisitions or construction activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalize assets (such as certain vehicles and other minor capital

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Fiscal Year Ended June 30, 2006

Capital projects funds (Cont.)

assets) have been reported in the fund from which financial resources were used for the purchase.

Prior to GASB No. 34, the Municipality was required to report governmental fund financial statements that presented a single aggregated column for each fund type. Each column presented the combined total of all funds of a particular type. Fund types are no longer the focus of the accompanying governmental fund financial statements. Under GASB No. 34, the focus of the governmental fund financial statements is on major funds, which generally represent the Municipality's most important funds. Accordingly, the Municipality is required to segregate governmental funds among major and nonmajor within the governmental fund financial statements. Major individual governmental funds are reported individually as separate columns in the governmental fund financial statements, while data from all nonmajor 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 fund is considered a major fund for financial reporting purposes if its total assets, liabilities, revenues or expenditures of that individual governmental fund are at least 10 percent of the corresponding element total (assets, liabilities, revenues or expenditures) for all governmental funds. For the purposes of applying the aforementioned major fund criteria, no eliminations of interfund balances have been made. Total revenues for these purposes means all revenues, including operating and nonoperating revenues (net of allowances), except for other financing sources. Total expenditures for these purposes mean all expenditures, including operating and nonoperating expenditures, 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) debt service fund, (3) Head Start program, and (4) \$12,065,000 loan.

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 income) 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

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Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

Governmental-wide financial statements (Cont.)

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 fees for licenses and permits, 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 nonexchange transactions are recorded using the criteria set forth by GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions* (GASB No. 33), which the Municipality adopted on July 1, 2002. GASB No. 33 established accounting and reporting standards for nonexchange transactions involving cash and financial or capital resources (for example, most taxes, grants and private donations). In a nonexchange 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 nonexchange transactions into the following four classes in the accompanying basic financial statements: (a) derived tax revenues, (b) imposed nonexchange revenues, (c) government mandated nonexchange transactions, and (d) voluntary nonexchange transactions.

In the case of derived tax revenue transactions (such as municipal license taxes), which result from assessments the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred (that generally is, when the taxpayers' net sales or revenues subject to tax take place).

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

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

- For reimbursement-type (commonly known as "expenditure-driven awards"), receivables and revenues are recorded when all eligibility requirements imposed

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Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

Governmental-wide financial statements (Cont.)

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 nonexchange transactions (such as donations and certain grants and entitlements) result from legislative or contractual agreements, other than exchanges, entered into willingly by two or more parties. In these types of transactions, receivables and revenues are generally accounted for in the same manner as government-mandated nonexchange transactions discussed above.

Receipts of any type of revenue sources collected in advance for use in the following period are recorded as deferred revenues.

Events that are neither exchange nor nonexchange transactions are recorded when it is probable that a loss has been incurred and the amount of loss is reasonably estimable.

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 GFFS. Therefore, the accompanying GFFS include reconciliations to better identify the relationship between the GWFS and the GFFS.

Governmental fund financial statements – The accompanying GFFS are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are generally recognized as soon as they are both measurable and available. Revenues are generally considered to be available when they are collectible within the current year or soon enough thereafter to pay liabilities of the current year. For this purpose, the Municipality considers most revenues to be available if collected within 60 days after June 30, 2006. Revenue sources not meeting this availability criterion or collected in advance are recorded as deferred revenues at June 30, 2006. The principal revenue sources considered susceptible to accrual include property taxes, municipal license taxes, intergovernmental grants and contributions and interest income. These principal revenue sources meet both measurability and availability criteria in the accompanying GFFS, except for amounts recorded as deferred revenues.

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Fiscal Year Ended June 30, 2006

Governmental fund financial statements (Cont.)

In a manner similar to the GWFS, but subject to and limited by the availability criteria discussed above, 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, fees for licenses and permits, 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 nonexchange transactions are recorded in a similar manner to the GWFS, using the previously discussed criteria set forth by GASB No. 33 for nonexchange transactions, but subject to and limited by the availability criteria discussed above. Accordingly, municipal license tax receivables and revenues are generally recorded when the underlying exchange has occurred. Property tax receivables are also generally recorded in the period when an enforceable legal claim has arisen while property tax revenues (net of amounts considered not collectible) are also generally recorded in the period when resources are required to be used or the first period that the use of the resources is permitted. Receivables and revenues from reimbursement-type grants, contributions, donations and entitlements are also generally recorded as qualifying reimbursable expenditures are incurred, while receivables and revenues from other types of grants are recorded when all eligibility requirements imposed by the provider have been met.

Interest income is recorded when earned only if collected within 60 days after year-end since these would be considered both measurable and available.

As previously discussed the Municipality adopted the provisions of GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements* (GASBI No. 6), which modifies the recognition criteria for certain expenditures and liabilities reported under the modified accrual basis of accounting and clarifies a number of situations in which the Municipality should distinguish between governmental fund liabilities and general long-term liabilities.

Pursuant to the provisions of GASBI No. 6, expenditures and related liabilities are generally recorded in the accompanying governmental fund financial statements in the accounting period in which the liability is incurred, as under the accrual basis of accounting, but only to the extent that they are normally expected to be liquidated with expendable financial resources.

Modifications to the accrual basis of accounting include:

- Employees' accumulated vacation, sick leave and compensatory time (compensated absences) is recorded as expenditure when consumed. The amount of the unpaid

COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

Governmental fund financial statements (Cont.)

compensated absences has been reported only in the accompanying statements of net assets.

- Principal on bonds and notes payable are recorded when they mature (when payment is due), except for principal and interest due in July 1 of the following fiscal year, which are recorded when resources are available in the debt service fund (generally June 30)
- Accounts payable and accrued liabilities not expected to be liquidated with available and expendable financial resources are recorded in the accompanying statement of net assets but not in the governmental funds.

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

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

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

f) Stewardship, Compliance and Accountability

Budgetary Control

According to the Autonomous Municipalities Act of the Commonwealth of Puerto Rico, 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 for both funds. 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 budget is prepared.

The Mayor must submit an annual budgetary resolution project (the Project) to the Commissioner of Municipal Affairs of Puerto Rico (the Commissioner) and the

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Fiscal Year Ended June 30, 2006

Budgetary Control (Cont.)

Municipal Legislature no later than each May 10 and May 15, respectively. 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 each June 13.

The Municipal Legislature has 10 business days, up to 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 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 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 3 days to sign and approve it.

If the budgets are not adopted prior to the end of the deadlines referred to above, the annual budgets for the preceding fiscal year, as approved by the Legislature and the Mayor, are automatically renewed for the ensuing fiscal year until the Municipal Legislature and the Mayor approve new budgets. This permits the Municipality to continue making 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 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 and Budget has the responsibility to ensure that budgetary spending control is maintained. For day-to-day management control, 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 functions/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.

COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

Budgetary Control (Cont.)

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 under the budgetary (statutory) basis of accounting, which is not in accordance with GAAP.

Under the budgetary basis of accounting, revenue is generally recognized 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 year after the end of the fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment. Unencumbered appropriations and encumbrances lapse at 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 provides information about the general fund's original budget, the amendments made to such budget, and the actual general fund's results of operations under the budgetary basis of accounting for the fiscal year ended June 30, 2006. 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, 2006, which is prepared by the Municipality's Department of Finance and Budget. Copies of that report may be obtained by writing to the Municipality's Director of Finance and Budget.

Accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present the governmental fund financial statements in conformity with GAAP. Accordingly, the accompanying budgetary comparison schedule is accompanied by a reconciliation of the differences between the budgetary basis and GAAP actual amounts.

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Budgetary Accounting (Cont.)

The Municipality does not legally adopt budgets for the state legislative joint resolutions capital fund. The financial resources received by these funds are not subject to budgeting by the Municipality since the resources received each year from the respective grantors varies from year to year, and the respective amounts are granted at their discretion.

g) Unrestricted and Restricted Deposits

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

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

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

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

h) Unrestricted and Restricted Accounts and Notes Receivable

In the accompanying GWFS, receivables consist of all revenues earned but not collected at June 30, 2006. Major receivable balances for the governmental activities include municipal license taxes, property taxes and intergovernmental receivables. Tax receivables in the general fund represent uncollected property taxes and municipal license taxes

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h) Unrestricted and Restricted Accounts and Notes Receivable (Cont.)

Intergovernmental receivables are composed of: (1) amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federal and state funded programs (recorded in the general fund, special revenue funds and capital project funds).

These accounts receivables are stated net of estimated allowances for uncollectible 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.”

i) Capital Assets

Capital assets used in governmental activities include land and improvements, buildings and other facilities, machinery and equipment, licensed vehicles, construction in progress, and infrastructure. These assets are capitalized and reported in the accompanying statement of net assets. Infrastructure assets are generally stationary in nature and include roads, bridges, streets and sidewalks, drainage systems and other similar assets.

The Municipality defines capital assets as assets with an individual cost of \$500 or more at the date of acquisition or construction, and with useful lives extending beyond one year. All assets with individual costs under \$500 or with useful lives not exceeding one year, are charged directly to expense in the accompanying statement of activities. In the governmental funds, all capital assets are recorded as expenditures.

In the statement of net assets, all capital assets are recorded at cost or estimated historical cost if actual cost was unavailable, except for donated capital assets, which are recorded at their estimated fair value at the date of donation. Estimated historical costs based on deflated current costs were used to value a significant portion of certain land, buildings, structures and building improvements constructed or acquired prior to June 30, 2002. The method to deflate the current costs using an approximate price index was used only in the case of certain items for which their historical cost documentation was not available. Actual historical costs were used to value land, building, structures, building improvements, construction in progress, machinery and equipment and licensed vehicles constructed or acquired during or after the year ended June 30, 2003. At June 30, 2006 the Municipality has not made a study to determine an actual or historical cost to infrastructure.

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i) Capital Assets (Cont.)

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

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>
Improvements	40
Buildings, structures and building improvements	50
Infrastructure	60
Licensed vehicles	5
Furniture and fixtures	10
Machinery and equipment, excluding those held under capital leases	3

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

j) Deferred Revenues

The Municipality reports deferred revenue on its GFFS and GWFS. In the GFFS, deferred revenue arises when:

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

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

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k) Compensated Absences

Compensated absences are accounted for under the provisions of Statement No. 16, *Accounting for Compensated Absences*, issued by GASB (GASB No. 16). Compensated absences include paid time off made available to employees in connection with vacation, sick leave and compensatory time. The liability for compensated absences recorded in the accompanying statement of net assets is limited to leave that: (1) is attributable to services already rendered on or before June 30, 2006 and (2) is not contingent on a specific event (such as illness) that is outside the control of the Municipality and the employee.

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

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

l) Long-term Debt

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

All long-term debt to be repaid from governmental resources is reported as liabilities in the accompanying statement of net assets. Principal and interest payments on bonds due in July 1 of the following fiscal year, are recorded as fund liabilities in the GFFS when resources are available in the debt service fund (generally at June 30). In the GFFS, the face amount of debt issued is reported as other financing sources when issued.

In the GWFS debt issuance costs are reported as deferred charges and are amortized under the straight-line method over the life of the debt while in the GFFS such costs are recognized as expenditures during the current period.

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m) Accounting for Pension Costs

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

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

n) Risk Management

The Municipality carries commercial insurance covering casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department (the Treasury Department) on behalf of all municipalities of Puerto Rico. The Treasury Department pays the insurance premiums on behalf of the Municipality and then is reimbursed each year through monthly equal payments deducted from the Municipality's gross property tax collections made by CRIM.

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 discretely 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 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 ("FSE" by its Spanish acronym), 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

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n) Risk Management (Cont.)

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 quarterly basis.

The Municipality also obtains medical insurance coverage for its employees. The current insurance policies have not been canceled or terminated at June 30, 2006. In the past three years, the Municipality has not settled claims that exceeded insurance coverage.

o) Reservations of Fund Balances

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

- ***Encumbrances*** – Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts represent reservations of unexpired appropriations and generally will become liabilities in future periods as the goods or services are received.
- ***Debt Service*** – Represent fund balances available to finance future debt service payments.
- ***Other Specified Purposes*** – Represent resources set aside for use in federal and state grant programs accounted for in the special revenue and capital project funds.

p) Interfund Activities

Permanent reallocations of resources among the Municipality's funds are classified as interfund transfers. The Municipality has the following types of activities recorded among funds in the accompanying GFFS:

- ***Transfers*** – Represent legally required transfers that are reported when incurred as "transfers-in" by the recipient fund and as "transfer-out" by the disbursing fund.

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Fiscal Year Ended June 30, 2006

p) Interfund Activities (Cont.)

- *Intra-entity Activities* – Represent transfers among funds that are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.
- *Advances* – Represent amounts advanced among funds, which are not considered to be currently available financial resources.

In the GFFS, interfund 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.

2. Cash

The Municipality maintains its deposits in various commercial banks located in Puerto Rico and GDB. Proceeds from bonds and funds related to certain grant awards are required by law to be held with GDB.

The balances deposited in commercial banks are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$100,000 per depositor. Under the laws and regulations of the Commonwealth, public funds deposited in commercial banks must be 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 with GDB are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2006.

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. The Municipality has no credit risk policy, since there are no investments.

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Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

2. Cash (Cont.)

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 limiting the weighted average maturity of its investments portfolio (cash equivalents consisting of certificates of deposit) to less than three months.

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. The Municipality has no deposit policy for custodial credit risk.

Foreign exchange risk – The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. The Municipality has no policy for foreign exchange risk, since there are no foreign exchange deposits or investments.

Cash and cash equivalents as of June 30, 2006, are classified in the accompanying financial statements as follows:

Statement of net assets:		
Restricted cash and cash equivalents		\$40,876,160
Total cash and cash equivalents		<u>\$40,876,160</u>

Cash and cash equivalents as of June 30, 2006, consist of the following:

	Bank Balance	Carrying Amount
Cash in commercial banks	\$ 11,672,604	\$10,835,370
Cash in fiscal agent	<u>30,040,790</u>	<u>30,040,790</u>
Total cash and cash equivalents	<u>\$41,713,394</u>	<u>\$40,876,160</u>

Pursuant to the Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico, the Municipality may invest in 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.

