

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES

BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2012

(WITH INDEPENDENT AUDITOR'S REPORT THEREON)



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**TORRES, HERNANDEZ & PUNTER, CPA, CSP**  
Certified Public Accountants

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**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**

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**MUNICIPALITY OF VIEQUES**

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**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 of the Commonwealth of Puerto Rico (the Municipality), as of and for the year ended June 30, 2012, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Municipality's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinions.

Management has not recorded certain capital assets in governmental activities and, accordingly, has not recorded depreciation expenses 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 the assets, net assets and expenses of the governmental activities is not reasonably determinable.

Also, as discussed in Note 2.D-11 to the financial statements, the Municipality has not recorded a provision for liability of closure and postclosure care costs related to the operation of the landfill. Accounting principles generally accepted in the United States of America require that a provision for liability related to closure and postclosure care costs be recorded to comply with applicable federal and state regulations. The amount by which this departure would affect the liabilities, net assets, expenses of governmental activities is not reasonable determinable.

In our opinion, except for the effects of not recording certain capital assets in governmental activities and the related depreciation expense and for the effects of not providing a provision for liability of closure and postclosure care costs related to the operation of the landfill as described in the preceding paragraphs, the financial statements referred to previously present fairly, all material respects, the respective financial position of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality as of June 30, 2012 and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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In accordance with Government Auditing Standards, we have also issued our report dated March 26, 2013, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 14 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's financial statements as a whole. The budgetary comparison schedule of the general fund and related notes on pages 48 to 49 are presented for purposes of additional analysis and are not a required part of the financial statements. The accompanying schedule of expenditures of federal awards and related notes on pages 50 and 51 are presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the financial statements. The budgetary comparison schedule of the general fund and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Torres, Hernández & Punter, CPA, PSC*

**Torres, Hernández & Punter, CPA, PSC**  
**Certified Public Accountants**

March 26, 2013

Stamp #E23413 of the  
College of CPA's of  
Puerto Rico is affixed  
to the original.

The following discussion and analysis of the Municipality of Vieques' (Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended June 30, 2012. Please read it in conjunction with the Financial Statements which follow this section.

## FINANCIAL HIGHLIGHTS

### Highlights for Government-wide Financial Statements

The government-wide financial statements report information about the Municipality as a whole using the economic resources measurement focus and accrual basis of accounting:

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2012 by \$122,421,207 (net assets).
- Revenues increased by \$1,267,094 (4%) and expenses decreased by \$66,027 (0.2%) in comparison with year 2011, as restated.
- Net decrease in net assets amounted to \$1,655,817, a decrease of \$1,201,067 with respect to prior year (2011) net change, as restated.

### Highlights for Fund Financial Statements

The fund financial statements provide detailed information about the Municipality's most significant funds using the current financial resources measurement focus and modified accrual basis of accounting:

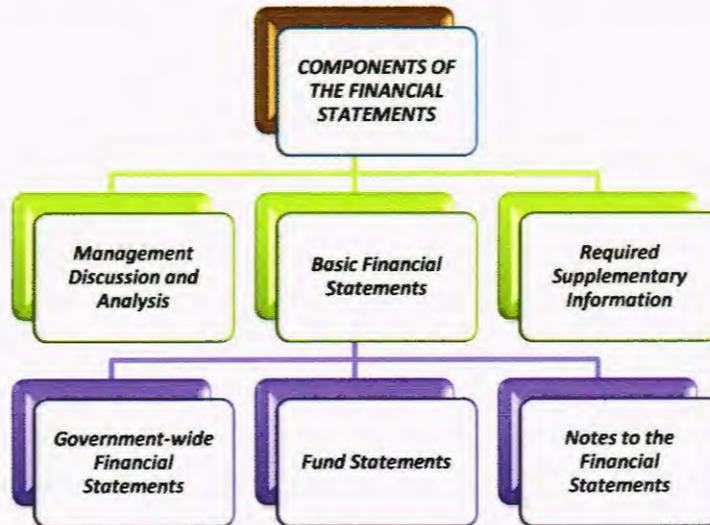
- At the close of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$4,895,137, an increase of (\$1,052,629) in comparison with the prior year, as restated.
- The General Fund reported an excess of revenues and other financing sources over expenditures and other financing uses of (\$108,112) and an unassigned (deficit) fund balance of (\$6,672,774).

### General Financial Highlights

- The investment in net capital assets as of June 30, 2012 was \$125,365,893 (net of related debt).
- Long-term debt general and special obligation bonds increased to \$12,705,040, approximately 10% with respect to prior year balance. The Municipality issued a general obligation bond for \$2,190,000 for construction purposes. In addition, two bonds were issued for operational purposes, a general obligation bond of \$385,000 and a special obligation bond of \$291,000.
- Other long term debts increases and net reductions from payments amounted to \$265,463 and \$496,503, respectively.
- On a budgetary basis, actual expenditures exceeded actual revenues and transfers by (\$1,094,487).

## OVERVIEW OF THE FINANCIAL STATEMENTS

The Municipality's basic financial statements comprise three components: (1) management discussion and analysis (presented here), (2) basic financial statements, and (3) required supplementary information.



The Municipality's basic financial statements consist of two kinds of statements, each with a different view of the Municipality's finances. The government-wide financial statements provide both long-term and short-term information about the Municipality's overall financial status. The fund financial statements focus on major aspects of the Municipality's operations, reporting those operations in more detail than the government-wide statements:

### Basic Financial Statements

#### ◆ *Government-Wide Financial Statements*

The government-wide statements report information about the Municipality as a whole using accounting methods similar to those used by private-sector businesses. They are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. The first government-wide statement – the *Statement of Net Assets* – presents information on all of the Municipality's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in the Municipality's net assets are an indicator of whether its financial health is improving or deteriorating. Other non-financial factors such as the condition of the Municipality's roads and other infrastructure may need to be considered to assess the overall health of the Municipality. The second statement – the *Statement of Activities* – presents information showing how the net assets changed during the year. All of the current year's revenues and expenses are taken into account in the statement of activities regardless of when cash is received or paid.

#### ◆ *Fund Financial Statements*

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

The Municipality implemented **GASB Statement 54, Fund Balance Reporting and Governmental Fund Type Definitions** effective with the June 30, 2011 financial statements. Fund balances for the governmental funds are reported in classifications that comprise a hierarchy based on the extent to which the government honors constraints on the specific purposes for which amounts in those funds can be spent.

In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. At the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$4,895,137. Approximately \$7.1 million of this isn't available for spending at the government's discretion [Unassigned Fund Balance (Deficit)]. The remainder of fund balance is restricted, committed or assigned to indicate that is not available for new spending because it has already been committed.

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

The governmental fund statements focus on major funds. The Municipality's major funds are the general fund (which accounts for the main operating activities of the Municipality) and funds that complies with a minimum criterion (percentage of the assets, liabilities, revenues or expenditures). Funds that do not comply with this criterion are grouped and presented in a single column as other governmental funds.

◆ **Notes to the Financial Statements**

Provides integral information needed to explain the basis for the numbers used within the Basic Financial Statements and provide more detailed data.

◆ **Required Supplementary Information**

Provides additional information to better understand the financial position of the Municipality and contains the Budgetary Comparison Schedule for the General Fund.

## FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

### Net Assets

The following table presents a summary of the Statements of Net Assets as of June 30, 2012 and 2011:

Net assets (assets over liabilities) may serve over time as a useful indicator of a government's financial position. Net assets for the year were maintained stable with a decrease of only 1% with respect to prior year as restated. The most significant changes were a decrease in Restricted Net Assets of (\$717,641) and a decrease of the Investment in Capital Assets by (\$562,220). The decrease in Restricted Net Assets is due to an increase in expenses related to General Administration.

The following table presents a summary of the Statements of Net Assets as of June 30, 2012 and 2011:

**Table 1**

**Commonwealth of Puerto Rico  
Municipality of Vieques, Puerto Rico  
Statement of Net Assets  
As of June 30,**

	<u>2012</u>	<u>2011</u>
Current and Non-Current Assets	\$ 10,794,580	\$ 9,855,835
Capital Assets	130,980,499	131,180,523
<b>Total Assets</b>	<b><u>141,775,079</u></b>	<b><u>141,036,358</u></b>
Current Liabilities	1,748,352	1,521,408
Deferred Revenues	418,587	398,613
Long-Term Liabilities	17,186,933	15,029,313
<b>Total Liabilities</b>	<b><u>19,353,872</u></b>	<b><u>16,949,334</u></b>
Net Assets:		
Investment in Capital Assets, Net of Related Debt	125,365,893	125,928,113
Restricted	4,843,756	5,561,397
Unrestricted	(7,788,442)	(7,402,486)
<b>Total Net Assets</b>	<b><u>\$ 122,421,207</u></b>	<b><u>\$ 124,087,024</u></b>

The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure) for \$130,980,499; total capital assets (\$173,202,842) less accumulated depreciation (\$42,222,343) and less any related outstanding debt (\$5,614,606) used to acquire those assets. The Municipality uses these assets to provide services to its citizens and consequently, these assets are not available for future spending. The resources needed to repay the debt related to these capital assets must be provided from other sources, because capital assets are not generally liquidated for the purpose of retiring debt.

Restricted net assets represent resources that are subject to external restrictions on how they may be used.

Unrestricted net assets are the part of the net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements.

As of June 30, 2012 the Municipality presented unrestricted (deficit) net assets of (\$7,788,442). This balance was affected by long term obligations such as compensated absences \$1,481,797, Law 42 \$2,207,477, general and special obligations for \$3,746,400 (used for operating purposes), and other debts for the amount of \$792,619 for which the Municipality did not provide funding in previous budgets. Historically, such obligations have been budgeted on a pay as you go basis without providing funding for their future liquidation.

**Changes in Net Assets**

The following table summarizes the changes in net assets for the years ended June 30, 2012 and 2011:

With respect to prior year, revenues increased by approximately \$1.3 million or 4%, principally on operating grants and contributions, and intergovernmental revenue.

Expenses decreased 0.2% or \$66 thousands in comparison with 2011 year. Significant decreases were registered on urban development.

**Table 2**

**Commonwealth of Puerto Rico  
Municipality of Vieques, Puerto Rico  
Changes in Net Assets  
For Fiscal Year Ending June 30,**

	<u>2012</u>	<u>2011</u>
<b>Revenues:</b>		
Program Revenues:		
Operating Grants and Contributions	\$ 2,788,657	\$ 2,091,179
Capital Grants and Contributions	371,273	692,842
General Revenues:		
Property Taxes	1,460,712	1,738,758
Volumen of Business Taxes	532,182	542,911
Sales and Usage Taxes	923,418	721,570
Construction Excise Taxes	595,365	290,587
Intergovernmental	7,570,145	6,807,210
Other General Revenues	877,405	967,006
<b>Total Revenues</b>	<b><u>15,119,157</u></b>	<b><u>13,852,063</u></b>
<b>Expenses:</b>		
General Administration	8,314,410	7,532,606
Public Safety	1,201,094	1,135,468
Public Works	1,803,589	1,715,179
Culture and Recreation	892,394	913,275
Health and Sanitation	602,383	459,066
Human Services and Welfare	1,911,213	1,551,349
Urban Development	1,535,447	2,944,564
Interest Costs	524,444	467,440
<b>Total Expenses</b>	<b><u>16,784,974</u></b>	<b><u>16,718,947</u></b>
<b>Changes in Net Assets</b>	<b>(1,665,817)</b>	<b>(2,866,884)</b>
Net Assets-Beginning, as Restated	124,087,024	126,953,908
<b>Net Assets-Ending</b>	<b><u>\$ 122,421,207</u></b>	<b><u>\$ 124,087,024</u></b>

Figure 1 presents revenues comparison by sources of the governmental activities during the past two years:

FIGURE 1

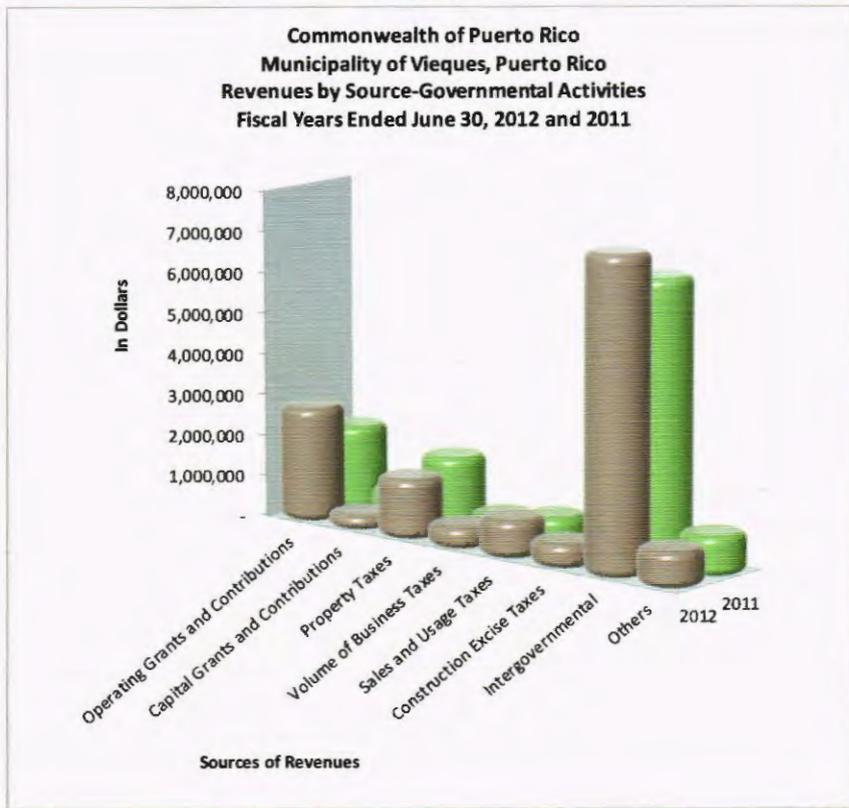
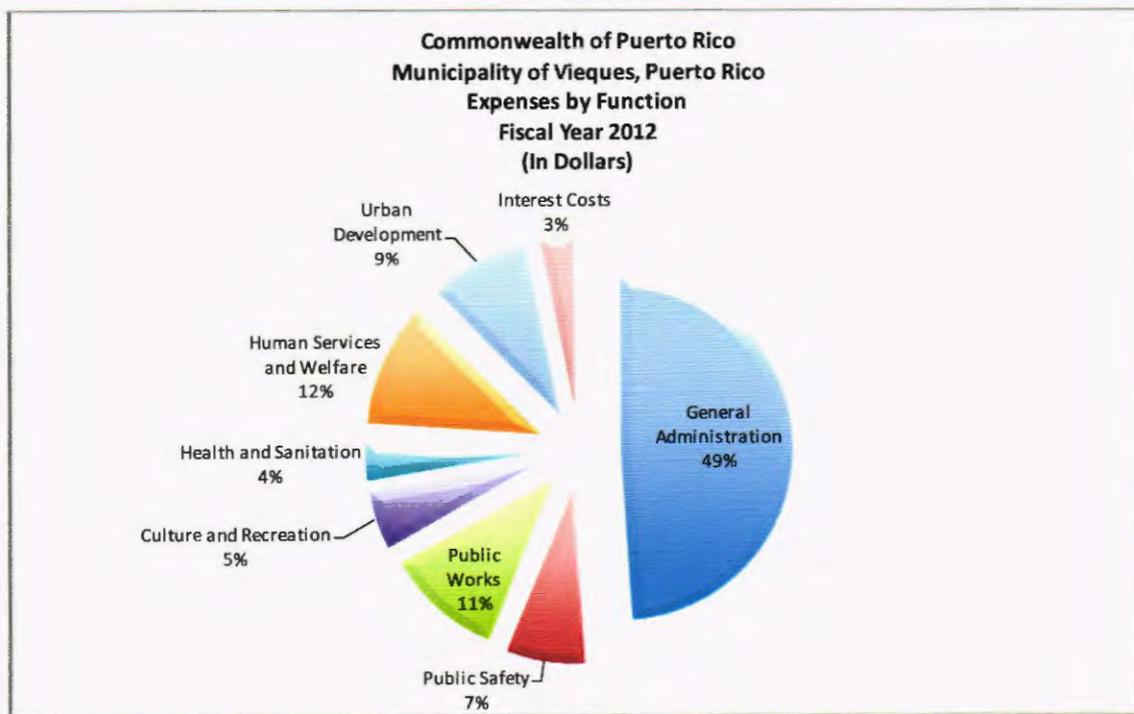


Figure 2 presents expenses by function of the governmental activities during the fiscal year 2011-2012:

FIGURE 2



Approximately 50.1% of the Municipality's revenues came from intergovernmental, 9.7% from property taxes, 18.4% from grants and contributions, and 21.8% from other sources. The Municipality's expenses cover a range of services. The largest expenses are general administration with 48.9%, public works with 10.9%, urban development with 9.3, human service and welfare with 11.5 % and public safety with 7.3%. Program revenues of the Municipality covered 19% of total expenses.

The following table focuses on the cost of each of the Municipality's largest functions/programs as well as each functions/program's net cost (total cost less fees generated by the programs and program-specific intergovernmental aid):

**Table 3**

**Commonwealth of Puerto Rico  
Municipality of Vieques, Puerto Rico  
Net Cost of Municipality's Governmental Activities  
Fiscal Years ended June 30,**

Functions/Programs	Total Cost of Services		Net Cost of Services	
	2012	2011	2012	2011
General Administration	\$ 8,314,410	\$ 7,532,606	\$ 7,876,484	\$ 7,258,532
Public Safety	1,201,094	1,135,468	1,087,621	1,057,734
Public Works	1,803,589	1,715,179	872,705	1,715,179
Culture And Recreation	892,394	913,275	890,729	912,000
Health and Sanitation	602,383	459,066	602,383	459,066
Human Services and Welfare	1,911,213	1,551,349	1,198,372	716,768
Urban Development	1,535,447	2,944,564	572,306	1,348,207
Others	524,444	467,440	524,444	467,440
<b>Total</b>	<b>\$ 16,784,974</b>	<b>\$ 16,718,947</b>	<b>\$ 13,625,044</b>	<b>\$ 13,934,926</b>

Some of the cost of governmental activities in 2012 was paid from other governments and organizations that subsidized certain programs with grants and contributions (\$3,159,930). The \$13,625,044 net cost of services was substantially covered by other general revenues including property, volume of business, sales and usage, and construction excise taxes, and intergovernmental revenues.

## FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

### Governmental Funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending. Such information is useful in assessing the Municipality's financing requirements. Municipality implemented **GASB Statement 54, Fund Balance Reporting and Governmental Fund Type Definitions** effective with the June 30, 2011 financial statements. Fund balances for the governmental funds are reported in classifications that comprise a hierarchy based on the extent to which the government honors constraints on the specific purposes for which amounts in those funds can be spent.

**Table 4**

**Commonwealth of Puerto Rico  
Municipality of Vieques, Puerto Rico  
Fund Balance  
As of June 30,**

	2012	2011
<b>Fund Balances:</b>		
Nonexpendable	\$ -	\$ -
Restricted	11,974,450	10,618,589
Committed	30,516	41,128
Assigned	-	33,740
Unassigned	(7,109,829)	(6,850,949)
<b>Total</b>	<b>\$ 4,895,137</b>	<b>\$ 3,842,508</b>

At the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$5.1 million. An increase in the Restricted Fund Balance was mainly due to the proceeds of a general obligation bond for construction purposes.

The General Fund is the operating fund of the Municipality. The General Fund experienced a \$108,112 increase from a fund balance (deficit) of (\$6,780,886) (as restated) in the previous year to a fund balance (deficit) of (\$6,672,774) at the end of the current year.

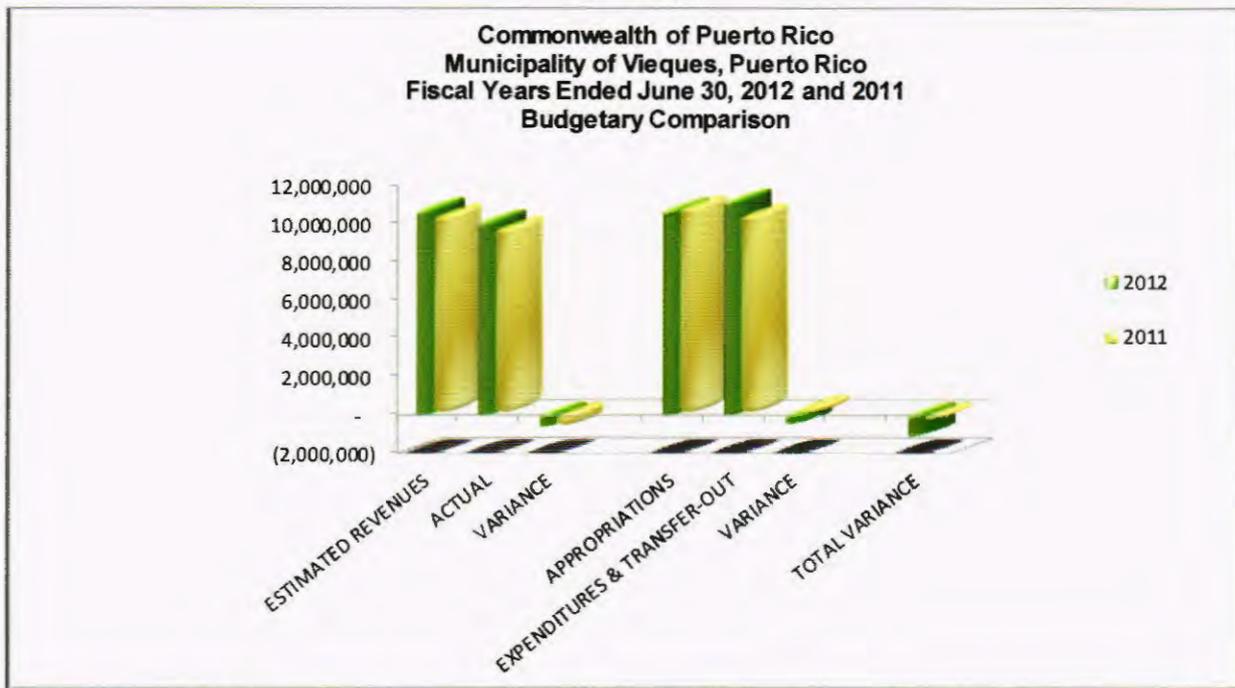
At the end of the Fiscal Year 2012, the General Fund presented only Unassigned Fund Balance (Deficit). In order to accomplish with the provisions stated on our Ordinance that implemented the GASB Statement No. 54, regarding the Minimum Fund Balance Policy, the Municipality is in the process of making the arrangements to comply.

