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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES**

**BASIC FINANCIAL STATEMENTS  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2008**

**ORTIZ, RIVERA, RIVERA & CO.**

CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

Suite 152, PO Box 70250, San Juan, P.R. 00936-7250 • Phone (787) 756-8524, Fax (787) 274-0562

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MUNICIPALITY OF VIEQUES  
BASIC FINANCIAL STATEMENTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

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**PART I - FINANCIAL SECTION**

**ORTIZ, RIVERA, RIVERA & CO.**

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American Institute of Certified  
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Puerto Rico Board of Certified  
Public Accountants  
Management Consulting  
Services Division

## INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and  
Municipal Legislature  
Municipality of Vieques  
Vieques, 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 Vieques, as of and for the year ended June 30, 2008, which collectively comprise the Municipality's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

The accounting records of the Municipality of Vieques related to interfund transactions were not adequate. Accordingly, we were unable to obtain sufficient evidence to support and satisfy ourselves about the amount recorded in each major funds and the aggregate remaining funds information as due from/due to other funds, stated at \$12,138,597 in the total governmental funds column of the balance sheet.

In addition, management has not recorded certain capital assets in governmental activities and, accordingly, has not recorded depreciation expense on those assets. Accounting principles generally accepted in the United States of America require that those capital assets be capitalized and depreciated, which would increase the assets, net assets, and expenses of the governmental activities. The amount by which this departure would affect

expenses of the governmental activities. The amount by which this departure would affect the assets, and expenses of the governmental activities is not reasonably determinable.

As discussed in Note 21, to the financial statements, management has not recorded a provision for liability of closure and postclosure care costs of the landfill. Accounting principles generally accepted in the United States of America require that a provision for liability of closure and postclosure care costs be recorded to comply with applicable state and federal regulations. The amount by which this departure would affect the liabilities, net assets, and expenses of the governmental activities is not reasonable determinable.

In our opinion, except for the effects of not provide a provision for liability of closure and postclosure care costs of the landfill and for not recorded certain capital assets with the respective depreciation expense, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities of the Municipality of Vieques as of June 30, 2008, and the respective changes in financial position, for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In addition, in our opinion, except for the effect of not maintain adequate records related to interfund transactions, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund and the aggregate remaining fund information of the Municipality of Vieques as of June 30, 2008, and the respective changes in financial position, thereof and the respective budgetary comparison for the general and debt service funds for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 15, 2008 on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grants, agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 4 through 10 is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial statements. The accompanying

schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U. S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of the Municipality. The schedule of expenditures of federal awards has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Ortiz, Rivera, Rivera & Co.*

San Juan, Puerto Rico  
December 15, 2008

The stamp 2363626 was affixed  
to the original of this report.





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Estado Libre Asociado de Puerto Rico  
**Gobierno Municipal de Vieques**  
Oficina de Finanzas

*Francisco R. Rivera Hernández*  
Director

HOJA DE TRÁMITE

A : José Velázquez, Comisionado Auxiliar  
Asesoramiento Reglamentación y Intervención Fiscal  
Oficina del Comisionado Asuntos Municipales

DE : Francisco R. Rivera Hernández, Director de Finanzas  
Municipio de Vieques

FECHA : 19 de marzo de 2009

ASUNTO : Adjunto le estoy enviando Estados Financieros para el año terminado  
en junio 30, 2008.

DIVISION REGALAMIENTOS  
E INTERVENCION  
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ADMINISTRACION TIC

*Carlos, 967*

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Management of the *Municipality of Vieques* of the Commonwealth of Puerto Rico (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, 2008**. 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.

**FINANCIAL HIGHLIGHTS**

- The Municipality's in the Governmental Activities has reported assets and net assets amounting to **\$137,696,496** and **\$120,492,887** respectively, in the accompanying statement of net assets, of which the most significant assets are capital assets (**pending for the property final costs**) amounting to **\$134,900,794 (98 percent of total Municipality's assets)**.
- The Municipality in the same activities has reported total liabilities amounting to **\$17,203,609** in the accompanying statement of net assets, of which the most significant liabilities are bonds, notes and other long-term debt amounting to **\$10,060,368 (58 percent of total liabilities)**.
- The Municipality has reported total revenues amounting to **\$12,835,655** in the accompanying Statement of Revenues, Expenditures and Changes in Fund Balances-Governmental Funds, for the Fiscal Year Ended **June 30, 2008**. The most significant revenues amounting in this statement are property taxes and municipal licenses taxes and, licenses and permits were to **\$1,539,372 (17 percent of total revenues)** and **\$735,820 (8 percent of total revenues)**, respectively.
- The Municipality has reported in the General fund a deficiency of revenues over expenditures amounting to **(\$1,227,741)** in the accompanying statement of revenues, expenditures and changes in fund balances.
- The Municipality's governmental funds reported combined ending fund balances of **(\$4,056,484)** which represent the fund balances of the general fund, capital projects funds, HUD Programs, Special Community Trust and debt service fund combined (**all known as the Municipality's major funds**).

- The Municipality has reported unreserved fund balance for the general fund amounting to **(\$11,431,904)**.
- The Municipality has reported a deficiency of revenues and other financing sources under expenditures and other financing uses amounting to **(\$1,743,962)** in the general fund. As a significant fact, the Municipality's outlays for capital projects during the year amounted **\$2,489,630** while to the disponible funds provine of the fund balance available at beginning of the fiscal year. Such outlays over financing sources and reducing the expected income for the incongruence on the State economy were the principal reasons of the deficiency in the governmental funds.

## OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The Municipality's financial statements include three components: **(1)** the government-wide financial statements, **(2)** the fund financial statements, and **(3)** the notes to the financial statements **(collectively known as the basic financial statements)**. This report also contains additional required supplementary information **(budgetary schedules)** and other supplementary information **(combining financial statements)** in addition to the basic financial statements themselves. These components are described below:

### Government-Wide Financial Statements

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, 2008** 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.

## **Statement of Activities**

The statement of activities presents information showing how the Municipality's net assets changed during the fiscal year ended **June 30, 2008**. 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 Municipality's fund financial statements, which consist of: **(1)** the balance sheet – governmental funds and **(2)** the statement of revenues, expenditures and changes in fund balances – governmental funds. These financial statements report the financial position and results of operations of the Municipality's governmental funds.

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

The fund financial statements focus on: **(1)** individual parts of the Municipality's government and **(2)** reporting the Municipality's operations in more detail than the government-wide financial statements. For financial reporting purposes, the Municipality classifies its funds within the following fund categories: **(1)** general fund, **(2)** debt service fund, **(3)** HUD Programs, **(4)** Special Community Trust and **(5)** capital projects funds (collectively known as the "governmental funds").

Governmental funds are used to account for all of the services provided by the Municipality. Governmental funds are used to account for essentially the same functions reported as governmental activities in the governmental-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources. They also focus on the balances of spendable resources available at the end of the fiscal year **(June 30, 2008)**. This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the Municipality's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the Municipality, that is, evaluating the Municipality's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the fund information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Municipality's near-term financial decisions.

For financial reporting purposes the Municipality has five major funds: **(1)** the General Fund, **(2)** Housing and Urban Development Program, **(3)** Capital Projects Fund, **(4)** Special Community Trust and **(5)** the Debt Service Fund.

### **Notes to the Basic Financial Statements**

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

### **Required Supplementary Information**

The basic financial statements are followed by a section of required supplementary information consisting of: **(1)** a combining financial statements referred in connection to nonmajor governmental funds is presented, and **(2)** a budgetary comparison between actual operating results with the original budget and the final amended budget for the general fund.

### **Government-wide Financial Statements Summary**

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, assets exceeded liabilities by **\$120,492,887** at **June 30, 2008**.

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:

**Condensed Statement of Net Assets:**

	<u>June 30, 2008</u>
Current assets	\$ 2,795,702
Capital assets	134,900,794
<b>Total assets</b>	<b><u>\$137,696,496</u></b>
Current liabilities	7,143,241
Non-current liabilities	10,060,368
<b>Total liabilities</b>	<b><u>\$ 17,203,609</u></b>
Net assets/(liabilities):	
Invested in capital assets, net of related debt	128,647,674
Restricted	7,503,264
Unrestricted	<u>(15,658,051)</u>
<b>Total net assets</b>	<b><u>\$120,492,887</u></b>

An additional portion of the Municipality's net assets (**4 percent**) represents resources that are subject to restrictions on how they may be used. At the end of the current fiscal year, the Municipality has reported positive balances in two categories of net assets.

