

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES

BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

YEAR ENDED JUNE 30, 2014

(WITH INDEPENDENT AUDITOR'S REPORT THEREON)

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES

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INDEPENDENT AUDITORS' REPORT

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

Report on the Basic Financial Statements

We have audited the accompanying basic 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, 2014, and the related notes to the financial statements, which collectively comprise the Municipality's 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.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 from material misstatement.

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

Basis for Qualified Opinion on Governmental Activities

Capital Assets

Management of the Municipality has not provided a subsidiary of capital assets that agreed with the amounts reported in the governmental activities of the Governmental-Wide Financial Statements, and accordingly, the depreciation expense on those capital assets is not supported. Accounting principles generally accepted in the United States of America require that those capital assets be supported to present the net assets, net position and expense of the governmental activities. The amount by which this departure would affect the assets, net position and expenses of the governmental activities cannot be reasonably determinable.

Basis for Qualified Opinion on Governmental Activities (Continued)

Liability for Closure and Postclosure Care Cost

Also, as discussed in Note 2.D-11 to the financial statements, the Municipality has not recorded a provision for liability related to the 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 and expenses of governmental activities can not be reasonably determinable.

Qualified Opinion

In our opinion, except for the effects of the matters discussed in the "Basis for Qualified Opinion" paragraph before, the financial statements referred to above present fairly, all material respects, the respective financial position of the governmental activities of the Municipality as of June 30, 2014 and the respective changes in the financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Unmodified Opinions

In our opinion, the financial statements referred to above present fairly, all material respects, the respective financial position of each major fund and the aggregate remaining fund information of the Municipality as of June 30, 2014 and the respective changes in the financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America requires that the management's discussion and analysis on pages 4 through 15 and the budgetary comparison schedule of the general fund and related notes on pages 66 through 67 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 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 financial statements, and other knowledge we obtained during our audit of the 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.

Other Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial statements as a whole. The accompanying Schedule of Expenditures of Federal Awards, as required by U.S. Office of Management and Budget (OMB) Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, on pages 68 through 69, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying 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. Such 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

Other Supplementary Information (Continued)

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 Schedule of Expenditures of Federal Awards are fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated March 25, 2015, on our consideration of the Municipality's internal control over financial reporting and our test 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 in considering the Municipality's internal control over financial reporting and compliance.

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

Carolina, Puerto Rico

March 25, 2015

Stamp #E156294 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, 2014. 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 2014 by \$118,989,675 (net position).
- Revenues increased by (\$682,384) (3%) and expenses decreased by (\$1,488,651) (4.88%) in comparison with year 2013.
- Net decrease in net position amounted to (\$606,734), an increase of \$2,171,035 with respect to prior year (2013) 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:

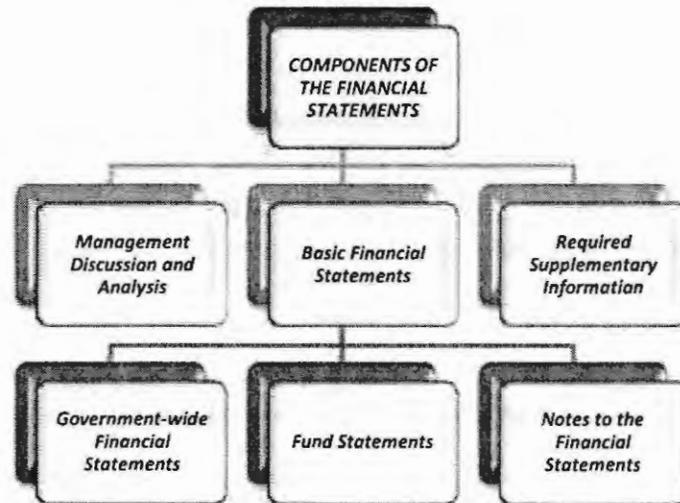
- At the close of the current fiscal year, the **Municipality's** governmental funds reported combined ending fund balances of \$4,509,494, an increase of \$133,079 in comparison with the prior year, as restated.
- The General Fund reported an excess of revenues and other financing sources over expenditures and other financing uses of \$434,748 and an unassigned (deficit) fund balance of (\$3,208,677).

General Financial Highlights

- The investment in net capital assets as of June 30, 2014 was \$121,466,825 (net of related debt).
- Long-term debt general and special obligation bonds decreased to \$11,696,400, approximately 2% with respect to prior year balance.
- Other long term debts increases and net reductions from payments amounted to \$582,190 and \$503,000, respectively.
- On a budgetary basis, actual expenditures exceeded actual revenues and transfers by (\$222,591).

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.

Statement of Net Position –The *Statement of Net Position* presents information on all of the **Municipality's** assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference between them reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether its financial position 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 financial position of the **Municipality**.

Statement of Activities – The *Statement of Activities* presents information showing how the **Municipality's** net position changed during the year. All changes in net position (current year's revenues less expenses) are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave). The *Statement of Activities* is focused on both the gross and net cost of various activities (including governmental and business-type activities). This is intended to summarize and simplify the reader's analysis of the revenues and costs of various state activities and the degree to which activities are subsidized by general revenues.

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

The governmental activities of the **Municipality** include general government, public works and sanitation; public safety, culture and recreation, housing, welfare, and community development and education. These activities are primarily financed through property taxes, other local taxes and intergovernmental revenues.

The government-wide financial statements can be found on pages 16-17 of this report.

◆ **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.

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 \$4,509,494. Approximately \$3.5 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

Statement of Net Position

The following table presents a summary of the Statements of Net Position as of June 30, 2014 and 2013:

Net position (assets plus deferred outflows of resources over liabilities plus deferred inflows of resources) may serve over time as a useful indicator of a government's financial status. Net position for the year had a decrease of only 0.25% with respect to prior year as restated. The most significant change was an increase of the restricted by \$5,265,344. Also, a decrease in assets by (\$2,080,831), and a decrease in long-term liabilities by (\$2,417,158).

The following table presents a summary of the Statements of Net Position as of June 30, 2014 and 2013:

Commonwealth of Puerto Rico Municipality of Vieques Statement of Net Position As of June 30,		
	<u>2014</u>	<u>2013</u>
Current and Non-Current Assets	\$ 8,144,672	\$ 7,995,550
Capital Assets	128,192,215	129,694,426
Total Assets	<u>136,336,887</u>	<u>137,689,976</u>
Current Liabilities	2,939,921	1,244,849
Deferred Revenues	416,465	440,734
Long-Term Liabilities	13,990,826	16,407,984
Total Liabilities	<u>17,347,212</u>	<u>18,093,567</u>
Net Position:		
Investment in Capital Assets, Net of Related Debt	121,466,825	123,547,656
Restricted	8,425,791	3,160,447
Unrestricted	(10,902,941)	(7,111,694)
Total Net Position	<u>\$ 118,989,675</u>	<u>\$ 119,596,409</u>

The largest portion of the **Municipality's** net position reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure) for \$121,466,825; total capital assets (\$174,565,010) less accumulated depreciation (\$46,372,795) and less any related outstanding debt (\$6,725,390) 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 position represents resources that are subject to external restrictions on how they may be used. Unrestricted net position is the part of the net position 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, 2014 the **Municipality** presented unrestricted (deficit) net position of (\$10,902,941). This balance was affected by long term obligations such as compensated absences \$1,619,152, Law 42 \$2,092,450, and other debts for the amount of \$550,372 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.

Statement of Activities

The following Table compares the revenues and expenses for the current and previous fiscal year.

With respect to prior year, revenues increased by approximately \$682 thousand or 3%, principally on operating grants and contributions, and intergovernmental revenue.