<b>Commonwealth of Puerto Rico</b>		
<b>Municipality of Vieques, Puerto Rico</b>		
<b>General Fund</b>		
<b>As of June 30,</b>		
Description	2012	2011
<b>Revenues:</b>		
Property Taxes	\$ 966,242	\$ 1,029,483
Volume of Business Taxes	532,182	542,911
Sales and Usage Taxes	423,668	324,262
Intergovernmental	6,769,544	6,717,956
Construction Excise Taxes	595,365	290,587
Miscellaneous	828,805	45,116
Total Revenues	<u>10,115,806</u>	<u>8,950,315</u>
<b>Expenditures:</b>		
General Government	7,195,622	6,192,165
Public Safety	836,211	796,246
Public Work	728,504	1,121,085
Culture and Recreation	671,890	735,828
Health and Sanitation	602,383	459,066
Human Services and Welfare	595,814	671,968
Urban Development	171,631	7,671
Capital Outlay	8,159	20,605
Total Expenditures	<u>10,810,214</u>	<u>10,004,634</u>
Net Transfer In (Out)	802,520	218,524
Other Financing Sources	-	-
<b>Net Increase (Decrease) in Fund Balance</b>	<b><u>\$ 108,112</u></b>	<b><u>\$ (835,795)</u></b>

**GENERAL FUND BUDGETARY HIGHLIGHTS**

The general fund original budget for the fiscal period 2011-2012 presented a decrease of 0.5% with respect to prior year budget. The Municipality did not include as an amendment to the budget the positive and negative changes on revenues, principally in construction excise taxes of (\$683,635), volume of business taxes of \$164,731, and intergovernmental revenues of (\$170,066).

**FIGURE 3**



The negative variance of (\$1,094,487) between revised budget and actual results was due mainly to a decrease in revenues as explained in the preceding paragraph. In addition, the Municipality reported more expenditure than appropriations in those functions for payments of salaries and fringe benefits, and purchase of supplies.

**CAPITAL ASSETS AND DEBT ADMINISTRATION**

**Capital Assets**

At the end of the fiscal year, the Municipality has invested \$130,980,499 (net of accumulated depreciation) in a broad range of capital assets, including buildings, land, infrastructure, construction in progress and equipment. This amount represents a net decrease of \$200,024 or .08% from the prior year.

**Table 6**  
Commonwealth of Puerto Rico  
Municipality of Vieques, Puerto Rico  
Capital Assets (Net)  
As of June 30,

	Governmental Activities	
	2012	2011
<b>Non-depreciable assets:</b>		
Land	\$ 65,650,752	\$ 65,650,752
Construction in Progress	5,837,228	4,047,439
<b>Depreciable assets:</b>		
Buildings	17,845,754	18,454,199
Equipment and Vehicles	499,836	515,537
Furniture and Fixtures	-	31,839
Infrastructure	41,146,929	42,480,757
<b>Total</b>	<b>\$ 130,980,499</b>	<b>\$ 131,180,523</b>

The Municipality invested a total of \$1,895,069 of capital assets during the fiscal year 2011-2012 as follows:

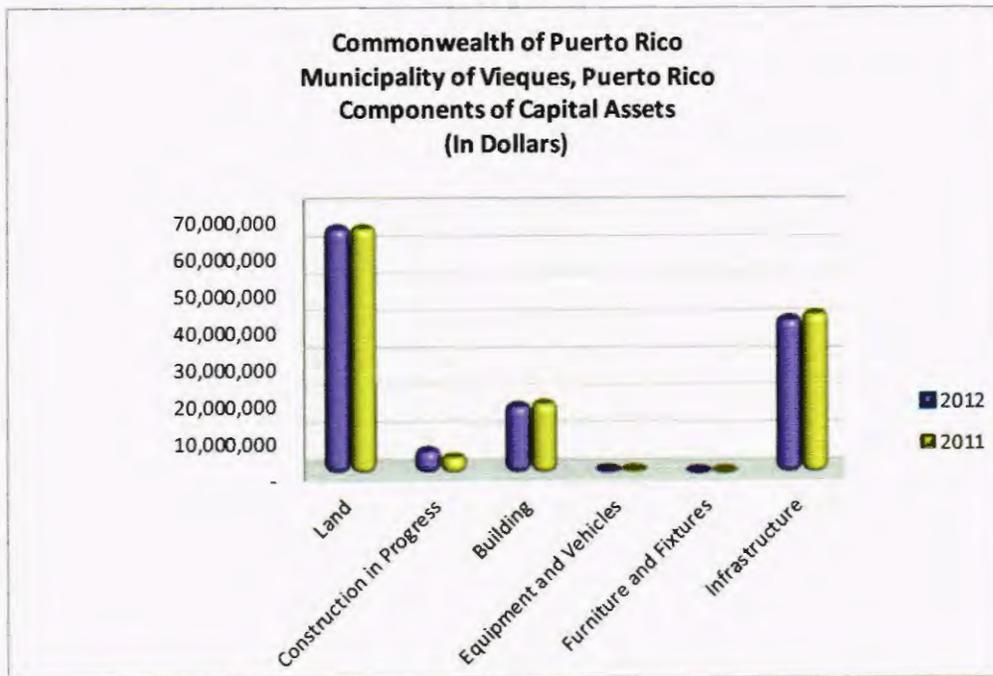
- Construction in Progress – \$1,789,789
- Acquisition of Furniture and Fixtures – \$105,280

Other projects related to repair and maintenance of roads (not capitalized) was developed during the year 2012.

Construction in progress was principally for improvement to the Market Place, Fine Art School and the "Malecon".

Figure 4 below presents the components of capital assets during the fiscal years 2012 and 2011:

FIGURE 4



### Long-Term Debt

At year-end, the Municipality had \$12,705,040 in general and special obligations, an increase of 10% with respect to prior year, due to new issuance of general and special obligation bonds of \$2,575,000 and \$291,000, respectively; and the repayment of principal of \$477,340. The following is a summary of the Municipality's outstanding debt as of June 30, 2012 and 2011:

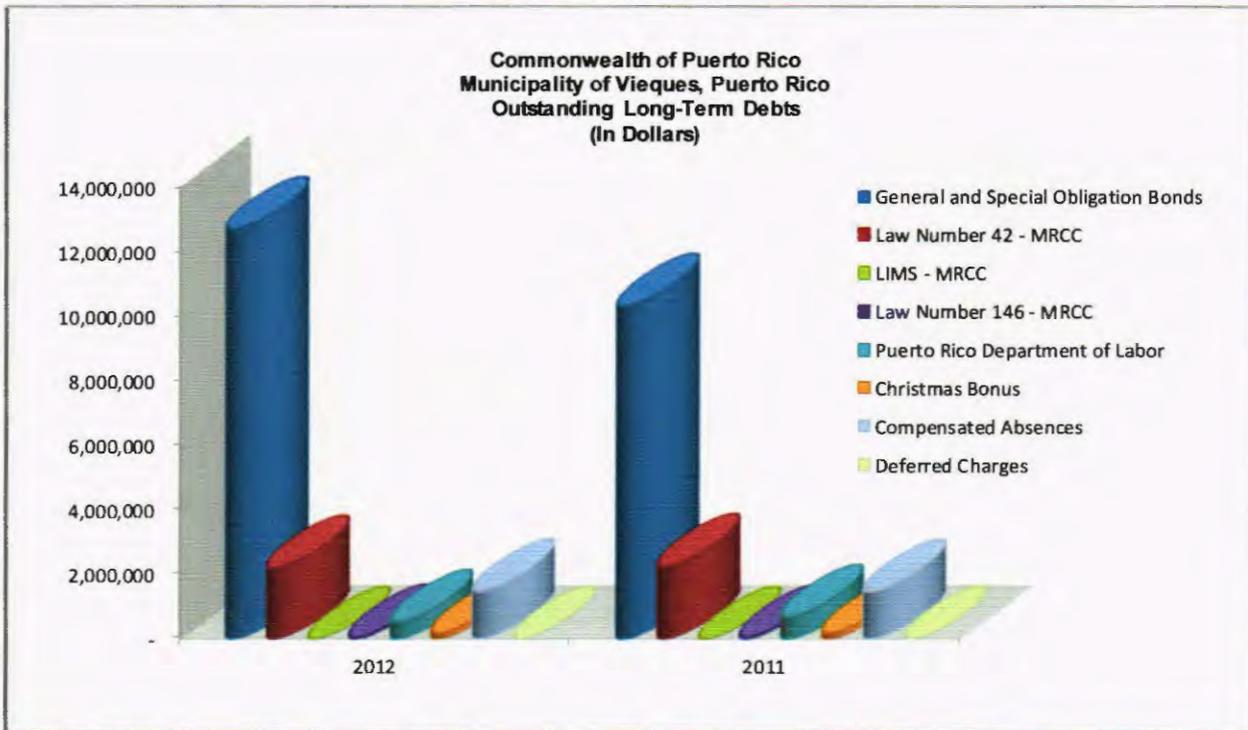
Table 7

**Commonwealth of Puerto Rico  
Municipality of Vieques, Puerto Rico  
Outstanding Long-term Debt  
As of June 30,**

	2012	2011
General and Special Obligation Bonds	\$ 12,705,040	\$ 10,316,380
Law Number 42 - MRCC	2,207,477	2,259,938
LIMS - MRCC	-	4,970
Law Number 146 - MRCC	71,808	75,398
Puerto Rico Department of Labor	522,939	687,563
Deferred Charges	15,464	13,433
Christmas Bonus	182,408	191,050
Compensated Absences	1,481,797	1,480,581
<b>Total</b>	<b>\$ 17,186,933</b>	<b>\$ 15,029,313</b>

Figure 5 presents the components of long-term debts during the fiscal year 2012 and 2011:

FIGURE 5



More detailed information about the Municipality's long-term liabilities is presented in Note 9 and 10 to the financial statements.

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGET**

The Municipality's selected and appointed officials considered many factors when setting the fiscal year 2011-2012 budget. One of these factors is the economy. Among economic areas considered are the population growth estimates, personal income, housing statistics and unemployment rates. The Municipality's unemployment rate now stands at 12.6%, which compares with the Commonwealth rate of 13.9%.

The Municipality applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2012-2013 are \$11.2 million, approximately \$500,000 more than the fiscal year 2011-2012. The Municipality expects an increase in revenues as per prior year. Budgeted expenditures are expected to stabilize accordingly to the projected revenues. Among planned projects, this budget may be adjusted in accordance with economic injection projected when the construction project promoted by the Municipality and others private projects were develop during the year.

**AMERICAN RECOVERY AND REINVESTMENT ACT**

The Municipality expended the following federal awards from the American Recovery and Reinvestment Act during fiscal year 2011-2012. These awards corresponded to fiscal year 2009-2010 that were carryforward during current year:

<b>Federal Program</b>	<b>CFDA Number</b>	<b>Total Award</b>	<b>Total Expended</b>
Homelessness Prevention and Rapid Re-Housing Program [Provide financial assistance (payment of delinquent utility and rental payments.)]	14.257	\$ 120,282	\$ 83,230
Energy Efficiency and Conservation Block Grant Program [To identify potential energy conservation opportunities and evaluate feasible savings on Governmental Buildings.]	81.128	<u>147,500</u>	<u>147,500</u>
<b>Total</b>		<b><u>\$ 267,782</u></b>	<b><u>\$ 230,730</u></b>

**CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT**

This report is designed to provide a general overview of the Municipality's finances and to demonstrate the accountability for the money it receives. If you have any questions about this report or need additional information, contact the Municipality's Finance Department at (787) 741-5000, or Carlos Lebrum Street #449, Vieques, PR 00765.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO**

**STATEMENT OF NET ASSETS**

**JUNE 30, 2012**

	<b>GOVERNMENTAL ACTIVITIES</b>
<b>ASSETS:</b>	
Cash	\$ 1,344,383
Cash with Fiscal Agent	5,352,659
Receivables (net):	
Property Taxes	-
Sales and Usage Taxes	34,663
Due from Governmental Units	285,697
Federal Grants	3,329,685
Others	385,000
<b>Total Currents Assets</b>	<u>10,732,087</u>
Deferred Charges	<u>62,493</u>
Capital Assets:	
Land, Improvement and Construction in Progress	71,487,980
Other Capital Assets [Net of Depreciation]	<u>59,492,519</u>
<b>Total Capital Assets</b>	<u>130,980,499</u>
<b>TOTAL ASSETS</b>	<u><b>141,775,079</b></u>
<b>LIABILITIES:</b>	
Accounts Payable and Accrued Expenses	1,451,616
Accrued Interest	142,573
Due to Governmental Units	154,163
Deferred Revenues	418,587
Long-Term Liabilities:	
Due Within One Year	1,996,427
Due in More than One Year	<u>15,190,506</u>
<b>TOTAL LIABILITIES</b>	<u><b>19,353,872</b></u>
<b>NET ASSETS:</b>	
Investment in Capital Assets, Net of Related Debt	125,365,893
Restricted for:	
Capital Projects	38,656
Debt Service	1,745,649
Community Development Projects	3,059,451
Unrestricted (Deficit)	<u>(7,788,442)</u>
<b>TOTAL NET ASSETS</b>	<u><b>\$ 122,421,207</b></u>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO

STATEMENT OF ACTIVITIES

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenues and Changes in Net Assets
		Charges For Services	Operating Grants and Contributions	Capital Grants and Contributions	
<b>Governmental Activities:</b>					
Mayor and Municipal Legislature	\$ 1,332,929	\$ -	\$ -	\$ -	\$ (1,332,929)
General Government	6,981,481	-	437,926	-	(6,543,555)
Public Safety	1,201,094	-	113,473	-	(1,087,621)
Public Works	1,803,589	-	930,884	-	(872,705)
Culture and Recreation	892,394	-	1,665	-	(890,729)
Health and Sanitation	602,383	-	-	-	(602,383)
Human Services and Welfare	1,911,213	-	712,841	-	(1,198,372)
Urban Development	1,535,447	-	591,868	371,273	(572,306)
Interest on Long-Term Debt	524,444	-	-	-	(524,444)
<b>Total Governmental Activities</b>	<b>\$ 16,784,974</b>	<b>\$ -</b>	<b>\$ 2,788,657</b>	<b>\$ 371,273</b>	<b>(13,625,044)</b>
<b>General Revenues:</b>					
Taxes:					
Property Taxes, levied for General Purposes					966,242
Property Taxes, levied for Debt Service					494,470
Volume of Business Taxes					532,182
Sales and Usage Taxes					923,418
Construction Excise Taxes					595,365
Intergovernmental					7,570,145
Rent					104,150
Miscellaneous					773,255
Special Item – Sale of Land					-
Total General Revenues					<u>11,959,227</u>
<b>CHANGES IN NET ASSETS</b>					<b>(1,665,817)</b>
Net Assets – Beginning of Year, As Restated					<u>124,087,024</u>
<b>NET ASSETS – ENDING OF YEAR</b>					<b>\$ <u>122,421,207</u></b>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO  
BALANCE SHEET – GOVERNMENTAL FUNDS  
JUNE 30, 2012

	GENERAL FUND	SBGP FUNDS	STATE ASSIGNMENT FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
<b>ASSETS:</b>						
Cash	\$ 88,030	\$ 35,714	\$ 50,541	\$ -	\$ 1,170,098	\$ 1,344,383
Cash with Fiscal Agent	173	-	-	1,888,222	3,464,264	5,352,659
Receivables:						
Property Taxes	-	-	-	-	-	-
Sales and Usage Taxes	34,663	-	-	-	-	34,663
Federal Grants	-	3,329,685	-	-	-	3,329,685
Due from Other Funds	366,087	-	5,980,368	-	903	6,347,358
Due from Governmental Units	285,697	-	-	-	-	285,697
Other Receivables	385,000	-	-	-	-	385,000
<b>Total Assets</b>	<b>\$ 1,159,650</b>	<b>\$ 3,365,399</b>	<b>\$ 6,030,909</b>	<b>\$ 1,888,222</b>	<b>\$ 4,635,265</b>	<b>\$ 17,079,445</b>
<b>LIABILITIES AND FUND BALANCES:</b>						
<b>Liabilities:</b>						
Account Payable	\$ 993,609	\$ -	\$ -	\$ -	\$ 458,007	\$ 1,451,616
Bonds Payable	-	-	-	363,500	-	363,500
Account Interest	-	-	-	142,573	-	142,573
Due to Governmental Units	154,163	-	-	-	-	154,163
Due to Other Funds	5,980,368	312,948	903	-	53,139	6,347,358
Deferred Revenues:						
Volume of Business Taxes	418,587	-	-	-	-	418,587
Commonwealth of Puerto Rico	285,697	-	-	-	-	285,697
Federal Grants	-	3,020,814	-	-	-	3,020,814
<b>Total Liabilities</b>	<b>7,832,424</b>	<b>3,333,762</b>	<b>903</b>	<b>506,073</b>	<b>511,146</b>	<b>12,184,308</b>
<b>Fund Balances:</b>						
Restricted	-	31,637	6,030,006	1,382,149	4,530,658	11,974,450
Committed	-	-	-	-	30,516	30,516
Assigned	-	-	-	-	-	-
Unassigned (Deficit)	(6,672,774)	-	-	-	(437,055)	(7,109,829)
<b>Total Fund Balances</b>	<b>(6,672,774)</b>	<b>31,637</b>	<b>6,030,006</b>	<b>1,382,149</b>	<b>4,124,119</b>	<b>4,895,137</b>
<b>Total Liabilities and Fund Balances</b>	<b>\$ 1,159,650</b>	<b>\$ 3,365,399</b>	<b>\$ 6,030,909</b>	<b>\$ 1,888,222</b>	<b>\$ 4,635,265</b>	<b>\$ 17,079,445</b>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE – GOVERNMENTAL FUNDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	GENERAL FUND	SBGP FUNDS	STATE ASSIGNMENT FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
<b>REVENUES:</b>						
Property Taxes	\$ 966,242	\$ -	\$ -	\$ 494,470	\$ -	\$ 1,460,712
Volume of Business Taxes	532,182	-	-	-	-	532,182
Sales and Usage Taxes	423,668	-	-	499,750	-	923,418
Federal Grants	-	1,144,357	-	-	1,695,327	2,839,684
Intergovernmental	6,769,544	-	610,429	-	827,063	8,207,036
Construction Excise Taxes	595,365	-	-	-	-	595,365
Rent	104,150	-	-	-	-	104,150
Miscellaneous	724,655	-	-	-	94,272	818,927
<b>Total Revenues</b>	<b>10,115,806</b>	<b>1,144,357</b>	<b>610,429</b>	<b>994,220</b>	<b>2,616,662</b>	<b>15,481,474</b>
<b>EXPENDITURES:</b>						
Current:						
Mayor and Municipal Legislature	704,401	-	-	-	-	704,401
General Government	6,491,221	-	30,530	-	494,054	7,015,805
Public Safety	836,211	-	-	-	113,472	949,683
Public Works	728,504	-	-	-	551,312	1,279,816
Culture and Recreation	671,890	-	-	-	52,897	724,787
Health and Sanitation	602,383	-	-	-	-	602,383
Human Services and Welfare	595,814	-	-	-	1,043,037	1,638,851
Urban Development	171,631	1,191,285	-	-	53,110	1,416,026
Capital Outlay	8,159	-	581,084	-	1,305,826	1,895,069
Debt Service:						
Bond Issue Cost	-	-	-	11,719	-	11,719
Principal	-	-	-	531,861	-	531,861
Interest and Other Charges	-	-	-	524,444	-	524,444
<b>Total Expenditures</b>	<b>10,810,214</b>	<b>1,191,285</b>	<b>611,614</b>	<b>1,068,024</b>	<b>3,613,708</b>	<b>17,294,845</b>
Excess of Revenues Over (Under) Expenditures	(694,408)	(46,928)	(1,185)	(73,804)	(997,046)	(1,813,371)
<b>OTHER FINANCING SOURCES (USES):</b>						
Proceed of Bonds	676,000	-	-	-	2,190,000	2,866,000
Transfer – In	575,000	-	-	458,395	-	1,033,395
Transfer – Out	(448,480)	-	-	(505,000)	(79,915)	(1,033,395)
<b>Total Other Financing Sources and Uses</b>	<b>802,520</b>	<b>-</b>	<b>-</b>	<b>(46,605)</b>	<b>2,110,085</b>	<b>2,866,000</b>
Special Item – Sale of Land						
Net Change in Fund Balance	108,112	(46,928)	(1,185)	(120,409)	1,113,039	1,052,629
Fund Balance – Beginning, As Restated	(6,780,886)	78,565	6,031,191	1,502,558	3,011,080	3,842,508
<b>FUND BALANCE – ENDING</b>	<b>\$ (6,672,774)</b>	<b>\$ 31,637</b>	<b>\$ 6,030,006</b>	<b>\$ 1,382,149</b>	<b>\$ 4,124,119</b>	<b>\$ 4,895,137</b>

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06/05/2013*

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

JUNE 30, 2012

**Total Fund Balances – Government Funds (Page 17)** **\$ 4,895,137**

Amount reported for Governmental Activities in the Statement of Net Assets (Page 15)  
are different because:

Capital Assets used in governmental activities are not financial resources and therefore  
are not reported in the funds. In the current period, these amounts are:

Non Depreciable Capital Assets	\$ 71,487,980	
Depreciable Capital Assets	35,023,473	
Infrastructure Assets	66,691,389	
Accumulated Depreciation	<u>(42,222,343)</u>	
<b>Total Capital Assets</b>		<b>130,980,499</b>

Other Assets used in governmental activities are not financial resources and therefore  
are not reported in the funds:

Deferred Charges		62,493
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Some of the **Municipality's** revenues will be collected after year-end but are not available  
soon enough to pay for the current period's expenditures and therefore are deferred in the funds:

CDBG	3,020,814	
Intergovernmental	194,493	
Christmas Bonus	<u>91,204</u>	3,306,511

Some liabilities are not due and payable in the current period and therefore are not reported  
in the funds. Those liabilities consist of:

General Special Obligation Bonds	(12,341,540)	
PR Department of Labor	(522,939)	
Christmas Bonus	(182,408)	
Compensated Absences	(1,481,797)	
Law Number 146 – MRCC	(71,808)	
Law Number 42 – MRCC	(2,207,477)	
Deferred Charges	<u>(15,464)</u>	
<b>Total Long-Term Liabilities</b>		<b><u>(16,823,433)</u></b>

**Total Net Assets of Governmental Activities (Page 15)** **\$ 122,421,207**

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES  
IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<b>Net Change in Fund Balances – Government Funds (Page 19)</b>	<b>\$ 1,052,629</b>
Amount reported for Governmental Activities in the Statement of Activities (Page 16) 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. In the current period, these amounts are:	
Capital Assets	\$ 1,895,069
Depreciation Expense	<u>(2,095,093)</u>
Excess of Capital Assets over Depreciation Expense	(200,024)
Governmental Fund Report the effect of Bond Issuance Costs as Expenditure when Debt is first issued, and amortized in the Statement of Activities. This amounts is the effect of these differences:	
Bond Issuance Costs	11,719
Amortization of Deferred Charges	<u>(3,704)</u>
	8,015
Revenues in the Statement of Activities that do not provide current financial resources are reported as revenues in the funds:	
Christmas Bonus	(4,321)
Intergovernmental	194,493
Community Development Block Grant	<u>(552,489)</u>
Total of Revenues	(362,317)
Bonds proceeds provide current financial resources to governmental funds, but issuing debt increase Long-Term Liabilities in the Statement of Net Assets. In the current period, proceeds received was	
	(2,866,000)
Repayment of long-term principal is expenditure in the governmental funds, but issuing debt reduced Long-Term Liabilities in the Statement of Net Assets. In the current period repayments were	
	531,861
Some expenses reported in the Statement of Activities do not require the use of current financial resouces and therefore are not reported as expenditures in governmental funds. These activities consist of:	
Decrease in Christmas Bonus	8,642
Increase in Deferred Charges	(2,031)
Decrease in Debt to PR Department of Labor	164,624
Increase in Compensated Absences	<u>(1,216)</u>
Total Additional Expenses	<u>170,019</u>
<b>Change in Net Assets of Governmental Activities (Page 16)</b>	<b>\$ <u>(1,665,817)</u></b>

## 1. FINANCIAL REPORTING ENTITY

The accompanying financial statements present information on the financial activities of the Municipality of Vieques, Puerto Rico (Municipality) over which the Mayor and the Municipal Legislature, have direct or indirect governing and fiscal control. These financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP).

### A. Organization

The Municipality was founded in the year 1844, and operates as a governmental unit of the Commonwealth of Puerto Rico, under Law Number 81 of August 30, 1991, known as "Autonomous Municipalities Law of the Commonwealth of Puerto Rico". The governmental system of the Municipality is composed of the executive and legislative bodies. The Mayor is the Chief Executive Officer and is elected every four years in the general elections of the Commonwealth of Puerto Rico. The legislative body consists of 12 Legislators also elected in the general elections of Puerto Rico for a four-year period.

The Municipality provides services such as: health, public works, sanitation, aids and services to low-income and elderly citizens, public safety, housing and urban development, culture and recreation, planning, zoning and other general and administrative services. As a government entity, the Municipality is exempt from both federal and state taxes.

### B. Reporting Entity

A reporting entity is comprised of (1) the primary government, (2) component unit organizations for which the primary government is financial accountable (blended component units), and (3) other organizations for which the nature and significance of their relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete, and they are financially accountable to the primary government (discrete component units). The primary government consists of all funds, departments, boards and agencies that are not legally separate from the Municipality and for which the Municipality is financial accountable.

The accompanying basic financial statements include all departments and organizations units whose funds are under the custody and control of the Municipality. In evaluating the Municipality as a reporting entity, management has addressed all the potential component units. GASB Accounting Standards Codification Section 2600, *Reporting Entity and Component Unit Presentation and Disclosure*, requires the inclusion of organizations that raise and hold funds for the direct benefit of the primary government.

GASB Accounting Standards Codification Section 2100, *Defining the Financial Reporting Entity*, describes the criteria for determining which organizations, functions, and activities should be considered part of the Municipality for financial reporting purposes. The primary criteria include appointing a voting majority of an organization's governing body, and the Municipality's ability to impose its will on that organization or the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Municipality.

There are two methods of presentation of the component unit in the financial statements: blending – the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balance; and discrete – presentation of the component unit's financial data in column separate from the Municipality's balances and transactions.

The relative importance of each criterion must be evaluated in light of specific circumstances in order to determine which components units are to be included as part of the reporting entity. Our specific evaluations of the criteria applicable to the Municipality indicate no organizations meet the criteria to be included as component units. Accordingly, these basic financial statements present only the Municipality as the reporting entity.

These financial statements present the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2012, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### A. Financial Statement Presentation

The basic financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America as applicable to local governmental units (GAAP). The basic financial statements include both government-wide (based on the Municipality as a whole) and fund financial statements, which provide a more detailed level of financial information. Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as governmental type.

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

#### ***Management's Discussion and Analysis***

Management's discussion and analysis is required supplementary information that introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.

#### ***Government-wide Financial Statements (GWFS)***

The GWFS (the *Statement of Net Assets* and the *Statement of Activities*) report information of all the activities of the Municipality. For the most part, the effect of interfund activity has been removed from these financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely, to a significant extent, on fees and charges for support.

The focus of the *Statement of Net Assets* is designed to be similar to bottom line results for the Municipality's governmental activities and business type activities. This statement combines and consolidates governmental fund's current financial resources (short-term spendable resources) with capital assets and long-term obligations. The *Statement of Net Assets* presents the reporting entities' assets and liabilities, with the difference reported as net assets. Net assets are restricted when constraints are placed on them that are imposed by external parties or by laws or regulations. Designations solely imposed by the Municipality's management are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, the Municipality's policy is to use the restricted resources first.

The *Statement of Activities* demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. In addition, to the extent that indirect costs are allocated to the various functions, the program expenses will include both direct and indirect costs. *Program Revenues* include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment, and grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items properly excluded from program revenues are reported instead as *general revenues*.

#### ***Governmental Funds Financial Statements (GFFS)***

The GFFS [the *Balance Sheet*, and the *Statement of Revenues, Expenditures and Changes in Fund Balance*] provide information about the Municipality's funds. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. Non-major funds are summarized into a single column.

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is on major funds, rather than the previous financial model's fund types. This is the manner in which these funds are normally budgeted. This presentation deemed most appropriate to (1) demonstrate legal and covenant compliance, (2) demonstrate the source and use of liquid resources, and (3) demonstrate how the Municipality's actual experience conforms to the budgeted fiscal plan.

The Municipality reports the following major governmental funds:

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

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

SBGP Fund – This is the fund used to account for all the transactions of the State Block Grant Program. The primary objectives of this program is the development of viable communities by providing decent housing, a suitable living environment and expanded economic opportunities, principally for persons of low and moderate income.

State Assignments Fund – This is the fund used to account for all the transactions of the State Assignments by Legislature Resolutions. The primary objectives of these assignments is the development of projects on communities, not-for-profit organizations, purchase of equipment and indirect assignment to persons of low and moderate income.

Debt Service Fund – This is used to account for the accumulation of resources for, and the payment of, long-term debt principal and interests.

The non-major funds are combined in a single column in the GGFS. As a general rule the effect of interfund activity has been eliminated from the GWFS.

The Municipality reports its financial position (Balance Sheet) and results of operations (Statement of Revenues, Expenditures and Changes in Fund Balance) in funds, which are considered separate accounting entities. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions.

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

The notes to the financial statements provide information that is essential to a user's full understanding of the data provided in the basis financial statements

### ***Required Supplementary Information***

The basic financial statements are followed by a section of required supplementary information. This section includes a *Budgetary Comparison Schedule – General Fund*, which includes reconciliation between the statutory fund balance for budgetary purposes and the fund balance for the General Fund as presented in the GFFS.

## **B. Measurement Focus and Basis of Accounting**

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

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as current financial resources or economic resources. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

The government-wide and proprietary financial statements are reported using the *economic resources measurement focus* and the *full accrual basis of accounting*. Revenue (including interest on deposits and investments) is generally recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Nonexchange transactions, in which the Municipality gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Receipts on any type of revenue sources collected in advance for use in the following fiscal year are recorded as deferred revenues.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

### ***Governmental Funds Financial Statements***

The GFFS are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Under this method, 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 these purposes, the Municipality considers revenues to be available if they are collected within sixty (60) days after the end of the current fiscal period. Revenues that the Municipality earns by incurring obligations are recognized in the same period as when the obligations are recognized. At June 30, 2012, all revenues sources met this availability criterion.

Expenditures are recorded when the related fund 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. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases, if any, are reported as other financing sources.

Property taxes, volume of business taxes, sales and usage taxes, construction excise taxes, 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. Entitlements are recorded as revenues when all eligibility requirements are met, including any time requirements and the amount is received during the period or within the availability requirements have been met, and the amount is received during the period or within the availability period for this revenue source (60 days of year-end). Expenditures-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). All other revenue items are considered to be measurable and available only when cash is received by the Municipality.

The accompanying balance sheet – governmental funds generally reflects only assets that will not be converted into cash to satisfy current liabilities. Long-term assets and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying balance sheet – governmental funds.

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

### **C. Stewardship, Compliance, and Accountability**

#### ***Budgetary Information***

The Municipality's annually adopts the Budget Resolution for all operating funds of the Municipality except for certain restricted accounts Special Revenue Funds. Budgetary control is legally maintained at the fund level. The budget is prepared using the modified accrual basis of accounting with encumbrance included as budgetary basis expenditures. The Municipality's Budget Resolution provides transfer authority (1) to the Mayor and the Management and Budget Director, within and between departments and funds, as long as the total budget of the Municipality (net of interfund transfers) is not increased; (2) to the Management and Budget Director to implement grant budgets as the grant applications are accepted by the Municipality; and (3) to the Management and Budget Director to amend (re-appropriate) each new year's budget, to the extent of outstanding encumbrances, and/or unexpended project/grant appropriations at year end. Municipality's Legislature action is required for (1) use of the budgeted Legislature contingency, and (2) the approval of a supplemental appropriation(s). During the year, several supplemental appropriations were necessary.

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

The unencumbered balance of any appropriation at the end of the 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.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

The Municipality follows these procedures, in accordance with law, in order to establish the budgetary data reflected in the Budgetary Comparison Schedule – General Fund:

### *Original Budget*

1. Prior of May 15 of each fiscal year, the Mayor submits to the Municipal Legislature a proposed budget for the fiscal year commencing the following July 1 in addition of a budget message.
2. The budget document is available for public inspection prior to its approval by the Municipal Legislature.
3. The Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law.
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance to be effective on July 1.

Since the budgetary basis differs from accounting principles generally accepted in the United States of America (GAAP), actual amounts for the General Fund in the accompanying Budgetary Comparison Schedule, is presented on the budgetary basis to enhance comparability.

### *Final Budget*

The final budgetary data presented in the Budgetary Comparison Schedule – General Fund reflects the following changes to the original budget:

1. Certain annual appropriations are budgeted on a project basis. If such projects are not completed at the end of the fiscal year, unexpended appropriations, including encumbered funds, and unexpended grant appropriations, are carried forward to the following year. In certain circumstances, other regular annual appropriations may be carried forward after appropriate approval. Annually appropriated funds, not authorized to be carried forward, lapse at the end of the fiscal year. Appropriations carried forward from the prior year are included in the final budgetary data.
2. Appropriations may be adjusted during the year with the approval of the Mayor and the Municipal Legislature, e.g. supplemental appropriations. Additionally, the Mayor is authorized to make certain transfer of surplus within the departments. Such adjustments are reflected in the final budgetary data.

The Annual Appropriation Ordinance adopts the budget at the character level of expenditure within departments. As described above, the Mayor is authorized to make certain transfers of appropriations within departments. Accordingly, the legal level of budgetary control by the Municipal Legislature is the department Level.

The principal differences between the budgetary and GAAP bases are the following:

1. Encumbrances are recorded as expenditures under the budgetary basis and as a reserve of fund balances under GAAP.
2. Interfund transactions of the General Fund are not included in the budgetary basis.
3. Certain accrued liabilities and other debts are not included in the budgetary basis.
4. Certain revenues susceptible to accrual, i.e., both measurable and available, are not included in the budgetary data.

The Special Revenue Fund has not been included in the budgetary comparison because balances are not budgeted. Also the budget prepared for the Federal Financial Awards Programs included in the Capital Projects and Special Revenue Funds is based on a program period which is not necessarily the same fiscal year. Accordingly, it's not practical to present an annual comparison of budget for such programs.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

D. Assets, Liabilities, and Net Assets

1) *Cash and Investment, and Cash with Fiscal Agent*

The Municipality's cash and investment are composed of demand deposits in commercial banks, demand deposits in the Governmental Development Bank of Puerto Rico (GDB), and cash equivalents in commercial banks. The Municipality has adopted the *Statement of Uniform Investment Guidelines for the Municipalities of the Government of Puerto Rico*, issued by the GDB as promulgated by Law No. 113 of August 3, 1995. The Finance Director of the Municipality, follow the guidelines, is responsible for investing the available resources in certificates of deposit and other short-term investments. Investments are made from the available combined funds of the Municipality and, accordingly, it is not practical to disclose certificates of deposit and other short-term investments individually by fund in the combined financial statements. Interest earned on certificates of deposit and interest bearing commercial bank accounts are recognized as revenue in the General Fund, Art Center Fund and in Multiuses Coliseum Fund in accordance with amount invested. Cash in the Special Revenue and Capital Project Funds are restricted; accordingly, resources available were not used for pool investments.

Cash with fiscal agent in the Debt Service Fund represents special additional property tax collections retained by the Government, deposit in the GDB and restricted for the payment of the Municipality's debt service, as established by law. Cash with fiscal agent in other governmental funds consists of undisbursed proceeds of certain bonds and notes issued for the acquisition and construction of major capital improvements, or grants which are maintained in a cash custodian account by the GDB. This sinking fund is maintained by the GDB, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

2) *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." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statement as "interfund balances".

Advance between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Receivables consist of all revenues earned but not collected at June 30, 2012. These account receivables are shown net of estimated allowances for uncollectible accounts, which are determined upon past collection experience, historical trends, and current economic conditions. Intergovernmental receivables in the general fund represent mostly sales and usage taxes, federal grant and contributions, property tax accounts that are levied by Municipal Revenue Collection Center (MRCC), a governmental entity created by the Government. Intergovernmental receivables in the other governmental funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded grant and contributions and state appropriations, and the amount in the debt service fund represents the distribution of property tax collected which is restricted for the debt service.

3) *Inventories*

The Municipality used the purchase method to account for the purchases office and printing supplies, gasoline, oil and other expendable supplies held for consumption. This method records items as expenditures, in the appropriate fund, when they are acquired and, accordingly, the inventory is not recorded in the basic financial statements.

4) *Deferred Charges*

Deferred charges in the accompanying *Statement of Net Assets* consist of bond issuance costs, net of accumulated amortization. Deferred charges are amortized over the term of the related debt using the straight-line method. In the GFFS, bond issuance costs are recorded in the current period as expenditures, whether or not withheld from the actual debt proceeds received.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

5) *Capital Assets*

Capital assets, which include land, buildings and improvement, machinery and equipment, motor vehicles, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the GWFS. Capital assets, other than infrastructure assets, are defined by the government as assets with an initial, individual cost of more than \$500 (amount not rounded) and an estimated useful life in excess of two years. For improvements other than buildings, the capital outlay must be greater than \$10,000, extend the estimated useful life for ten years, and be greater than 10% of the original cost of the asset. The Municipality reports infrastructure assets on a network and subsystem basis. Accordingly, the amounts spent for the construction or acquisition of infrastructure assets are capitalized and reported in the government-wide financial statements regardless of their amount.

In the case of the initial capitalization of general infrastructure assets (i.e., those reported by governmental activities) the government chose to include all such items regardless of their acquisition date or amount.

The Municipality was able to estimate the historical cost for the initial reporting of these assets through back trending (i.e., estimating the current replacement cost of the infrastructure to be capitalized and using an appropriate price-level index to deflate the cost to the acquisition year or estimated acquisition year). As the government constructs or acquires additional capital assets each period, including infrastructure assets, they are capitalized and reported at historical cost. The reported value excludes normal maintenance and repairs which are essentially amounts spent in relation to capital assets that do not increase the capacity or efficiency of the item or extend its useful life beyond the original estimate. In the case of donations the government values these capital assets at the estimated fair value of the item at the date of its donation.

Capital outlay is recorded as expenditures of the General Fund and other governmental funds and as assets in the GFFS to the extent the Municipality capitalization threshold is met. Depreciation and amortization expense is recorded only in the GWFS. Depreciable capital assets are generally depreciated or amortized over their estimated useful lives under the straight-line method, except for equipment held under capital leases which is depreciated over the shorter of its estimated useful life or the lease term. No depreciation is recorded for land and construction in progress. The estimated useful lives of major capital asset categories are:

CAPITAL ASSETS	YEARS
Infrastructure	25-50
Building and Building Improvements	20-50
Furniture and Fixtures	5-10
Vehicles and Equipment	5-20

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

Impaired capital assets that will no longer be used by the Municipality, if any, are reported at the lower of carrying value or fair value. Impairment losses on capital assets with physical damages that will continue to be used by the Municipality are measured using the restoration cost approach. Impairments of capital assets that are subject to a change in the manner or duration of use, or assets affected by enactment or approval of laws or regulations or other changes in environmental factors or assets that are subject to technological changes or obsolescence, if any, are measured using the service units approach.

The Municipality is prevented legally from entering into obligations extending beyond one fiscal year, and most lease agreements entered by the Municipality contain fiscal funding clauses or cancellation clauses that make the continuation of the agreements subject to future appropriations. The Municipality's lease agreements do not include contingent rental payments no escalation clauses. Accordingly, lease payments are recorded in the GWFS as expense when incurred.

In the accompanying GFFS, the lease payments are recorded as expenditures in the governmental fund.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

6) *Deferred and Unearned Revenues*

In the GWFS, deferred revenues arise only when the Municipality receives resources before it has a legal claim to them. In the GFFS, arises when one of the following situations occur: (1) potential revenue does not meet both the measurable and available criteria for revenue recognition in the current period (unavailable revenue), and (2) the Municipality receives resources before it has a legal claim to them (unearned revenue).

7) *Long-Term Obligations, Bonds Issuance Costs, and Premium or Discount*

The liabilities reported in the GWFS include the general and special obligation bonds, long-term notes, other long-term liabilities (e.g., vacation, sick leave, claims and judgments, long-term liabilities to other governmental entities and third parties, and landfill post closure care costs). Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount.

In the GFFS, governmental fund types recognize bond premiums and discounts as other financing sources and uses, respectively, and bond issuance costs as debt service expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

8) *Compensated Absences*

The Municipality accrues accumulated unpaid vacation and sick leave and associated employee-related costs when earned (or estimated to be earned) by the employee. The Municipality's employees are granted 30 days of vacations and 18 days of sick leave annually. Vacations may be accumulated up to a maximum of sixty (60) days and sick leave up to a maximum of ninety (90) days. In the event of employee resignation, the employee is paid for accumulated vacation days up to the maximum allowed at the current rate. Separation from employment prior to use of all or part of the sick leave terminates all rights for compensation, except for employees with ten years of service who are entitled to sick leave pay up to the maximum allowed. The Municipality accrued a liability for compensated absences, which meet the following criteria: (1) the Municipality's obligation relating to employee's rights to receive compensation for future absences is attributable to employee's services already rendered; (2) the obligation relates to rights that vest or accumulate; (3) payment of the compensation is probable; and (4) the amount can be reasonably estimated.

In accordance with the above criteria and requirements in conformance with GASB Accounting Standards Codification Section C60, *Compensated Absences*, the Municipality has accrued a liability for compensated absences, which has been earned but not taken by Municipality's employees, including its share of social security and Medicare payments made on behalf of the employees in the accrual for vacation and sick leave pay using salary rates effective at June 30, 2012. All vacation pay is accrued when incurred in the GWFS and PFFS. For the GWFS, the current portion is the amount estimated to be used in the following year. For the GFFS, all of the compensated absences are considered long-term and therefore, are not a fund liability and represents a reconciling item between the fund level and government-wide presentations.

9) *Claims and Judgments*

The estimated amount of the liability for claims and judgments, if any, which is due on demand, such as from adjudicated or settled claims, is recorded in the General Fund when the liability is incurred. The Long-Term Liabilities includes, when appropriate, an amount estimated as a contingent liability or liabilities with a fixed or expected due date, which will require future available financial resources for its payment.

10) *Accounting for Pension Costs*

The Municipality adopted the provisions of GASBS No. 50, *Pension Disclosure*, which amended Section Pe5 of the GASB Codification *Pension Plans – Defined Benefit*, by requiring disclosure of how the contractually required contribution rate is determined by governments participating in multi-employer cost-sharing pension plans.