Certificates of deposit of the general and the special revenue fund, which amounted to \$5,000,000 as of June 30, 2006 earns interest at 5.19% maturing in July 31, 2006, renewable at option of the Municipality, interests earned on certificates of deposit are recognized as revenues of the corresponding fund.

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 Toa Baja. 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, 2006, the municipal tax rates imposed for taxpayers engaged in any type of business, except financial institutions, sales tax to be paid is 0.50% of 1.00% of its business volume during

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Fiscal Year Ended June 30, 2006

3. Municipal License Taxes (Cont.)

fiscal year. Financial institutions are required to pay 1.5% of its volume of business. These rates were effective for fiscal year 1993-1994 and beyond through sale tax Law No. 113, of 1974, as amended by Law No. 82 of August 30, 1991.

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 \$1 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 on GFFS.

4. Property Taxes

The Municipality is authorized by Law No. 81 to impose and collect personal and real property taxes. Under the laws and regulations of the Commonwealth, personal property taxes can be imposed to any natural or legal person that at January 1 of each year is engaged in trade or business and is the owner of personal property used in trade or business.

Personal property taxes are self-assessed by taxpayers every year generally 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, 2006 was 6.28% (of which taxpayers pay 6.08% and 0.20% is reimbursed by the Department of Treasury). 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.

Residential real property occupied by its owner is exempt by law from property taxes on the first \$15,000 of the assessed value (at 1957 market prices). For such exempt amounts, the Department of Treasury assumes payment of the basic tax (4% and 6% for personal and real property, respectively) to the Municipality, except for property assessed of less than \$3,500 (at 1957 market prices), for which no payment is made.

CRIM is responsible for the billing and collections of real and personal property taxes on behalf of the Municipality. Prior to the beginning of each fiscal year, CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, CRIM advances funds to the Municipality based on the initial estimated collections. CRIM is required by law to prepare a settlement

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Fiscal Year Ended June 30, 2006

4. Property Taxes(Cont.)

statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than each December 31. If CRIM remits to the Municipality property tax advances, which are less than the property tax actually collected, an additional property tax receivable is recorded at June 30. However, if advances exceed the amount actually collected by CRIM, an intergovernmental payable is recorded at June 30.

Law No. 81 provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation. Such special tax is levied and collected by CRIM. Collections of this special tax are remitted to the Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth.

In addition, 1.40% of the total personal and real property taxes collected by CRIM is restricted for the Municipality's debt service requirements and is retained by GDB for such purposes.

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

- i. Thirty five percent (35%) 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 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.
- ii. An additional amount not exceeding \$16 million, on an annual basis, is distributed to the Municipal Equalization Fund, provided it is within the 35% corresponding to the municipalities of the Commonwealth. 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 the Health Insurance Administration, a component unit of the Commonwealth.

5. Interfund Transactions

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, 2006 are as follows:

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5. Interfund Transactions(Cont.)

<u>Due to:</u>	<u>General Fund</u>
Major funds:	
Debt service fund	\$ 86,881
Head start program	839,715
Nonmajor funds:	<u>2,708,411</u>
Total:	\$ 3,635,007

At June 30, 2006 all amounts due to among funds are considered collectible by the Municipality's management.

6. Capital Assets

The municipality is organizing its property records to determine the amount invested in capital assets. This process requires the identification of all real and personal property through physical inventories and their subsequent valuation. Once this process is completed, the Municipality will determine the correct amount of its investment in capital assets recorded in the Statement of Net Assets. As of June 30, 2006, the Municipality has identified most of its capital assets and is in the process to validate records with original documents.

Capital assets activity for the year ended June 30, 2006, was as follows:

Capital Assets	Beginning Balance	Additions	Retirements	Reclasses	Ending Balance
Non-depreciable assets					
Land	\$ 3,191,186	\$ 45,253	-	-	\$ 3,236,439
Construction in progress	<u>12,565,737</u>	-	-	-	<u>12,565,737</u>
Total non-depreciable assets	15,756,923	45,253	-	-	15,802,176
Depreciable assets					
Buldings and other facilities	34,780,738	1,414,951	-	-	36,195,689
Improvements	16,896,125	881,423	-	-	17,777,548
Machinery and equipment	4,526,939	2,707,411	-	-	7,234,350
Vehicles	7,644,272	1,200	-	-	7,645,472
Infrastructure	<u>39,696,772</u>	-	-	-	<u>39,696,772</u>
	103,544,846	5,004,985	-	-	108,549,831
Less: Accumulated depreciation	<u>(27,238,953)</u>	<u>(2,520,734)</u>	-	-	<u>(29,759,687)</u>
Depreciable assets, net	<u>76,305,893</u>	<u>2,484,251</u>	-	-	<u>78,790,144</u>
	<u>\$ 92,062,816</u>	<u>\$ 2,529,504</u>	-	-	<u>\$ 94,592,320</u>

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Fiscal Year Ended June 30, 2006

6. Capital Assets(Cont.)

Depreciation expense was charged to functions as follows:

Mayor and municipal assembly	\$ 19,179
General government	718,450
Urban and economic development	283,161
Culture and recreation	98,408
Health and sanitation	455,056
Public housing and welfare	946,480
	<u>\$2,520,734</u>

7. Employees Retirement System

The Municipality's employees participate in the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (the "System"). The System is the administrator of a multi-employer cost-sharing (as related to the Municipality's reporting entity) defined pension plan established by the Commonwealth. The System was created under Act. No. 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. The System covers all regular employees of the Commonwealth and its instrumentalities, the Municipality and other municipalities of the Commonwealth.

The System is independent, thus assets may not be transferred to another system or used for any purpose other than to benefit each system's participants. The System issued publicly available financial reports that include its basic financial statements and required supplementary information for each of them, including required six-year trend information. Those reports may be obtained by writing to the administrator of the System.

The System provides for retirement, death and disability benefits. Death and disability retirement benefits are available to members for occupational and non-occupational death and disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after 10 years of plan participation.

Retirement benefits are determined by the application of 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 plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75 percent of the average compensation.

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

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Fiscal Year Ended June 30, 2006

7. Employees Retirement System (Cont.)

System 2000 is a hybrid defined contribution plan, also known as cash balance plan. Under this new plan, there is a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. The Commonwealth neither the Municipality will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employees' contribution (with a minimum of 8.275 percent of the employees' salary up to a maximum of 10.00 percent) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity U.S. Treasury Note; (2) earn a rate equal to 75 percent of the return of the System 2000's investment portfolio (net of management fees); or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The employer's contributions (9.275 percent of the employees' salary which is applicable to the Municipality) will be used to fund the current plan.

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

Funding Policy:

Contribution requirements are established by law and are as follows:

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

On August 12, 2000, Act No. 174 was approved to allow certain participants of the ERS to be eligible for early retirement upon attaining at least age 55 with 25 years of service, provided they made their election on or before April 1, 2001. Those who elected early retirement under this law will receive monthly benefits of 75 percent (if 25 or more year of service and 55, or 30 or more years or services and age 50) or benefits of 65 percent (if 25 years of service by less than age 55) of their average compensation which is computed based on the highest 36 months of compensation recognized by the System. In these cases, the employer (including the Municipality) is responsible for contributing to the System the amount needed to cover the benefit payments and employer contribution with respect to the participants covered until the participants reaches the normal retirement age.