Expenses decreased 4.88% or \$1.4 million in comparison with 2013 year. Significant decreases were registered on urban development and on the reimbursement to grantor agency that was present last year, but not this year.

Commonwealth of Puerto Rico Municipality of Vieques Changes in Net Position For Fiscal Year Ending June 30,		
	<u>2014</u>	<u>2013</u>
Revenues:		
Program Revenues:		
Operating Grants and Contributions	\$ 2,205,518	\$ 1,319,076
Capital Grants and Contributions	339,577	-
General Revenues:		
Property Taxes	1,725,887	1,533,002
Volumen of Business Taxes	162,848	560,591
Sales and Usage Taxes	1,099,653	1,029,438
Construction Excise Taxes	360,217	576,468
Intergovernmental	7,482,204	7,102,157
Other General Revenues	510,422	1,083,210
Total Revenues	<u>13,886,326</u>	<u>13,203,942</u>
Expenses:		
General Administration	7,026,978	7,039,316
Public Safety	1,304,961	1,149,998
Public Works	1,481,346	1,467,688
Culture and Recreation	901,532	810,681
Health and Sanitation	522,042	625,840
Public Instruction	-	253,675
Human Services and Welfare	1,793,910	1,631,357
Urban Development	961,502	1,519,005
Reimbursement to Grantor Agency	-	748,560
Interest Costs	500,789	735,591
Total Expenses	<u>14,493,060</u>	<u>15,981,711</u>
Changes in Net Position	(606,734)	(2,777,769)
Net Position-Beginning, as Restated	119,596,409	122,374,178
Net Position-Ending	<u>\$ 118,989,675</u>	<u>\$ 119,596,409</u>

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

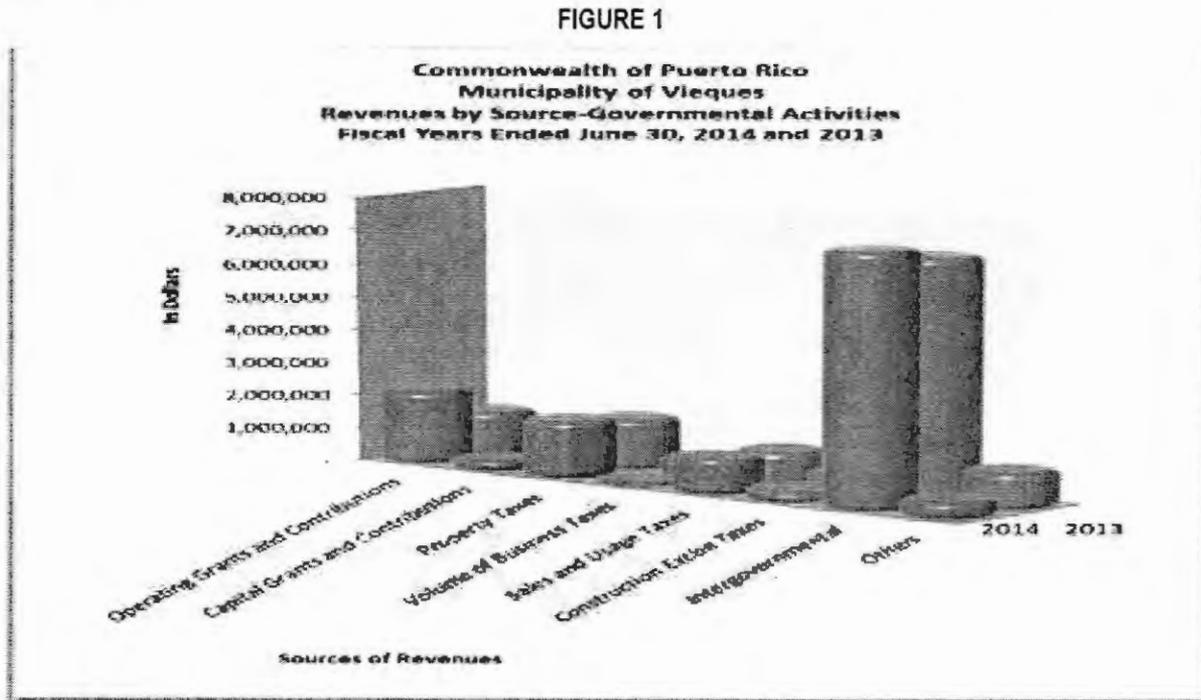
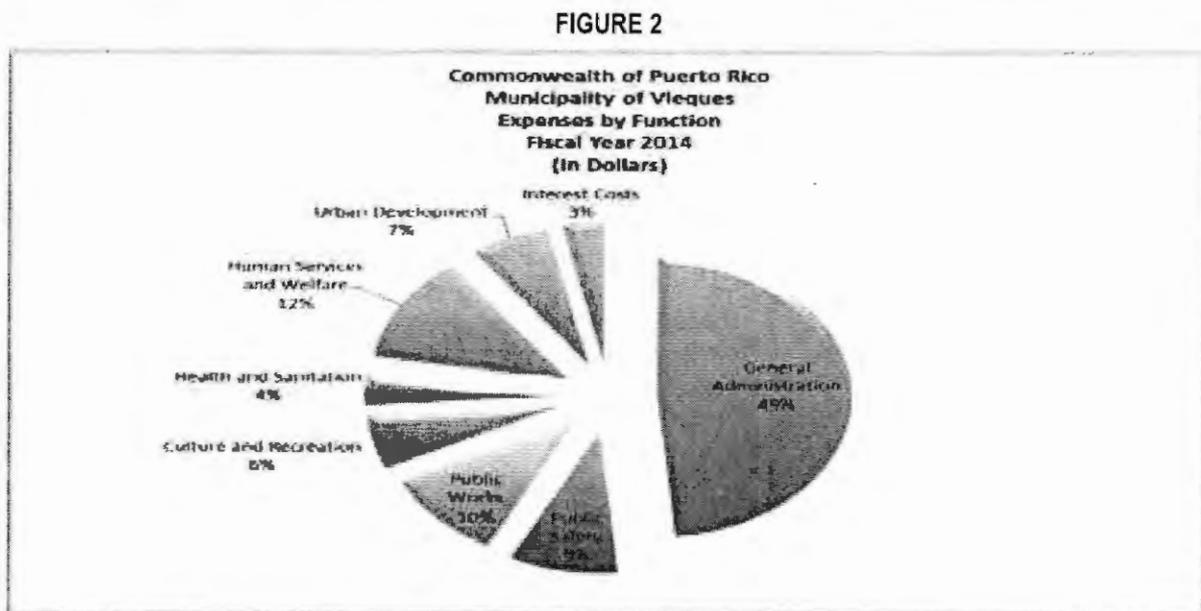


Figure 2 presents expenses by function of the governmental activities during the fiscal year 2013-2014:



Approximately 54% of the **Municipality's** revenues came from intergovernmental, 12% from property taxes, 16% from grants and contributions, and 18% from other sources. The **Municipality's** expenses cover a range of services. The largest expenses are general administration with 48.5%, public works with 10.2%, urban development with 6.6%, human service and welfare with 12.4 % and public safety with 9%. Program revenues of the **Municipality** covered 13% 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
Net Cost of Municipality's Governmental Activities
Fiscal Years ended June 30,**

Functions/Programs	Total Cost of Services		Net Cost of Services	
	2014	2013	2014	2013
General Administration	\$ 7,026,978	\$ 7,039,316	\$ 6,612,228	\$ 7,039,316
Public Safety	1,304,961	1,149,998	1,258,712	1,100,798
Public Works	1,481,346	1,467,688	1,481,346	1,319,833
Culture And Recreation	901,532	810,681	726,877	810,681
Health and Sanitation	522,042	625,840	522,042	625,840
Human Services and Welfare	1,793,910	1,631,357	1,162,443	921,367
Urban Development	961,502	1,519,005	(316,472)	1,106,974
Others	500,789	735,591	500,789	735,591
Total	\$ 14,493,060	\$ 14,979,476	\$ 11,947,965	\$ 13,660,400

Some of the cost of governmental activities in 2014 was paid from other governments and organizations that subsidized certain programs with grants and contributions (\$1,913,910). The \$11,947,965 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. 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.