The Municipality accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

For the purpose of applying the requirements of GASB Accounting Standards Codification Section Pe5, *Pension Plans – Defined Benefit*, the State Government is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multiemployer cost-sharing defined benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate. The Municipality is considered a participant, and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Government and the basic financial statements of such retirement systems are part of the financial reporting entity of the Government.

11) *Landfill*

State and Federal laws and regulations require that the Municipality place a final cover on its landfill when closed and perform certain maintenance and monitoring functions at the landfill site for the next thirty years. In addition to operating expenses related to current activities of the landfill, an expense provision and related liability should be recognized based on the future closure and postclosure care costs that will be incurred near or after the date the landfill no longer accepts waste. The recognition of these landfill closure and postclosure care costs is based on the amount of the landfill used during the year. The Municipality hasn't performed a study of the activities that need to be implemented at the Municipality's landfill to comply with applicable laws and regulations. Accordingly, any provision for liabilities related to closure and post-closure care costs are included in the accompanying GWFS, *Statement of Net Assets*, under the provisions of Section L10 of the GASB Codification *Landfill Closure and Post-Closure Care Costs*.

12) *Net Assets/Fund Balance*

A) *Net Assets*

The GWFS and Proprietary Funds Financial Statements utilize a net assets presentation, which are categorized as follow:

- *Invested in Capital Assets, Net of Related Debt* – These consists of capital assets, net of accumulated depreciation and amortization, reduced by the outstanding balances of bonds payable, notes payable and other debts that are attributed to the acquisition, construction or improvements of those assets. For the purposes of determining the outstanding debt attributed to capital assets, the total long-term debt related to the acquisition, construction or improvements of capital assets has been reduced by any related unspent debt proceeds and any related unamortized debt issuance costs. In addition, the outstanding debt attributed to capital assets does not include accrued interest payable, non-capital accrued liabilities, inter-fund loans and other financial assets. Net assets invested in capital assets, net of related debt is comprised of the following:

	<u>Governmental Activities</u>
Capital Assets, Net of Accumulated Depreciation .....	\$130,980,499
Outstanding Balance on Related Debt .....	(8,955,580)
Unspent Capital Debt Proceeds .....	<u>3,340,974</u>
Total Invested in Capital Assets, Net of Related Debt.....	<u>\$125,365,893</u>

- *Restricted Net Assets* – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- *Unrestricted Net Assets* – These consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

**B) Fund Balance**

The Municipality implemented GASB Statement 54, *Fund Balance Reporting and Governmental Fund Type Definitions* effective with the June 30, 2011 financial statements. Fund balances for the governmental funds are reported in classifications that comprise a hierarchy based on the extent to which the government honors constraints on the specific purposes for which amounts in those funds can be spent.

The nonspendable classification contains amounts not in spendable form or legally or contractually required to be maintained intact. Restricted amounts contain restraints on their use externally imposed by creditors, grantors, contributors, or laws or regulation of other governments; or imposed by law through constitutional provisions or enabling legislation. Committed amounts can only be used for specific purposes imposed by formal action of the government's highest level of decision-making authority. The highest level of decision-making authority is the Municipal Legislature and it takes a resolution to establish a fund balance commitment. Amounts intended to be used for specific purposes are assigned. Assignments should not cause deficits in the Unassigned Fund Balance. Unassigned Fund Balance is the residual classification for the General Fund.

**Comprehensive Fund Balance Policy**

The Municipality believes that sound financial management principles require that sufficient funds be retained by the Municipality to provide a stable financial base at all times. To retain this stable financial base, the Municipality needs to maintain a General Fund balance sufficient to fund all cash flows of the Municipality, to provide financial reserves for unanticipated expenditures and/or revenue shortfalls of an emergency nature, to provide funds for the disparity in timing between property tax collection and other principal revenues, and expenditures, and to secure and maintain investment grade bond ratings. The purpose of this policy is to specify the size and composition of the Municipality's financial reserves and to identify certain requirements for replenishing any fund balance reserves utilized.

In February 2009, the Governmental Accounting Standards Board (GASB) issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB 54). This new standard has substantially altered the categories and terminology used to describe the fund balance in governmental funds. The purpose of GASB 54 is to provide clarity to understand the extent of restrictions on the use of balances of the funds presented in the financial statements. One objective of this standard was to improve, including the understandability, the usefulness of fund balance information by providing clear fund balance classifications. GASB 54 abandons the reserved, unreserved, and designated classifications of fund balance and replaced them with five classifications: nonspendable, restricted, committed, assigned, and unassigned. The requirements of this statement are effective for the Municipality's financial statements for the fiscal year ending June 30, 2011.

GASB 54 requires local governments to focus on the constraints imposed upon resources when reporting fund balance in governmental funds. The fund balance classifications indicate the level of constraints placed upon how resources can be spent and identify the sources of those constraints. The following five classifications serve to inform readers of the financial statements of the extent to which the Municipality is bound to honor constraints on the specific purposes for which resources in a fund can be spent.

- *Nonspendable Fund Balance* – Fund balance reported as “nonspendable” represents fund balance that is (a) not in a spendable form such as prepaid items or (b) legally or contractually required to be maintained intact such as an endowment.
- *Restricted Fund Balance* – Fund balance reported as “restricted” consists of amounts that can be spent only on the specific purposes stipulated by law or by the external providers of those resources.
- *Committed Fund Balance* – Fund balance reported as “committed” are self-imposed limitations set in place prior to the end of the fiscal period. These amounts can be used only for the specific purposes determined by a formal action of the Municipal Legislature, which is the highest level of decision-making authority, and that require the same level of formal action to remove the constraint.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

- *Assigned Fund Balance* – Fund balance reported as “assigned” consists of amounts that are subject to a purpose constraint that represents an intended use established by the Municipal Legislature or by their designated body or official. The purpose of the assignment must be narrower than the purpose of the General Fund. Formal action is *not* necessary to impose, remove, or modify a constraint in Assigned Fund Balance. Additionally, this category is used to reflect the appropriation of a portion of existing fund balance to eliminate a projected deficit in the subsequent year’s budget.
- *Unassigned Fund Balance* – Fund balance reported as “unassigned” represents the residual classification of fund balance and includes all spendable amounts not contained within the other classifications.

### ***Policy on Committing Funds***

In accordance with GASB 54, it is the policy of the Municipality that fund balance amounts will be reported as “Committed Fund Balance” only after formal action and approval by Municipal Legislature. The Municipal Legislature has the authority to separate funds for specific purposes. Any separate fund as Committed Fund Balance requires the adoption of a resolution by a simple majority of votes. The adoption of the resolution should be carried out before June 30 of the fiscal year to implement. If the actual amount of the commitment is not available through June 30, the resolution should establish the process or formula required to calculate the exact amount as soon as information is available in the following fiscal year.

For example, the Municipal Legislature may approve a motion prior to year end to report within the year-end financial statements, if available, up to a specified dollar amount as Committed Fund Balance for capital projects. The exact dollar amount to be reported as Committed Fund Balance for capital projects may not be known at the time of approval due to the annual financial audit not yet being completed. This amount can be determined at a later date when known and appropriately reported within the year-end financial statements due to the Municipal Legislature approving this action before year-end.

It is the policy of the Municipality that the Municipal Legislature may commit fund balance for any reason that is consistent with the definition of Committed Fund Balance contained within GASB 54. Examples of reasons to commit fund balance would be to display intentions to use portions of fund balance for future capital projects, stabilization funds, or to earmark special General Fund revenue streams unspent at year-end that are intended to be used for specific purposes.

After approval by the Municipal Legislature, the amount reported as Committed Fund Balance cannot be reversed without utilizing the same process required to commit the funds. Therefore, in accordance with GASB 54, it is the policy of the Municipality that funds can only be removed from the Committed Fund Balance category after motion and approval by the Municipal Legislature.

### ***Policy on Assigning Funds***

In accordance with GASB 54, funds that are *intended* to be used for a specific purpose but have not received the formal approval action at the Municipal Legislature level may be recorded as Assigned Fund Balance. Likewise, redeploying assigned resources to an alternative use does not require formal action by the Municipal Legislature.

Having reviewed the requirements for assigning fund balance, therefore, is the policy of the Municipality that Mayor shall have the authority to assign fund balance of the Municipality based on the intentions of the use of funds by the Municipal Legislature. In addition, the Mayor can delegate to the Finance Director or other employee of the Municipality, the authority to assign the funds.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

**Policy on Unassigned General Fund Balance**

It is the goal of the Municipality to achieve and maintain an Unassigned General Fund Balance equal to 15% of budgeted expenditures. The Municipality considers a balance of less than 10% to be a cause for concern, barring unusual or deliberate circumstances, and a balance of more than 20% as excessive. An amount in excess of 20% is to be considered for reservation to accumulate funding for the purchase of machinery and equipment, for capital projects, and/or reduces tax levy requirements, and shall be determined in conjunction with the annual budget process. In the event that the Unassigned General Fund Balance is less than the policy anticipates, the Municipality shall plan to adjust budget resources in the subsequent fiscal years to restore the balance.

Appropriation from unassigned General Fund balance shall require the approval of the Municipal Legislature and shall be only for specific disbursements, such as one-time expenditures and capital asset purchases, and not for ongoing expenditures unless a viable plan designated to sustain the expenditures is simultaneously adopted.

**Prioritization of Fund Balance Use**

In circumstances where expenditure is to be made for a purpose for which amounts are available in multiple fund balance classifications, the order in which resources will be expended is as follows: Restricted Fund Balance, followed by Committed Fund Balance, Assigned Fund Balance, and lastly, Unassigned Fund Balance.

**C) Components of Fund Balance**

	GENERAL FUND	SBGP FUND	STATE ASSIGNMENT FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
Nonexpendable	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Restricted For:						
Debt Repayment	-	-	-	1,382,149	-	1,382,149
Improvement of Streets and Sidewalks	-	31,637	6,030,006	-	787,984	6,849,627
Improvement and Construction of Facilities	-	-	-	-	3,035,361	3,035,361
Welfare	-	-	-	-	651,224	651,224
Capital Outlay - Purchase of Equipment	-	-	-	-	56,089	56,089
Total Restricted	-	31,637	6,030,006	1,382,149	4,530,658	11,974,450
Committed To:						
Recreational Activities	-	-	-	-	30,516	30,516
Professional Services	-	-	-	-	-	-
Total Committed	-	-	-	-	30,516	30,516
Assigned	-	-	-	-	-	-
Unassigned	(6,672,774)	-	-	-	(437,055)	(7,109,829)
Total Fund Balances	\$ (6,672,774)	\$ 31,637	\$ 6,030,006	\$ 1,382,149	\$ 4,124,119	\$ 4,895,137

**E. Interfund Transactions**

Interfund transactions are reflected as loans, reimbursements or transfers. Loans are reported as receivables and payables as appropriate and are subject to elimination upon consolidation. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers between governmental or proprietary funds are netted as part of the reconciliation to the government-wide columnar presentation. The Municipality has the following types of transactions among funds:

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

*Interfund Transfers* – Legally required transfers that are reported when incurred as transfers-in by the recipient fund and as transfers-out by the disbursing fund, with receivables and payables presented as amounts due to and due from other funds.

*Intra-Entity Transactions* – Advances between funds are also presented as amounts due to and due from other funds. However, these transfers and related amounts receivables and payables are considered internal balances and activities that have been eliminated in the government-wide financial statements.

### F. Risk Financing

The Municipality carries commercial insurance to cover property and casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the municipalities of Puerto Rico. Also, principal officials of the Municipality are covered under various surety bonds. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the MRCC for the year ended June 30, 2012 amounted to approximately \$197,427. The current insurance policies have not been cancelled or terminated. In addition, MRCC deducted approximately \$279,337 for workers compensation insurance covering all municipal employees for the same period.

### G. Use of Estimates

The preparation of the basic 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 disclosures of contingent assets and liabilities at the date of the basic financial statements and the reported revenue and expenses during the reporting period. Actual result could differ from those estimates.

### H. Reclassifications

Various reclassifications have been made in the accompanying basic financial statements which affect the comparability with the basic financial statements issued for previous fiscal years.

### I. Future Adoption of Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) issued the following pronouncements that have effective dates after June 30, 2012:

GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*. The objective of this Statement is to improve financial reporting by addressing issues related to service concession arrangements (SCAs), which are a type of public-private or public-public partnership. As used in this Statement, an SCA is an arrangement between a transferor (a government) and an operator (governmental or nongovernmental entity) in which (1) the transferor conveys to an operator the right and related obligation to provide services through the use of infrastructure or another public asset (a "facility") in exchange for significant consideration and (2) the operator collects and is compensated by fees from third parties.

This Statement requires disclosures about an SCA including a general description of the arrangement and information about the associated assets, liabilities, and deferred inflows, the rights granted and retained, and guarantees and commitments. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2011 (FY 2012-2013). The provisions of this Statement generally are required to be applied retroactively for all periods presented.

GASB Statement No. 61, *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34*. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. The requirements of Statement No. 14, *The Financial Reporting Entity*, and the related financial reporting requirements of Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, were amended to better meet user needs and to address reporting entity issues that have arisen since the issuance of those Statements.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

This Statement modifies certain requirements for inclusion of component units in the financial reporting entity. For organizations that previously were required to be included as component units by meeting the fiscal dependency criterion, a financial benefit or burden relationship also would need to be present between the primary government and that organization for it to be included in the reporting entity as a component unit. Further, for organizations that do not meet the financial accountability criteria for inclusion as component units but that, nevertheless, should be included because the primary government's management determines that it would be misleading to exclude them, this Statement clarifies the manner in which that determination should be made and the types of relationships that generally should be considered in making the determination.

This Statement also amends the criteria for reporting component units as if they were part of the primary government (that is, blending) in certain circumstances. Lastly, additional reporting guidance is provided for blending a component unit if the primary government is a business-type activity that uses a single column presentation for financial reporting. This Statement also clarifies the reporting of equity interests in legally separate organizations. It requires a primary government to report its equity interest in a component unit as an asset. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2013 (FY 2013-2014). Earlier application is encouraged.

The Municipality's financial statements were not affected by the implementation of these statements.

GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements:

1. Financial Accounting Standards Board (FASB) Statements and Interpretations
2. Accounting Principles Board Opinions
3. Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure.

Hereinafter, these pronouncements collectively are referred to as the "FASB and AICPA pronouncements." This Statement also supersedes Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, thereby eliminating the election provided in paragraph 7 of that Statement for enterprise funds and business-type activities to apply post-November 30, 1989 FASB Statements and Interpretations that do not conflict with or contradict GASB pronouncements. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2011 (FY 2012-2013). Earlier application is encouraged. The provisions of this Statement generally are required to be applied retroactively for all periods presented.

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. Concepts Statement No. 4, *Elements of Financial Statements*, introduced and defined those elements as a consumption of net assets by the government that is applicable to a future reporting period, and an acquisition of net assets by the government that is applicable to a future reporting period, respectively. Previous financial reporting standards do not include guidance for reporting those financial statement elements, which are distinct from assets and liabilities.

Concepts Statement 4 also identifies net position as the residual of all other elements presented in a statement of financial position. This Statement amends the net asset reporting requirements in Statement No. 34, *Basic Financial Statements— and Management's Discussion and Analysis—for State and Local Governments*, and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2011 (FY 2012-2013). Earlier application is encouraged.

The Municipality has not yet determined the effect these statements will have on the Municipality's financial statements.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.

Concepts Statement No. 4, *Elements of Financial Statements*, introduced and defined the elements included in financial statements, including deferred outflows of resources and deferred inflows of resources. In addition, Concepts Statement 4 provides that reporting a deferred outflow of resources or a deferred inflow of resources should be limited to those instances identified by the Board in authoritative pronouncements that are established after applicable due process. Prior to the issuance of this Statement, only two such pronouncements have been issued. Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, requires the reporting of a deferred outflow of resources or a deferred inflow of resources for the changes in fair value of hedging derivative instruments, and Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, requires a deferred inflow of resources to be reported by a transferor government in a qualifying service concession arrangement. This Statement amends the financial statement element classification of certain items previously reported as assets and liabilities to be consistent with the definitions in Concepts Statement 4.

This Statement also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term deferred in financial statement presentations. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012 (FY 2013-2014). Earlier application is encouraged.

GASB Statement No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

This Statement amends Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, by removing the provision that limits fund-based reporting of an entity's risk financing activities to the general fund and the internal service fund type. As a result, governments should base their decisions about fund type classification on the nature of the activity to be reported, as required in Statement 54 and Statement No. 34, *Basic Financial Statements— and Management's Discussion and Analysis—for State and Local Governments*.

This Statement also amends Statement 62 by modifying the specific guidance on accounting for (1) operating lease payments that vary from a straight-line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current (normal) servicing fee rate. These changes clarify how to apply Statement No. 13, *Accounting for Operating Leases with Scheduled Rent Increases*, and result in guidance that is consistent with the requirements in Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, respectively. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012 (FY 2013-2014). Earlier application is encouraged.

GASB Statement No. 67, *Financial Reporting for Pension Plans*. This Statement replaces the requirements of Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* and Statement No. 50, *Pension Disclosures—an amendment of GASB Statements No. 25 and No. 27*, as they relate to pension plans that are administered through trusts or similar arrangements meeting certain criteria. The Statement builds upon the existing framework for financial reports of defined benefit pension plans, which includes a statement of fiduciary net position (the amount held in a trust for paying retirement benefits) and a statement of changes in fiduciary net position. Statement No. 67 enhances note disclosures and RSI for both defined benefit and defined contribution pension plans. Statement No. 67 also requires the presentation of new information about annual money-weighted rates of return in the notes to the financial statements and in 10-year RSI schedules. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2014 (FY 2014-2015). Earlier application is encouraged.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. This Statement replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* and Statement No. 50, *Pension Disclosures*—an amendment of GASB Statements No. 25 and No. 27, as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Statement No. 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. The Statement also enhances accountability and transparency through revised and new note disclosures and required supplementary information. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2014 (FY 2014-2015). Earlier application is encouraged.

The Municipality has not yet determined the effect this statement will have on the Municipality's financial statements.

## 3. CASH AND INVESTMENTS

### *Cash in Banks*

The Municipality's cash and investments at June 30, 2012 are composed of: (1) demand deposits in commercial banks, and (2) demand deposits in the Government Development Bank of Puerto Rico (GDB, fiscal agent).

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or the Government. The Municipality is also allowed to invest in bank acceptances, other bank obligations and certificates of deposit in financial institutions authorized to do business under the federal and Government laws.

The Municipality follows the practice of pooling cash. At June 30, 2012, the cash are maintained in commercial banks with a balance of \$1,344,383 of which \$88,030 in the General Fund, \$35,714 in SBGP Fund, \$50,541 in State Assignments Fund, and \$1,170,098 in Other Governmental Funds. The balance in cash account is available to meet current operating requirements and any unrestricted excess, if any, is generally invested in certificates of deposit with commercial banks. Any deficiency in the cash account is assumed by the general fund and covered through future budgetary appropriation.

Under the laws and regulations of the Government, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the Federal Deposit Insurance Corporation (FDIC) coverage. All securities pledged as collateral are held by agents designated by the Government's Secretary of the Treasury, but not in the Municipality's name.

Cash with fiscal agent in the debt service fund consists principally of property tax collections and sales and usage tax amounting to \$1,888,222 that are restricted for the payment of the Municipality's debt service, as required by law. Cash with Fiscal Agent of \$3,464,264 in other governmental funds, and \$173 in the General Fund consist principally of unspent proceeds of bonds that are restricted for the acquisition, construction or improvement of major capital assets. The amounts deposit in GDB is maintained in interest bearing accounts and is not collateralized.

Municipality follows the provisions of GASB Accounting Standards Codification Section C20, *Cash Deposit with Financial Institutions*, related with cash deposit and interest-earning investment contract with financial institutions. Accordingly, the following is essential information about credit risk, interest rate risk, custodial credit risk, and foreign exchange exposure of deposits and investments of the Municipality at June 30, 2012:

### *Credit Risk*

This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2012, the Municipality has invested only in cash in banks of \$1.3 million which are insured by the FDIC, generally up to a maximum of \$250,000. As previously mentioned, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the FDIC coverage. No investments in debt or equity securities were made during the Fiscal Year ended June 30, 2012. Therefore, the Municipality's management has concluded that the credit risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2012.

3. CASH AND INVESTMENTS – continuation

**Custodial Credit Risk**

This is the risk that, in the event of the failure of a depository financial institution, the Municipality will not be able to recover its cash and investments or will not be able to recover collateral securities that are in the possession of an outside party. Pursuant to the Investment Guidelines for the Government adopted by GDB, the Municipality may invest in obligations of the Government, obligations of the United States, certificates of deposit, commercial paper, banker's acceptance, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. At June 30, 2012, the Municipality has balances deposited in commercial banks amounting to \$1.3 million which are insured by the FDIC up to the established limit and the excess are fully collateralized as explained above. Deposits in GDB, amounting to \$5.4 million are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2012. It is management's policy to only maintain deposits in banks affiliated to FDIC to minimize the custodial credit risk, except for GDB. Therefore, the Municipality's management has concluded that at June 30, 2012, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

**Interest Rate Risk**

This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt or equity investments in its investments portfolio at June 30, 2012, (2) limiting the weighted average maturity of its investments in certificates of deposit to periods of three months or less, and (3) keeping most of its banks deposits and certificates of deposit in interest bearing accounts generating interest at prevailing market rates. Therefore, at June 30, 2012, the interest risk associated with the Municipality's cash and cash equivalent is considered low.

**Foreign Exchange Risk**

This is the risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, adopted by the Municipality, the Municipality is prevented from investing in foreign securities or any other types of investments for which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2012.

4. DUE FROM GOVERNMENTAL UNITS

The due from governmental units for the fiscal year ended June 30, 2012 corresponds to the portion of the Christmas Bonus received from the Commonwealth for the amount of \$91,204, and the Liquidation from the MRCC for the amount of \$194,493.