**Condensed Statement of Activities:**

	<u>June 30, 2008</u>
<b>Revenues:</b>	
Program revenues:	
Charges for services	\$ 780,303
Operating grants and contributions	1,375,291
Capital grants and contributions	1,351,028
General revenues:	
Property taxes	1,539,372
Municipal license taxes	303,663
Sales and use tax	588,672
Grants and contributions	6,207,410
Interest, fines and penalties	32,423
Miscellaneous	657,493
<b>Total Revenues</b>	<b><u>\$ 12,835,655</u></b>

**Expenses:**

General government	\$ 5,643,593
Public safety	710,292
Public works	5,870,611
Recreation	264,023
Health and welfare	1,693,595
Depreciation expense	2,866,636
Interest on long-term debt	534,267
<b>Total expenses</b>	<b>\$ 17,583,017</b>

Change in net assets (4,747,362)

<b>Net assets – at beginning of year</b>	<b><u>125,240,249</u></b>
<b>Net assets – at end of year</b>	<b><u>\$ 120,492,887</u></b>

**Fund Financial Statements Summary**

As discussed 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 balance 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 fiscal year. The following is a condensed presentation of the Municipality's balance sheet and results of operations of governmental funds:

**Condensed Balance Sheet – Governmental funds:**

	<b><u>June 30, 2008</u></b>
Total Assets – Major Funds	\$14,875,979
Total Assets – Nonmajor Funds	58,320
<b>Total assets</b>	<b><u>\$14,934,299</u></b>
Total Liabilities – Major Funds	\$18,929,088
Total Liabilities – Nonmajor Funds	61,695
<b>Total liabilities</b>	<b><u>\$18,990,783</u></b>
Fund Balances – Major Funds	(\$ 4,053,109)
Fund Balances – Nonmajor Funds	(3,375)
<b>Total Fund Balance</b>	<b><u>(\$ 4,056,484)</u></b>

**Condensed Statement of Operations – Governmental funds:**

Total Revenues – Major Funds	\$12,089,509
Total Revenues – Nonmajor Funds	746,146
<b>Total revenues</b>	<b><u>\$12,835,655</u></b>
Total expenditures – Major Funds	\$15,017,584
Total expenditures – Nonmajor Funds	749,854
<b>Total expenditures</b>	<b><u>\$15,767,438</u></b>
Other financing sources (uses) Major	3,357,000
Other financing sources (uses) Nonmajor	-0-
Revenues Over Expenses – Major	428,925
Revenues (Under) Expenses – Nonmajor	(3,708)
	<u>(425,217)</u>
Beginning Fund Balance (Deficit)	<u>(4,481,701)</u>
<b>Ending Fund Balance (Deficit)</b>	<b><u>(\$4,056,484)</u></b>

**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 on the 2nd floor of the **Vieques City Hall, Vieques, Puerto Rico.**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
STATEMENT OF NET ASSETS  
JUNE 30, 2008**

<u>Assets</u>	<u>Governmental Activities</u>
Cash (Notes 2 and 5)	\$ 171,672
Cash with fiscal agent (Notes 2 and 5)	1,799,950
Due from other agencies (Note 9)	824,080
Capital assets, net (Note 11)	<u>134,900,794</u>
 Total assets	 <u>\$ 137,696,496</u>
 <u>Liabilities and Net Assets</u>	
<b>Liabilities</b>	
Bank overdraft	\$ 2,734,914
Accounts payable and accrued liabilities	2,693,637
Due to other agencies (Note 12)	980,613
Deferred revenues (Note 13):	
Municipal license tax	408,808
Federal government	34,214
Accrued interest	291,055
Noncurrent liabilities (Note 15):	
Due within one year	471,258
Due in more than one year	9,589,110
Total liabilities	<u>17,203,609</u>
<b>Net Assets</b>	
Investment in capital assets, net of related debt	128,647,674
Restricted for:	
Debt service	704,829
Capital projects	6,798,435
Unrestricted	<u>(15,658,051)</u>
 Total net assets	 <u>\$ 120,492,887</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
STATEMENT OF ACTIVITIES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenues</u>			<u>Net (Expense) Revenue and Changes in Net Assets</u>
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>	
General government	\$ 5,643,593	\$ 780,303	\$ -	\$ -	\$ (4,863,290)
Public safety	710,292				(710,292)
Public works	5,870,611			1,351,028	(4,519,583)
Recreation	264,023				(264,023)
Health and welfare	1,693,595		1,375,291		(318,304)
Depreciation	2,866,636				(2,866,636)
Interest on long-term debt	534,267				(534,267)
Total primary government	<u>\$ 17,583,017</u>	<u>\$ 780,303</u>	<u>\$ 1,375,291</u>	<u>\$ 1,351,028</u>	<u>(14,076,395)</u>
General revenues:					
Property taxes					1,539,372
Municipal license tax					303,663
Sales and use tax					588,672
Grants and contributions not restricted to specific programs					6,207,410
Interest, fines and penalties					32,423
Miscellaneous					657,493
Total general revenues					<u>9,329,033</u>
Change in net assets					(4,747,362)
Net assets at beginning of year, as restated (Note 22)					<u>125,240,249</u>
Net assets at end of year					<u>\$ 120,492,887</u>

The accompanying notes are an integral part of these basic financial statements.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
BALANCE SHEET-GOVERNMENTAL FUNDS  
JUNE 30, 2008

<u>Assets</u>	<u>General</u>	<u>Housing and Urban Development Programs</u>	<u>Special Community Trust</u>	<u>Debt Service</u>	<u>Capital Projects</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Cash (Notes 2 and 5)	\$ 6,020	\$ 107,332	\$ -	\$ -	\$ -	\$ 58,320	\$ 171,672
Cash with fiscal agent (Notes 2 and 5)				700,163	1,099,787		1,799,950
Due from other agencies (Note 9)	819,414			4,666			824,080
Due from other funds (Note 10)	3,119,013		330,000		8,689,584		12,138,597
<b>Total assets</b>	<b>\$ 3,944,447</b>	<b>\$ 107,332</b>	<b>\$ 330,000</b>	<b>\$ 704,829</b>	<b>\$ 9,789,371</b>	<b>\$ 58,320</b>	<b>\$ 14,934,299</b>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
BALANCE SHEET-GOVERNMENTAL FUNDS  
JUNE 30, 2008**

<u>Liabilities and Fund Balance (Deficit)</u>	<u>General</u>	<u>Housing and Urban Development Programs</u>	<u>Special Community Trust</u>	<u>Debt Service</u>	<u>Capital Project</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
<b>Liabilities</b>							
Bank overdraft	\$ 2,734,914	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,734,914
Account payable and accrued liabilities	2,232,432		339,084		114,936	7,185	2,693,637
Due to other funds (Note 10)	9,019,584	222,717			2,876,000	20,296	12,138,597
Due to other agencies (Note 12)	980,613						980,613
Deferred revenues: (Note 13)							
Municipal license tax	408,808						408,808
Federal government						34,214	34,214
Total liabilities	<u>15,376,351</u>	<u>222,717</u>	<u>339,084</u>	<u>-</u>	<u>2,990,936</u>	<u>61,695</u>	<u>18,990,783</u>
<b>Commitments and Contingencies (Notes 19 and 20)</b>							
<b>Fund Balances (Deficit)</b>							
Reserved for:							
Encumbrances	481,600						481,600
Debt service				704,829			704,829
Capital projects					6,798,435		6,798,435
Unreserved fund balance (deficit)	(11,913,504)	(115,385)	(9,084)			(3,375)	(12,041,348)
Total fund balance (deficit)	<u>(11,431,904)</u>	<u>(115,385)</u>	<u>(9,084)</u>	<u>704,829</u>	<u>6,798,435</u>	<u>(3,375)</u>	<u>(4,056,484)</u>
<b>Total liabilities and fund balance (deficit)</b>	<u>\$ 3,944,447</u>	<u>\$ 107,332</u>	<u>\$ 330,000</u>	<u>\$ 704,829</u>	<u>\$ 9,789,371</u>	<u>\$ 58,320</u>	<u>\$ 14,934,299</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
RECONCILIATION OF THE GOVERNMENTAL FUNDS  
BALANCE SHEET TO STATEMENT OF NET ASSETS  
JUNE 30, 2008**

Total fund balances - governmental funds	\$ (4,056,484)
Amounts reported for governmental activities in the statement of net assets are different because:	
• Capital assets, net used in governmental activities are not current financial resources and therefore are not reported in the governmental funds balance sheet	134,900,794
• Some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds. <b>(Note 4)</b>	<u>(10,351,423)</u>
Net assets of governmental activities	<u>\$ 120,492,887</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES (DEFICIT) - GOVERNMENTAL FUNDS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

	General	Housing and Urban Development Programs	Special Community Trust	Debt Service	Capital Project	Other Governmental Funds	Total Governmental Funds
<b>REVENUES</b>							
Property taxes (Note 6)	\$ 1,291,578	\$ -	\$ -	\$ 247,794	\$ -	\$ -	\$ 1,539,372
Municipal license taxes (Note 7)	303,663						303,663
Sales and use taxes (Note 8)						588,672	588,672
Licenses and permits	735,820						735,820
Charges for service and rents	44,483						44,483
Intergovernmental revenues (Note 14):							
Federal grants and contributions		1,217,817				157,474	1,375,291
State contributions	6,207,410		867,211		483,817		7,558,438
Interest, fines, and penalties	16,971			15,452			32,423
Other revenues	657,493						657,493
Total revenues	<u>9,257,418</u>	<u>1,217,817</u>	<u>867,211</u>	<u>263,246</u>	<u>483,817</u>	<u>746,146</u>	<u>12,835,655</u>
<b>EXPENDITURES</b>							
Current:							
General government	6,399,289						6,399,289
Public safety	710,292						710,292
Public works	2,337,804	497,699				589,214	3,424,717
Recreation	264,023						264,023
Health and welfare	773,751	759,204				160,640	1,693,595
Capital outlays					1,711,393		2,489,630
Debt service:							
Principal retirement				309,879			309,879
Interest and other				476,013			476,013
Total expenditures	<u>10,485,159</u>	<u>1,256,903</u>	<u>778,237</u>	<u>785,892</u>	<u>1,711,393</u>	<u>749,854</u>	<u>15,767,438</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(1,227,741)</u>	<u>(39,086)</u>	<u>88,974</u>	<u>(522,646)</u>	<u>(1,227,576)</u>	<u>(3,708)</u>	<u>(2,931,783)</u>
<b>OTHER FINANCING SOURCES (USES)</b>							
Loan issuance					3,357,000		3,357,000
Transfers in	27,453			543,674			571,127
Transfers out	<u>(543,674)</u>			<u>(27,453)</u>			<u>(571,127)</u>
Total other financing sources (uses)	<u>(516,221)</u>			<u>516,221</u>	<u>3,357,000</u>		<u>3,357,000</u>
Excess (deficiency) of revenues and other sources over expenditures and other uses	<u>(1,743,962)</u>	<u>(39,086)</u>	<u>88,974</u>	<u>(6,425)</u>	<u>2,129,424</u>	<u>(3,708)</u>	<u>425,217</u>
<b>FUND BALANCE (DEFICIT) AT BEGINNING OF YEAR, AS RESTATED (Note 22)</b>	<u>(9,687,942)</u>	<u>(76,299)</u>	<u>(98,058)</u>	<u>711,254</u>	<u>4,669,011</u>	<u>333</u>	<u>(4,481,701)</u>
<b>FUND BALANCE (DEFICIT) AT END OF YEAR</b>	<u>\$ (11,431,904)</u>	<u>\$ (115,385)</u>	<u>\$ (9,084)</u>	<u>\$ 704,829</u>	<u>\$ 6,798,435</u>	<u>\$ (3,375)</u>	<u>\$ (4,056,484)</u>