At the end of the current fiscal year, the **Municipality's** governmental funds reported combined ending fund balances of \$4.5 million. A decrease in the Restricted Fund Balance and Unassigned Fund Balance was mainly due to a restatement of debts between funds.

Table 4

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

	2014	2013
Fund Balances:		
Nonexpendable	\$ -	\$ -
Restricted	7,832,346	11,203,300
Committed	196,273	12,037
Assigned	-	-
Unassigned	(3,519,125)	(6,838,922)
Total	\$ 4,509,494	\$ 4,376,415

The General Fund is the operating fund of the **Municipality**. The General Fund experienced a \$285,426 decrease from a fund balance (deficit) of (\$313,502) (as restated) in the previous year to a fund balance (deficit) of \$121,246 at the end of the current year.

At the end of fiscal year 2014, the General Fund presented both Restricted and Unassigned Fund Balance (Deficit). Restricted Fund Balance of \$3,329,923 comes from a reclassification of the State Assignment Fund as part of the General Fund, in accordance with GASB 54 as explained in the notes to the Financial Statements. 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.

Table 5

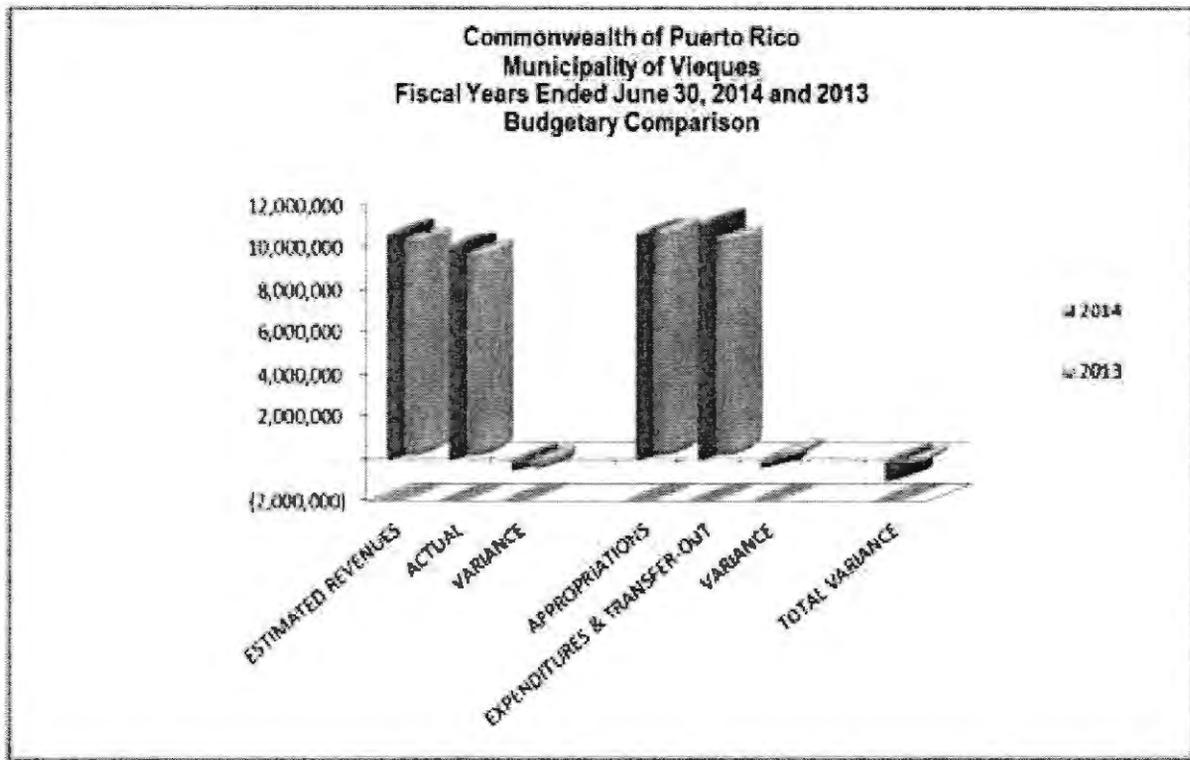
**Commonwealth of Puerto Rico
Municipality of Vieques
General Fund
As of June 30,**

Description	2014	2013
Revenues:		
Property Taxes	\$ 1,037,834	\$ 976,935
Volume of Business Taxes	162,848	560,591
Sales and Usage Taxes	537,876	418,701
Intergovernmental	7,474,088	6,721,370
Construction Excise Taxes	360,217	576,468
Miscellaneous	510,422	1,077,984
Total Revenues	<u>10,083,285</u>	<u>10,332,049</u>
Expenditures:		
General Government	5,924,180	6,475,146
Public Safety	962,869	898,587
Public Work	647,920	744,139
Public Instruction	-	253,675
Culture and Recreation	711,510	609,623
Health and Sanitation	522,042	625,840
Human Services and Welfare	642,831	443,472
Urban Development	66,688	-
Capital Outlay	30,123	23,944
Total Expenditures	<u>9,508,163</u>	<u>10,074,426</u>
Net Transfer In (Out)	(140,374)	27,803
Other Financing Sources	-	-
Net Increase (Decrease) in Fund Balance	<u>\$ 434,748</u>	<u>\$ 285,426</u>

GENERAL FUND BUDGETARY HIGHLIGHTS

The general fund original budget for the fiscal period 2013-2014 presented an increase of 0% 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 Miscellaneous of (\$962,728), Intergovernmental Revenues of (\$852,048), and Volume of Business Taxes of (\$181,527).

FIGURE 3



The positive variance of \$323,544 between revised budget and actual results was due mainly to a decrease in expenditures, especially in General Government of \$2,599,645 which compensated for the negative variance in revenues.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of the fiscal year, the **Municipality** has invested \$128,192,215 (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 \$1,502,211 or 1% from the prior year.

The **Municipality** invested a total of \$553,148 of capital assets during the fiscal year 2013-2014, all of it from Construction in Progress.