5. DEFERRED AND UNEARNED REVENUES

Governmental funds report *deferred revenue* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of *deferred revenue* and *unearned revenue* reported in the governmental funds were as follows:

	UNAVAILABLE	UNEARNED
<b>Governmental Funds:</b>		
Volume of Business Taxes	\$ -	\$ 418,587
Federal Government	3,020,814	-
Governmental Units	285,697	-
<b>Total Deferred/Unearned Revenues</b>	<b>\$ 3,306,511</b>	<b>\$ 418,587</b>

6. INTERFUND RECEIVABLE, PAYABLES AND TRANSFERS

A. Interfund Receivable and Payable Balances

Due to/from Other Funds at June 30, 2012 are summarized as follows:

INTERFUND RECEIVABLE	INTERFUND PAYABLE	AMOUNT
State Assignments	General Fund	\$ 5,980,368
Other Governmental Funds	State Assignment	903
General Fund	Other Governmental Fund	53,139
General Fund	SBGP Fund	312,948
<b>TOTAL</b>		<b>\$ 6,347,358</b>

6. INTERFUND RECEIVABLE, PAYABLES AND TRANSFERS – continuation

B. Interfund Transfers

Transfers are indicative of funding for capital projects or debt service, and subsidies of various operations.

INTERFUND TRANSFERS WITHIN THE GOVERNMENTAL FUNDS			
Sources	Transfer to	Amount	Purpose
General Fund	Debt Service Fund	\$ 448,480	Debt Payment
Other Governmental Funds	Debt Service Fund	9,915	Bond Issue Costs
Other Governmental Funds	General Fund	70,000	Residual Equity Transfer
Debt Service Fund	General Fund	505,000	Residual Equity Transfer
TOTAL		<u>\$ 1,033,395</u>	

7. DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2012, balance due to other governmental units of the General Fund for services rendered to the Municipality, consists of the following:

	AMOUNT
Retirement System Administration	<u>\$ 154,163</u>

8. CAPITAL ASSETS

Capital Assets activities for the fiscal year ended June 30, 2012 was as follows:

DESCRIPTION	BALANCE JULY 1, 2011	INCREASES	DECREASES	BALANCE JUNE 30, 2012
Non-Depreciable Capital Assets:				
Land	\$ 65,650,752	\$ -	\$ -	\$ 65,650,752
Construction in Progress	4,047,439	1,789,789	-	5,837,228
Total Non-Depreciable Capital Assets	<u>69,698,191</u>	<u>1,789,789</u>	-	<u>71,487,980</u>
Depreciable Capital Assets:				
Buildings and Buildings Improvements	30,422,254	-	-	30,422,254
Equipment and Vehicles	2,314,341	105,280	-	2,419,621
Furniture and Fixtures	2,181,598	-	-	2,181,598
Infraestructure	66,691,389	-	-	66,691,389
Total Depreciable Capital Assets	<u>101,609,582</u>	<u>105,280</u>	-	<u>101,714,862</u>
Less Accumulated Depreciation:				
Buildings and Buildings Improvements	(11,968,055)	(608,445)	-	(12,576,500)
Equipment and Vehicles	(1,798,804)	(120,981)	-	(1,919,785)
Furniture and Fixtures	(2,149,759)	(31,839)	-	(2,181,598)
Infraestructure	(24,210,632)	(1,333,828)	-	(25,544,460)
Total Accumulated Depreciation	<u>(40,127,250)</u>	<u>(2,095,093)</u>	-	<u>(42,222,343)</u>
Total Depreciable Capital Assets (Net)	<u>61,482,332</u>	<u>(1,989,813)</u>	-	<u>59,492,519</u>
CAPITAL ASSETS, NET	<u>\$ 131,180,523</u>	<u>\$ (200,024)</u>	<u>\$ -</u>	<u>\$ 130,980,499</u>

8. CAPITAL ASSETS – continuation

Depreciation expenses were charged to governmental functions/programs as follows:

	AMOUNT
General Government	\$ 131,991
Mayor and Municipal Legislature	628,528
Public Safety	251,411
Public Works and Transportation	523,773
Culture and Recreation	167,608
Health and Sanitation	272,362
Urban Development	119,420
<b>Total Depreciation Expenses</b>	<b>\$ 2,095,093</b>

9. GENERAL LONG-TERM DEBTS

A. General Obligations Bonds and Special Obligations Bonds

The principal long-term obligations of the Municipality are general obligations bonds and special notes issued to finance the construction and improvements of public facilities and purchase of equipment. The Municipality's obligations long-term debt retirements are appropriated and paid from resources accumulated in the Debt Service Fund (See Note 11).

During January 2012, the Municipality issued general obligation bond of 2012 in the amount of \$2,190,000 for construction purpose. The principal and interest at 6.00% for the first year, and 7.00% for the remaining installments are payable semi-annually ranging from \$40,000 to \$185,000 on the 1<sup>st</sup> days of July and January of each year through July 2034.

During February 2012, the Municipality issued special obligation bond of 2012 in the amount of \$291,000 for operational purpose. The principal and interest at 6.00% for the first year, and 7.00% for the remaining installments are payable semi-annually ranging from \$33,500 to \$50,500 on the 1<sup>st</sup> days of July and January of each year through July 2018.

During May 2012, the Municipality issued general obligation bond of 2012 in the amount of \$385,000 for operational purpose. The principal and interest at 6.00% for the first year, and 7.00% for the remaining installments are payable semi-annually ranging from \$5,000 to \$35,000 on the 1<sup>st</sup> days of July and January of each year through July 2038.

General and special obligations bonds as of June 30, 2012, are comprised of the following individual issues:

Type of Obligation and Purpose	Maturity Date	Interest Rate	Amount
<b>General Obligation Bonds – Property Taxes:</b>			
\$720,000, Series 1999 – Acquisition of Building	2023	4.86 to 6.50%	\$ 495,000
\$655,000, Series 2002 – Construction Purpose	2026	2.70 to 5.60%	500,000
\$290,000, Series 2007 – Land Purchase	2031	6.60 to 7.50%	265,000
\$1,135,000, Series 2007 – Construction Purpose	2032	3.93 to 7.50%	1,060,000
\$435,000, Series 2009 – Operational Purpose	2013	4.75 to 6.50%	195,000
\$1,080,000, Series 2011 – Construction Purpose	2030	6.00 to 7.50%	1,060,000
\$2,190,000, Series 2012 - Construction Purpose	2034	6.00 to 7.00%	2,190,000
\$385,000, Series 2012 - Operational Purpose	2038	6.00 to 7.00%	385,000
<b>Total General Obligation Bonds</b>			<b>6,150,000</b>
<b>Special Obligation Bonds – General Revenues:</b>			
\$283,000, Series 1991 – Construction Purpose	2011	3.27 to 7.81%	3,640
\$315,000, Series 2009 – Construction Purpose	2018	5.40 to 7.50%	245,000
\$3,240,000, Series 2009 – Construction Purpose	2033	2.43 to 7.00%	3,075,000
\$380,000, Series 2003 – Operational Purpose	2029	5.00 to 6.00%	305,000
\$837,000, Series 2002 – Operational Purpose	2026	5.00 to 6.00%	646,400
\$2,222,000, Series 2008 – Operational Purpose	2027	3.93 to 7.50%	1,924,000
\$85,000, Series 2010 – Purchase of Equipment	2016	1.60 to 6.00%	65,000
\$291,000, Series 2012 - Operational Purpose	2018	6.00 to 7.00%	291,000
<b>Total Special Obligation Bonds</b>			<b>6,555,040</b>
<b>Total General and Special Obligation Bonds</b>			<b>\$ 12,705,040</b>

9. GENERAL LONG-TERM DEBTS – continuation

According to Sections 103 and 148 through 150 of the US Internal Revenue Code and Sections 1.148 through 1.150 of the US Treasury Regulation, the Municipality's tax-exempt bonds are subject to the arbitrage rebate requirements. At June 30, 2012, the Municipality had no federal arbitrage liability on bonds since interest income earned from the investment of unspent bond proceeds were made in bank deposits that generate yields lower than the rates applicable to the debt service payments.

**B. Legal Debt Limit and Legal Debt Margin**

On March 9, 2009, the Commonwealth of Puerto Rico approves Law Number 7 that provides for revision of the valuation of property subject to taxation and imposes special property taxes for the Commonwealth. The Municipality debt limits are 10% of valuation of property subject to taxation, plus the balance of the special ad valorem taxes in the Debt Service Fund. In addition, before any new bonds are issued, the revenues of the Debt Service Fund should be sufficient to cover the projected debt service requirement. Additional legal debt margin was determine for the issuance of the special obligations bonds that are paid through retention made by the MRCC from monthly advance of annual property tax and subsidy send to the Municipality.

**C. Other Long-Term Debts**

***Borrowing from MRCC***

On July 1, 2002, the Municipality entered into a repayment agreement with the GDB and MRCC to repay the excess of property taxes advances from fiscal years up to 2001. The repayment agreement is payable in semiannual aggregate principals installments from \$49,360 plus annual interest of 6.1876%. The original amount of debt is \$2,597,475 under the enacted Law Number 42 to be paid during 22 years.

On November 28, 2001, the Municipality entered into a repayment agreement with the GDB and MRCC to pay for the proportional debt to cover the Land Information Management System (LIMS), system established by MRCC with the capacity to maintaining cadastre and photos of all real property of Puerto Rico. The original debt was \$76,312 to be paid during 10 years plus annual interest of 5.95%. Final payment was made during this fiscal year.

On July 1, 2007, the Municipality entered into a repayment agreement with the GDB and MRCC to repay the uncollectible property tax sale authorized by the enacted Law Number 146. The original amount of debt is \$89,759 to be paid during 25 years plus annual interest of 6.22%.

***Department of Labor and Human Resources***

On August 6, 2010, the Municipality entered into a repayment agreement with the Department of Labor and Human Resources to repay the unemployment benefit as of June 30, 2010. The repayment agreement is payable in monthly aggregate installments of principals and interest of 8.00% of \$17,079.68. The original amount of debt is \$728,719 under the agreement to be paid during 4 years.

***Deferred Charges Liabilities***

This amount represents the unpaid balance of the bond issue cost of the following obligation: \$3,240,000, Series 2009 and \$85,000, Series 2010 special obligation bonds, \$1,080,000, Series 2011 general obligation bonds, \$2,190,000, Series 2012 general obligation bonds, and \$291,000, Series 2012 special obligation bonds.

***Christmas Bonus***

This amount represents the estimated accrued Christmas bonus accumulated as of June 30, 2012 and payroll related benefits, representing the benefit to employees to be paid during the first week of December 2012.

***Compensated Absences***

This amount represents the estimated accrued vacation benefits, accrued sick leave benefits and payroll related benefits, representing the Municipality's commitment to fund such costs from future operations.

9. GENERAL LONG-TERM DEBTS – continuation

Following are the Other Long-Term Debts:

DESCRIPTION	BALANCE JULY 1, 2011	NEW ISSUES	RETIREMENTS AND ADJUSTMENTS	BALANCE JUNE 30, 2012	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER NEXT YEAR
Law Number 42 – MRCC	\$ 2,259,938	\$ -	\$ (52,461)	\$ 2,207,477	\$ 55,767	\$ 2,151,710
LIMS – MRCC	4,970	-	(4,970)	-	-	-
Law Number 146 – MRCC	75,398	-	(3,590)	71,808	3,590	68,218
Dept of Labor and Human Resources	687,563	-	(164,624)	522,939	164,623	358,316
Deferred Charges Liabilities	13,433	2,031	-	15,464	-	15,464
Christmas Bonus	191,050	182,408	(191,050)	182,408	182,408	-
Compensated Absences	1,480,581	81,024	(79,808)	1,481,797	1,112,199	369,598
<b>TOTAL</b>	<b>\$ 4,712,933</b>	<b>\$ 265,463</b>	<b>\$ (496,503)</b>	<b>\$ 4,481,893</b>	<b>\$ 1,518,587</b>	<b>\$ 2,963,306</b>

D. Changes in General Long-Term Debts

The following is a summary of changes in long-term debts for the year ended June 30, 2012:

DESCRIPTION	BALANCE JULY 1, 2011	NEW ISSUES	RETIREMENTS AND ADJUSTMENTS	BALANCE JUNE 30, 2012	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER NEXT YEAR
General	\$ 3,850,000	\$ 2,575,000	\$ (275,000)	\$ 6,150,000	\$ 225,000	\$ 5,925,000
Special	6,466,380	291,000	(202,340)	6,555,040	252,840	6,302,200
Other Debts	4,712,933	265,463	(496,503)	4,481,893	1,518,587	2,963,306
<b>TOTAL</b>	<b>\$ 15,029,313</b>	<b>\$ 3,131,463</b>	<b>\$ (973,843)</b>	<b>\$ 17,186,933</b>	<b>\$ 1,996,427</b>	<b>\$ 15,190,506</b>

E. Debt Compliance

There are a number of limitations and restrictions contained in the various bond indentures. The Municipality believes it is in compliance with all significant limitations and restrictions. The annual requirements to amortize the general long-term debts outstanding as of June 30, 2012 are as follows:

YEAR ENDING JUNE 30,	General Obligation Bonds		Special Obligation Bonds		Other Long-Term Obligations		TOTAL	
	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL	INTEREST
<b>Governmental Funds:</b>								
2013	\$ 225,000	\$ 255,109	\$ 252,840	\$ 200,110	\$ 1,518,587	\$ 197,308	\$ 1,996,427	\$ 652,527
2014	270,000	372,482	258,800	394,685	227,473	193,581	756,273	960,748
2015	165,000	379,230	284,600	391,103	231,197	189,635	680,797	959,968
2016	185,000	374,594	306,800	378,230	99,602	137,867	591,402	890,691
2017	195,000	367,110	323,400	356,693	74,738	123,922	593,138	847,725
2018-2022	1,215,000	8,641,145	1,576,400	1,474,894	446,630	543,332	3,238,030	10,659,371
2023-2027	1,530,000	1,120,317	2,017,200	1,128,887	599,325	385,035	4,146,525	2,634,239
2028-2032	1,590,000	564,667	1,025,000	363,475	806,405	172,466	3,421,405	1,100,608
2033-2037	740,000	95,100	510,000	36,400	92,874	2,873	1,342,874	134,373
2038-2042	35,000	1,225	-	-	-	-	35,000	1,225
UNMATURED	-	-	-	-	385,062	-	385,062	-
<b>TOTAL</b>	<b>\$ 6,150,000</b>	<b>\$ 12,170,979</b>	<b>\$ 6,555,040</b>	<b>\$ 4,724,477</b>	<b>\$ 4,481,893</b>	<b>\$ 1,946,019</b>	<b>\$ 17,186,933</b>	<b>\$ 18,841,475</b>

## 10. DEBT RETIREMENT

Revenues of the debt service fund consists of the ad-valorem property taxes which are recognized as revenue when collected from taxpayers and reported by the Municipal Revenue Collection Center of the Commonwealth of Puerto Rico to the Municipality (See Note 11).

These property taxes are accumulated by the Municipal Revenue Collection Center in costs of the general obligations bonds issued by the Municipality (See Note 9). Payments are made to the Government Development Bank of the Commonwealth of Puerto Rico from such accumulated funds by the Municipal Revenue Collection Center of Puerto Rico.

## 11. PROPERTY TAXES

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

The MRCC is responsible for the assessment of all real and personal property located within the Municipality and for the levy, administration and collection of the corresponding tax contribution.

The personal property tax is self-assessed by the taxpayer on a return, which is to be filed and paid in full by May 15 of each year with the MRCC and based on current values as of December 31 of previous year. Real property tax is assessed by the MRCC on each piece of real estate and on each building or residence. The property tax contribution is levied each year over the appraised value of the real property at the beginning of the calendar year. The real property assessment is based on the current value existing in the year 1957.

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

The tax rate for fiscal year 2012 is 9.03% for real property and 7.03% for personal property of which 1.03% of both are for the redemption of public debt issued by the Commonwealth of Puerto Rico and 8.00% and 6.00%, respectively, belongs to the Municipality. The Commonwealth of Puerto Rico also contributes an annual tax rate of 0.20% of the property tax collected. The remaining percentage is distributed as follows: (a) 6.00% and 4.00%, respectively, represents the Municipality's basic tax rate that is appropriated for general purposes and therefore accounted for through the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. The remaining portion belonging to the Municipality of 2.00% represents the ad-valorem property taxes withheld by the MRCC and restricted for debt service, which is accounted for through the debt service fund (See Note 10). The Municipality has reached the maximum statutory tax rate limit for the basic tax while there is no limitation for the ad-valorem tax rate.

The Commonwealth of Puerto Rico grants complete real property tax exoneration on the first \$15,000 has assessed valuation on residential units occupied by their owners. For such exempted amounts, the Puerto Rico Treasury Department assumes payment of the basic tax to the Municipality, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. As part of Law No. 83 of August 30, 1991, as amended, the exempt amount to be paid by the Puerto Rico Treasury Department to the Municipality was frozen as of January 1, 1992.

In addition, the law grants a complete exemption from personal property taxes up to an assessment value of \$50,000 to retailers with an annual net sales volume of less than \$150,000. The MRCC advances to the Municipality, on monthly payments, 100% of the contribution assessed over property for each fiscal year. In accordance to Law, these advances will be contributions by the MRCC from taxpayers. The MRCC periodically informs to the Municipality the amounts collected from taxpayers and applied to outstanding advances.

#### 11. PROPERTY TAXES – continuation

The Municipality records as revenue in the general fund the property tax contribution when received from monthly advances from MRCC. Due to the fact that collections of property tax are applied to the advances of property tax paid by the MRCC, the amortization of the advance at end of year was not available due to that is in process of verification by external auditors.

#### 12. VOLUME OF BUSINESS TAXES

The volume of business taxes is levied each year based on the prior year's gross revenues for all commercial and industrial organizations doing business in the Municipality and which are not totally or partially exempt from this tax under the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due five working days after April 15 of each year. Entities with sales volume of \$3 million or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2012, the tax rates were as follows:

- a. 1.50% to financial institutions and savings and loan associations
- b. 0.5% to all other organizations

Taxes are payable in two equal semi-annual installments on July 1 and January 1 following the date of levy. If they are paid with declaration on or before the due date, the taxpayer is granted a 5% of discount. The volume of business tax receivable represents filed tax returns that were uncollected as of June 30, 2012. Collections of taxes during current fiscal year corresponding of the tax return based on the prior year gross sales, are applicable to the next fiscal year and recorded as deferred revenues in the General Fund.

#### 13. SALES AND USAGE TAXES

Municipality imposes a Sales and Usage Taxes of 1.5% (1.0% collected and belong to the Municipality and 0.5% collected by the Puerto Rico Secretary of the Treasury) on the sales price of a taxable item or on the purchase price of all usage, storage or consumption of a taxable item. All merchants required to collect the Sales and Usage Taxes, are required to file a monthly Sales and Use Tax Return Form, no later than the 10<sup>th</sup> of the following month from the month being reported. The Act also provides for restrictions on the use of the resources (including the 0.5% collected by the Puerto Rico Secretary of Treasury) to be invested in solid waste and recycling programs, capital improvements and health and public safety costs.

The amount collected by the Puerto Rico Secretary of Treasury will be deposited in accounts or special funds in GDB, subject to restrictions imposed and distributed as follows:

- a. 0.2% will be deposited in a "Municipal Development Fund" to finance costs as restricted by the Act;
- b. 0.2% will be deposited in a "Municipal Redemption Fund" to finance loans to municipalities subject to restrictions imposed by the Act; and
- c. 0.1% 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.

Sales tax receivable represents filed sales tax returns that were collected subsequent to June 30, 2012, but pertaining to the current year period.

#### 14. CONSTRUCTION EXCISE TAXES

Municipality imposes and collects municipal construction excise taxes to most natural and legal persons and any governmental instrumentality that carry out activities related to construction, expansion, major repairs, relocations, alterations and other types of permanent improvements to residential, commercial and industrial buildings, and any structures within the territorial area of the Municipality. The tax is also applicable to infrastructure projects, the installation of machinery, equipment, cable TV, commercial antennas and fixtures, and other types of construction-related activities.

**14. CONSTRUCTION EXCISE TAXES – continuation**

The construction excise tax generally is a self-assessed tax imposed over the cost of the project, net of certain exemptions such as the costs associated with the acquisition of land, existing buildings and improvements, project design and other engineering fees, licenses and permits, consulting and legal fees. The tax is paid by the taxpayer before the beginning of the construction project. The activities covers by this tax and the exemption granted are as follows:

- a. Total exemption are granted to projects self-administering by federal government, state government (including public corporation), and the municipalities of Puerto Rico.
- b. Low income resident of Vieques that received federal, state or municipal funds for construction or improvement of their home, a total exemption is granted.
- c. Civic, religions and communities non-for-profit organization should have an exemption for the first \$15,000 of the total cost of the projects. In excess of \$15,000, a 3.50% of construction excise taxes should be paid.
- d. Resident of Vieques should paid construction excise taxes in accordance with the following scale:

TOTAL COST	CONSTRUCTION EXCISE TAX
From \$1,000 to \$10,000	2.00% of Total Cost
From \$10,001 to \$15,000	2.50% of Total Cost
From \$15,001 to \$20,000	2.75% of Total Cost
From \$20,001 to \$25,000	3.00% of Total Cost
From \$25,001 to \$30,000	4.00% of Total Cost
In excess of \$30,000	5.00% of Total Cost

- e. All other projects should paid 5.00% of total cost.

**15. INTERGOVERNMENTAL REVENUES**

Intergovernmental revenues consist primarily of funds received from the Commonwealth of Puerto Rico, "in lieu of tax" payments from the Quasi-public Corporation, Puerto Rico Electric Power Authority, and federal financial assistance received from federal government.

Grants and subsidies received from the Commonwealth of Puerto Rico and federal agencies include, among others, a general subsidy for urban development and capital improvements. Intergovernmental revenues are accounted for through the General Fund except for those directly related to urban development and capital improvements, which are accounted for through the Special Revenue and the Capital Project Funds. Federal Financial Assistance is recorded in the Special Revenue Fund.