The accompanying notes are an integral part of these basic financial statements.

*CAJ*  
*5-11-09*

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND  
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE  
STATEMENT OF ACTIVITIES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Net change in fund balances - total governmental funds	\$ 425,217
Amounts reported for governmental activities in the statement of activities are different because:	
• Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.	43,736
• Depreciation expense on capital assets is reported in the statement of activities, but do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditure in governmental funds.	(2,866,636)
• Governmental funds report issuance of long-term debt as other financial resources because provided current financial resources.	(3,357,000)
• Governmental funds report principal payments on long-term obligations as expenditures, whereas the principal payments reduces the long-term obligations in the statement of activities.	309,879
• Change in accrued interest expense which does not require the use of current financial resources.	(58,254)
• Some expenses reported in the statement of activities do not require the use of current financial resources; therefore, are not reported as expenditures in governmental funds.	<u>755,696</u>
Changes in net assets of governmental activities	<u><u>\$(4,747,362)</u></u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
STATEMENT OF REVENUES AND EXPENDITURES - BUDGET AND ACTUAL-GENERAL AND DEBT SERVICE FUNDS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

	General Fund				Debt Service Fund			
	Budgeted Amounts		Actual	Variance with Final Budget- Positive (Negative)	Budgeted Amounts		Actual	Variance with Final Budget- Positive (Negative)
	Original	Final			Original	Final		
<b>REVENUES</b>								
Property taxes	\$ 99,246	\$ 99,246	\$ 99,246	\$ -	\$ 284,654	\$ 284,654	\$ 247,794	\$ (36,860)
Municipal license taxes	500,000	500,000	312,359	(187,641)				
Licenses and permits	1,083,000	1,083,000	735,407	(347,593)				
Charges for services and rent	115,000	115,000	46,483	(68,517)				
Intergovernmental revenues:								
State contributions	7,343,163	7,343,163	7,090,026	(253,137)				
Interest, fines and penalties	4,000	4,000	8,688	4,688			15,452	15,452
Other revenues	1,855,591	1,855,591	655,493	(1,200,098)				
<b>Total revenues</b>	<b>11,000,000</b>	<b>11,000,000</b>	<b>8,947,702</b>	<b>(2,052,298)</b>	<b>284,654</b>	<b>284,654</b>	<b>263,246</b>	<b>(21,408)</b>
<b>EXPENDITURES</b>								
Current:								
General government	6,466,344	6,466,344	6,699,153	(232,809)				
Public safety	1,002,624	1,002,624	710,292	292,332				
Public works	2,666,804	2,666,804	2,123,201	543,603				
Recreation	334,749	334,749	214,653	120,096				
Health and welfare	529,479	529,479	407,875	121,604				
Debt service:								
Principal					201,721	201,721	309,879	(108,158)
Interest					82,933	82,933	476,013	(393,080)
<b>Total expenditures</b>	<b>11,000,000</b>	<b>11,000,000</b>	<b>10,155,174</b>	<b>844,826</b>	<b>284,654</b>	<b>284,654</b>	<b>785,892</b>	<b>(501,238)</b>
Deficiency of revenues under expenditures	\$ -	\$ -	\$ (1,207,472)	\$ (1,207,472)	\$ -	\$ -	\$ (522,646)	\$ (522,646)

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**1. ORGANIZATION**

The Municipality of Vieques, Puerto Rico (Municipality) was founded in 1844. The Municipality is a political legal entity with full legislative and administrative faculties in every affair of municipal character, with perpetual succession existence and legal identity, separate and independent from the central government of the Commonwealth of Puerto Rico. The Municipality provides a full range of services including: public safety, public works, culture, recreation, health and welfare, education and other miscellaneous services.

The Municipal Government comprises the executive and legislative branches. The executive power is exercised by the Mayor and the legislative by the Municipal Assembly, which has 12 members. The members of these branches are elected every four years in the Puerto Rico general elections.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accompanying financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

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

- Management's Discussion and Analysis - Introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.
- Government - Wide Financial Statements - This reporting model includes financial statements prepared using full accrual of accounting for all of the government's activities. This approach includes not just current assets and liabilities, but also capital assets and long-term liabilities (such as buildings and infrastructure, including bridges and roads, and general obligation debt).
- Statement of Net Assets - The statement of net assets is designed to display the financial position of the Municipality, including capital assets and infrastructure.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

The net assets of the Municipality will be broken down into three categories; invested in capital assets, net of related debt; restricted; and unrestricted.

- **Statement of Program Activities** - The government - wide statements of activities report expenses and revenues in a format that focuses on the cost of each of the government's functions. The expense of individual functions is compared to the revenues generated directly by the function.
- **Budgetary comparison schedules** - Demonstrating compliance with the adopted budget is an important component of a government's accountability to the public. Under the new reporting model, the Municipality will continue to provide budgetary comparison information in their financial statements. An important change, however, is a requirement to add the government's original budget to the current comparison of final budget and actual results.

The following is a summary of the more significant policies.

**a. Reporting Entity**

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, as amended by Statement No. 39, "Determining whether Certain Organizations are Component Units" - an amendment of GASB Statement No. 14, "The Financial Reporting Entity," of the GASB. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government appoint a voting majority of the entity's governing body, and if either one of the following conditions exists: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete.

GASB Statement No. 39 provided additional guidance to determine whether certain organization for which the primary government is not financially

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

accountable should be reported as component units. A legally separate, tax-exempt organization should be discretely presented as a component unit if all of the following criteria are met: (a) the economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents; (b) the primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and; (c) the economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

GAAP details two methods of presentation: blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component units' financial data in columns separate from the Municipality's balances and transactions. Based on the aforementioned criteria, the Municipality has no component units.

**b. Government-Wide and Fund Financial Statements**

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all the activities of the Municipality. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities are supported mainly by taxes and intergovernmental revenues.

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

The fund financial statements segregate transactions related to certain functions

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

or activities in separate funds in order to aid financial management and to demonstrate legal compliance. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

**c. Measurement Focus, Basis of Accounting and Financial Statement Presentation**

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

Governmental fund financial statements are reported using the *current financial resources measurement focus and the modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

The Municipality reports the following major governmental funds:

1) General Fund

This is the operating fund of the Municipality and accounts for all financial resources, except those required to be accounted for in another fund.

2) Housing and Urban Development Programs (HUD Programs)

This fund account for revenue sources for the development of viable urban communities, decent housing, suitable living environment, rental assistance to help very low-income families afford decent, safe and sanitary housing by encouraging property owners to rehabilitate substandard housing and lease the units with rental subsidies to low-income family.

3) Debt Service Fund

This fund is used to account for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

4) Capital Project Fund

This fund is used to account for the financial resources used for the acquisition and construction of major capital facilities, financed with the proceeds of general obligation bonds.

5) Special Community Trust

This fund accounts for revenue sources for improvements and construction of housing projects for low-income people.

Private-section standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements.

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

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

**d. Cash, Cash with Fiscal Agent, and Investments**

The Municipality's Finance Director is responsible for investing available resources. The Municipality is restricted by law to invest only in savings accounts, certificates of deposit, and investments with banks qualified as a depository of public funds by the Puerto Rico Treasury Department (PRTD) or in instruments of the Government Development Bank for Puerto Rico (GDB).

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

**e. Interfund Receivables and Payables**

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**f. Capital Assets**

Capital assets purchased or acquired are carried at historical cost or estimated historical cost. Contributed assets are recorded at fair market value as of the date donated. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation in capital assets is calculated on the straight-line basis over the following estimated useful lives:

	<u>Useful Life</u>
Infrastructure	25-50 years
Buildings and building improvements	20-50 years
Furniture and fixtures	5-10 years
Vehicles and equipment	5-20 years

**g. Reservation of Fund Balance**

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

1) Encumbrances

Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.

2) Debt Service

Represents net assets available to finance future debt service payments.