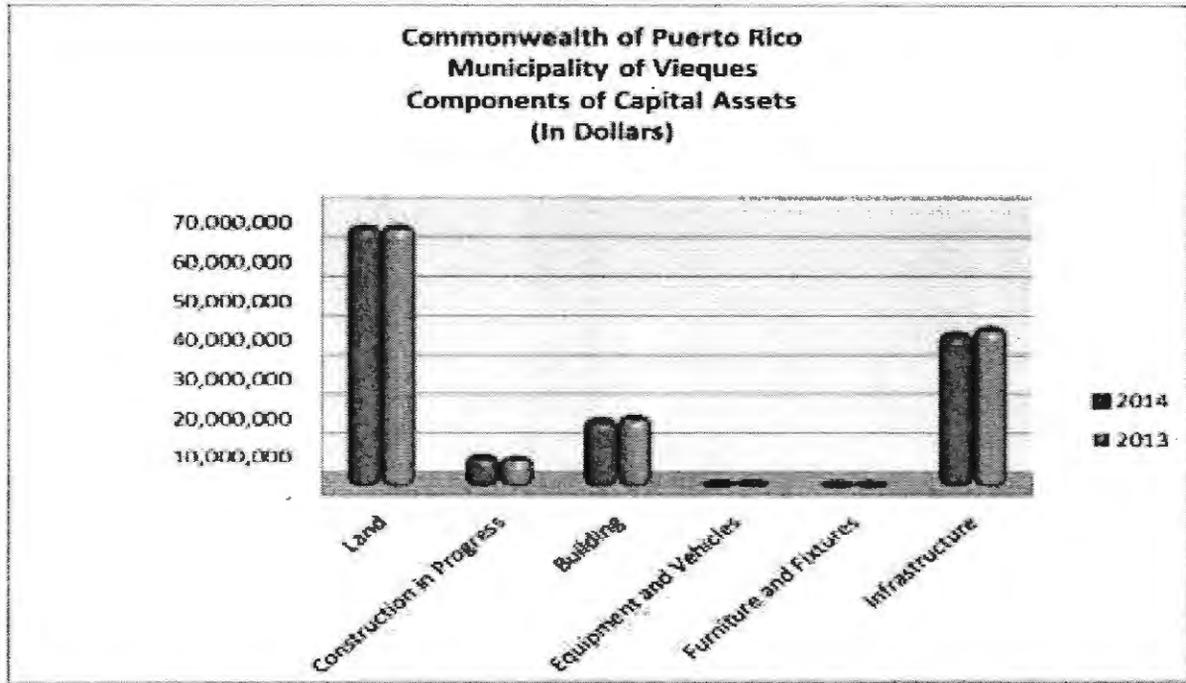
Other projects related to repair and maintenance of roads (not capitalized) was developed during the year 2014.

	Governmental Activities	
	2014	2013
Non-depreciable assets:		
Land	\$ 65,650,752	\$ 65,650,752
Construction in Progress	7,175,452	6,622,304
Depreciable assets:		
Buildings	16,628,864	17,237,309
Equipment and Vehicles	257,874	370,960
Furniture and Fixtures	-	-
Infrastructure	38,479,273	39,813,101
Total	\$ 128,192,215	\$ 129,694,426

Construction in progress was principally for improvement to a passive park and the "Municipal Coliseum".

Figure 4 below presents the components of capital assets during the fiscal years 2014 and 2013:

FIGURE 4



Long-Term Debt

At year-end, the Municipality had \$11,696,400 in general and special obligations, a decrease of 2% with respect to prior year, due to the repayment of principal of \$528,800. The following is a summary of the Municipality's outstanding debt as of June 30, 2014 and 2013:

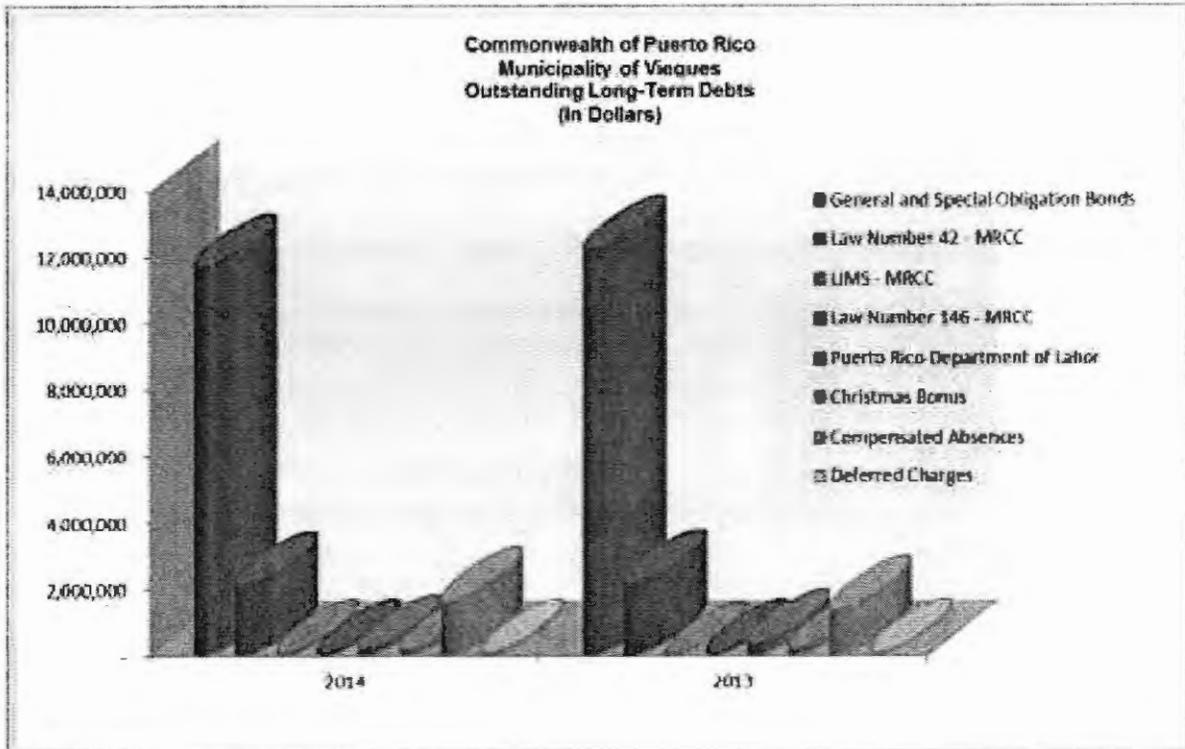
Table 7

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

	2014	2013
General and Special Obligation Bonds	\$ 11,696,400	\$ 12,225,200
Law Number 42 - MRCC	2,092,450	2,151,710
Puerto Rico Aqueduct and Sewer Authority	58,000	-
Law Number 146 - MRCC	64,638	68,228
Puerto Rico Department of Labor	193,692	358,315
Deferred Charges	68,027	68,027
Christmas Bonus	166,015	177,444
Compensated Absences	1,619,152	1,359,060
Total	\$ 15,958,374	\$ 16,407,984

Figure 5 presents the components of long-term debts during the fiscal year 2014 and 2013:

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 2013-2014 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 13.5%, which compares with the Commonwealth rate of 13.1%.

The **Municipality** applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2014-2015 are \$13.1 million, approximately \$1.3 million more than the fiscal year 2013-2014. 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 developed during the year.

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 POSITION

JUNE 30, 2014

	<u>GOVERNMENTAL ACTIVITIES</u>
ASSETS:	
Cash	\$ 1,817,793
Cash with Fiscal Agent	4,244,018
Receivables (Net):	
Property Taxes	8,220
Federal Grants	1,938,049
Due from Government Units	96,838
Sales and Usage Taxes	39,754
Capital Assets:	
Land and Construction in Progress	72,826,204
Other Capital Assets [Net of Accumulated Depreciation]	<u>55,366,011</u>
Total Capital Assets	<u>128,192,215</u>
TOTAL ASSETS	<u>136,336,887</u>
LIABILITIES:	
Accounts Payable and Accrued Expenses	623,276
Accrued Interest	171,730
Due to Governmental Units	177,367
Unearned Revenues - Volume of Business Taxes	416,465
Noncurrent Liabilities:	
Due Within One Year	1,967,548
Due in More than One Year	<u>13,990,826</u>
TOTAL LIABILITIES	<u>17,347,212</u>
NET POSITION:	
Net Investment in Capital Assets	121,466,825
Restricted for:	
Debt Service	1,477,673
Community Development Projects	397,172
Other Purposes	6,550,946
Unrestricted (Deficit)	<u>(10,902,941)</u>
TOTAL NET POSITION	<u>\$ 118,989,675</u>