**16. PENSION PLAN**

*Description of the Plan*

Employees of the Municipality participate in the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). The ERS is cost-sharing multiple-employer defined benefit pension plan sponsored by the Government under the Act No. 447, approved on May 15, 1951, as amended. ERS covers all regular employees of the Government and its instrumentalities and of certain municipalities and components units not covered by their own retirement systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Head of Agencies and Public Instrumentalities, Assistants to the Governor, the Comptroller of the 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.

16. PENSION PLAN – continuation

Members who have attained at least 55 years of age and have completed at least 25 years of creditable service or members who have attained at least 58 years of age and have completed at least 10 years of creditable service are entitled to an annual benefit, payable monthly for life. The amount of the annuity shall be 1.5% of the average salary, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average salary, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive up to a maximum of 65% of the average salary, as defined, or if they have attained 55 years of age will receive up to a maximum of 75% of the average salary, as defined. Disability retirement benefits are available to members for occupational disability up to a maximum benefit of 50% of the average salary, as defined. However, for non-occupational disability, a member must have at least 10 years of creditable services.

The contribution requirements for both employees and employers are established by law and are not actuarially determined. Employees are required to contribute 5.775% for the first \$550 of monthly salary plus 8.275% for the excess of this amount, or on the alternative, 8.275% of their monthly gross salary. The Municipality is required by Act No. 447 to contribute 9.275% of its employees' gross salaries.

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

Law Number 305 was enacted on September 24, 1999, amended the Act Number 447 for the purpose of establishing a new program (System 2000). System 2000 became effective on January 1, 2000. Employees participating in the current system (ERS) as of December 31, 1999, may elect either to stay in the defined-benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000, will only be allowed to become members of System 2000.

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

If at time of retirement accumulated benefits amount to \$10,000 or less may elect to receive a lump sum distribution up to the accumulated benefits. Under the new program the retirement age is reduced from 65 to 60 for those employees who joined the current plan on or after April 1, 1990.

**Funding Policy**

The authority under which the funding policy and the obligations to contribute to the ERS and System 2000 by the plans' members, employers and other contributing entities (state of municipal contributions), are established or may be amended by law.

Contribution requirements are established by law and are as follows:

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

16. PENSION PLAN – continuation

**Annual Contribution**

Total employee contributions to the above-mentioned plans during the three years period ended June 30, 2012 amounted to \$829,457. The Municipality's contributions during those years are recognized as total pension expenditures/expenses in the category of administration as follow:

FISCAL YEAR	LAW NO. 447	SYSTEM 2000
2012	\$ 154,757	\$ 191,559
2011	109,959	109,086
2010	184,913	182,854

These amounts represented the 100% of the required contribution for the corresponding year. Additionally, changes made in the types and amounts of benefits offered by special laws and costs of living adjustments, led to a one-time recommended contribution to fund the retroactive adjustment related to the changes.

The Employee's Retirement System of the Government of Puerto Rico provides additional information of the ERS and System 2000. They issue a publicly available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Government. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, PR 00940-2003.

17. CONTINGENCIES

a. Claims and Judgments

The Municipality is, at present, a defendant in a number of legal matters that arise from alleged improper application of policies and negligence in the ordinary course of the Municipality's activities. The legal counsel of the Municipality has advised that at this stage in the proceedings of lawsuits he cannot offer an opinion as to the probable outcome.

In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in discovery stage. Certain of these claims are covered by insurance. Legal counsel with the information currently available cannot determine the final outcome of these claims. Accordingly, the financial statements do not include adjustment, if any, that could result from the resolution of this legal proceeding. However, it has been the Municipality's experience that such actions are settled for amounts substantially less than the claimed amounts.

B. Federal Grants

In the normal course of operations, the Municipality receives grants from various Federal and State agencies. The grant programs are subject to audit by agents of the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

18. COMMITMENTS

A. Construction and Improvement Commitments

The Municipality had encumbrances at June 30, 2012 for the construction, improvements, or renovation of several municipal facilities in the following funds:

	Encumbered For	Amount	Reported within Fund Balance Classification
Non Major Funds	Improvement of a High School	\$ 175,357	Restricted to Improvement and Construction of Facilities
Non Major Funds	Construction of a Gazebo	64,088	Restricted to Improvement and Construction of Facilities
Non Major Funds	Municipal Office Construction	16,526	Restricted to Improvement and Construction of Facilities
Non Major Funds	Installation of Sewer	30,000	Restricted to Improvement and Construction of Facilities
Non Major Funds	Rehabilitation of the Fishing Area	45,500	Restricted to Improvement and Construction of Facilities

18. COMMITMENTS – continuation

B. Other Commitments

At June 30, 2012, the general fund had a deficit of \$6,672,774 which will be covered with future budgetary appropriations of the general fund.

19. NET ASSETS/FUND BALANCES RESTATEMENTS

a. Net Assets Restatements

During the year, the Municipality adjusted the governmental net assets for recognized payable and receivables. The following schedule reconciles the June 30, 2011 Net Assets, as previously reported to Beginning Net Assets, as restated, July 1, 2011, for Governmental Activities.

	NET ASSETS
Net Assets, as Previously Reported, At June 30, 2011	\$ 123,441,790
Adjustment to Prior Year Expenditures	<u>645,234</u>
Beginning Net Assets, as Restated, At July 1, 2011	<u>\$ 124,087,024</u>

b. Fund Balances Restatements

The following reconciles the June 30, 2011 Fund Balance, as previously reported to Beginning Fund Balance, as restated, July 1, 2011 for the various funds:

	GENERAL FUND
Fund Balance (Deficit), as Previously Reported, At June 30, 2011	\$ (7,426,120)
Adjustment to Prior Year Expenditures	<u>645,234</u>
Beginning Fund Balance (Deficit), As Restated, At July 1, 2011	<u>\$ (6,780,886)</u>

20. SUBSEQUENT EVENT

Management has evaluated subsequent events through March 26, 2013, which is the date the financial statements were available to be issued and determined that no material subsequent events require an estimate to be recorded or disclosed as of June 30, 2012.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO  
REQUIRED SUPPLEMENTARY INFORMATION  
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND  
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	Budget Amounts		Actual Amounts	Variance with
	Original	Final	(Budgetary Basis) (See Note A)	Final Budget
<b>BUDGETARY FUND BALANCE (DEFICIT), AS RESTATED, JULY 1, 2011</b>	<b>\$ (7,421,523)</b>	<b>\$ (7,421,523)</b>	<b>\$ (7,421,523)</b>	<b>\$ -</b>
Resources (Inflows):				
Property Taxes	966,242	966,242	966,242	-
Volume of Business Taxes	367,451	367,451	532,182	164,731
Intergovernmental Revenues	6,883,558	6,883,558	6,713,492	(170,066)
Construction Excise Taxes	1,279,000	1,279,000	595,365	(683,635)
Sales and Usage Taxes	330,000	330,000	423,668	93,668
Miscellaneous	816,137	816,137	724,655	(91,482)
Rent	35,000	35,000	104,150	69,150
Transfer-In	-	-	-	-
<b>Total Resources (Inflows)</b>	<b>10,677,388</b>	<b>10,677,388</b>	<b>10,059,754</b>	<b>(617,634)</b>
Amounts Available for Appropriation	3,255,865	3,255,865	2,638,231	(617,634)
Charges to Appropriations (Outflows):				
Mayor and Municipal Legislature	864,940	923,210	780,579	142,631
General Government	5,855,876	5,702,111	6,243,584	(541,473)
Public Safety	933,346	892,265	836,211	56,054
Public Works	801,743	790,601	750,413	40,188
Culture and Recreation	529,600	533,253	676,574	(143,321)
Health and Sanitation	580,658	562,977	602,383	(39,406)
Human Services and Welfare	700,223	687,110	601,037	86,073
Urban Development	25,000	13,545	172,082	(158,537)
Capital Outlays	63,500	44,696	42,898	1,798
Transfer to Other Funds	322,502	527,620	448,480	79,140
Total Charges to Appropriations	10,677,388	10,677,388	11,154,241	(476,853)
<b>BUDGETARY FUND BALANCE (DEFICIT), JUNE 30, 2012</b>	<b>\$ (7,421,523)</b>	<b>\$ (7,421,523)</b>	<b>\$ (8,516,010)</b>	<b>\$ (1,094,487)</b>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO  
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND  
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION  
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

**1. Budgetary Reporting**

The Budgetary Comparison Schedule - General Fund is presented as Required Supplementary Information in accordance with GASB Accounting Standards Codification Section 1700, *The Budget and Budgetary Accounting*. Formal and legal budgetary control is based upon major classes of expenditures known as functions. All inflows, except volume of business taxes and transfer-in were less than expected. The Municipality's expenditures in General Government function exceeded the budgetary amount by \$92,958 due to far greater than expected increased for irregular employees.

**2. Explanation of Differences Between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures**

	<u>General Fund</u>
<b>Sources/Inflows of Resources:</b>	
Actual Amounts (Budgetary Basis) "Available for Appropriation" from the Budgetary Comparison Schedule (See Page 48)	\$ 2,638,231
Difference – Budget to GAAP:	
The Fund Balance at the Beginning of Year is a budgetary resource but is not a Current-Year Revenue for financial reporting purposes	7,421,523
Non budgetary revenues (revenues reclassification GASB 54)	<u>56,052</u>
Total Revenues as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 19)	<u>\$ 10,115,806</u>
<b>Uses/Outflows of Resources:</b>	
Actual Amounts (Budgetary Basis) "Total Charges to Appropriation" from the Budgetary Comparison Schedule (See Page 48)	\$ 11,154,241
Difference – Budget to GAAP:	
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes	(319,895)
Payments of encumbrances of prior year that are expenditures for financial reporting purposes but are not outflows for budgetary purposes	199,806
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	(448,480)
Non budgetary expenditures	<u>224,542</u>
Total Expenditures as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 19)	<u>\$ 10,810,214</u>

**3. Explanation of Differences Between Budgetary Fund Balance and GAAP Fund Balance**

Budgetary Fund Balance (Deficit), June 30, 2012	\$ (8,516,010)
Timing Differences:	
Change in Encumbrances	120,089
Cancelation of Prior Year Encumbrances	(33,165)
Non-budgetary Fund Balances	338,481
Revenues that are not Budgetary Uses	56,052
Restatement to Fund Balance	645,234
Transfer in - Non Budgetary	575,000
Non budgetary Items	(224,542)
Perspective Differences:	
Due from Other Funds not Available	<u>366,087</u>
Fund Balance (Deficit), June 30, 2012	<u>\$ (6,672,774)</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF VIEQUES, PUERTO RICO**

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

FEDERAL GRANTOR / PASS THROUGH GRANTOR / PROGRAM OR CLUSTER TITLE	Federal CFDA NUMBER	Pass-Through ENTITY IDENTIFYING NUMBER	FEDERAL EXPENDITURES
U.S. Department of Housing and Urban Development:			
Pass-Through State – Office of the Commissioner Of Municipal Affairs			
Community Development Block Grant/States Program (SBGP) And Non Entitlements Grants in Hawaii (Stated Administered Small Cities Program)	14.228	N/A	\$1,191,285
<b>ARRA</b> - Homeless Prevention and Rapid Rehousing Program.....	14.257		201,775
Direct Program:			
Section 8 Housing Choice Voucher.....	14.871		<u>749,099</u>
Total U.S. Department of Housing and Urban Development..			<u>2,142,159</u>
U. S. Department of Energy:			
Pass-Through Puerto Rico Energy Affairs Administration:			
<b>ARRA</b> -Energy Efficiency and Conservation Block Grant Program (EECBG).....	81.128		<u>53,110</u>
U. S. Department of Homeland Security:			
Disaster Grants – Public Assistance.....	97.036		<u>577,795</u>
<b>TOTAL EXPENDITURES OF FEDERAL AWARDS .....</b>			<b><u>\$2,773,064</u></b>

## 1. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the federal grant activities of the **Municipality of Vieques, Puerto Rico (Municipality)**. The information in this Schedule is presented in accordance with the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of **Municipality**, it is not intended to and does not present the financial position, or change in net assets of the **Municipality**.

Therefore, some amounts presented in this Schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements. The **Municipality** reporting entity is defined in Note (1) (A) to the basic financial statements. All federal financial awards received directly from federal agency as well as federal financial awards passed-through other government agencies are included on the Schedule.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- A. Expenditures reported on the Schedule are reported on the modified accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State and Local Government*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.
- B. Negative amounts, if any, shown on the Schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years.
- C. Pass-through entity identifying numbers are presented where available.

## 3. FEDERAL CFDA NUMBER

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

## 4. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Expenditures of federal awards are reported in the **Municipality's** Statement of Revenues, Expenditures and Changes in Fund Balances- Governmental Fund as follows: SBGP Funds – \$1,191,285 and Other Governmental Funds \$1,581,779.



TORRES, HERNANDEZ & PUNTER, CPA, CSP  
Certified Public Accountants

**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

We have audited the financial statements of the Municipality of Vieques of the Commonwealth of Puerto Rico (from now on the Municipality) as of and for the fiscal year ended June 30, 2012, and have issued our report thereon dated March 26, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

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

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Municipality's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs, as items #12-01 through #12-19, to be material weaknesses.

A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying schedule of findings and questioned costs, as items #12-01 through #12-19, to be significant deficiencies.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and

**Compliance and Other Matters - Continued**

accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs, as items #12-01 through #12-19.

Municipality's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs, on pages 56 to 79 and in their corrective action plan. We did not audit the Municipality's responses and, accordingly, we express no opinion on those responses.

This report is intended solely for the information and use of Municipality's management, the U.S. Department of Housing and Urban Development and other regulatory agencies and is not intended to be and should not be used by anyone other than these specified parties.

*Torres, Hernández & Punter, CPA, PSC*

**Torres, Hernández & Punter, CPA, PSC**  
**Certified Public Accountants**

March 26, 2013

Stamp #E23414 of the  
College of CPA's of  
Puerto Rico is affixed  
to the original.



TORRES, HERNANDEZ & PUNTER, CPA, CSP

Certified Public Accountants

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS  
THAT HAVE A DIRECT AND MATERIAL EFFECT ON 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

**Compliance**

We have audited the Municipality of Vieques of the Commonwealth of Puerto Rico (from now on the Municipality) compliance of with the types of compliance requirements described in OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of the Municipality's major federal programs for the year ended June 30, 2012. Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Municipality's management. Our responsibility is to express an opinion on Municipality's compliance based on our audit.

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

As described in the accompanying schedule of findings and questioned costs as items #12-15, #12-16, #12-17, #12-18 and #12-19, the Municipality did not comply with requirements regarding Cash Management, Davis-Bacon Act, Equipment and Real Property Management and Reporting that are applicable to the Community Development Block Grant/States Program (SBGP), and the Municipality did not comply with requirements regarding Cash Management, Eligibility and Equipment and Real Property Management that are applicable to Section 8 Housing Choice Voucher Program and Section 8 Moderated Rehabilitation Single Room Occupancy Programs. Compliance with such requirements are necessary, in our opinion, for the Municipality to comply with the requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items #12-9, #12-10, #12-11, #12-12, #12-13 and #12-14.

## Internal Control Over Compliance

Management of Municipality is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Municipality's 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 in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control over compliance.

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

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items #12-9 through #12-19 to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items #12-9 through #12-19 to be significant deficiencies.

Municipality's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs, on pages 56 to 79 and in their corrective action plan. We did not audit the Municipality's responses and, accordingly, we express no opinion on those responses.

This report is intended solely for the information and use of Municipality's management, the U.S. Department of Housing and Urban Development and other regulatory agencies and is not intended to be and should not be used by anyone other than these specified parties.

*Torres, Hernández & Punter, CPA, PSC*  
Torres, Hernández & Punter, CPA, PSC  
Certified Public Accountants

March 26, 2012

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**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**

**FOR THE YEAR ENDED JUNE 30, 2012**

**Part I - Summary of Audit Results:**

**Financial Statements**

The independent auditor's report on the basic financial statements expressed a qualified opinion.

**Internal Control Over Financial Reporting:**

Material weaknesses identified?	<u> X </u> yes	_____ no
Significant deficiencies identified?	<u> X </u> yes	_____ none reported
Noncompliance material to the Statement noted?	<u> X </u> yes	_____ no

**Federal Awards**

**Internal control over major programs:**

Material weaknesses identified?	<u> X </u> yes	_____ no
Significant deficiencies identified?	<u> X </u> yes	_____ none reported

The independent auditor's report on compliance with requirements applicable to major federal awards program expressed a qualified opinion.

The audit disclosed findings to be reported in accordance with OMB Circular A-133, Section 510(a).

X  yes                      \_\_\_\_\_ no

Municipality's major awards during the year ended June 30, 2011 were:

- CFDA #14.228 - Community Development Block Grant/States Program (SBGP),
- CFDA #14.871 - Section 8 Housing Choice Voucher Program
- CFDA #97.036 - Disaster Grants – Public Assistance

A threshold of \$300,000 was used to distinguish between type A and type B programs, as those terms are defined in OMB Circular A-133, Section 520 (a).

Municipality qualify as a low risk auditee?                      \_\_\_\_\_ yes                       X  no

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements:**

**FINDING NUMBER 12-01: REQUIRED CLAUSES NOT INCLUDED ON CONTRACTS**

**CONDITION:** We selected twenty-two (22) contracts for examination. We noted the following required clauses were not included, stating the following

1. A warning that services cannot be requested unless contract has been presented for registration at the Comptroller's Office of Puerto Rico (OCPR) (1 Contract),
2. That the invoice to be submitted to the Municipality must include a certification that services were provided and have not yet been paid. Also, to indicate that no employee of the contracting entity is a party or has an interest in the profits or benefits of the contract. (1 Contract),

For construction and public improvements contracts:

3. That the contracted party certifies that is in compliance with the permits required to work as a contractor (2 Contracts),
4. That a 10% will be retained from every partial payment until completion of the project (2 Contracts),
5. That the contract can be terminated in case of noncompliance and the establishment of penalties for late performance (2 Contracts) and
6. Clause that regulates the subcontracting of services and a waiver of responsibility (2 Contracts).

**CRITERIA:** Sound government management requires disclosure of such information when a contract is prepared in order to safeguard municipal interest. Also, to comply with the following applicable laws and regulations as detailed for each instance above as follows:

Instance 1 -

Article 1(e) Law No. 18 of October 20, 1975 as amended by Law No. 127 of May 31, 2004, and Memorandum No. 2004-11 from OCAM.

Instance 2 -

Article 3, J, Law No. 237 of August 31, 2004

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

**FINDING NUMBER 12-01: REQUIRED CLAUSES NOT INCLUDED ON CONTRACTS (CONTINUED)**

Instance 3-

Chapter 9, Section 6, OCAM Ruling for Municipal Administration.

Instance 4 -

Chapter 9, Section 6, OCAM Ruling for Municipal Administration.

Instance 5 -

Chapter 9, Section 6, OCAM Ruling for Municipal Administration.

Instance 6 -

Chapter 9, Section 6, OCAM Ruling for Municipal Administration.

**CAUSE:** Internal control procedures to assure that contracts include all clauses required by laws and regulations were not effective enough during this fiscal year. Contracts were not properly verified by the officials preparing them to assure this information was contained in contracts before signature.

**EFFECT:** The Municipality is not properly safeguarded.

**RECOMMENDATION:** To strengthen present control procedures to assure all contracts prepared contains all the necessary clauses and information, as required by present laws and regulations, and by state and federal agencies. One employee should be designated to verify contracts before signature to ensure they are complete in terms of required clauses before signature. We also recommend that an employee be designated as preintervention officer to verify all contracts prepared.

**MANAGEMENT RESPONSE:** See corrective action plan.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

**FINDING NUMBER 12-02: CERTIFICATIONS NOT INCLUDED AS PART OF CONTRACT**

**CONDITION:** We selected twenty-two (22) contracts for examination. We noted the following required certifications were not included as part of the contract awarded:

1. Certification that contracted party has submitted tax returns for the last five (5) years and that no amounts are due to the Treasury Department of PR for taxes or is under a payment plan (2 Contracts),
2. Has no debt outstanding with the Municipal Revenue Collection Center (CRIM) for real property taxes and other concepts or is under a payment plan, (2 Contracts),
3. Certification from the Department of Labor and Human Resources that no debt is outstanding for Unemployment and Disability taxes (2 Contracts), and
4. Certification from the Child Support Administration (ASUME) stating that no balance is due on alimony (2 Contracts).

**CRITERIA:** Government management shall ensure that before granting a contract, a contractor complies with state and local tax obligations. Also, to comply with the following applicable laws and regulations as detailed for each instance above as follows:

Instances 1 through 4 –

Article 5, A, Law No. 237 of August 31, 2004,  
Article 14, Law No. 164 of July 23, 1974, as amended,  
Article 9(j) Law No. 230 of July 23, 1974, as amended,  
Article 6(c) of OCPR Ruling No. 33, as amended,  
Administrative Bulletin No. OE-1991-24, as amended by Administrative Bulletin OE-1992-52,  
Circular Letter No. 1300-1-06 of TD, dated July 20, 2005,  
Memorandum No. 92-31 from the Office of the Commissioner of Municipal Affairs (OCAM),  
Circular Letter No. OC-06-15 of OCPR, and  
Chapter 9, Section 2, of OCAM Ruling for Municipal Administration.