Historically, the Commonwealth has reported the System as a single-employer plan (as relates only to the financial reporting entity of the Commonwealth) in its comprehensive annual financial report. Accordingly, any actuarial deficiency that may exist or arise related to the Municipality's participating employees will be assumed by the Commonwealth since

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

7. Employees Retirement System (Cont.)

the System does not allocate any actuarial deficiencies pertaining to municipal employees participating in the System. The Municipality is only required by law to make statutory contributions in the rates mentioned above. As a result, no net pension obligation nor net pension asset that may be allocable to the Municipality's participating employees, if any, has been recorded in the accompanying basic financial statements.

8. Due to Other Governmental Units

As of June 30, 2006, the balance due to other governmental units of the general fund, for services rendered to the municipality, consists of the following:

Water and Sewer Authority	\$ 132,249
Electric Power Authority	2,332,739
Puerto Rico Labor Department	6,208
Puerto Rico Telephone Company	318,912
Retirement System Administration	328,717
PR Treasury Department	310,498
State Insurance Corporation	<u>163,230</u>
	<u>\$3,592,553</u>

9. Long-Term Obligations

The Municipality's Legislature is legally authorized to determine the contracting of debts of the Municipality. Nevertheless, the laws and regulations of the Commonwealth also provide that:

- Direct obligations of the Municipality (evidenced principally by bonds and notes) are backed by the full faith, credit and taxing power of the Municipality; and
- Direct obligations are not to be issued if the amount of the principal of, and interest on, such bonds and notes (and on all such 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 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 to be repaid with the proceeds of property taxes restricted for debt service.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

9. Long-Term Obligations (Cont.)

In addition, before any new bonds or notes are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. At June 30, 2006, the Municipality is in compliance with the debt limitation requirements. The general long-term debt activity for the year ended June 30, 2006 was as follows:

	Balance June 30, 2005	Additions	Principal Payments	Balance June 30, 2006	Due within one year
General obligations	\$39,722,625	\$ 17,470,000	\$ 2,996,802	\$54,195,823	\$3,961,650
Special obligations	10,974,000	-	305,000	10,669,000	985,000
Compensated absences	6,960,164	163,798	-	7,123,962	3,937,484
Due to other government units	6,444,227	-	986,250	5,457,977	190,517
Reserve for federal cost disallowance	116,100	-	33,000	83,100	39,000
Landfill closure accrued liabilities	<u>21,944,531</u>	<u>2,878,936</u>	<u>-</u>	<u>24,823,467</u>	<u>-</u>
	<u>\$86,172,647</u>	<u>\$20,512,734</u>	<u>\$4,321,052</u>	<u>\$102,353,329</u>	<u>\$ 9,086,651</u>

a) Bonds Payable

The Municipality issues general and special obligations bonds and notes to provide for the acquisition and construction of major capital facilities and equipment, as well as, to cover certain operating needs.

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, 2006:

General Obligations - Bonds and Notes

\$9,725,000 series 1994, payable in annual installments raging from \$135,000 to \$850,000 through July 2019; interest at 8%.	\$7,510,000
\$8,150,000 series 1994, payable in annual installments raging from \$300,000 to \$880,000 through July 2009; interest at 12%.	3,150,000
\$1,670,000 series 1994, payable in annual installments raging from \$25,000 to \$145,000 through July 2019; interest ranging from 6.15% to 8.206%.	1,290,000
\$5,100,000 series 1994, payable in annual installments raging from \$185,000 to \$550,000 through July 1, 2009; interest ranging from 6.106% to 6.58%.	1,975,000

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

General Obligations - Bonds and Notes (continued)

\$2,755,000 series 1994, payable in annual installments raging from \$60,000 to \$265,000 through July 1, 2014; interest ranging from 7.25% to 6.58%.	1,755,000
\$1,540,000 series 1994, payable in annual installments raging from \$170,000 to \$240,000 through July 1, 2020; interest ranging from 5.4% to 6.875%.	1,235,000
\$1,020,000 series 1996, payable in annual installments raging from \$40,000 to \$135,000 through July 1, 2001; interest ranging from 4.87% to 6.75%.	550,000
\$3,530,000 series 1998, payable in annual installments raging from \$145,000 to \$305,000 through July 1, 2020; interest ranging from 6% to 7.08%.	2,890,000
\$1,500,000 series 1998, payable in annual installments raging from \$44,000 to \$108,000 through July 1, 2019; interest at 4.5%.	1,085,106
\$5,075,000 series 1999, payable in annual installments raging from \$195,000 to \$540,000 through July 1, 2015; interest ranging from 6.16% to 11.06%.	3,655,000
\$3,470,000 series 2000, payable in annual installments raging from \$140,000 to \$355,000 through June 2014; interest at approximately 8%.	2,475,000
\$605,000 series 2000, payable in annual installments raging from \$70,000 to \$105,000 through June 2006; interest at approximately 8%.	105,000
\$705,000 series 2000, payable in annual installments raging from \$95,000 to \$145,000 through July 1, 2006; interest ranging from 5.88% to 8%.	145,000
\$655,000 series 2000, payable in annual installments raging from \$25,000 to \$70,000 through July 1, 2015; interest ranging from 5.88% to 8%.	510,000

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

General Obligations - Bonds and Notes (continued)

\$875,000 series 2000, payable in annual installments raging from \$5,000 to \$75,000 through July 2025; interest ranging from 5.88% to 8%.	810,000
\$2,062,000 series 2001, payable in annual installments of \$62,800 through January 1, 2021; including interest at 2%.	1,620,717
\$3,200,000 series 2002, payable in annual installments raging from \$55,000 to \$245,000 through July 1, 2027; interest ranging from 5% to 6.5%.	3,025,000
\$3,040,000 series 2005, payable in annual installments raging from \$100,000 to \$220,000 through July 1, 2024; interest ranging from 3.28% to 5%.	2,940,000
\$2,515,000 series 2005, payable in annual installments raging from \$305,000 to 420,000 though July 2012 interest raging from 4.2% to 4.7%	2,515,000
12,065,000 series 2005, payable in annual installments raging from \$345,000 to \$960,000 though July 2025 interest raging from 4.4% to 5.3%	12,065,000
\$1,555,000 series 2006, payable in annual installments raging from \$180,000 to \$270,000 though July 2012 interest raging from 6.2% to 6,5%	1,555,000
\$1,335,000 series 2006, payable in annual installments raging from \$155,000 to \$230,000 though July 2012 interest raging from 6.2% to 6.5%	<u>1,335,000</u>
	\$54,195,823

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

Special Obligation – Notes

\$400,000 series 1996, payable in annual installments rasing from \$10,000 to \$40,000 through July 1, 2016; interest at 8%.	285,000
\$10,674,000 series 2005, payable in annual installments rasing from \$290,000 to \$1,392,000 through July 1, 2014; interest ranging from 5% to 5.5%.	<u>10,384,000</u>
	10,669,000
Total Long Term Debt	<u>\$ 64,864,823</u>

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

Interest rates on serial bonds subject to variable rates are reviewed periodically by GDB and are based on the fluctuation of GDB's weighted average rate for its commercial paper program, not to exceed 8%. Under this program, GDB issues commercial papers in the U.S. taxable and tax-exempt markets, in the Eurodollar market and to corporations that have tax exemption under the Commonwealth's Industrial Incentives Act and qualify for benefits provided by the U.S. Internal Revenue Code Section 936.