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES, PUERTO RICO

STATEMENT OF ACTIVITIES

FOR THE FISCAL YEAR ENDED JUNE 30, 2014

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenues and Changes in Net Position
		Charges For Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
Mayor and Municipal Legislature	\$ 1,268,554	\$ -	\$ -	\$ -	\$ (1,268,554)
General Government	5,758,424	291,608	123,142	-	(5,343,674)
Public Safety	1,304,961	-	46,249	-	(1,258,712)
Public Works	1,481,346	-	-	-	(1,481,346)
Culture and Recreation	901,532	-	174,655	-	(726,877)
Health and Sanitation	522,042	-	-	-	(522,042)
Human Services and Welfare	1,793,910	-	631,467	-	(1,162,443)
Urban Development	961,502	-	938,397	339,577	316,472
Interest on Long-Term Debt	500,789	-	-	-	(500,789)
Total Governmental Activities	\$ 14,493,060	\$ 291,608	\$ 1,913,910	\$ 339,577	(11,947,965)
General Revenues:					
Taxes:					
Property Taxes, levied for General Purposes					1,037,834
Property Taxes, levied for Debt Service					688,053
Sales and Usage Taxes					1,099,653
Volume of Business Taxes					162,848
Construction Excise Taxes					360,217
Intergovernmental					7,482,204
Miscellaneous					510,422
Total General Revenues					11,341,231
CHANGES IN NET POSITION					
					(606,734)
Net Position – Beginning of Year					119,596,409
NET POSITION – ENDING OF YEAR					\$ 118,989,675

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES, PUERTO RICO
BALANCE SHEET – GOVERNMENTAL FUNDS
JUNE 30, 2014

	GENERAL FUND	SBGP FUNDS	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS:					
Cash	\$ 900,701	\$ 102	\$ -	\$ 916,990	\$ 1,817,793
Cash with Fiscal Agent	60,613	-	1,959,683	2,223,722	4,244,018
Receivables:					
Property Taxes	-	-	8,220	-	8,220
Sales and Usage Taxes	39,754	-	-	-	39,754
Federal Grants	-	1,938,049	-	-	1,938,049
Due from Other Funds	97,011	-	-	207,119	304,130
Due from Governmental Units	96,838	-	-	-	96,838
<u>Total Assets</u>	<u>\$ 1,194,917</u>	<u>\$ 1,938,151</u>	<u>\$ 1,967,903</u>	<u>\$ 3,347,831</u>	<u>\$ 8,448,802</u>
LIABILITIES:					
Account Payable	\$ 314,954	\$ 10,138	\$ -	\$ 298,184	\$ 623,276
Bond Payable	-	-	318,500	-	318,500
Accrued Interest	-	-	171,730	-	171,730
Due to Governmental Units	38,295	-	-	139,072	177,367
Due to Other Funds	207,119	97,011	-	-	304,130
Unearned Revenues - Volume of Business Taxes	416,465	-	-	-	416,465
<u>Total Liabilities</u>	<u>976,833</u>	<u>107,149</u>	<u>490,230</u>	<u>437,256</u>	<u>2,011,468</u>
DEFERRED INFLOWS OF RESOURCES:					
Unavailable Revenues - Commonwealth of Puerto Rico	96,838	-	-	-	96,838
Unavailable Revenues - Federal Grants	-	1,831,002	-	-	1,831,002
<u>Total Deferred Inflows of Resources</u>	<u>96,838</u>	<u>1,831,002</u>	<u>-</u>	<u>-</u>	<u>1,927,840</u>
FUND BALANCES (DEFICITS):					
Restricted	3,329,923	-	1,477,673	3,024,750	7,832,346
Committed	-	-	-	196,273	196,273
Assigned	-	-	-	-	-
Unassigned (Deficit)	(3,208,677)	-	-	(310,448)	(3,519,125)
<u>Total Fund Balances</u>	<u>121,246</u>	<u>-</u>	<u>1,477,673</u>	<u>2,910,575</u>	<u>4,509,494</u>
Total Liabilities, Deferred Inflows of Resources and Fund Balances (Deficits)	\$ 1,194,917	\$ 1,938,151	\$ 1,967,903	\$ 3,347,831	\$ 8,448,802

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

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

JUNE 30, 2014

Total Fund Balances – Government Funds (Page 18) **\$ 4,509,494**

Amount reported for Governmental Activities in the Statement of Net Position (Page 16)
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	\$ 72,826,204	
Depreciable Capital Assets	35,047,417	
Infrastructure Assets	66,691,389	
Accumulated Depreciation	<u>(46,372,795)</u>	
Total Capital Assets		128,192,215

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 unavailable in the funds:

CDBG	1,831,002	
Christmas Bonus Reimbursement	<u>96,838</u>	
Total Unavailable Revenues		1,927,840

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

General and Special Obligation Bonds	(11,377,900)	
PR Department of Labor	(193,692)	
Christmas Bonus	(166,015)	
Compensated Absences	(1,619,152)	
Law Number 146 – MRCC	(64,638)	
AAA	(58,000)	
Law Number 42 – MRCC	(2,092,450)	
Claims and Judgments	<u>(68,027)</u>	
Total Long-Term Liabilities		<u>(15,639,874)</u>

Total Net Position of Governmental Activities (Page 16) **\$ 118,989,675**

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

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, 2014

	GENERAL FUND	SBGP FUNDS	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
REVENUES:					
Property Taxes	\$ 1,037,834	\$ -	\$ 688,053	\$ -	\$ 1,725,887
Volume of Business Taxes	162,848	-	-	-	162,848
Sales and Usage Taxes	537,876	-	561,777	-	1,099,653
Federal Grants	-	541,225	-	611,581	1,152,806
Intergovernmental	7,474,088	-	-	703,509	8,177,597
Construction Excise Taxes	360,217	-	-	-	360,217
Rent	9,805	-	-	-	9,805
Miscellaneous	500,617	-	-	291,608	792,225
Total Revenues	10,083,285	541,225	1,249,830	1,606,698	13,481,038
EXPENDITURES:					
Current:					
Mayor and Municipal Legislature	651,946	-	-	-	651,946
General Government	5,272,234	138,786	-	75,876	5,486,896
Public Safety	962,869	-	-	95,449	1,058,318
Public Works	647,920	-	-	319,586	967,506
Culture and Recreation	711,510	-	-	25,593	737,103
Health and Sanitation	522,042	-	-	-	522,042
Human Services and Welfare	642,831	-	-	883,883	1,526,714
Urban Development	66,688	434,076	-	343,583	844,347
Capital Outlay	30,123	-	-	523,025	553,148
Debt Service:					
Principal	-	-	499,150	-	499,150
Interest and Other Charges	-	-	500,789	-	500,789
Total Expenditures	9,508,163	572,862	999,939	2,266,995	13,347,959
EXCESS OF REVENUES OVER (UNDER)					
EXPENDITURES	575,122	(31,637)	249,891	(660,297)	133,079
OTHER FINANCING SOURCES (USES):					
Transfers – In	546,135	-	438,602	247,907	1,232,644
Transfers – Out	(686,509)	-	(406,815)	(139,320)	(1,232,644)
Total Other Financing Sources (Uses)	(140,374)	-	31,787	108,587	-
Net Change in Fund Balances	434,748	(31,637)	281,678	(551,710)	133,079
Fund Balances (Deficit) – Beginning	(313,502)	31,637	1,195,995	3,462,285	4,376,415
FUND BALANCES (DEFICIT) – ENDING	\$ 121,246	\$ -	\$ 1,477,673	\$ 2,910,575	\$ 4,509,494