3) Capital Projects Fund

Represents the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. The committed amounts generally will become liabilities in future periods as the projects are completed.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**h. Risk Financing**

The Municipality carries insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center (the "CRIM") for the year ended June 30, 2008 amounted to \$146,749. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$266,686 for workers' compensation insurance covering all municipal employees.

**i. Compensated Absences**

Employees are entitled to 30 days vacations leave and 18 days sick leave per year. Sick leave is recorded as an expenditure in the year paid. Employees are entitled to payment of unused sick leave upon retirement if have been employed for at least 10 years in the municipal government. On July 1997, state Law 152 supra amended the Article 12.016, Section b (2) of the Municipal Law, authorizing the Municipality to pay any excess of vacations and sick leave accumulated over the maximum previously permitted by law. Calculations must be made until December 31 of every year. Excess of sick leave must be paid until March 31 next every natural year. Excess of vacations can be paid after July 1 of every fiscal year.

**j. Future Adoption of Accounting Pronouncements**

The Governmental Accounting Standards Board has issued the following statements that the Municipality has not yet adopted:

<b>Statement Number</b>	<b>Statement Name</b>	<b>Adoption Required in Fiscal Year</b>
51	Accounting and Financial Reporting for Intangible Assets	2009-10
52	Land and Other Real Estate Held as Investments by Endocuments	2008-09

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Statement Number</u>	<u>Statement Name</u>	<u>Adoption Required in Fiscal Year</u>
53	Accounting and Financial Reporting for Derivative Instruments	2009-10

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

**k. Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. The most significant estimates consist of the contribution received from the Puerto Rico Electric Power Authority and the Municipal Revenue Collection Center caused by the delay of the notification of the actual revenues and expenditures to the presented in the financial statements of the agencies mentioned above.

**3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

**a. Budgetary Control**

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

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Revenues and Expenditures - Budget and Actual (Budgetary Basis), accordingly, includes only the operations of the general. The amounts budgeted under the Special Revenue Fund were excluded since they are received and expended over a period of time which generally exceeds the current year.

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

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

**b. Budget/GAAP Reconciliation**

The following schedule presents comparisons of the legally adopted budget with actual data on a budget basis. Because accounting principles applied for purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of entity and timing differences in the deficiency of revenues under expenditures for the year ended June 30, 2008 is presented below for the general fund:

	<u>General Fund</u>
Excess of expenditures over revenues - budgetary basis	(\$1,207,472)
Entity differences:	
Non-budgeted revenues, net	1,195,202
Timing differences:	
Prior year encumbrances recorded as current year expenditures for GAAP basis	( 300,600)
Current year encumbrances recorded as expenditures for budgetary basis	481,600

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Basis of accounting differences:	
Net change in receivables	(\$ 690,096)
Net change in accounts payable	( <u>706,375</u> )
Excess of expenditures over revenues - GAAP basis	( <u>\$1,227,741</u> )

**c. Legal Compliance**

The legal level of budgetary control is at the individual department level for general fund expenditures, and principal and interest due for the debt service fund.

**4. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS**

The governmental fund balance sheet includes a reconciliation between fund balance-governmental funds and net assets of governmental activities as reported in the government-wide statement of net assets. One element of that reconciliation explains that some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds. The details of the approximately \$10.4 million difference are as follows:

Bonds payable	\$ 6,253,120
Notes payable	2,496,002
Compensated absences	1,289,748
Accrued interest payable	291,055
Due to Treasury Department	<u>21,498</u>
Net adjustment to reduce fund balance governmental funds to arrive at net assets of governmental activities	<u>\$10,351,423</u>

**5. DEPOSITS**

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. Under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collaterals are

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

held by the Secretary of the Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

The deposits at GDB of approximately \$1.1 million that are restricted principally for capital projects, and the \$700,000 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

The Municipality maintains its deposits in one (1) bank located at Puerto Rico. All kind of deposit is guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000.

The excess is covered by collateral provided by banks and held by the Treasury Department of the Commonwealth of Puerto Rico pursuant to applicable laws and regulations.

**6. PROPERTY TAXES**

The Municipal Revenues Collection Center (CRIM) of the Commonwealth of Puerto Rico is responsible by law for the assessment, levy and collection of all real and personal property taxes. The tax on personal property is self assessed by the taxpayer. The assessment is made in a return which must be filed with the CRIM by May 15 of each year. The tax on real property is assessed by the CRIM. The assessment is made as of January 1 of each year and is based on estimated current values of the property as of year 1957. The tax on personal property must be paid in full together with the return on or before May 15. The tax on real property is due in two equal installments in July 1 and January 1, following the assessment date.

The rates are 8.83% for real property and 6.83% for personal property. The composition is as follows:

	<u>Real</u>	<u>Personal</u>
Basic property	6.00%	4.00%
Additional special property - state	1.03%	1.03%
Additional special property - municipal	2.00%	2.00%
Discounts made by state to tax payer	< .20% >	< .20% >
	<u>8.83%</u>	<u>6.83%</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

The Municipality's basic property tax rate represents the portion which is appropriated for general purposes and accounted for in the general fund.

The "Additional special property tax - municipal" is restricted for debt service and retained by GDB for such purposes and it is recorded as revenue in the Debt Service Fund when collected by the CRIM and reported to the Municipality.

The "Additional special property tax - state" is collected by the CRIM for the payment of principal and interest of general obligation bonds and certain other obligations issued by the state government.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the Department of Treasury assumes payment of the basic tax to the Municipality, except for property assessed at less than \$3,500, for which no payment is made. Revenue related to the basic tax on exempt property is recorded in the General Fund when payments are received from the CRIM.

Complete exemption from personal property taxes up to an assessment of \$50,000 is granted to merchants with an annual volume of net sales less than \$150,000.

Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year ends. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30.

Currently, the Municipality has received the preliminary settlement from CRIM related to fiscal year 2007-08, but not the final settlement as the six months period after a fiscal year end, provided by law to CRIM to issue this, has not yet expired.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Management believes, based in part on the experience from prior years, that when received, the final settlement from CRIM will not show a significant difference from the preliminary settlement and that such difference, if any, will not have a material effect on the financial condition of the Municipality.

Based on the preliminary settlement already received, during the year ended June 30, 2008, the amount collected by CRIM from taxpayers and charges exceeded the amount advanced by CRIM for the same period by approximately \$290,000. Such amount is presented as due from CRIM in the statement of net assets. (See Note 9).

**7. MUNICIPAL LICENSE TAX**

Municipal License Tax receivables are recorded in the fiscal year in which payment is due and, accordingly, represent taxes which are due and uncollected at June 30, 2008. The annual Municipal License Tax is determined based on the gross income of all commerce and industrial organizations who have operations in the Municipality of Vieques, and are not totally or partially exempt under the Industrial Incentive Law of Puerto Rico.

An annual return of business volume should be filed on or before April 15 of each year and payable in two equal installments due on July 1 and January 1. A discount of 5% is allowed when full payment is made on or before April 15. The rates of municipal license in the Municipality of Vieques, are as follows:

Financial institutions	=	1.5%
Other organizations:		
up to \$100,000	=	.3% of gross revenues
from \$100,001 to \$200,000	=	.4% of gross revenues
over \$200,000	=	.5% of gross revenues

The amounts collected in advance are recorded as deferred revenues in the General Fund. The Municipality invoiced and collected in advance during the current year approximately \$409,000, corresponding to the next fiscal year municipal license.

**8. SALES AND USE TAXES**

On July 29, 2007 the Commonwealth Legislature approved Act No. 80 ("Act 80") which imposed to all the Municipalities of Puerto Rico a uniform municipal sales and

**COMMONWEALTH OF PUERTO RICO  
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NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

use tax of 1.5%. Effective August 1, 2007 1% of the 1.5% will be collected by the Municipalities and the remaining .5% of the 1.5% will be collected by the Puerto Rico Department of Treasury.

Act 80 also provides for restrictions on the use of the resources (including the .5 of 1.5% collected by the Commonwealth Government) to be invested in solid waste and recycling programs, capital improvements and health and public safety costs. Amount collected by the Commonwealth Government will be deposited in accounts or special funds in the Governmental Development Bank of Puerto Rico ("GDB"), subject to restrictions imposed and distributed as follows:

- a. .2% of the .5% will be deposited in a "Municipal Development Fund" to finance costs as restricted by the Act,
- b. .2% of the .5% will be deposited in a "Municipal Redemption Fund" to finance loans to municipalities subject to restrictions imposed by the Act and,
- c. .1% of the .5% will be deposited in a "Municipal Improvement Fund" to finance capital improvement projects; these funds will be distributed based on legislation from the Commonwealth's Legislature.

**9. DUE FROM OTHER AGENCIES**

Represents grants and contributions due from local and federal agencies:

Puerto Rico Electric Power Authority	\$529,037
Municipal Revenues Collection Center (General Fund)	290,377
Municipal Revenues Collection Center (Debt Service Fund)	<u>4,666</u>
 Total	 <u>\$824,080</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**10. INTERFUND TRANSACTIONS**

**a. Due from/to Other Funds:**

The due from and due to other fund balances as of June 30, 2008, are as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
Capital Project	General	\$ 8,689,584
General	Capital Project	2,876,000
Special Community Trust	General	330,000
HUD Programs	General	222,717
General	Other Governmental Funds	<u>20,296</u>
Total		<u>\$12,138,597</u>

The balance of \$8.7 million due to the capital project fund from the general fund represents advances for working capital purposes. The \$2.9 million due to the general fund from the capital projects fund represent appropriation from the Commonwealth of Puerto Rico which were incorrectly recorded in the corresponding fund.