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

General Obligations - Bonds and Notes

Year Ending June 30,	Principal	Interest	Total
2007	\$ 3,961,650	\$ 2,910,000	\$ 6,871,650
2008	4,336,532	2,742,152	7,078,684
2009	4,281,452	2,483,694	6,765,146
2010	4,141,411	2,221,748	6,363,159
2011	3,301,409	1,996,790	5,298,199
2012-2016	15,844,455	7,242,901	23,087,356
2017-2021	11,438,914	3,396,766	14,835,680
2022-2026	6,415,000	973,349	7,388,349
2027-2031	<u>475,000</u>	<u>24,222</u>	<u>499,222</u>
	<u>\$ 54,195,823</u>	<u>\$ 23,991,622</u>	<u>\$ 78,187,445</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

Special Obligation – Notes

Year Ending June 30,	Principal	Interest	Total
2007	958,000	66,978	1,024,978
2008	1,006,000	602,938	1,608,938
2009	1,053,000	448,643	1,501,643
2010	1,109,000	389,287	1,498,287
2011	1,169,000	326,755	1,495,755
2012-2016	5,334,000	617,025	5,951,025
2017-2021	<u>40,000</u>	<u>1,000</u>	<u>41,000</u>
	<u>\$ 10,669,000</u>	<u>\$ 2,452,626</u>	<u>\$ 13,121,626</u>

b) Due to government units

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. CRIM retains the determined amount 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.

CRIM deficiency - The Municipality entered into a financing agreement with CRIM for the payment of delinquent property tax account sold to private investors. The financing agreement is in the form of a line of credit during the next 25 years.

c) Municipal Solid Waste Landfill Closure and Postclosure Care Costs

According to the regulations set forth by the U.S. Environment Protection Agency (EPA) in its “Solid Waste Disposal Facility Criteria”, issued on October 9, 1991, the Municipality is required to place a final cover on the Municipality’s landfill site when it stops accepting waste, and to perform certain maintenance and monitoring functions at the site for 30 years after closure. In accordance with GASB No. 18, the Municipality has performed a study of the activities that need to be implemented at the Municipality’s landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. Based on this study, the Municipality has recognized a liability of \$21,944,531 in the accompanying GWFS using current costs allocated based on the actual landfill capacity used at June 30, 2006. The portion of the estimated current costs to be incurred in future years is approximately \$30,755,469 which has not been recorded yet in the

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

c))Municipal Solid Waste Landfill Closure and Postclosure Care Costs(Cont.)

accompanying GWFS. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations. At June 30, 2006, the Municipality's landfill is still operating and approximately 83 cords of the Municipality's total capacity has been used at June 30, 2006.

d) Compensated Absences

At June 30, 2006, the liability for compensated absences is composed as follows:

	Due within One year	Due after One year	Total
Vacations	\$ 2,148,822	\$ 1,432,548	\$ 3,581,370
Sick leave	751,684	1,753,930	2,505,614
Compensatory time	<u>1,036,978</u>	<u>-</u>	<u>1,036,978</u>
Total:	\$ 3,937,484	\$ 3,186,478	\$ 7,123,962

e) Federal Cost Disallowance

The Municipality is a grantee in various Federal Financial Assistance Programs. Entitlement to the resources is generally based on compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of the resource for eligible purposes.

Substantially all grants are subject to financial and compliance audits by the grantors. Any disallowance cost because of these audits, become a liability of the fund that receives the grant and must be reimbursed to the Federal Government from the Municipality's local funds. The "Schedule of Reportable Conditions and Recommendations" for the year ended June 30, 2004, disclosed several instances of noncompliance with applicable laws and regulations and with internal accounting and administrative control structure. On March 28, 2003, the Department of Housing and Urban Development presented a Monitoring Review Report for the programs CDBG, Home Investment Partnership, Emergency Shelter Grant and Disaster Recovery Initiative, which disclosed several instances of noncompliance findings and concerns. The report disallowed the amount of \$318,941 and questioned costs of \$1,590,356. After submitting additional evidence in the response to the findings and concerns, the Municipality entered in an agreement with the Community Planning and Development Division to reimburse the amount of \$161,100 from its local funds to the following programs on a five years installment payment plan:

Program	Amount
HOME	\$ 80,000
CDBG	8,387
ESGP	<u>72,713</u>
	<u>\$161,100</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

e) Federal Cost Disallowance

Annual payments requirements are due on June 30 of each year as follows.

HOME		ESGP	
Year Ending June 30,	Principal	Year Ending June 30,	Principal
2007	22,000	2007	17,000
2008	<u>27,000</u>	2008	<u>17,000</u>
Total	<u>\$49,000</u>	Total	<u>\$34,000</u>

10. Commitments and Contingencies

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 authorized 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.

With respects to pending or threatened litigation, the Municipality has reported liabilities of \$585,592 for awarded or anticipated unfavorable judgments as of June 30, 2006.

The Municipality has encumbrances for a total of \$2,243,094 for future payments to contractors and suppliers. This amount has been accrued in GWFS. In addition, the Municipality has obligation for urban and economic development projects amounted \$957,416. Both amount are obligations of the General Fund, where only a provision of \$105,712 could be reserved at the fiscal year ended.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2006

11. Prior Period Adjustments

In the Statement of Activities the net assets at the beginning of year have been adjusted by \$(80,553), mainly due to an adjustments of approximately \$(1.3) to decrease the fund balance by the amount related to last year Christmas bonus payable, and \$4.0 millions to increase the fund balance by the amount restated in long term debts related to bonds and notes payables, at the beginning of the year. In the Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds the fund balances at the beginning of the year were adjusted by approximately \$2.8 millions as follows:

	Debt Service				Totals
	General Fund	Fund	Head Start	Other Funds	
Fund balances at beginning of year	\$ 4,229,690	\$ 6,613,953	\$ 475,952	\$ 14,413,343	\$ 25,732,938
Other				479	
Amount related to restatement on Debt Service					
Fund liabilities amounts	<u>41,977</u>	<u>(2,829,285)</u>	<u>-</u>	<u>-</u>	<u>(2,787,308)</u>
	<u>41,977</u>	<u>(2,829,285)</u>	<u>-</u>	<u>479</u>	<u>(2,786,829)</u>
Restated Fund Balances at beginning of year	<u>\$ 4,271,667</u>	<u>\$ 3,784,668</u>	<u>\$ 475,952</u>	<u>\$ 14,413,822</u>	<u>\$ 22,946,109</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
 Budgetary Comparison Schedule – General Fund
 Fiscal Year Ended June 30, 2006