**CAUSE:** Internal control procedures to assure that contracts include all certifications required by laws and regulations were not effective enough during this fiscal year. Contracts were not properly verified by the officials preparing them to assure this information was included as part of contracts before signature.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

**FINDING NUMBER 12-02: CERTIFICATIONS NOT INCLUDED AS PART OF CONTRACT (CONTINUED)**

**EFFECT:** The Municipality does not ensure that contractors are complying with state and local tax obligations.

**RECOMMENDATION:** To strengthen present control procedures to assure all contracts prepared contains all the necessary certifications and information, as required by present laws and regulations, and by state agencies. One employee should be designated to verify contracts before signature to ensure they are complete in terms of required certifications. We also recommend that an employee be designated as preintervention officer to verify all contracts prepared.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-03: BIDS FILES INCOMPLETE**

**CONDITION:** For two (2) bid files examined, we found one bid file was incomplete in terms of the following:

Conditions	Instances
1. One of the awarded bidder did not provide evidence of state insurance fund policy, certification from Treasury Department stating no debt, certification from ASUME,	1
2. No copy of the bid specifications detailing the requirements was included in the file, and	1
3. No evidence was available that bidder provided the required bid and performance bonds.	2

**CRITERIA:** To comply with Chapter VIII, part I, section 4 Regulations for Municipal Administration (OCAM) and Chapter 8, article 8.016(C)(2) of Law #81.

**CAUSE:** The Municipality does not have adequate control procedures to assure that bids files have all necessary documents required by law.

**EFFECT:** Bids are not properly documented and municipal could be liable if a bidder claims that the bid was not awarded properly.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

**FINDING NUMBER 12-03: BIDS FILES INCOMPLETE (CONTINUED)**

**RECOMMENDATION:** To implement review procedures to assure that all the bid files includes all documents required by applicable laws and regulations. An employee independent of the Finance Department and the Bid Board should be designated to oversee this procedure.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-04: DOCUMENTS NOT AVAILABLE ON MUNICIPAL EMPLOYEE FILES**

**CONDITION:** We selected twenty-five (25) employee files for examination. We noted the following documents were either not included or not appropriately filed:

1. Form I-9 "Employment Eligibility Verification" from the Department of Homeland Security, U.S. Citizenship and Immigration Services was not included (1 Employee file),
2. Form I-9 employee signature was not available (1 Employee file)
3. The following documentation was not available on employee files:
  - a. Physical examination or health certificate (9 Employee files),
  - b. Evidence of academic preparation (1 Employee file),
  - c. New Withholding Exemption Certificate form (499 R-4.1) from Treasury Department, revised as of 6/30/2011 (24 Employee files),
  - d. ID with photo (6 Employee files),
  - e. Good conduct certificate (1 Employee file),
  - f. Copy of social security card (2 Employee files), and
  - g. Beneficiary designation for retirement (3 Employee files).

**CRITERIA:** To comply with municipal internal controls related to required documents to be included on employee files and with applicable laws and regulations.

For Form I-9, employers must complete it for all newly hired employees to verify their identity and authorization to work in the United States, including a list of approved documents that employees can present to verify their identity and employment authorization.

For form 499 R-4.1 "Withholding Exemption Certificate" the employee must complete this form and submit it to the employer. Otherwise, the employer is required to withhold income taxes without taking into consideration the employees personal exemption, exemption for dependents and allowance based on deductions, pursuant to the

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

Internal Revenue Code of Puerto Rico (IRC). In addition, with the approval of the new IRC on January 31, 2011, form 499 R-4.1 was revised to adjust it to the changes brought by the new code.

**FINDING NUMBER 12-04: DOCUMENTS NOT AVAILABLE ON MUNICIPAL EMPLOYEE FILES (CONTINUED)**

**CAUSE:** The Municipality does not have in operation an appropriate internal control procedure to assure that all these forms are properly completed and included in employee files, and updated periodically.

**EFFECT:** For Form I-9 the U.S. Citizenship and Immigration Services could perform random inspections and fine from \$100 to \$1,100 per missing I-9 forms and documents and, if the problem is persistent, the fine could increase up to \$11,000 per employee. For form 499 R-4.1 "Withholding Exemption Certificate TD could impose penalties for each employee for which withholdings are being made and for whom the form was not prepared and included in their file.

**RECOMMENDATION:** The implementation of an internal control procedure requiring a checklist to be reviewed each time an employee is hired, and when an employee file is updated, to assure all required documents are available. Also, to schedule reviews of employee files for updating purposes.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-05: QUOTATIONS AND RECEIVING REPORTS FOR PURCHASES MADE WERE NOT AVAILABLE**

**CONDITION:** Of a sample of twenty-five (25) disbursements examined,

- a. One (1) disbursement made for a purchase under \$10,000 had only one written quotation instead of three (3) as evidence of price solicitation to suppliers, and
- b. One (1) disbursement made did not have a certification that merchandise received agrees in terms and quantities with the one specified in the purchase order.

**CRITERIA:** As an appropriate internal control procedure, quotations should be requested as evidence of protecting municipal interests. To comply with Chapter 4, sections 2, 14 and 15 of OCAM Ruling for Municipal Administration, which states municipal officials, are responsible for the legality, correctness, completeness and propriety of all disbursements authorized for payment. It also states that the official receiver should carefully check the merchandise and certify in the report that the goods received are consistent with the provisions of the purchase order.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

**FINDING NUMBER 12-05: QUOTATIONS AND RECEIVING REPORTS FOR PURCHASES MADE WERE NOT AVAILABLE (CONTINUED)**

**CAUSE:** The Municipality's internal control procedure to assure that all disbursements prepared have the quotations required by law and receiving reports was not effective enough during this fiscal year. Purchases were not properly verified by the municipal employees preparing them to assure this information was available before the actual purchase is made.

**EFFECT:** The Municipality is not in compliance with:

- a. Chapter 4, sections 2, 14 and 15 of the OCAM Ruling for Municipal Administration and,
- b. Informative Bulletin for the "Purchase Process of the Government of Puerto Rico" published by OCPR.

**RECOMMENDATION:** To strengthen control procedures to assure all purchases and the ultimate disbursements are reviewed in terms of supporting evidence and filed with all required supporting documents, including the written quotations and receiving reports. If quotations and receiving reports are solicited and not received, or if only one supplier is available, we recommend documenting request in a memorandum and attach it together with other supporting documents.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-06: REQUIRED 7% WITHHOLDING AT SOURCE WAS NOT MADE**

**CONDITION:** Of a sample of twenty-five (25) disbursements examined, one (1) disbursement did not have the required 7% withholding at source of payments to individuals for services rendered.

**CRITERIA:** To comply with section 1062.03 (a) of the Puerto Rico IRC of 2011, as amended, which states that the Commonwealth of Puerto Rico and all natural or legal person, who in the exercise of a trade or business activity or for the production of income in Puerto Rico, makes payments to another person for personal services provided in Puerto Rico, must withhold and retain a seven (7) percent from such payments.

**CAUSE:** The Municipality's internal control procedure to assure that all disbursements prepared for personal services have the required 7% withholding at source as required by law was not effective enough during this fiscal year. Disbursements for services rendered were not properly verified by the municipal employees preparing them to assure the withholding was made or if not, that a total waiver certificate was obtained from individual.

**EFFECT:** The Municipality is not in compliance with section 1062.03 (a) of the IRC.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

**FINDING NUMBER 12-06: REQUIRED 7% WITHHOLDING AT SOURCE WAS NOT MADE (CONTINUED)**

**RECOMMENDATION:** To strengthen control procedures to assure all disbursements for personal services are reviewed in terms of proper tax withholding or that an appropriate total waiver certificate is obtained and properly filed before making final payments to individuals.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-07: ASSISTANCE SHEETS NOT SIGNED BY THE SUPERVISOR OR EMPLOYEE AND INCOMPLETE ASSISTANCE SHEETS**

**CONDITION:** Of twenty five (25) assistance sheets requested, one (1) was not signed by the municipal supervisor, one (1) was not signed by the municipal employee, six (6) were not available and for eleven (11) the municipal supervisor did not certify total hours worked by municipal employee.

**CRITERIA:** A sound internal control policy requires that assistance sheets should be reviewed and signed by the municipal employee and supervisor, and properly certified by supervisor, to eliminate the possibility of payment for hours not worked. In addition, they should be properly filed for examination if requested, Also, to comply with general requirements of:

- a. OCAM Ruling for Municipal Administration,
- b. Law No. 81 "Autonomous Municipalities of the CPR", and
- c. Law No. 230 of July 23, 1974 "Puerto Rico Accounting Law", as amended.

**CAUSE:** The Municipality does not have in operation an appropriate internal control procedure to assure that all assistance sheets are reviewed, certified and approved before preparing the payroll. Also, filing procedures were not effective enough during fiscal year 2011-2012.

**EFFECT:** That could result in salaries paid for which the employee does not work or for hours not approved by supervisor. Also, for those not available, no information is available to assure hours worked or approved by supervisor.

**RECOMMENDATION:** One employee should be designated to verify each assistance sheet to be approved by the supervisor and signed by the employee before preparing the payroll. Also, an employee should be designated to oversee proper filing of assistance sheet forms.

**MANAGEMENT RESPONSE:** See corrective action plan.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part II - Findings Related to the Financial Statements: (Continued)**

**FINDING NUMBER: 12-08: LANDFILL CLOSURE AND POST-CLOSURE CARE COSTS NOT ACCUMULATED**

**CONDITION:** The Municipality has not recorded an expense provision and related liability based on the future closure and post-closure care costs that will be incurred near or after the date the landfill no longer accepts waste. This expense provision and related liability must be determined based on a study of the activities that need to be implemented at the Municipality's landfill to comply with applicable laws and regulations, and on the amount of the landfill used during the year.

**CRITERIA:** To comply with the provisions of Section L10 of the Governmental Accounting Standards Board (GASB) Codification related to Landfill Closure and Post-Closure Care Costs.

**CAUSE:** The Municipality has not scheduled or considered contracting the study of the activities that need to be implemented at the Municipality's landfill to comply with applicable laws and regulations.

**EFFECT:** The Statement of Net Assets is understated because the required debt related to closure and post-closure care costs has not being recognized in the financial statements.

**RECOMMENDATION:** As recommended for audit of fiscal year ended June 30, 2011, to consider the feasibility of including on next budget an amount for contracting the study of the activities that need to be implemented at the Municipality's landfill to comply with applicable laws and regulations.

**MANAGEMENT RESPONSE:** See corrective action plan.

**Part III - Findings and Questioned Costs Related to Federal Awards:**

Presentation follows compliance requirements included in the Compliance Supplement of OMB Circular A-133 "Audits of States, Local Governments, and Non-profit Organizations".

**A - Activities Allowed or Unallowed**

**FINDING NUMBER 12-09: DISBURSEMENT ORDER WITHOUT SIGNATURE OF MUNICIPAL OFFICIALS**

**FEDERAL PROGRAM:** CFDA #14.871 - Section 8 Housing Choice Voucher Program

**CONDITION:** Of a sample of ten (10) disbursements examined, one (1) disbursement order did not have the signature of the Municipal Official Payer.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**A - Activities Allowed or Unallowed**

**FINDING NUMBER 12-09: DISBURSEMENT ORDER WITHOUT SIGNATURE OF MUNICIPAL OFFICIALS (CONTINUED)**

**CRITERIA:** As an appropriate internal control procedure, all supporting documents of disbursement transactions should be authorized by Mayor, Disbursing Officer, Finance Director and Pre-intervention In-charge. Also, to comply with OMB A-87, which states that municipal officials are responsible for the legality, correctness, completeness and propriety of all disbursements authorized for payment.

**CONTEXT:** We selected ten (10) disbursements made during the fiscal year 2011-2012 and verified the supporting documents for the disbursements selected. Condition represents ten (10) percent of the sample selected.

**CAUSE:** The Municipality's internal control procedure to assure that all disbursements prepared have the appropriate authorizations from municipal officials was not effective enough during this fiscal year.

**EFFECT:** The Municipality is not in compliance with OMB-Circular A-87.

**RECOMMENDATION:** To strengthen control procedures to assure all disbursements are properly authorized by municipal officials and filed with all required supporting documents.

**QUESTIONED COSTS:** None.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-10: SUPPORTING DOCUMENTS NOT AVAILABLE FOR DISBURSEMENTS MADE**

**FEDERAL PROGRAM:** CFDA #14.228 - Community Development Block Grant/States Program (SBGP)

**CONDITION:** From a sample of ten (10) disbursements examined, two (2) disbursements made for permanent improvements did not have a contractor certification approved by a municipal inspector, supervisor and contractor.

**CRITERIA:** As an appropriate internal control procedure, for permanent improvements a certification from contractor should be requested as evidence of protecting municipal interests and price solicitation. Also, to comply with OMB A-87, which states that municipal officials are responsible for the legality, correctness, completeness and propriety of all disbursements authorized for payment.

Also, Title 24 - Housing and Urban Development, Volume 1 of the Code of Federal Regulations, Part 85, "Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments (Common Rule)", Subpart C - "Changes, Property, and Subawards", Section 20 (b)(6) requires that federal award disbursement be supported by appropriate documentation.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**A - Activities Allowed or Unallowed**

**FINDING NUMBER 12-10: SUPPORTING DOCUMENTS NOT AVAILABLE FOR DISBURSEMENTS MADE (CONTINUED)**

**CONTEXT:** We select ten (10) disbursements made during the fiscal year 2011-2012 and verified the supporting documents for the disbursements selected. Condition represents twenty (20) percent of the sample selected.

**CAUSE:** The Municipality's internal control procedure to assure that all disbursements prepared have all supporting documents required by law and regulations was not effective enough during this fiscal year.

**EFFECT:** The Municipality is not in compliance with OMB-Circular A-87 and could result in questioned cost.

**RECOMMENDATION:** To strengthen control procedures to assure all disbursements are reviewed in terms of supporting evidence and filed with all required supporting documents, including the certifications for construction projects.

**QUESTIONED COSTS:** \$178,462.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-11: SUPPORTING DOCUMENTS OF DISBURSEMENT TRANSACTIONS WERE NOT STAMPED AS CANCELLED PAID**

**FEDERAL PROGRAM:** CFDA #14.228 - Community Development Block Grant/States Program (SBGP)

**CONDITION:** Two (2) disbursements out of a sample of 10 (ten) were not cancelled as paid.

**CRITERIA:** Sound Government management requires that supporting documents of disbursement transactions be identified as paid, to avoid duplication of payment in the future. Also, OMB Circular A-87, "Costs Principles for State, Local, and Indian Tribal Governments", states general requirements for the allowability of costs charged to a federal award. As stated in that circular, disbursements should be identified as "cancelled paid", to eliminate the possibility of duplicating disbursements.

**CONTEXT:** We select ten (10) disbursements made during the fiscal year 2011-2012 and verified the supporting documents for the disbursements selected. Condition represents twenty (20) percent of the sample selected.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**A - Activities Allowed or Unallowed**

**FINDING NUMBER 12-11: SUPPORTING DOCUMENTS OF DISBURSEMENT TRANSACTIONS WERE NOT STAMPED AS CANCELLED PAID (CONTINUED)**

**CAUSE:** The Municipality's internal control procedure to assure that all disbursements prepared were identified as paid was not effective enough during this fiscal year.

**EFFECT:** If invoices and other supporting documents of the disbursements are not identified as paid, payment of invoices already paid could be made.

**RECOMMENDATION:** The municipality should strengthen control procedures to ascertain that all disbursement vouchers and its supporting documents are properly identified as "canceled paid", to avoid the possibility of paying twice.

**QUESTIONED COSTS:** None.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-12: REQUIRED WITHDRAWAL OF 10% ON DISBURSEMENTS FOR PERMANENT IMPROVEMENTS WAS NOT MADE**

**FEDERAL PROGRAM:** CFDA #14.228 - Community Development Block Grant/States Program (SBGP)

**CONDITION:** From a sample of ten (10) disbursements examined, two (2) disbursements made for partial payment of permanent improvements did not have the required ten (10) percent withholding.

**CRITERIA:** To properly safeguard municipal interests, for permanent improvements a ten (10) percent withholding at source from each partial payment is required until permanent improvement is completed. Also, to comply with OMB A-87, which states that municipal officials are responsible for the legality, correctness, completeness and propriety of all disbursements authorized for payment.

Also, Title 24 - Housing and Urban Development, Volume 1 of the Code of Federal Regulations, Part 85, "Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments (Common Rule)", Subpart C - "Changes, Property, and Subawards", Section 20 (b)(6) requires that federal award disbursement be supported by appropriate documentation.

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

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**A - Activities Allowed or Unallowed**

**CONTEXT:** We select ten (10) disbursements made during the fiscal year 2011-2012 and verified the supporting documents for the disbursements selected. Condition represents twenty (20) percent of the sample selected.

**CAUSE:** The Municipality's internal control procedure to assure that the required ten (10) percent withholding is made for all partial payments for permanent improvements was not effective enough during this fiscal year.

**EFFECT:** The Municipality is not in compliance with OMB-Circular A-87 and could result in questioned cost. Also, the Municipality is not properly safeguarding its interests in the event a contractor fails to finish a construction project.

**RECOMMENDATION:** To strengthen control procedures to assure all disbursements for partial payment of permanent improvements are reviewed in terms of the required ten (10) percent withholding.

**QUESTIONED COSTS:** None.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-13: QUOTATIONS NOT AVAILABLE FOR PURCHASES MADE**

**FEDERAL PROGRAM:** CFDA #14.228 - Community Development Block Grant/States Program (SBGP)

**CONDITION:** Four (4) disbursements made for purchases under \$10,000 from a sample of ten (10) disbursements examined did not include, as part of the supporting documents, written quotations as evidence of price solicitation to suppliers.

**CRITERIA:** As an appropriate internal control procedure, written quotations should be requested as evidence of protecting municipal interests and documenting price solicitation under federal awards. Also, to comply with OMB Circular A-87 "Cost Principles for State, Local and Indian Tribal Governments", which states that officials managing federal awards are responsible for the legality, correctness, completeness and propriety of all disbursements authorized for payment.

Also, Title 24 - Housing and Urban Development, Volume 1 of the Code of Federal Regulations, Part 85, "Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments" (Common Rule), Subpart C - "Changes, Property, and Subawards", Section 20 (b)(6) requires that disbursements under federal awards be supported by appropriate documentation, including written quotations.

**CONTEXT:** We selected ten (10) disbursements made under CDBG funds during the fiscal year 2011-2012 and verified their related supporting documents available. Condition represents forty (40) percent of the sample selected.

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

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**A - Activities Allowed or Unallowed**

**FINDING NUMBER 12-13: QUOTATIONS NOT AVAILABLE FOR PURCHASES MADE (CONTINUED)**

**CAUSE:** The internal control procedures implemented by the Federal Awards Department of the Municipality to assure that all disbursements prepared have the quotations required by laws and regulations, was not effective enough during this fiscal year. Purchases were not properly verified by the Federal Awards Department employees preparing them to assure this information was available before the actual purchase is made.

**EFFECT:** Price solicitation under federal awards is not properly documented and disbursements under federal awards are not properly supported by appropriate documentation, representing a noncompliance with OMB-Circular A-87 and with Title 24 - Housing and Urban Development, as described above.

**RECOMMENDATION:** To strengthen control procedures to assure all disbursements are reviewed in terms of supporting evidence and filed with all required supporting documents, including the written quotations. If quotations are solicited and not received, or if only one supplier is available, we recommend documenting request in a memorandum and attach it together with other supporting documents.

**QUESTIONED COSTS:** \$7,570.

**MANAGEMENT RESPONSE:** See corrective action plan.

**FINDING NUMBER 12-14: SUPPORTING DOCUMENTS OF DISBURSEMENT TRANSACTIONS INCOMPLETE**

**FEDERAL PROGRAM:** CFDA #14.228 - Community Development Block Grant/States Program (SBGP)

**CONDITION:** Of a sample of ten (10) disbursements examined,

- a. One (1) disbursement made for a purchase under \$10,000 does not include a written certification stating that merchandise was received and agrees in quantities and specifications to the purchase order, and
- b. One (1) disbursement made for a transaction over \$10,000 did not have its supporting documents stamped and signed as pre-intervened by the Pre-intervention Officer.

**CRITERIA:** As an appropriate internal control procedure, written receiving reports should be requested as evidence that merchandise was received. Also, pre-intervention officer should review disbursement orders and its supporting documents at all times. Doing so helps protect municipal interests. Also, to comply with OMB Circular A-87 "Cost Principles for State, Local and Indian Tribal Governments", which states that officials managing federal awards are responsible for the legality, correctness, completeness and propriety of all disbursements authorized for payment.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**A - Activities Allowed or Unallowed**

**FINDING NUMBER 12-14: SUPPORTING DOCUMENTS OF DISBURSEMENT TRANSACTIONS INCOMPLETE (CONTINUED)**

Also, Title 24 - Housing and Urban Development, Volume 1 of the Code of Federal Regulations, Part 85, "Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments" (Common Rule), Subpart C - "Changes, Property, and Subawards", Section 20 (b)(6) requires that disbursements under federal awards be supported by appropriate documentation, including receiving reports.

**CONTEXT:** We selected ten (10) disbursements made under CDBG funds during the fiscal year 2011-2012 and verified their related supporting documents available. Condition represents twenty (20) percent of the sample selected.

**CAUSE:** The internal control procedures implemented by the Federal Awards Department of the Municipality to assure that all disbursements prepared have the receiving reports and reviewed by the pre-intervention officer, as required by laws and regulations, was not effective enough during this fiscal year. Purchases were not properly verified by the Federal Awards Department employees preparing them to assure this information was available before the actual disbursement is made.

**EFFECT:** Purchase of merchandise is not properly documented and disbursements under federal awards are not properly supported by appropriate documentation, representing a noncompliance with OMB-Circular A-87 and with Title 24 - Housing and Urban Development, as described above.

**RECOMMENDATION:** To strengthen control procedures to assure all disbursements are reviewed in terms of supporting evidence, filed with all required supporting documents, and reviewed by the pre-intervention officer. We recommend that the Official Payer return back any disbursement order that lacks signature of the pre-intervention officer for his/her review before making actual disbursement.