**b. Interfund Transfers:**

Interfund transfers for the year ended June 30, 2008 consisted of the following:

<u>Transfer In</u>	<u>Transfer Out</u>	<u>Amount</u>
General	Debt Service	\$ 27,453
Debt Service	General	<u>543,674</u>
Total		<u>\$571,127</u>

The transfer from the general fund to the debt service fund of \$543,674 represents funds used for the payment of debt service as become due.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**11. CAPITAL ASSETS**

Capital asset activity for the year ended June 30, 2008 was as follows:

	<u>Balance June 30, 2007</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2008</u>
Capital assets, not being depreciated:				
Land	\$ 65,520,752	\$ -	\$ -	\$ 65,520,752
Construction in progress	647,500			647,500
Total capital assets, not being depreciated	<u>66,168,252</u>	<u>-</u>	<u>-</u>	<u>66,168,252</u>
Capital assets, being depreciated:				
Buildings and building improvements	30,422,254			30,422,254
Furniture and fixtures	2,079,944	43,736		2,123,680
Vehicles and equipment	2,314,341			2,314,341
Infrastructure	66,691,389			66,691,389
Total capital assets, being depreciated	<u>101,507,928</u>	<u>43,736</u>	<u>-</u>	<u>101,551,664</u>
Less accumulated depreciation for:				
Buildings and building improvements	9,094,291	828,437		9,922,728
Furnitures and fixtures	1,521,256	151,496		1,672,752
Vehicles and equipment	1,184,502	191,434		1,375,936
Infrastructure	18,152,437	1,695,269		19,847,706
Total accumulated depreciation	<u>29,952,486</u>	<u>2,866,636</u>	<u>-</u>	<u>32,819,122</u>
Total capital assets, being depreciated, net	<u>71,555,442</u>	<u>(2,822,900)</u>	<u>-</u>	<u>68,732,542</u>
Governmental activities capital assets, net	<u>\$ 137,723,694</u>	<u>\$ (2,822,900)</u>	<u>\$ -</u>	<u>\$134,900,794</u>

**12. DUE TO OTHER AGENCIES**

Due to other agencies at June 30, 2008 are as follows:

Puerto Rico Electric Power Authority	\$674,070
Puerto Rico Aqueduct and Sewer Authority	34,583
Internal Revenue Service	78,227
Puerto Rico Labor Department	77,361
Puerto Rico Employee's Retirement System	115,602
Puerto Rico General Services Administration	<u>770</u>
 Total	 <u>\$980,613</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**13. DEFERRED REVENUES**

**a. Municipal License Tax**

The deferred revenues of approximately \$409,000 in the general fund related to municipal license tax collected in fiscal year 2007-08 that will be earned in fiscal year 2008-09.

**b. Federal Government**

The deferred revenues presented as federal government represents the portion of federal grants received for which qualifying expenditures have not been incurred. The amounts were determined taking into consideration the specific years of the grant. These were related to other governmental funds.

**14. INTERGOVERNMENTAL REVENUES**

Intergovernmental revenues in the general and capital projects funds consist mainly of collections from the Commonwealth of Puerto Rico and the CRIM, and payments in lieu of taxes from the Puerto Rico Electric Power Authority.

**15. LONG-TERM DEBTS**

Bonds and notes payable and other debts outstanding at June 30, 2008 are as follows:

**Bonds**

\$720,000 series of 1999, payable in semiannual installments ranging from \$10,000 to \$65,000 until July 1, 2023, excluding interest ranging from 4.86 to 6.5%.	\$ 565,000
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\$655,000 series of 2002, payable in semiannual installments ranging from \$5,000 to \$50,000 until July 1, 2026, excluding interest ranging from 2.7% to 5.6%.	560,000
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**COMMONWEALTH OF PUERTO RICO  
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NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

\$283,000 series of 1991, payable in quarterly installments of \$3,640, until October 1, 2011, excluding interest ranging from 3.27% to 7.81%	\$ 47,320
\$837,000 series of 2002, payable in semiannual installments ranging from \$12,400 to \$72,700, until July 1, 2026, excluding interest ranging from 5% to 6%.	734,800
\$380,000 series of 2003, payable in semiannual installments ranging from \$5,000 to \$30,000, until July 1, 2029, excluding interest ranging from 5% to 6.5%.	345,000
\$595,000 series of 2005, payable in annual installments ranging from \$70,000 to \$100,000, until July 1, 2011, excluding interest ranging from 4.73% to 5%.	290,000
\$260,000 series of 2005, payable in annual installments ranging from \$30,000 to \$45,000, until July 1, 2011, excluding interest of 5%.	125,000
\$290,000 series of 2007, payable in annual installments ranging from \$5,000 to \$25,000, until July 1, 2031, excluding interest ranging from 6.6% to 7.5%.	280,000
\$1,135,000 series of 2007, payable in semiannual installments ranging from \$15,000 to \$100,000, until July 1, 2032, excluding interest ranging from 3.93% to 7.5%.	1,135,000
\$2,222,000 series of 2008, payable in semiannual installments ranging from \$51,000 to \$203,000, until July 1, 2027, excluding interest ranging from 3.93% to 7.5%.	<u>2,171,000</u>
Total bonds	<u>\$6,253,120</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**Notes Payable - CRIM (Law 42)**

Note payable of \$2,377,919 represents a repayment agreement with GDB and CRIM to repay the excess of property taxes advances from fiscal years up to 2001. The CRIM will retain the principal and interest from the property taxes advances. The amounts retained by CRIM will be remitted to GDB on July 1 of each year through 2032. The repayment agreement is payable in semiannual aggregate principal installments of \$95,748 plus an interest rate of 6.1876%.

**Note Payable - CRIM (Law 146)**

The Municipality entered into a financing agreement with the CRIM in the amount of \$89,759, to finance delinquent property tax accounts sold to private investors, under the provision of Law No. 146 of October 11, 2001. The agreement is in the form of a nonrevolving line of credit bearing interest of 22% and is due on March 31, 2032.

**Note Payable - CRIM (LIMS)**

On June 27, 2001 the Municipality entered into a financing agreement with the CRIM in the amount of \$76,312 for the payment of the Municipality's share of the cost of a management information system (LIMS) acquired by the CRIM for the management of taxpayer's properties located in Puerto Rico. The note is payable in semiannual installments of \$5,118, including interest of 5.95% and is due on November 28, 2011. Amount is financed with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM).

**Note Payable due to Treasury Department**

Note payable of \$21,498 represents a non-interest bearing property tax advances, payable in annual installments of \$7,166 until July 1, 2010.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

The annual debt service requirements for the bonds and notes payable from CRIM at June 30, 2008, are as follows:

	<u>Bonds</u>		<u>Note Payable - Law 42</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2009	\$ 294,160	\$ 387,819	\$ 45,048	\$ 146,448
2010	309,760	415,343	47,878	143,617
2011	326,460	396,362	50,887	140,609
2012	177,340	376,350	54,084	137,412
2013	195,700	364,320	57,482	134,013
2014-2018	1,204,000	1,593,019	346,343	611,133
2019-2023	1,718,600	1,113,910	469,710	487,766
2024-2028	1,597,100	463,952	637,020	320,456
2029-2033	430,000	78,752	669,467	
	<u>\$ 6,253,120</u>	<u>\$ 5,189,827</u>	<u>\$2,377,919</u>	<u>\$ 2,121,454</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

	<i>Note Payable - Law 146</i>		<i>Note Payable - LIMS</i>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2009	\$ 3,590	\$ 5,360	\$ 8,460	\$ 1,775
2010	3,590	5,136	8,971	1,264
2011	3,590	4,914	9,513	722
2012	3,590	4,690	4,970	148
2013	3,590	4,466		
2014-2018	17,950	18,984		
2019-2023	17,950	13,400		
2024-2028	17,950	7,816		
2029-2033	14,369	2,234		
	<u>\$ 86,169</u>	<u>\$ 67,000</u>	<u>\$ 31,914</u>	<u>\$ 3,909</u>

As described in Note 6, the Municipality levies an annual special tax of 2% of the assessed value of real property. The proceeds of this tax are required to be credited to the Debt Service Fund for payment of general obligation bonds and notes of the Municipality. The property taxes are collected and retained by the CRIM.

<u>Primary Government</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Payments</u>	<u>Ending Balance</u>	<u>Due within One Year</u>
<b>Governmental Activities:</b>					
Bonds payable	\$ 3,144,880	\$ 3,357,000	\$ 248,760	\$ 6,253,120	\$ 294,160
Note payable - Law 42	2,420,304		42,385	2,377,919	45,048
Note payable - LIMS	39,892		7,978	31,914	8,460
Note payable - Law 146	89,759		3,590	86,169	3,590
Total long-term debt	<u>5,694,835</u>	<u>3,357,000</u>	<u>302,713</u>	<u>8,749,122</u>	<u>351,258</u>
Due to PR Health Insurance Administration	387,764		387,764	-	
Department	28,664		7,166	21,498	
Compensated absences	1,657,680		367,932	1,289,748	120,000
Total other liabilities	<u>2,074,108</u>	<u>-</u>	<u>762,862</u>	<u>1,311,246</u>	<u>120,000</u>
Total noncurrent liabilities	<u>\$ 7,768,943</u>	<u>\$ 3,357,000</u>	<u>\$ 1,065,575</u>	<u>\$ 10,060,368</u>	<u>\$ 471,258</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**16. RETIREMENT PLAN**

**a. Plan Description**

The Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) is the administrator of a cost-sharing multiple-employer retirement system established by the Commonwealth of Puerto Rico. The System was created under the Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952.

ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentalities and of certain municipalities and components units not covered by their own retirements systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Heads for Agencies and Public Instrumentalities, Assistants to the Governor, the Comptroller of Puerto Rico, Gubernatorial Board and Committee appointees and Experimental Service Station employees.

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

Members who have attained an age of at least fifty-five (55) years and have completed at least twenty-five (25) years of creditable service or members who have attained an age of at least fifty-eight (58) years and have completed at least fifty-eight (58) years and have completed at least ten (10) years of creditable service, are entitled to an annual benefit, payable monthly for life.

The amounts of the annuity should be one and one-half percent of the average compensation multiplied by the number of years of creditable service up to twenty years, plus 2% of the average compensation multiplied by the number of years of creditable service in excess of twenty years. In no case the annuity will be less than \$200 per month.

Participants who have completed at least thirty (30) years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained fifty-five

**COMMONWEALTH OF PUERTO RICO  
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NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

(55) years of age will receive 65% of the average compensation or if they have attained fifty-five (55) years of age will receive 75% of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten (10) years of service.

No benefit is payable if the participant receives a refund of his accumulated contributions.

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

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**b. Contribution Requirements**

Commonwealth legislation requires employees to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600. The Municipality's contributions are 9.275% of gross salary. Contributions' requirements are established by law. The actuarially determined contribution requirement and contributions actually made for the year ended June 30, 2008 was approximately \$263,000. The Municipality's payroll for employees covered by ERS was approximately \$2.8 million. The Municipality total payroll for all employees was approximately \$6.1 million.

Additional information on the ERS is provided in its financial statements for the year ended June 30, 2008, a copy of which can be obtained from the ERS, Minillas Station, PO Box 42003, San Juan, PR 00940.

**17. RISK MANAGEMENT**

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

**18. LEASES**

**Operating Leases**

Leasing Arrangement with the Municipality as Lessor:

- a. The Municipality leases spaces in its Market Place and Transportation center under operating lease agreements with terms ranging from one to five years.
- b. Total income from leases during the year ended June 30, 2008 was approximately \$44,000.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

- c. The Municipality retains title to its leased property. The lessee pays taxes, licenses, insurance, and maintenance costs of the leased assets.

Leasing arrangements with the Municipality as lessee:

The Municipality is obligated under noncancellable operational leases, with periods not longer than one year.

**19. CONTINGENCIES**

- a. The Municipality receives Federal Grants for specific purposes that are subject to review and audit by the grantor agencies. Although such audits could generate expenditure disallowances under the terms of the grants, management believes that any required reimbursements would not be material.
- b. The Municipality is a defendant and/or co-defendant in various lawsuits which claims for actual damages. Some of these lawsuits are covered by insurance. The Municipality's management and outside counsels believe that is probable that any potential liability that might exist, if any, in excess of the insurance, will not affect significantly the financial position of the Municipality.

**20. COMMITMENTS**

The Municipality of Vieques had several outstanding or planned construction projects as of June 30, 2008. These projects are evidenced by contractual commitments with contractors. The construction projects are commitments of the Capital Projects' funds that amounted to approximately \$4.7 million.

**21. MUNICIPAL SOLID WASTE LANDFILL POSTCLOSURE**

State and federal laws and regulations require the Municipality to place a final cover on the Municipality's landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. In accordance with Statement No. 18 of the GASB (GASB 18), "Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Costs," the Municipality has to perform a study of the activities that need to be implemented at the Municipality's

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. As of June 30, 2008, the Municipality has not performed a study of the estimated closing and postclosing costs that will be recognized in the basic financial statements as required by the GASB 18.

**22. RESTATEMENTS**

**a. Fund Balance**

The beginning fund balance of the other governmental funds has been restated to correct for accounting errors as follows:

Beginning deficit, as previously reported	\$ (95,962)
To adjust deferred revenue	<u>96,295</u>
Beginning fund balance, as restated	<u><u>\$ 333</u></u>

**b. Net Assets**

Net assets at beginning of year have been adjusted to reflect the following restatements:

Net assets at beginning of year, as previously reported:	\$125,143,954
To adjust deferred revenue	<u>96,295</u>
Net assets at beginning of year, as restated	<u><u>\$125,240,249</u></u>

**PART II - SINGLE AUDIT SECTION**

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**ORTIZ, RIVERA, RIVERA & CO.**

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Federal Grantor/Program Title</u>	<u>Federal CDFA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Federal Disbursements/ Expenditures</u>
<b>U.S. Department of Housing and Urban Development (HUD)</b>			
Pass-through Office of Commissioner of Municipal Affairs			
State Block Grant Program (SBGP)	14.228		\$ 497,699
Section 8 - Housing Choice Vouchers	14.871		341,999
Section 8 - Project Based Cluster:			
Lower Income Housing Assistance Program			
Section 8 - Moderate Rehabilitation	14.856		<u>417,205</u>
<b>Total</b>			<u>\$1,256,903</u>

See notes to schedule of expenditures of federal awards.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**1. SIGNIFICANT ACCOUNTING POLICIES**

The accompanying Schedule of Expenditures of Federal Awards is a summary of the activity of the Municipality of Vieques' federal award programs presented on the modified accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

**2. BASIS OF PRESENTATION**

The expenditures of the schedule are included in the Municipality's basic financial statements within the U.S. Housing and Urban Development Programs Fund.



ORTIZ, RIVERA, RIVERA & CO.

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American Institute of Certified  
Public Accountants (AICPA)  
Puerto Rico Board of Certified  
Public Accountants  
Management Consulting  
Services Division

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

To the Honorable Mayor  
and Municipal Legislature  
Municipality of Vieques  
Vieques, Puerto Rico

We have audited the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Vieques as of and for the year ended June 30, 2008, which collectively comprise the Municipality of Vieques' basic financial statements, and have issued our report thereon dated December 15, 2008. The report on the governmental activities was qualified because management has not recorded a liability for estimated landfill postclosing costs and, accordingly, has not recorded an expense for the current period and management has not recorded certain capital assets in governmental activities and, accordingly, has not recorded depreciation expense on those assets. In addition, the balance sheet of the governmental funds was qualified because the accounting records of the Municipality related to the interfund transactions were not adequate. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Municipality of Vieques' ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Municipality's financial statements that is more than inconsequential will not be prevented or detected by the Municipality's internal control. We consider the deficiencies described in the accompanying schedule of findings and responses to be significant deficiencies in internal control over financial reporting and included as items 08-A thru 08-D.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Municipality's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 08-A and 08-D to be material weaknesses.

#### Compliance and Other Matters

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

We noted certain matters that we reported to management of Municipality in a separate letter dated December 15, 2008.

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

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

*Ortiz, Rivera, Rivera & Co.*

San Juan, Puerto Rico  
December 15, 2008

The stamp 2363627 was affixed  
to the original of this report.





ORTIZ, RIVERA, RIVERA & CO.

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Services Division

**INDEPENDENT AUDITORS' 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 Municipal Legislature  
Municipality of Vieques  
Vieques, Puerto Rico

Compliance

We have audited the compliance of Municipality of Vieques with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2008. Municipality of Vieques' major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Municipality of Vieques' management. Our responsibility is to express and opinion on Municipality of Vieques' compliance based on our audit.

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

In our opinion, the Municipality of Vieques 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, 2008. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings as questioned costs as item 08-1 thru 08-4.

#### Internal Control over Compliance

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

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 08-3 and 08-4 to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, we consider items 08-3 and 08-4 to be material weaknesses.

Municipality's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Municipality's response and, accordingly, we express no opinion on it.

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

*Ortiz, Rivera, Rivera & Co*

San Juan, Puerto Rico  
December 15, 2008

The stamp 2363628 was affixed  
to the original of this report.



**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**1. SUMMARY OF AUDIT RESULTS**

- a. The auditors' report expresses a qualified opinion on the basic financial statements of the Municipality of Vieques.
- b. There were significant deficiencies on internal controls over financial reporting.
- c. Instances of noncompliance material to the financial statements of Municipality of Vieques were disclosed during the audit.
- d. There were significant deficiencies on internal controls over major programs.
- e. The auditors' report on compliance with requirements applicable to federal award programs for the Municipality of Vieques expressed a qualified opinion.
- f. Audit findings relative to the major federal award programs for Municipality of Vieques are reported in number 3 of this schedule.
- g. The programs tested as major programs include:
  - Section 8 - Housing Choice Vouchers - CFDA No. 14.871
  - State Block Grant Program - CFDA No. 14.228
- h. The threshold for distinguishing types A and B programs was \$300,000.
- i. Municipality of Vieques was determined to be a high-risk auditee.

**2. FINDINGS - FINANCIAL STATEMENTS AUDIT**

**a. Finding 08-A - General Ledger**

The Municipality does not have the accounting practices, policies or internal controls in place to provide for the preparation of financial statements, on a timely basis, in accordance with accounting principles generally accepted in the United States of America ("generally accepted accounting principles"). The accounting system does not provide for a self balancing set of accounts for each fund operated by the Municipality, recording cash and other financial resources,

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

together with all related assets, liabilities, revenues, expenditures and changes in fund balances. Therefore, the financial statements must be prepared using financial information obtained from various departments and accounting records. The records are not integrated, and do not follow a double entry system (debits and credits). As a result, the records required significant adjustments in order to present the financial position and results of operations of the Municipality in conformity with generally accepted accounting principles.