	Budgeted amounts		Actual amounts (budgetary basis) (see note 1)	Variance with final budget-over (under)
	Original	Final		
Revenues:				
Property taxes	\$ 14,516,176	\$ 14,516,176	\$ 14,516,176	-
Municipal license taxes	10,595,000	10,595,000	10,931,231	336,231
Construction excise taxes	6,000,000	6,000,000	1,369,709	(4,630,291)
Charges for services	11,195,000	11,195,000	9,529,451	(1,665,549)
Intergovernmental grants and contributions	5,463,686	5,803,321	3,547,553	(2,255,768)
Interest on deposits and investments	800,000	800,000	918,092	118,092
Miscellaneous	1,924,000	3,262,721	3,781,942	519,221
Total revenues	<u>50,493,862</u>	<u>52,172,218</u>	<u>44,594,154</u>	<u>(7,578,064)</u>
Expenditures:				
General government	22,150,065	24,102,876	23,691,973	(410,903)
Urban and economic development	3,826,638	3,807,291	3,772,044	(35,247)
Public safety	11,952,960	10,316,923	10,225,341	(91,582)
Public housing and welfare	3,516,073	3,161,450	3,105,359	(56,091)
Culture, education and recreation	3,770,275	3,910,908	3,853,145	(57,763)
Health and sanitation	5,277,851	5,058,523	5,026,005	(32,518)
Capital outlays	-	259,707	259,707	-
Transfers to others funds	-	1,554,540	1,554,540	-
Total expenditures	<u>\$ 50,493,862</u>	<u>52,172,218</u>	<u>51,488,114</u>	<u>\$ (684,104)</u>
Net change in fund balance:			<u>(6,893,960)</u>	<u>(6,893,960)</u>

Explanation of Differences:

Sources/inflows of financial resources:

Actual amounts (budgetary basis) "available for appropriations from budgetary comparison schedule	\$ 44,594,154
Differences - budget basis to GAAP:	
Differences in assets and liabilities resulting from modified accrual basis of accounting in comparison with budgetary basis	(2,413,827)
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting.	(3,040,261)
Total revenues as reported on the statement of revenues, expenditures and changes in fund balances - general fund	<u>\$ 39,140,066</u>

Uses/outflows of financial resources:

Actual amounts (budgetary basis) "total charges to appropriations" from budgetary comparison schedule	\$ 51,488,114
Differences - budget basis to GAAP:	
Transfers to other funds are outflows of budgetary resources	(1,554,540)
Differences in assets and liabilities resulting from modified accrual basis of accounting in comparison with budgetary basis	(1,652,081)
Prior year encumbrances recorded as current year expenditures for GAAP basis	5,497,932
Current year encumbrances recorded as expenditures for budgetary purposes	(8,987,683)
Total expenditures as reported on the statement of revenues, expenditures and changes in fund balances - general fund	<u>\$ 44,791,742</u>

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to Budgetary Comparison Schedule – General Fund
Fiscal Year Ended June 30, 2006

The Municipality's annual budget is prepared under the budgetary basis of accounting, which is not in accordance with GAAP.

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

Under the budgetary basis of accounting 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 the actual expenditure. In the governmental funds, encumbrances 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 year after the end of fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment. Unencumbered appropriations and encumbrances lap at 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, provides information about the general fund's original budget, the amendments made to such budget, and the actual general fund's results of operations under the budgetary basis of accounting for the fiscal year ended June 30, 2006.

Except for the General Fund, the Municipality legally does not adopt budgets for its major special revenues and capital projects funds. Accordingly, the neither accompanying basic financial statements, nor required supplementary information include statements or revenues and expenditures – budget and actual-budgetary basis, or budgetary comparison schedules, respectively, for these major programs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Expenditure of Federal Awards
For the Year Ended June 30, 2006

Federal Grantor/Pass-Through Grantor/ Program or Cluster Title	Federal CFDA Number	Federal Expenditures
<u>U.S. Department of Housing and Urban Development</u>		
Community Development Block Grants/Entitlement Grants	14.218	\$ 3,313,835
Emergency Shelter Grants Program (ESGP)	14.231	30,654
Home Investment Partnerships Program	14.239	468,686
Housing Opportunities to Person with AIDS	14.241	156,063
Community Development Block Grants-Section 108 Loan Guarantees	14.248	14
Housing Assistance Payments Programs Program for low-income Families Voucher Housing (Rental Voucher)	14.871	<u>1,487,920</u>
Total U.S. Department of Housing and Urban Development		<u>5,457,172</u>
<u>U.S. Department of Health and Human Services/Pass Through the Puerto Rico Governor's Office for Human Development</u>		
Child Care and Development Block Grant	93.575	495,754
Head Start	93.600	<u>9,147,078</u>
Total U.S. Department of Health and Human Services/Pass Through the Puerto Rico Governor's Office for Human Development		9,642,832
<u>U.S. Department of Agriculture/Pass Through the Puerto Rico Department of Education</u>		
Child and Adult Care Food Program	10.558	<u>748,417</u>
Total U.S. Department of Agriculture/Pass Through the Puerto Rico Department of Education		<u>748,417</u>
Total Federal Awards Expended		<u>\$ 15,848,421</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Notes to the Schedule of Expenditures of Federal Award
For the Year ended June 30, 2006

NOTE 1 – GENERAL

The accompanying schedule of federal awards presents balances expended, including loan guarantee assistance, of all federal award programs of the Municipality. The reporting entity is defined in Note 1 (A) to the basic financial statements.

NOTE 2 - FEDERAL CFDA NUMBER

The CFDA number included in this schedule were determined based on the program name, review of grant contract information and the Office of Management and Budgets Catalogue of Federal Domestic Assistance.

NOTE 3 - SECTION 8 PROGRAMS

Both Section 8 programs, existing rental certificate and rental voucher, receive a reimbursement income, arising from rents paid to participants under the Section 8 Program, pertaining to another Municipality, but for which the property is rented in the Municipality of Toa Baja. In addition, the Municipality charges an administrative fee for this service. Therefore, expenditures include those paid by the Municipality under this agreement, not included in program award amount.

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

To the Honorable Mayor and
the Municipal Assembly
Municipality of Toa Baja
Toa Baja, Puerto Rico

We have audited the financial statements of the Municipality of Toa Baja as of and for the year ended June 30, 2006, and have issued our report thereon dated December 28, 2006. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Municipality of Toa Baja financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such as an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs Section II.

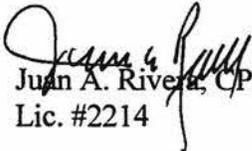
Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Municipality of Toa Baja internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Municipality of Toa Baja ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions in federal award are described in the accompanying schedule of findings and questioned costs Section II and also we have reported to the management of Municipality of Toa Baja those reportable condition that affect the internal control of the Municipality operations in a separate letter.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weakness. However, we believe that none of the reportable conditions described above is a material weakness.

This report is intended for the information of the audit committee, the Municipality's management, the Department of Housing and Urban Development (Cognizant Agency), and federal awarding agencies and pass-through entities and not is intended to be and should not be used by anyone other than these specified parties.


Juan A. Rivera, CPA
Lic. #2214

December 28, 2006
Toa Baja, Puerto Rico



NOTE: Stamp No.2195609 of the Puerto Rico State Society of Certified Public Accountants was affixed to the original report.

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

To the Honorable Mayor and
the Municipal Assembly
Municipality of Toa Baja
Toa Baja, Puerto Rico

Compliance

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

As described in item Section II in the accompanying schedule of findings and questioned costs, the Municipality of Toa Baja did not comply with requirements regarding administrative requirements that are applicable to its Section 8, CDBG, HOME, HOPWA, Child Care, and Head Start Programs. Compliance with such requirements is necessary for the Municipality of Toa Baja to comply with the federal regulations.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality of Toa Baja complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2006.