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14/04/2015

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

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, 2014

Net Change in Fund Balances – Government Funds (Page 20)	\$ 133,079
Amount reported for Governmental Activities in the Statement of Activities (Page 17) 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	\$ 553,148
Depreciation Expense	<u>(2,055,359)</u>
Excess of Capital Outlays over Depreciation Expense	(1,502,211)
Revenues in the Statement of Activities that do not provide current financial resources are reported as revenues in the funds and vice versa:	
Christmas Bonus	8,116
Community Development Block Grant	<u>397,172</u>
Total of Revenues	405,288
Repayment of long-term principal is expenditure in the governmental funds, but issuing debt reduced Noncurrent Liabilities in the Statement of Net Position. In the current period repayments were	
	499,150
Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:	
Decrease in Christmas Bonus	11,429
Increase in Debt to Puerto Rico Acueduct and Sewer Authority	(58,000)
Decrease in Debt to PR Department of Labor	164,523
Increase in Compensated Absences	<u>(260,092)</u>
Total Additional Expenses	<u>(142,040)</u>
Change in Net Position of Governmental Activities (Page 17)	<u>\$ (606,734)</u>

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

1. FINANCIAL REPORTING ENTITY

The accompanying financial statements present information on the financial activities of the Municipality of Vieques of the Commonwealth of 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, 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. 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. A second criteria used in evaluating potential component units is if the nature and significance of the relationship between the organization and a primary government are such that to exclude the organization from the financial reporting entity would render the financial statements misleading or incomplete.

A legally separate, tax-exempt organization should be discretely presented as a component unit if all of the following criteria are met: (1) the economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents; (2) the primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and; (3) the economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

FINANCIAL REPORTING ENTITY – continuation

GASB Statement 61, *The Financial Reporting Entity: Omnibus an Amendment of GASB Statements No. 14 and No. 34*, provides additional criteria for classifying entities as component units to better assess the accountability of elected officials by ensuring that the financial reporting entity includes only organizations for which the elected officials are financially accountable or that are determined by the government to be misleading to exclude.

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 balances and transactions; 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. Based on these criteria, there are no other organizations which should be included in these basic financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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, 2014, and the respective changes in financial position, and the cash flows, where applicable, thereof for the fiscal year then ended.

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 Activities.

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

Required Supplementary Information – 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)

While separate government-wide and fund financial statements are presented, they are interrelated. The GWFS (the *Statement of Net Position* 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. Exceptions to this general rule are payments in lieu of taxes where the amounts are reasonably equivalent in value to the interfund services provided and other charges between the government's Puerto Rico Electric Power Authority function of the government. Elimination of this charges would distort the direct cost and program revenue reported for the various functions concerned.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

The focus of the *Statement of Net Position* is designed to be similar to bottom line results for the Municipality's Governmental 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 Position* presents the reporting entities' assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as net position. Net positions are classified as net investment in capital assets, restricted when constraints are placed on them that are imposed by external parties or by laws or regulations, and unrestricted. Designations solely imposed by the Municipality's management are not presented as restricted net position.

The *Statement of Activities* presents a comparison between direct expenses and program revenues for the different Governmental Activities of the Municipality and for each function. *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. Separate statements for each fund category (Governmental Activities) are presented. 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.

Each fund is a separate accounting entity with a self-balancing set of accounts used to record the financial transactions and balances of that entity. Individual funds have been established as stipulated by legal provisions or by administrative discretion. The Municipality uses fund accounting, which is designed to demonstrate legal compliance and to segregate transactions related to certain government functions or activities.

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.

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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

The Municipality periodically undertakes a comprehensive evaluation of its fund structure to ensure that it complies with all aspects that are of importance to users of general purpose external financial reports. Consequently, all superfluous funds and some operational funds currently used by the Municipality in the day-to-day accounting procedures have not been reported as individual governmental funds in the accompanying fund financial statements. Accordingly, the accompanying fund financial statements include only the minimum number of funds consistent with legal and operating requirements and, consequently, certain types of similar operational funds have been combined into single funds in the accompanying fund financial statements.

The financial statements of the governmental funds are the following:

Balance Sheet – Reports information at June 30, 2014 about the current financial resources (assets, liabilities, deferred inflows of resources and fund balances) of each major governmental fund.

Statement of Revenues, Expenditures and Changes in Fund Balance – Reports information about the inflows, outflows and balances of current financial resources of each major governmental fund for the fiscal year ended June 30, 2014.

Since the GFFS are presented in different measurement focus and basis of accounting than the GWFS, reconciliation is presented and separate explanation for each differences.

During the course of operations the Municipality has activity between funds for various purposes. Any residual balances outstanding at year end are reported as due from/to other funds. While these balances are reported in fund financial statements, certain eliminations are made in the preparation of the GWFS. Balances between the funds included in Governmental Activities (i.e., the governmental funds) are eliminated so that only the net amount is included as internal balances in the Governmental Activities column.

Further, certain activity occurs during the fiscal year involving transfers of resources between funds. In GFFS these amounts are reported at gross amounts as transfers in/out. While reported in GFFS, certain eliminations are made in the preparation of the GWFS. Transfers between the funds included in Governmental Activities are eliminated so that only the net amount is included as transfers in the Governmental Activities column.

The Municipality reports its financial position (Balance Sheet) and results of operations (Statement of Revenues, Expenditures and Changes in Fund Balances) 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

B. Measurement Focus and Basis of Accounting

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.

Government-wide Financial Statements

The government-wide 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. 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 met, other than time requirements. These resources relate to a future period (when the advance is first permitted to be used in accordance with the government-mandated nonexchange transaction or a voluntary nonexchange transaction) and, therefore, should be classified as a deferred inflow of resources until such time as the resources are first permitted to be used. Receipts on any type of revenue sources collected in advance for use in the following fiscal year are recorded as unearned revenues.

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, 2014, all revenues sources met this availability criterion.

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). However, those resources not available for spending in the current period and, therefore should be classified as a deferred inflow of resources. 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). Accordingly, such resources should be reported as unearned revenue in the liability section of the general fund's *Balance Sheet*. All other revenue items are considered to be measurable and available only when cash is received by the Municipality.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

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. Principal and interest on bonds payable are recorded when they matured (when payment is due), except for principal and interest of bonds due on July 1, 2014, which are recorded as governmental fund liabilities of June 30, 2014 which is the date when resources were available in the debt service fund. Proceeds of general long-term debt and acquisitions under capital leases, if any, are reported as other financing sources.

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 (Unassigned Fund Balance up to the maximum of cash available). 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. Unexpended appropriations at the end of the fiscal year generally lapse. However, they may be re-appropriated for expenditures in the following fiscal year.

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 utilized to the extent necessary to assure effective budgetary control and accountability and to facilitate effective cash planning and control. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP reporting purposes, encumbrances outstanding at year-end are reported as assigned 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 restricted, committed and assigned 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

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.

Excess of Expenditures over Appropriations

For the year ended June 30, 2014, expenditures exceeded appropriations in the following function (the legal level of budgetary control) of the General Fund: Mayor and Municipal Legislature by \$395,318, Public Safety by \$27,217, Culture and Recreation by \$42,244, Human Services and Welfare by \$78,059, Urban Development by \$66,688, Capital Outlays by \$30,123, and Transfer to Other Funds by \$686,509. This overspending of appropriation is authorized by law up to 5% if related to cases involving imminent public endangerment (e.g., natural disaster, or fire), which wasn't the case this year, it is considered a budgetary violation. The budgetary variance during the year present a deficiency of revenues of \$1,798,405, and economies in expenditures of \$1,575,814 for a total decrease in Budgetary Fund Balance of \$222,591.