The continued failure to have an adequate accounting system prevents the Municipality from having current accurate and reliable financial reports and information necessary for management to take efficient and effective actions, including corrective actions when plans and objectives are not being met.

Recommendation

The Municipality should adopt and implement a plan to convert its accounting system to an integrated system that would allow for the monthly closing of the general ledger, as well as the preparation of year-end financial statements in accordance with generally accepted accounting principles.

This plan should provide for:

- Assessment of the financial accounting and reporting needs in order to take the necessary steps to meet the financial reporting requirements of GASB Statement No. 34.
- The implementation of a double entry accounting system, the integration of all subsidiary ledgers and the reconciliation with the records maintained for the federal funds.
- The preparation of periodic financial reports to be submitted to the Finance Director and all other interested entities.
- Adequate training of all accounting personnel to improve the understanding of the system and to promote operational efficiency.
- Reconciliation of financial records with the reports prepared and submitted to the federal government.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**b. Finding 08-B**

The Municipality does not have a reliable financial reporting system that ensures the preparation and submission of the Budgetary Liquidation to the Municipal Affairs Commissioner's Office on or before September 30 of each year. This condition results from the failure of the Municipal management to monitor compliance with the required reporting requirements by ensuring the timely preparation and submission of financial reports.

Recommendation

The Municipality should establish a reporting calendar which informs to the Municipality's management of the due dates of each financial report. Chapter II, Section 10 of the Basic Standards requires to the Finance Director to prepare and submit to the Municipal Affairs Commissioner's Office the Budgetary Liquidation on or before September 30.

**c. Finding 08-C - Budget**

The Municipality's system of internal control relating to the Budgeting function does not adequately prevent operating management from incurring expenditures in excess of the level of funds appropriated and available. The Municipality closed its fiscal year ended June 30, 2008 with an unreserved fund balance deficiency in the general fund approximately \$11.4 million.

This occurs because the budgeting system does not reflect actual available revenues and therefore cannot prevent the obligation of expenditures for which current resource will not be available.

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

The continued occurrence of this situation could result in the eventual reduction or elimination of municipal services since future revenues will need to be used to pay for accumulated liabilities.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Recommendation

The Municipality should revise and amend the budget as current information related to collections of budgeted revenues became available.

**d. Finding 08-D**

The Municipality realized on prior years several transfers from its special revenue fund accounts to its General Fund during prior years amounting approximately to \$9.29 million.

Criteria

Article 8 of the Resource Allocation for the Realization of Permanent Works, Acquisition of Equipment, Purchase of Materials and Other Social Interest Activities Act (Law 179 of August 16, 2002) requires municipalities to utilize funds from state grants only for the intended purpose established by the Joint Resolution of the Puerto Rico Legislature and may not expend these in any activity not specifically and categorically addressed in the legislative grant. The use of funds from state grants in activities other than those mentioned in the Joint Resolution requires the prior approval of the Puerto Rico Legislature.

Cause

The bank transfers were authorized by the Finance Director through letters to bank. These transfers were made to compensate cash deficiency the Municipality was facing to pay current operating obligations. The Mayor and the Finance Director performed these transfers in violation of state law.

Recommendation

We recommend the Municipality refer this case to the appropriate regulatory bodies.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

**3. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAM  
AUDIT**

**a. SBGP - CFDA No. 14.228**

● **Condition 08-1**

The Municipality does not have effective internal controls over compliance with the requirement to ensure that all laborers and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by Federal assistance funds are paid wages not less than those established for the locality of the project (prevailing wage rates) by the Department of Labor (DOL) (40 USC 276a to 276a-7). For the construction projects selected for testing, none of the contracts selected have the certified payrolls.

Criteria

The Davis Bacon Act requires that all laborers and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by Federal assistance funds must be paid wages not less than those established for the locality of the project (prevailing wage rates) by the DOL (40 USC 276a to 276a-7).

Cause

The program's management failed to monitor the laborers employed by contractors to assure they are paid the prevailing wage rates and includes the certified payrolls.

Effect

The continued failure to implement internal controls and ensure compliance with the above requirement may expose the Municipality to cost disallowances.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Recommendation

The Municipality should require to the construction contractors to make interviews to laborers to assure that wages paid are not less than those established by the DOL.

Questioned Costs

\$ -0-

● **Condition 08-2**

The Municipality did not comply with the requirement of preparing and filing its federal financial reports on a timely basis. During our examination of the Federal Financial Reports, we noted that the Municipality did not send on time the quarterly report for the following period ended:

<u>Quarter Ended</u>	<u>Due Date</u>	<u>Date Submitted</u>
September 2007	11-10-07	11-27-07
June 2008	08-10-08	08-13-07

Criteria

The Municipality is not in compliance with 24 CFR 85.40 (b) (1) which requires federal fund recipients to periodically monitor the performance of grant-supported activities to ensure that time schedules are being met, projected work units by time periods are being accomplished, and other performance goals are being achieved by the preparation of federal financial reports. To achieve these goals, program management should prepare accurate and timely federal financial reports. The Municipality should submit quarterly or semi-annual reports 30 days after the reporting period.

Cause

The above situation occurred because the Municipality did not ensure to verify and understand its reporting requirements for this program.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Effect

The continued failure to file the required reports may result in sanctions by the Federal grantor, such as grant payment withholdings.

Recommendation

The Municipality should verify and become familiar with all administrative requirements applicable to each federal financial assistance program, especially when new grants are received. This can be achieved by obtaining the information applicable to the program from the pass-thru grantor, federal grantor, or the Catalog of Federal Domestic Assistance ("CFDA"), which is available from the federal government.

Questioned Costs

\$ -0-

**b. Section 8 Housing Choice Voucher - CFDA No. 14.871**

• **Condition 08-3**

In order to test the allowability of the disbursements for the fiscal year ended June 30, 2008, we selected 7 disbursements which totaled \$138,881 or 28% of the program. The Municipality could not provide adequate supporting documentation in 2 out of the 7 disbursements tested, or 6% of our sample, amounting to \$68,646.02 as follows:

<u>Check Number</u>	<u>Payee</u>	<u>Date</u>	<u>Amount</u>
1885	Bieke Contractor	08-07-07	\$46,365.15
1887	The Bezel Concrete Group	08-24-07	<u>22,280.87</u>
			<u>\$68,646.02</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Criteria

As per OMB A-87, to be allowable under federal awards, costs must be adequately documented. In addition, 24 CFR (b) requires that except as otherwise provided, records must be retained for three years starting the day the grantee submits to the awarding agency its expenditure report.

Cause

The Municipality does not keep adequate internal control procedures regarding the filing of documents.

Effect

Failure to maintain adequate accounting records may result in disallowance of costs by the awarding agency.

Recommendation

The Municipality's management should ascertain that adequate source documentation exists to support amounts and items reported as expenditures. The Municipality should also establish a recordkeeping system to ensure that accounting records and documentation are retained for the time period required by applicable requirements and the provisions of laws, regulations, contracts or grant agreements applicable to the program.

Questioned Costs

\$68,646.02

● **Condition 08-4**

The Municipality's system of internal control over compliance with the documentation of participant files is not working effectively. During our audit of the participant files in the Section 8 program, we noted that the Municipality was not maintaining the required documents and information in each file to support participant's eligibility as required by Section 8 Program regulations.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

During our test of eligibility requirements we tested seventeen (17) participant files and noted the following exceptions:

<u>Participant Name</u>	<u>Condition</u>
Lorraine N. Alicea Pérez	1, 9
Migdalia Belardo	3, 4, 5, 7, 8, 9, 12, 13
Cesario Crmona Cádiz	1, 3, 4
Shamayra Colón	3, 9
Dimara Cruz Soto	3, 9, 11
Mariam Encarnación	2, 3, 7
Damira García	3, 9
Cándida Guadalupe	3, 9
Alma Malavé	11
Silvia Navedo	11, 13
Julie Quiles Colón	8, 9
Saida Rodríguez González	7, 9
Ana L. Santana	7, 9, 13
María L. Santos Alvarado	3, 4, 5
Liseyda Santos Pérez	3, 7, 9, 11, 12
María I. Simons	10, 11
Genoveva Velázquez	10, 11, 12, 13

Legend:

- 1) Familiar group photo
- 2) Good Behavior Certificate
- 3) Evidence of expenses of child care
- 4) Evidence of income
- 5) Nutritional assistance letter
- 6) Recertification Form (HUD 50058)
- 7) Allowance for tenant furnished utilities and other services (HUD 52667)
- 8) Housing assistant payment contract (HUD 52646)
- 9) Verification of comparable units
- 10) Annual Inspection Form (HUD 52580)
- 11) Evidence that the improvements were made timely
- 12) Release of Information to Third Parties (HUD 9886)
- 13) Privacy Note Act

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Criteria

24 CFR Sections 882-113, 882-209, 882-214, 882-412, 882-514, 882-515, 882-518, 883-711, 883-704, 889-103, 982.4, 982.54 (d) (15), 982.158 (f) (7), 982.158 (d), 982.405 (b), and 982.404 establish that the PHA is required to accept applications for admission to the projects, determine whether the applicants are initially eligible, and on a yearly basis, reexamine family income, composition, and contribution to rent, utilities reasonable rent and housing quality standards' inspections. In addition, the Municipality should verify that the information submitted by participants is reliable.