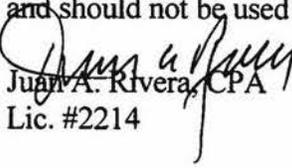
Internal Control Over Compliance

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

Our noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Municipality of Toa Baja ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs in Section II.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

However, we believe that none of the reportable conditions described above is a material weakness. This report is intended for the information of the audit committee, the Municipality's management, the Department of Housing and Urban Development (Cognizant Agency), and federal awarding agencies and pass-through entities. However, this report is not intended to be and should not be used by anyone other than these specified parties.


Juan A. Rivera, CPA
Lic. #2214

December 28, 2006
Toa Baja, Puerto Rico



NOTE: Stamp No. 2195610 of the Puerto Rico State Society of Certified Public Accountants was affixed to the original report.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Findings and Questioned Cost
For the Year Ended June 30, 2006

Section II. Federal Awards Findings and Questioned Costs

Compliance findings:

Our examination of compliance with federal requirements for the Municipality of Toa Baja for the year ended June 30, 2006, disclosed that grants funds were generally administered in a satisfactory manner, except for the following situations:

A. Department of Housing and Urban Development

Housing Choice Voucher Program- CFDA 14.871

Documents and information required in the Municipality Administrative Plan (voucher program) met all requirements except for the following:

Condition 06-1

Cash Management

The Housing Choice Voucher has a large balance in its bank account as of June 30, 2006.

Criteria

Code of Federal Regulation 24 §985.157(b)(1)

PHA use of program receipts- Program receipts must be used in accordance with the PHA's HUD-approved budget. Such program receipts may only be used for:

- (i) Housing assistance payments; and*
- (ii) PHA administrative fees.*

Housing Voucher Program Guide Book Chapter 20 p.20-1

A year-end settlement report will be prepared to reconcile any differences between the PHA's estimated requirements and the level of funds actually needed.

Cause

The Municipality probably is not paying all the vouchers approved in the proposal submitted to Housing and Urban Development Agency.

Effect

The Municipality does not comply with the law referred above.

Recommendation

Comment this problem with HUD office about the amount in the Housing Choice Voucher bank account and request a solution for this situation or request fund for less amount until this situation has been resolved.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Findings and Questioned Cost
For the Year Ended June 30, 2006

Community Development Block Grant - CFDA 14.218

Documents and information required for the test the Compliance of CDBG Program met all requirements except for the following:

Condition 06-2

Cash Management

The reconciliation of CDBG banks and books for June has an ending balance due to payments corresponding to June and made it in July.

Criteria

Code of Federal Regulation 24 §85.21

(5) Written procedures to minimize the time elapsing between the transfer of funds to the recipient from the U.S. Treasury and the issuance or redemption of checks, warrants or payments by other means for program purposes by the recipient. To the extent that the provisions of the Cash Management Improvement Act (CMIA) (Pub. L. 101-453) govern, payment methods of State agencies, instrumentalities, and fiscal agents shall be consistent with CMIA Treasury-State Agreements or the CMIA default procedures codified at 31 CFR part 205, "Withdrawal of Cash from the Treasury for Advances under Federal Grant and Other Programs."

Cause

The Municipality did not make payments as soon as they receive the funds.

Effect

The Municipality does not follows the procedures establish by federal law.

Recommendation

Establish the procedures necessary to do the disbursements within a reasonable time after receive the funds from HUD as establish the Federal Regulation.

Housing Opportunities for Person with AIDS -CFDA 10.854

From the compliance test of other federal programs we observed the following exception:

Condition 06-3

Cash Management

A check of \$12,273 received from San Juan Municipality in August were deposited erroneously in the Housing Voucher bank account and not in a separate bank account for the specific program as required, and maintain the deposit in this account for approximately a year.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Findings and Questioned Cost
For the Year Ended June 30, 2006

Condition 06-3(Cont.)
Cash Management

Criteria

Code of Federal Regulation 24 §570.500

(a) General. Grantees are responsible for ensuring that grants are administered in accordance with the requirements of this part and other applicable laws. Grantees are responsible for ensuring that their respective project sponsors carry out activities in compliance with all applicable requirements.

(b) Grant agreement. The grant agreement will provide that the grantee agrees, and will ensure that each project sponsor agrees, to:

(1) Operate the program in accordance with the provisions of these regulations and other applicable HUD regulations; ...

Cause

The Municipality did not deposit the federal fund mentioned above in the correct bank account.

Effect

The Municipality is not in compliance with federal regulations.

Recommendation

The Municipality must ensure that federal funds received are deposited in the correct bank account.

B. Department of Health and Human Services

Head Start and Early Head Start - CFDA 93.600

Documents and information required for the test the compliance of the Program met all requirements except for the following:

Condition 06-4

Disbursement

The Municipality did not follow the procedures necessary to document the voucher for payment and maintain good internal controls. In a disbursement voucher test with a sample of 12, 33% of purchase orders were missing.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Findings and Questioned Cost
For the Year Ended June 30, 2006

Condition 06-4(Cont.)
Disbursement

Criteria

Code of Federal Regulation 45 §1301.13

(a) Upon request by the responsible HHS official, each Head Start agency or its delegate agency shall submit an accounting system certification, prepared by an independent auditor, stating that the accounting system or systems established by the Head Start agency, or its delegate, has appropriate internal controls for safeguarding assets, checking the accuracy and reliability of accounting data, and promoting operating efficiency.

Code of Federal Regulation 45 §1301.12

(a) An audit of the Head Start program covering the prior budget period of each Head Start agency and its delegate agencies, if any, shall be made by an independent auditor to determine:

- (1) Whether the agency's financial statements are accurate;*
- (2) Whether the agency is complying with the terms and conditions of the grant;*
and
- (3) Whether appropriate financial and administrative procedures and controls have been installed and are operating effectively. Head Start agencies shall either include delegate agency audits as a part of their own audits or provide for separate independent audits of their delegate agencies.*

Cause

The Municipality has incomplete disbursement vouchers leading in problems with the good internal controls that must be implemented by the program.

Effect

The Municipality did not follow the procedures establish to maintain good internal controls in order to comply with federal regulation.

Recommendation

Revise that disbursement voucher contain all of the documents necessary to the records completeness and good internal control procedures followed.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Findings and Questioned Cost
For the Year Ended June 30, 2006

Condition 06-5
Cash Management

The Head Start has a large balance in its books as of June 30, 2006.

Criteria

Code of Federal Regulation 45§1302.25

Responsible HHS officials will place strict controls on the release of grant funds to grantees which are scheduled for change by cessation of their grants under section 519 of the Act. Specifically, the following controls will be established:

- (a) Funds will be released on a monthly basis regardless of the form of grant payment.*
- (b) Funds released each month will be limited to the amount required to cover actual disbursements during that period for activities authorized under the approved **Head Start** program.*
- (c) The amount of funds released must be approved each month by the responsible HHS official .established the following controls:*

Cause

The Municipality did not make payments as soon as they receive the funds.

Effect

The Municipality does not follows the procedures establish in the federal law.