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 Commonwealth of Puerto Rico*, issued by the GDB as promulgated by Act 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, if available. Cash in the Special Revenue and Capital Project Funds are restricted; accordingly, resources available were not used for pool investments. Cash Equivalents are investments with an original maturity of 90 days or less.

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."

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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

Receivables consist of all revenues earned but not collected at June 30, 2014. 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 Commonwealth. 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.

Accounts payable represent amounts, including salaries and wages, owed for goods and services received prior to year-end.

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) 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 Municipality 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 GWFS regardless of their amount.

In the case of the initial capitalization of general infrastructure assets (i.e., those reported by Governmental Activities) the Municipality 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 Municipality 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 Municipality values these capital assets at the estimated fair value of the item at the date of its donation.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

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.

5) Deferred Outflows/Inflows of Resources

In addition to assets, the *Statement of Financial Position* will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expense/expenditure) until then. The Municipality has no items that qualify for reporting in this category.

In addition to liabilities, the *Statement of Net Position* will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Municipality has no items that qualify for reporting in this category.

The Municipality has items, which arises only under a modified accrual basis of accounting that qualifies for reporting in deferred inflows of resources. Accordingly, the items, *unavailable revenue*, is reported only in the governmental funds Balance Sheet. The governmental funds report *unavailable revenues* from two sources: Christmas Bonus Reimbursement from the Commonwealth and Federal Grants. These amounts are deferred and recognized as an inflow of resources in the period that the amounts become available.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

6) *Unearned Revenues*

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

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 noncurrent liabilities (e.g., vacation, sick leave, claims and judgments, noncurrent liabilities to other governmental entities and third parties, and landfill post closure care costs). Bond premiums and discounts, if any, 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, if any. As per GASB Statement No. 65, Bond Issuance Costs incurred are reported as expense in the fiscal year incurred.

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. Expenditures for principal and interest payments for governmental fund general and special obligations bonds are recognized in the Debt Service Fund when due.

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, 2014. All vacation pay is accrued when incurred in the GWFS. 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. Also, GFFS record expenditures when employees are paid for leave or the balance due in accrued upon the employee's separation from employment.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

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 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.

For the purpose of applying the requirements of GASBS No. 27, as amended, the state government of the Commonwealth is considered to be the sponsor of the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (ERS), a multiemployer cost-sharing defined benefit pension plan and System 2000, a hybrid defined contribution plan, 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 Commonwealth and the basic financial statements of such retirement systems are part of the financial reporting entity of Commonwealth. Act No. 3 was enacted on April 4, 2013, amended the Act No. 447 for the purpose of establishing a major reform of the ERS effective on July 1, 2013 (see Note 18).

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*.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - continuation

12) *Net Position/Fund Balance*

A) *Net Position*

Net position represent the difference between assets, deferred outflows of resources, liabilities, and deferred inflows of resources in the government-wide financial statements.

The GWFS utilize a net position presentation, which are categorized as follow:

- *Net Invested in Capital Assets* – 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 investment in capital assets is comprised of the following:

	<u>Governmental Activities</u>
Capital Assets, Net of Accumulated Depreciation.....	\$128,192,215
Outstanding Balance on Related Debt.....	(11,696,400)
Unspent Capital Debt Proceeds.....	<u>4,971,010</u>
Net Investment in Capital Assets	<u>\$121,466,825</u>

- *Restricted Net Position* – 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 Position* – These consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net position often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net position often have constraints on resources that are imposed by management, but can be removed or modified.

Net Position Flow Assumption

Sometimes the Municipality will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the GWFS, a flow assumption must be made about the order in which the resources are considered to be applied. It is the Municipality's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

B) Fund Balance

Fund Balance Classification

Fund balances for the governmental funds are reported in classifications that comprise a hierarchy based on the extent to which the Municipality 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 Municipality'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.

Fund Balance Flow Assumption

Sometimes the Municipality will fund outlays for a particular purpose from both restricted and unrestricted resources (the total committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the GFFS a flow assumption must be made about the order in which the resources are considered to be applied. It is the Municipality's policy to consider restricted fund balance to have been depleted before using any of the components or unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

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 the collection of property taxes and other main income. 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.

Restrictions of Fund Balance

Restrictions of fund balance represent portions of fund balances that are legally segregated for a specific future use or are not appropriate for expenditure. The Municipality has implemented the provisions of the GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* as of July 1, 2010, in which it is required to classify and report amounts in the appropriate fund balance classification by applying their accounting policies that determine whether restricted, committed, assigned, and unassigned amounts are considered to have been spent.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

Policy on Committing Funds

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 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, it is the policy of the **Municipality** that funds can only be removed from the Committed Fund Balance category after resolution and approval by the Municipal Legislature.

Policy on Assigning Funds

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. The Municipality hasn't met its GASB 54 fund balance targets at June 30, 2014.

Prioritization of Fund Balance Use

In circumstances where the payment is for a purpose that quantities are available in multiple classifications of funds balance, the order in which resources will be used shall be as follows: Restricted Fund Balance, followed by Committed Fund Balance, Assigned Fund Balance, and last but not least, Unassigned Fund Balance.

C) *Components of Fund Balance*

	GENERAL FUND	SBGP FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
Nonexpendable	\$ -	\$ -	\$ -	\$ -	\$ -
Restricted For:					
Debt Repayment	-	-	1,477,673	-	1,477,673
Improvement of Streets and Sidewalks	3,329,923	-	-	770,890	4,100,813
Improvement and Construction of Facilities	-	-	-	1,467,992	1,467,992
Welfare	-	-	-	740,707	740,707
Resident Airfare Subsidy	-	-	-	21,697	21,697
Capital Outlay - Purchase of Equipment	-	-	-	23,464	23,464
Total Restricted	3,329,923	-	1,477,673	3,024,750	7,832,346
Committed To:					
Sale and Maintenance of Municipal Land	-	-	-	21,024	21,024
Recreational Activities	-	-	-	175,249	175,249
Total Committed	-	-	-	196,273	196,273
Assigned	-	-	-	-	-
Unassigned (Deficit)	(3,208,677)	-	-	(310,448)	(3,519,125)
Total Fund Balances (Deficit)	\$ 121,246	\$ -	\$ 1,477,673	\$ 2,910,575	\$ 4,509,494

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

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:

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. Advances between funds are also presented as amounts due to and due from other funds. However, these advances, transfers, and related amounts receivable and payable are considered internal balances and activities that have been eliminated in the government-wide financial statements.

Intra-Entity Transactions – There are two types of intra-entity transactions: First, the flow of resources between the primary government and its component units, and among the component units. This flow of resources and the related outstanding balances are reported as if they were external transactions. However, flow of resources between the primary government and blended component units are classified as interfund activity, as described above. Second, the intra-entity balances between the primary government and discretely presented component units that are tantamount to long-term debt financing. The primary government's liability is reported in the *Statement of Net Position*, the proceeds in the primary government's funds, and the asset in the discretely presented component units' *Statement of Net Position*. For the fiscal year there are not intra-entity transactions.

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, 2014 amounted to approximately \$241,712. The current insurance policies have not been cancelled or terminated.

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

The Municipality obtains workers compensation insurance through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth of Puerto Rico. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the MRCC for the year ended June 30, 2014 amounted to \$158,280.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

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

Under Act No. 63 of June 21, 2010, the Legislative Assembly of the Commonwealth of Puerto Rico, authorized the municipalities to procure and manage at their own discretion all insurance policies, including those related to health plans been provided to the municipal employees. The Municipality also obtains medical insurance coverage from one health insurance company for its employees. Different health coverage and premium options are negotiated each year by the Municipality. Premiums are paid on a monthly basis directly to the insurance company.