**QUESTIONED COSTS:** \$65,456.

**MANAGEMENT RESPONSE:** See corrective action plan.

**B - Allowable Costs/Costs Principles**

See A above, also applies to allowable costs/cost principles.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**C - Cash Management**

**FINDING NUMBER: 12-15: FEDERAL ASSISTANCE NOT USED TO COVER IMMEDIATE EXPENDITURES**

**FEDERAL PROGRAM: CFDA #14.228 - Community Development Block Grant/States Program (SBGP), CFDA #14.871 - Section 8 Housing Choice Voucher Program**

**CONDITION:** Municipality requested federal financial assistance and was not used to cover immediate expenditures incurred. On those instances, the Municipality required approximately from four (4) to ninety (84) labor days to disburse the amounts requested.

<b>Federal Awards Receipt Date</b>	<b>Date Awards Were Used</b>	<b>Lapse of Time Between Receipt and Use of Awards</b>	<b>Deposited Amount</b>
<b>Program: SBGP</b>			
7/06/2011	9/28/2011	84	\$ 202,882
1/18/2012	1/30/2012	12	200,378
6/18/2012	6/22/2012	4	401,394
<b>Program: Section 8</b>			
12/1/2011	12/05/2011	4	22,870
3/01/2012	3/30/2012	29	52,086
5/01/2012	6/05/2012	35	50,410

**CRITERIA:** As stated on U.S. Treasury Department Circular 1075, Code of Federal Regulations, 45 CFR, Part 74, Subpart C, Section 74.21(b)(5) "Standards for financial management systems" and CFR 74.22(a) "Payments", written procedures must be implemented to minimize the time elapsing between the transfer of funds to the recipient from the U.S. Treasury Department and the issuance or redemption of checks, warrants or payments by other means for program purposes by the recipient.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**C - Cash Management**

**FINDING NUMBER: 12-15: FEDERAL ASSISTANCE NOT USED TO COVER IMMEDIATE EXPENDITURES (CONTINUED)**

**CONTEXT:** We selected eight deposits received by the Municipality during the year. Then we verified the checks disbursed beginning the same date of the amount deposited. We verified the time frame used by the Municipality to disburse all the amount deposited and determine if the Municipality is in compliance with the cash management requirement. Also, we verified the bank accounts in order to determine if the amount on bank is reasonable or not.

**CAUSE:** Municipality submits a request of federal funds to federal agency and takes more than 3 (three) days to expend the funds. Therefore, the Municipality's internal control procedures to comply with this requirement were not effective enough during fiscal year 2011-12.

**EFFECT:** The federal programs department is requesting funds in excess of the immediate expenditures incurred or their immediate program needs, not complying with CFR 45 CFR, Part 74, Subpart C, Section 74.21, mentioned above.

**RECOMMENDATION:** To strengthen the system for requesting federal funds to be adequate enough to satisfy immediate expenditures incurred by each federal programs, and to avoid maintaining excessive cash balances in bank accounts. Also to assure that each disbursement is identified to specific needs detailed on funds request.

**QUESTIONED COSTS:** None.

**MANAGEMENT RESPONSE:** See corrective action plan.

**D - Davis - Bacon Act**

**FINDING NUMBER 12-16: CONTRACTOR'S PAYROLL NOT AVAILABLE FOR VERIFICATION**

**FEDERAL PROGRAM:** CFDA #14.228 - Community Development Block Grant/States Program (SBGP)

**CONDITION:** For a sample of two (2) contractor contracts selected, for one (1) the Municipality did not required to its contractors the submission of payrolls, to ascertain that laborers and mechanics were paid the prevailing wages rates established by the Department of Labor at the time of the construction payroll.

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

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**D - Davis - Bacon Act**

**FINDING NUMBER 12-16: CONTRACTOR'S PAYROLL NOT AVAILABLE FOR VERIFICATION (CONTINUED)**

**CRITERIA:** The United States Code (USC) Title 40, Sections 276 a to 276 a-7, states that "for every contract in excess of \$ 2,000, for construction, alteration, and/or repair, including painting and decorating, of public buildings, and which requires or involves the employment of mechanics and/or laborers, the contractor shall pay all mechanics and laborers employed directly upon the site of the work, the full amounts accrued at time of payment, computed at wage rates not less than those stated in the advertised specifications, regardless of any contractual relationship which may be alleged to exist between the contractor or subcontractor and such laborers and mechanics". Therefore, the municipality is responsible to ensure that contractors and subcontractors comply with these requirements.

**CONTEXT:** We requested two (2) contractor's payroll in order to verify the wage rates paid by the contractor and if laborers and mechanics were paid full amounts accrued at time of payment, computed at wage rates not less than those stated in the advertised specifications. For one contract the Federal Awards Department of the Municipality did not perform the procedure. Condition represents fifty (50) percent of the sample selected.

**EFFECT:** The municipality is not in compliance with The United States Code (USC) Title 40, Sections 276 a to 276 a-7, and in the event that any laborer or mechanic employed by the contractor or subcontractor directly on the site of the work covered by the contract has been paid or is being paid a rate of wages less than the rate of wages required by the contract to be paid as aforesaid, the government may, by written notice to the contractor or subcontractor, terminate his right to proceed with the work or such part of the work as to which there has been a failure to pay said required wages and to prosecute the work to completion by contract or otherwise.

**RECOMMENDATION:** To strengthen control procedures to assure that contractors paid with federal funds submit payrolls for all employees of contractors and/or subcontractors working at project sites, to ensure prevailing wages are paid throughout the contract. Also to instruct a person to monitor payment of prevailing wage rates in those contracts. This includes requiring contractors and/or subcontractors to submit payroll reports and rates paid to employees by their job classifications, to permit verification of compliance.

**QUESTIONED COSTS:** None.

**MANAGEMENT RESPONSE:** See corrective action plan.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**E - Eligibility**

**FINDING NUMBER 12-17: TENANTS'S FILES INCOMPLETE**

**FEDERAL PROGRAM: CFDA #14.871 - Section 8 Housing Choice Voucher Program**

**CONDITION:** For twelve (12) tenants files observed, the following documents were not available:

- HUD form 52517 "Request for Tenancy Approval" was not available in tenant file", 1 instance, representing 8% of sample,
- HUD form 52641 "Housing Assistance Payments Contract" (HAP) was not available, 4 instances, representing 33% of sample,
- HUD form 9886 "Authorization for the Release of Information/Privacy Act Notice" was not available, 2 instances, representing 17% of sample,
- Municipal memorandum of family obligations (Participant's Obligations) was not available, 1 instance, representing 8% of sample,
- Criminal background checks (Good Conduct Certificate) for one or more tenants over 18 years was not available for all members of the family, 3 instances, representing 25% of sample,
- Unit failed inspection but a notice to landlord was not found in tenant file, 2 instances, representing 17% of sample, and
- Utility allowance in HUD 52667 does not match amount claimed in current 50058, 1 instance, representing 8% of sample.

**CRITERIA:** Title 24 Housing and Urban Development, Volume 1, Code of Federal Regulations, Sections 5.230 and 5.617 requires the tenant and other family members, as a condition of admission or continued occupancy, to provide the necessary information, documentation, and releases for the Public Housing Administration to verify income eligibility. This is necessary to document proper verification and determination of eligibility of tenants. Regarding tenant's applications, the Public and Indian Housing Compliance Supplement for Annual Audits of Public Housing Agencies and Indian Housing Authorities (Sections B183 to B184 Chapter 6 Occupancy), requires the housing administrator to keep tenant's applications in files.

In addition, data collected on Form HUD-50058 provides the Municipality and the Department of Housing and Urban Development (HUD) with a picture of the people who participate in subsidized housing programs.

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

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**E - Eligibility**

**FINDING NUMBER 12-17: TENANTS'S FILES INCOMPLETE (CONTINUED)**

**CONTEXT:** We selected twelve (12) tenant's files for section 8 programs and verify the documents available on files. Percentage relation of conditions to findings is included above in the condition section.

**CAUSE:** The Federal Awards Department of the Municipality has available a checklist with all the necessary forms required to document eligibility verification on tenant's files, nevertheless, due care is not exercised to assure that this checklist is properly completed and that all documentation is available and provided by tenants.

**EFFECT:** Public Housing Administration may be qualifying tenants that do not provide the necessary documentation for occupancy, and therefore, there is no complete documentation of the Public Housing Administration verification of eligibility, since documents are not available on files.

**RECOMMENDATION:** The Municipality should strengthen verification to assure they include all the necessary documents required to document eligibility verification to tenants.

**QUESTIONED COSTS:** None.

**MANAGEMENT RESPONSE:** See corrective action plan.

**F - Equipment and Real Property Management**

**FINDING NUMBER 12-18: PROPERTY RECORDS OF ALL FEDERAL AWARDS (Finding Also Applies to the Financial Statements)**

**FEDERAL PROGRAMS:** CFDA #14.228 - Community Development Block Grant/States Program (SBGP), CFDA #14.871 - Section 8 Housing Choice Voucher Program, CFDA #97.036 – Disaster Grants – Public Assistance

**CONDITION:** According to Code of Federal Regulations (CFR), Title 24, Housing and Urban Development, Part 85, Subpart C, Section 85.32, (d)(1); (2):

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**F - Equipment and Real Property Management**

**FINDING NUMBER 12-18: PROPERTY RECORDS OF ALL FEDERAL AWARDS (Finding Also Applies to the Financial Statements)(CONTINUED)**

1. Property records must be maintained that include a description of the property, a serial number or other identification number, the source of property, who holds title, the acquisition date, and cost of the property, percentage of federal participation in the cost of the property, the location, use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property, and
2. A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years.

As indicated on auditors' reports of prior fiscal years, the Municipality does not have available complete property records, based on a physical inventory counts. At present, records are maintained by the property office, by dependency, with a description of the property items, amount of items, property number assigned, cost, the property items acquired during the year, items retired from property records, and final balance. The records do not provide information as to acquisition dates, disbursement order number, property transfer, and if property was acquired with state or federal funds. Also, property records lack information on Municipal building and facilities, land lots acquired, and the amount of construction in progress for the buildings and facilities in construction stages is not accurately maintained as of June 30, 2012. Therefore, there is no reasonable assurance that property records includes all property physically in existence and owned by the Municipality, and excludes all property not in existence or damaged, as of June 30, 2012.

**CRITERIA:** As an appropriate internal control procedure, and to comply with CFR 24, Title 85, Subpart C, Section 85.32, which states that a complete set of records should be maintained in order to assure all balances are correct and properly recorded.

**CAUSE OF CONDITION:** There is no uniform control procedure requiring a standard and complete set of property records, as required by Common Rule.

**EFFECT:** Accurate and complete financial information of property is not available.

**RECOMMENDATION:** The Municipality should perform a physical inventory and reconcile it with the present accounting records, adjust any differences found and identify if property item as are acquired with state or federal awards. Also, to implement a procedure that includes the recording of every property items purchased or constructed in the subsidiary records before use it.

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

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**F - Equipment and Real Property Management**

**FINDING NUMBER 12-18: PROPERTY RECORDS OF ALL FEDERAL AWARDS (Finding Also Applies to the Financial Statements) (CONTINUED)**

**QUESTIONED COSTS:** None

**MANAGEMENT RESPONSE:** See corrective action plan.

**G - Matching, Level of Effort and Earmarking**

No Conditions Detected.

**H - Period of Availability of Federal Funds**

No Conditions Detected.

**I - Procurement and Suspension and Debarment**

No Conditions Detected.

**J - Program Income**

No Conditions Detected.

**K - Real Property Acquisition and Relocation Assistance**

No Conditions Detected.

**L - Reporting**

**FINDING NUMBER: 12-19: SUBMISSION OF SBGP FINANCIAL REPORTS TO OCAM**

**FEDERAL PROGRAM: #14.228 - Community Development Block Grant/States Program (SBGP)**

**CONDITION:** During fiscal year 2011-12 the Federal Awards Department of the Municipality is not delivering, within the required time limits, the financial reports related to the administration of the federal awards to neither the awarding agency nor the Commissioner's Office for Municipal Affairs (OCAM).

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF VIEQUES**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2012**

**Part III - Findings and Questioned Costs Related to Federal Awards: (Continued)**

**L - Reporting**

**FINDING NUMBER: 12-19: SUBMISSION OF SBGP FINANCIAL REPORTS TO OCAM (CONTINUED)**

**CRITERIA:** As required by federal regulations, recipients of federal awards should use the standard financial reporting forms or such other forms as may be authorized by OMB. These other forms may include financial, performance, and special reporting. Each recipient must report program outlays and program income on a cash or accrual basis, as prescribed by the Federal awarding agency, and submit reports within due dates, in this case, five (5) days after end of quarter.

**CONTEXT:** We select the four (4) quarterly reports for the SBGP programs and reviewed the reports in terms of completeness and submission date. There is no evidence that the quarterly reports of September 2011, December 2011, March 2012, and June 2012 were not submitted on time, representing this condition 100% of the reports submitted during the fiscal year.

**CAUSE:** The Municipality's internal control procedure to assure that reports related to the administration of the federal awards are prepared and send to the respective agencies within time limits required was not effective enough during fiscal year 2011-2012

**EFFECT:** The Federal Programs Department of the municipality is not in compliance with federal regulations regarding financial reporting.

**RECOMMENDATION:** The Federal Awards Department should strengthen control procedures to assure that financial reports of the federal awards are prepared and send to awarding agencies within required time limits. Once reports are prepared, the Federal Awards Department should trace the amounts reported to accounting records that support the schedule of expenditures of Federal awards and verify agreement, accuracy and completeness of the reports and that they agree with the accounting records, and send them within five (5) days after quarter end.

**M - Subrecipient Monitoring**

No Conditions Detected.

**N - Special Tests and Provisions**

No Conditions Detected.

(1) Audit Findings that have been Fully Corrected:

NONE

(2) Audit Findings not Corrected or Partially Corrected:

FISCAL YEAR 2011

**Finding Number** 11-07 **Activities Allowed or Unallowed**  
Disbursement order without signature of Municipal Officials.

**CFDA Number** 14.228

**Questioned Cost** None

**Auditee Comments** Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number** 11-08 **Activities Allowed or Unallowed**  
Supporting documents not available for disbursements made.

**CFDA Number** 14.228, 14.871

**Questioned Cost** None

**Auditee Comments** Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number** 11-09 **Activities Allowed or Unallowed**  
Supporting documents of disbursement transactions were not stamped as cancelled paid.

**CFDA Number** 14.228, 14.871, 14.249

**Questioned Cost** None

**Auditee Comments** Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number** 11-10 **Cash Management**  
Federal Assistance not used to cover immediate expenditures.

**CFDA Number** 14.228, 14.871, 14.249

**Questioned Cost** None

**Auditee Comments** Pending of final determination of the US Department of Housing and Urban Development.

(2) Audit Findings not Corrected or Partially Corrected (cont.):

<b>Finding Number</b>	<b>11-11</b>	<b>Davis-Bacon Act</b> Contractor's payroll not available for verification.
<b>CFDA Number</b>	14.228	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>11-12</b>	<b>Eligibility</b> Tenant's files incomplete.
<b>CFDA Number</b>	14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>11-13</b>	<b>Eligibility</b> Section 8 Programs incomplete waiting list.
<b>CFDA Number</b>	14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>11-14</b>	<b>Equipment and Real Property Management</b> Property records of all federal awards (finding also applies to the Financial Statements).
<b>CFDA Number</b>	14.228, 14.871, 14.249	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>11-15</b>	<b>Reporting</b> Submission of SBGP financial reports to OCAM.
<b>CFDA Number</b>	14.228	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	

(2) Audit Findings not Corrected or Partially Corrected (cont.):

**Finding Number**                      **11-16**                      **Reporting**  
Submission of Section 8 financial reports to the Real Estate Assessment Center's (REAC).

**CFDA Number**                              14.871

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number**                      **11-17**                      **Reporting**  
Section 8 Moderated Rehabilitation Single Room Occupancy Program.

**CFDA Number**                              14.249

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**FISCAL YEAR 2010**

**Finding Number**                      **10-09**                      **Activities Allowed or Unallowed**  
Supporting Documents of Disbursement transactions were not stamped as cancelled paid.

**CFDA Number**                              14.228, 14.871

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number**                      **10-10**                      **Cash Management**  
Federal Assistance not used to cover immediate expenditures.

**CFDA Number**                              14.228, 14.871

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number**                      **10-11**                      **Davis Bacon Act**  
Contractor's payrolls not available for verification.

**CFDA Number**                              14.228

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

(2) Audit Findings not Corrected or Partially Corrected (cont.):

<b>Finding Number</b>	<b>10-12</b>	<b>Eligibility</b> Tenant's Files incomplete.
<b>CFDA Number</b>	14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>10-13</b>	<b>Eligibility</b> Section 8 Programs using different incomplete waiting lists.
<b>CFDA Number</b>	14.871, 14.249	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>10-14</b>	<b>Equipment and Real Property Management</b> Property records of all federal awards.
<b>CFDA Number</b>	14.228, 14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>10-15</b>	<b>Reporting</b> Late submission of the Single Audit Reporting Package.
<b>CFDA Number</b>	14.228, 14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>10-16</b>	<b>Reporting</b> Submission of SBGP Financial Reports to OCAM.
<b>CFDA Number</b>	14.228	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	

(2) Audit Findings not Corrected or Partially Corrected (cont.):

**Finding Number**                      **10-17**                      **Reporting**  
Submission of Section 8 Financial Reports to the Real Estate Assessment Center's (REAC).

**CFDA Number**                              14.871

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**FISCAL YEAR 2009**

**Finding Number**                      **09-1**                      **Davis Bacon Act**  
Deficiencies in the documentation supporting compliance with Davis Bacon Act.

**CFDA Number**                              14.228

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number**                      **09-2**                      **Reporting**  
Quarterly reports were not submitted on a timely basis.

**CFDA Number**                              14.228

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**Finding Number**                      **09-3**                      **Eligibility**  
Missing documentation in participants' files.

**CFDA Number**                              14.871

**Questioned Cost**                              None

**Auditee Comments**                              Pending of final determination of the US Department of Housing and Urban Development.

**FISCAL YEAR 2008**

**Finding Number**                      **08-1**                      **Davis Bacon Act**  
Deficiencies in the documentation supporting compliance with Davis Bacon Act.

**CFDA Number**                              14.228

**Questioned Cost**                              None

<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>(2) Audit Findings not Corrected or Partially Corrected (cont.):</b>		
<b>Finding Number</b>	<b>08-2</b>	<b>Reporting</b> Quarterly reports were not submitted on a timely basis.
<b>CFDA Number</b>	14.228	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>08-3</b>	<b>Allowable Cost/Cost Principles</b> Missing documentation on disbursement vouchers.
<b>CFDA Number</b>	14.228	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>08-4</b>	<b>Eligibility</b> Missing documentation in participants' files.
<b>CFDA Number</b>	14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>FISCAL YEAR 2007</b>		
<b>Finding Number</b>	<b>07-2</b>	<b>Davis Bacon Act</b> Quarterly reports were not submitted on a timely basis.
<b>CFDA Number</b>	14.228	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>FISCAL YEAR 2006</b>		
<b>Finding Number</b>	<b>06-7</b>	<b>Eligibility</b> Missing documentation in participants' files.
<b>CFDA Number</b>	14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	

**(2) Audit Findings not Corrected or Partially Corrected (cont.):**

**FISCAL YEAR 2006**

<b>Finding Number</b>	<b>06-7</b>	<b>Eligibility</b> Missing documentation in participants' files.
<b>CFDA Number</b>	14.871	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	
<b>Finding Number</b>	<b>06-9</b>	<b>Eligibility</b> Missing documentation in participants' files.
<b>CFDA Number</b>	14.856	
<b>Questioned Cost</b>	None	
<b>Auditee Comments</b>	Pending of final determination of the US Department of Housing and Urban Development.	

**(3) Corrective action taken is significantly different from corrective action previously reported:**

NONE

**(4) Audit findings is no longer valid:**

NONE



TORRES, HERNANDEZ & PUNTER, CPA, CSP  
Certified Public Accountants

To the clients and users of the financial statements  
reported upon by Torres, Hernández & Punter CPA, PSC  
Certified Public Accountants

The partners and staff of Torres, Hernández & Punter CPA, CSP are pleased to announce the successful completion of an independent peer review of our accounting and auditing practice. This review was undertaken as a condition of membership in the American Institute of Certified Public Accountants (AICPA), the national organization of CPA's in public practice, industry, government and education. Our participation in the Peer Review Program demonstrates our firm's commitment and desire of maintaining and improving the quality of our practice.

After thorough study of our policies and procedures, the team conducting the review concluded our firm complies with the quality control standards established by the AICPA and the Puerto Rico Society of CPA's (PRSCPA). Our firm is committed to periodic peer review to foster quality performance.

Bankers, bonding agents, investors, suppliers, legal advisors and others use the financial statements our firm audits, reviews, or compiles. We think those people, our clients, and our own staff deserve independent quality assurance that our firm provides quality services. We are proud of our peer review results and would be happy to answer any questions you might have.

Sincerely,

*Torres, Hernández & Punter, CPA, PSC*  
Torres, Hernández & Punter, CPA, CSP

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## System Review Report

To the Partners of  
Torres, Hernandez & Punter, CPA, PSC  
And the Colegio de Contadores Publicos Autorizados  
de Puerto Rico

We have reviewed the system of quality control for the accounting and auditing practice of Torres, Hernandez & Punter, CPA, PSC (the firm) in effect for the year ended October 31, 2009. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants. The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review. The nature, objectives, scope, limitations of, and the procedures performed in a System Review are described in the standards at [www.aicpa.org/prsummary](http://www.aicpa.org/prsummary).

As required by the standards, engagements selected for review included engagements performed under Governmental Auditing Standards and an audit of Employee Benefit Plan.

In our opinion, the system of quality control for the accounting and auditing practice of Torres, Hernandez & Punter, CPA, PSC in effect for the year ended October 31, 2009 has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of pass, pass with deficiency (ies) or fail. Torres, Hernandez & Punter, CPA, PSC has received a peer review rating of pass.

*Ocariz, Gitlin, & Zomerfeld, LLP*

June 17, 2010

Members of:

American Institute of  
Certified Public Accountants

Florida Institute of  
Certified Public Accountants

National Association of  
Certified Valuation Analysts