Cause

All of the above matters occur because the Municipality's system of internal control relating to the compliance requirements is not effectively identifying and correcting these matters through the proper review of participant files for completeness of documents, signatures and information, as well as for their accuracy. The current procedures do not effectively reduce the risk of ineligible participants receiving program benefits.

Effect

The continued failure to establish internal control over compliance with the above requirements exposes the Municipality to unauthorized user or disposition of the program's resources.

Recommendation

The Municipality should design and adopt a checklist that includes all the related documents that must be completed for each participant file. The checklist should be completed during the initial processing and revised for changes during the annual review. Once completed, the participant files should then be reviewed for completeness by another official or supervisor prior to the final approval. These procedures will help to improve controls and documentation concerning the eligibility of participants and will reduce the possibility of cost disallowances.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Questioned Costs

\$ -0-

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF STATUS OF PRIOR YEAR  
AUDIT FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

During the current examination, follow-up was given to the findings informed to the Municipality in prior years. It was noted that corrective action has been taken, except for certain conditions that still exist and require further action. These are included in the accompanying Schedule of Prior Year Audits Findings and Questioned Costs.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF STATUS OF PRIOR YEAR  
AUDIT FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Program</u>	<u>Condition/Noncompliance</u>	<u>Status</u>
Section 8 - Housing Choice Voucher CFDA No. 14.871	<b>Condition 06-1</b>  Through our test of activities allowed, we observed some disbursements with Section 8 Vouchers federal funds not allowable by the program. Those disbursements correspond to the SBGP federal program. We do not observe the HUD-approved form to use the funds in those activities.	Condition was corrected.
Section 8 - Housing Choice Voucher CFDA No. 14.871	<b>Condition 06-2</b>  The Section 8 program internal controls relating to compliance with the cash management requirement are not effective since they are not minimizing the time elapsed between the receipt of funds and the final disbursement for payment.	Condition was corrected.
Section 8 - Housing Choice Voucher CFDA No. 14.871	<b>Condition 06-3</b>  The Municipality's system of internal control over compliance with the documentation of participant files is not working effectively. During our audit of the participant files in the Section 8 programs, we noted that the Municipality does not maintain the required documents and information in each file to support participant's eligibility requirements.	Condition still prevails.
Section 8 - Housing Choice Voucher CFDA No. 14.871	<b>Condition 06-4</b>  The Section 8 Program does not have an effective system of internal control to ensure the accurate preparation of federal financial reports of the Program. The information submitted in the VMS did not match with the accounting books.	Condition was corrected.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF STATUS OF PRIOR YEAR  
AUDIT FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Program</u>	<u>Condition/Noncompliance</u>	<u>Status</u>
<p><b>Section 8 - Housing Choice Voucher</b> CFDA No. 14.871</p>	<p><b>Condition 06-5</b></p> <p>We selected a sample of two new participants in the program and one of them wasn't observed in the waiting list. In addition, they didn't comply with selection policies because they didn't follow a sequence.</p>	<p>Condition was corrected.</p>
<p><b>Section 8 - Housing Choice Voucher</b> CFDA No. 14.871</p>	<p><b>Condition 06-6</b></p> <p>During the audit, we reviewed 12 participants' files. We observed that none of the files observed contains evidence of the method used by the Program to determine that the rent to the owner is reasonable in comparison to the rent for other comparable unassisted units.</p>	<p>Condition was corrected.</p>
<p><b>Section 8 - Housing Choice Voucher</b> CFDA No. 14.871</p>	<p><b>Condition 06-7</b></p> <p>During our eligibility test, we examined a sample of 12 participants' files. The followings were the exceptions found:</p> <p>In four (4) cases, evidence that the repairs to be completed by the participants were not observed and the contract was not properly completed.</p>	<p>Condition still prevails.</p>
<p><b>Section 8 - Lower Income Housing Assistance Program</b> CFDA No. 14.856</p>	<p><b>Condition 06-8</b></p> <p>The Section 8 program internal controls relating to compliance with the cash management requirement are not effective since they are not minimizing the time elapsed between the receipt of funds and the final disbursement for payment.</p>	<p>Condition was corrected.</p>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF STATUS OF PRIOR YEAR  
AUDIT FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Program</u>	<u>Condition/Noncompliance</u>	<u>Status</u>
<p><b>Section 8 - Lower Income Housing Assistance Program CFDA No. 14.856</b></p>	<p><b>Condition 06-9</b></p> <p>The Municipality's system of internal control over compliance with the documentation of participant files is not working effectively. During our audit of the participant files in the Section 8 programs, we noted that the Municipality was not maintaining the required documents and information in each file to support participants' eligibility requirements.</p>	<p>Condition was not observed.</p>
<p><b>Section 8 - Lower Income Housing Assistance Program CFDA No. 14.856</b></p>	<p><b>Condition 06-10</b></p> <p>The Federal Program Office maintains a detail of equipment with some deficiencies in relation to the acquisition date, unit acquisition cost and do not include all the equipment that the Municipality has. In addition, a physical inventory will be taken and the results reconciled with the equipment records at least once every two years.</p>	<p>Condition was corrected.</p>
<p><b>Section 8 - Lower Income Housing Assistance Program CFDA No. 14.856</b></p>	<p><b>Condition 06-11</b></p> <p>The program did not adjust the utility data schedule within the last 14 years. In addition, contracts rent weren't adjusted either.</p>	<p>Condition was not observed.</p>
<p><b>Section 8 - Lower Income Housing Assistance Program CFDA No. 14.856</b></p>	<p><b>Condition 06-12</b></p> <p>During our eligibility test, we examined a sample of 13 participants' files. The followings were the exceptions found:</p> <p>In ten (10) cases, evidence that the repairs to be completed by the participants were not observed and the contract was not properly terminated.</p>	<p>Condition was not observed.</p>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES  
SCHEDULE OF STATUS OF PRIOR YEAR  
AUDIT FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Program</u>	<u>Condition/Noncompliance</u>	<u>Status</u>
SBGP - CFDA No. 14.228	<b>Condition 07-1</b>  The Municipality' internal control over compliance with the cash management requirements of the federal program is not effective since it is not minimizing the time elapsed between the receipt and final disbursements of funds.	Condition still prevails.
SBGP - CFDA No. 14.228	<b>Condition 07-2</b>  The Municipality did not comply with the requirement of preparing and filing its federal financial reports on a timely basis. During our examination of the Federal Financial Reports, we noted that the Municipality did not send on time the quarterly report.	Condition was corrected.
Section 8 - Housing Choice Voucher CFDA No. 14.871	<b>Condition 07-3</b>  The Section 8 program internal controls relating to compliance with the cash management requirement are not effective since they are not minimizing the time elapsed between the receipt of funds and the final disbursement for payment.	Condition was corrected.



Estado Libre Asociado de Puerto Rico  
GOBIERNO MUNICIPAL DE VIEQUES  
Honorable Dámaso Serrano López  
Alcalde

## CORRECTIVE ACTION PLAN

December 15, 2008

Cognizant or Oversight Agency for Audit:

Municipality of Vieques respectfully submits the following corrective action plan for the year ended June 30, 2008

Name and address of independent public accounting firm: Ortiz, Rivera, Rivera & Co., Suite 152, PO Box 70250, San Juan, Puerto Rico 00936-7250.

Audit period: Fiscal year ended June 30, 2008

The findings from the June 30, 2008 schedule of findings and questioned costs are discussed below. The findings are numbered consistently with the numbers assigned in the schedule.

### FINDINGS - FEDERAL AWARD PROGRAM AUDITS

**Finding 08-1: SBGP - CFDA No. 14.228**

Reportable Condition: See Condition 08-1

#### Recommendation

The Municipality should require to the construction contractors to make interviews to laborers to assure that wages paid are not less than those established by the DOL.

#### Action Taken

**Finding 08-2: SBGP - State Block Grant Program - CFDA No. 14.228**

Reportable Condition: See Condition 08-2

Recommendation

The Municipality should verify and become familiar with all administrative requirements applicable to each federal financial assistance program, especially when new grants are received. This can be achieved by obtaining the information applicable to the program from the pass-thru grantor, federal grantor, or the Catalog of Federal Domestic Assistance ("CFDA"), which is available from the federal government.

Action Taken

**Finding 08-3: Section 8 Housing Choice Voucher - CFDA No. 14.871**

Reportable Condition: See Condition 08-3

Recommendation

The Municipality's management should ascertain that adequate source documentation exists to support amounts and items reported as expenditures. The Municipality should also establish a recordkeeping system to ensure that accounting records and documentation are retained for the time period required by applicable requirements and the provisions of laws, regulations, contracts or grant agreements applicable to the program.

Action Taken

**Finding 08-4: Section 8 Housing Choice Voucher - CFDA No. 14.871**

Reportable Condition: See Condition 08-4

Recommendation

The Municipality should design and adopt a checklist that includes all the related documents that must be completed for each participant file. The checklist should be completed during the initial processing and revised for changes during the annual review. Once completed, the participant files should then be reviewed for completeness by another official or supervisor prior to the final approval. These procedures will help to improve controls and documentation concerning the eligibility of participants and will reduce the possibility of cost disallowances.

Action Taken

If the Cognizant or Oversight Agency for Audit has questions regarding this plan, please call Edwin Torres, Finance Director, at (787) 741-500, ext. 239.

Cordially,



Edwin Torres  
Finance Director  
Municipality of Vieques