Recommendation

Establish the procedures necessary to make payments within a reasonable time after receive the funds from ACUDEN as establish the Federal Regulation.

Child Care and Development Block Grant - CFDA 93.575

Documents and information required o for the test the Compliance of the Program met all requirements except for the following:

Condition 06-6
Disbursement

The Municipality did not follow the procedures needed to document the voucher for payment. In a disbursement voucher test with a sample of 6, the following documents 43% of purchase order were missing.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Findings and Questioned Cost
For the Year Ended June 30, 2006

Condition 06-6(Cont.)
Disbursement

Criteria

Code of Federal Regulation 45 § 98.67

(a) Lead Agencies shall expend and account for CCDF funds in accordance with their own laws and procedures for expending and accounting for their own funds.

Cause

The Municipality has incomplete disbursement vouchers leading in problems with the good internal controls that must be implemented by the program.

Effect

The Municipality did not follow the procedures establish to maintain good internal controls in order to comply with federal regulation.

Recommendation

Revise that disbursement voucher contain all of the documents necessary to the records completeness and good internal control procedures followed.

Condition 06-7

Cash Management

The Child Care has a large balance in its books as of June 30, 2006.

Criteria

Code of Federal Regulation 45 § 98.60

(f) Cash advances shall be limited to the minimum amounts needed and shall be timed o be in accord with the actual, immediate cash requirements of the State Lead Agency, its subgrantee or contractor in carrying out the purpose of the program in accordance with 31 CFR part 205.

Cause

The Municipality did not make payments as soon as they receive the funds.

Effect

The Municipality does not follows the procedures establish in the federal law.

Recommendation

Establish the procedures necessary to make payments within a reasonable time after receive the funds from ACUDEN as establish the Federal Regulation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Prior Year Findings and Questioned Cost
Fiscal Year Ended June 30, 2006

<u>Program</u>	<u>Finding/Noncompliance</u>	<u>Status</u>
Various Federal Assisted Program	Condition 01-1 to 8, 00-01 Disbursement Voucher without proper documentation.	Partially Corrected
05-01 Housing Voucher 148.71	Cash Management The section 8 has a large balance on this bank account as of February 28, 2005 and as of the fiscal year ended June 30, 2006	Still Prevail
05-02 14.239 HOME	Cash Management The Home Program bank account has a large balance as of March 31, 2005	Corrected
05-3 14.239 HOME	Parameters of Assistance the Home tenant- based program has people receiving the assistance for more than the time establish by HUD as maximum	Corrected
05-4 14.218 CDBG	Cash Management The reconciliation we did for CDBG for March, in order to evaluate how the funds have been utilize, we observed at the end of the month a large balance in CDBG's books.	Still Prevail
05-5 10.854 HOPWA	Cash Management There was funds received in January that were deposited on the Section 8 bank account and not in a separate bank account for the specific program as required and maintaining in this account for approximately four months.	Still Prevail
05-6 93.600 Head Start	Disbursement The Municipality does not followed the procedures they need to documentate the voucher for payment and maintain good internal controls.	Partially Corrected

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF TOA BAJA
Schedule of Prior Year Findings and Questioned Cost
Fiscal Year Ended June 30, 2006

<u>Program</u>	<u>Findings/Noncompliance</u>	<u>Status</u>
05-7 93.600 Head Start	Cash Management The Head Start bank account has a large balance as of March 31, 2005.	Still Prevail
05-8 93.575	Disbursement The Municipality does not followed the procedures they need to documentate the voucher payment.	Partially Corrected

Estado Libre Asociado de Puerto Rico
Gobierno Municipal de Toa Baja
Oficina del Alcalde



Aníbal Vega Borges
Alcalde

December 21, 2006

Cognizant or Oversight Agency for Audit
Juan Rivera, CPA
Urb. Levittown
1818 Del Valle Avenue
Toa Baja, Puerto Rico 00949

CORRECTIVE ACTION PLAN

The Municipality of Toa Baja respectfully submits the following corrective action plan in responses to the single audit for the fiscal year that ended June 30, 2006.

FINDINGS – FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Housing Choice Voucher Program - CFDA 14.871

Reportable Condition: See Condition 06-1 **Cash Management**

Recommendation:

Comment this problem with HUD office about the amount in the Housing Choice Voucher bank account and request a solution for this situation or request fund for less amount until this situation has been resolved.

Action taken:

The Municipality will deposit this excess balance in the Section 8 Voucher bank account into another savings certificate to use as a reserve account. The savings certificate will be cancelled when the vouchers pending are ready to pay. A system of priority will be established by The Municipality for trammital of vouchers to make payments as soon as the funds are received.

Community Development Block Grant – CFDA 14.218

Reportable Condition: See Condition 06-2 **Cash Management**

Recommendation:

Establish the necessary procedures so that the disbursements of funds are made within a reasonable time after being received from HUD, as established by the Federal Regulation.

Action taken:

A system of priority will be established by The Municipality for trammital of vouchers to make payments as soon as the funds are received.

Housing Opportunities for Person with AIDS -CFDA 14.241

Reportable Condition: See condition 06-3 **Cash Management**

Recommendation:

The Municipality must ensure that federal funds received are deposit in the correct bank account.

Action taken:

This situation has been corrected by the Department of Finance and it has been communicated with them to avoid this situation in the future.

FINDINGS – FEDERAL AWARD PROGRAM, DEPARTMENT OF HEALTH AND HUMAN SERVICES

Head Start and Early Head Start - CFDA 93.600

Reportable Condition: See condition 06-4 **Disbursement**

Recommendation:

Revise that disbursement voucher contain all of the documents necessary to the records completeness and good internal procedures followed.

Action taken:

The Municipality will enforce as an internal control that vouchers contain the information, documents and signatures required. Upon December 29, 2005 we implemented the procedure of making a purchase order for every service contracted; this includes professional and non professional services. The new Office Clerks will be oriented in order to guarantee this procedure.

Head Start and Early Head Start - CFDA 93.600

Reportable Condition: See condition 06-5 **Cash Management**

Recommendation:

Establish the procedures necessary to do the disbursments within a reasonable time after receive the funds from ACUDEN as establish the Federal Regulation.

Action taken:

A system will be established so that request for funds will only be made once proof of all required documents are complete.

Child Care and Development Block Grant - CFDA 93.575

Reportable Condition: See condition 06-6 **Cash Management**

Recommendation:

Revise that disbursement voucher contain all of the documents necessary to the records completeness and good internal control procedures followed.

Action taken:

A system will be established so that request for funds will only be made once proof of all required documents are complete.

Child Care and Development Block Grant - CFDA 93.575

Reportable Condition: See condition 06-7 **Cash Management**

Recommendation:

Establish the procedures necessary to make payments within a reasonable time after receive the funds from ACUDEN as establish the Federal Regulation.

Action taken:

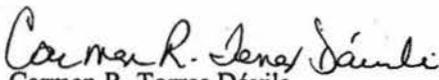
A system will be established so that request for funds will only be made once proof of all required documents are complete.

I hope that this information will clarify the findings made by office.

Cordially,



Eneida Pinto Ortiz
Director
Department of Housing and Community Development



Carmen R. Torres Dávila
Director
Department of Head Start