G. Use of Estimates

The preparation of the basic financial statements in conformity with GAAP 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, 2014:

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 primary government of the Commonwealth, as well as its component units and the municipalities, are considered "cost-sharing" employers of the Retirement Systems; therefore, they would report its allocated share of the Commonwealth's resulting Net Pension Liability from Statement 67 as follows:

- Based on their respective individual proportion to the collective net pension liability of all the governments participating

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

- The proportion should be consistent with the method used to assess contributions (percentage of payroll). The use of their respective long term expected contribution effort to Retirement Systems divided by those of all governments in the plan, is encouraged.

The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2014 (FY2014-2015). Earlier application is encouraged. The Commonwealth and the Retirement Systems are in the process of evaluating the impact of this Statement on its agencies and component units and also on the municipalities of the Commonwealth. The information to adopt this Statement will be based on the new actuarial reports to be prepared under the new Statement No. 67.

GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*. This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term *government combinations* includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations.

The distinction between a government merger and a government acquisition is based upon whether an exchange of significant consideration is present within the combination transaction. Government mergers include combinations of legally separate entities without the exchange of significant consideration. This Statement requires the use of carrying values to measure the assets and liabilities in a government merger. Conversely, government acquisitions are transactions in which a government acquires another entity, or its operations, in exchange for significant consideration. This Statement requires measurements of assets acquired and liabilities assumed generally to be based upon their acquisition values. This Statement also provides guidance for transfers of operations that do not constitute entire legally separate entities and in which no significant consideration is exchanged. This Statement defines the term *operations* for purposes of determining the applicability of this Statement and requires the use of carrying values to measure the assets and liabilities in a transfer of operations.

A disposal of a government's operations results in the removal of specific activities of a government. This Statement provides accounting and financial reporting guidance for disposals of government operations that have been transferred or sold. The requirements of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013 (FY 2014-2015), and should be applied on a prospective basis.

GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date— an amendment of GASB Statement No. 68*. This Statement eliminates a potential source of understatement of restated beginning net position and expense in a government's first year of implementing GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. To correct this potential understatement, Statement 71 requires a state or local government, when transitioning to the new pension standards, to recognize a beginning deferred outflow of resources for its pension contributions made during the time between the measurement date of the beginning net pension liability and the beginning of the initial fiscal year of implementation. This amount will be recognized regardless of whether it is practical to determine the beginning amounts of all other deferred outflows of resources and deferred inflows of resources related to pensions. The provisions are effective simultaneously with the provisions of Statement 68, which is required to be applied in fiscal years beginning after June 15, 2014 (FY 2014-2015).

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

3. CASH AND INVESTMENTS

Cash in Banks

Municipality's cash and investments at June 30, 2014 are composed of: (1) demand deposits in commercial banks, (2) demand deposits in the Government Development Bank of Puerto Rico (GDB, fiscal agent), and (3) cash equivalents in commercial banks. Cash equivalents of \$6.0 million are deposits in commercial bank accounts and interest bearing accounts in GDB, and are recorded at cost, which approximates fair value.

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or the Commonwealth. 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 Commonwealth laws. Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the Federal Deposit Insurance Corporation (FDIC) coverage. All securities pledged as collateral are held by agents designated by the Commonwealth's Secretary of the Treasury, but not in the Municipality's name.

The Municipality follows the practice of pooling cash. At June 30, 2014, the cash are maintained in commercial banks with a balance of \$1,817,793 of which \$900,701 in the General Fund, \$102 in the SBGP Funds, and \$916,900 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 amounting to \$1,959,683 that are restricted for the payment of the Municipality's debt service, as required by law, and \$60,613 is a balance of a previous bond issue available for the General Fund. Cash with Fiscal Agent of \$2,223,722 in other governmental funds consist principally of unspent proceeds of bonds that are restricted for the acquisition, construction or improvement of major capital assets and operational purposes. 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, 2014:

Credit Risk

This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2014, the Municipality has invested only in cash in banks of \$1.8 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 of equity securities were made during the Fiscal Year ended June 30, 2014. 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, 2014.

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, 2014, the Municipality has balances deposited in commercial banks amounting to \$1.8 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 \$4.2 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, 2014. 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, 2014, 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, 2014, (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, 2014, 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, 2014.

4. ACCOUNTS RECEIVABLE – FEDERAL GRANTS

The due from federal grants of the Other Governmental Funds for the fiscal year ended June 30, 2014 corresponds to \$1,938,151 from the Community Development Block Grant/States Program (SBGP) (through the Office of the Commissioner of Municipal Affairs).

5. INTERFUND RECEIVABLE, PAYABLES AND TRANSFERS

A. Interfund Receivable and Payable Balances

During the course of operations, numerous transactions occur between the Municipality's funds for goods provided and services rendered and for the reimbursement of expenditures. Related interfund receivables and payables are classified as "Due from Other Funds" and "Due to Other Funds" on the *Balance Sheet* and *Statement of Net Position* and will be settled within one year. Due to/from Other Funds at June 30, 2014 are summarized as follows:

INTERFUND RECEIVABLE	INTERFUND PAYABLE	AMOUNT
Other Governmental Funds	General Fund	\$ 207,119
General Fund	SBGP Fund	97,011
TOTAL		<u>\$ 304,130</u>

B. Interfund Transfers

During the course of the fiscal year, transactions occur between the Municipality's funds for operating subsidies. Related interfund receipts and disbursements are classified as "Transfers In" and "Transfers Out" on the *Statement of Revenues, Expenditures/Expenses, and Changes in Fund Balances/Net Position*. The transfers are routine and consistent with the activities of the funds. Principality, 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	\$ 438,602	Debt Payment
General Fund	Other Governmental Funds	247,907	Operating Costs
Other Governmental Funds	General Fund	139,320	Residual Equity Transfer
Debt Service Fund	General Fund	<u>\$ 406,815</u>	Residual Equity Transfer
TOTAL		<u>\$ 1,232,644</u>	

6. DUE FROM/TO OTHER GOVERNMENTAL UNITS

As of June 30, 2014, the amount of \$88,722 corresponds to the Christmas Bonus, amount to be provided by the Puerto Rico Treasury Department.

As of June 30, 2014, balance due to other governmental units of the General Fund for services rendered to the Municipality for the Puerto Rico Retirement Administration (\$30,412).

7. UNEARNED REVENUES

Government-wide *Statement of Net Position* does not report *deferred inflows of resources*, but report *unearned revenues* for resources receive before it has a legal claim to them. Governmental funds *Balance Sheet* report *unearned revenues* in connection with cash collected for revenues that are not considered to be available to liquidate liabilities of the current period as follows:

Governmental Funds:	
Volume of Business Taxes	\$ 416,465
Total Unearned Revenues	<u>\$ 416,465</u>

8. DEFERRED INFLOW OF RESOURCES

Governmental funds balance sheet report *deferred inflows of resources* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period (unavailable). 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 inflows of resources* reported in the basic financial statements were as follows:

Governmental Funds:	
Christmas Bonus - Commonwealth	\$ 96,838
Federal Grants:	
CDBG	1,831,002
Total Deferred Inflows of Resources	\$ 1,927,840

9. CAPITAL ASSETS

Capital Assets activities for the fiscal year ended June 30, 2014 was as follows:

DESCRIPTION	BALANCE		INCREASES	DECREASES	BALANCE	
	JULY 1, 2013				JUNE 30, 2014	
Non-Depreciable Capital Assets:						
Land	\$ 65,650,752	\$ -	\$ -	\$ -	\$ 65,650,752	
Construction in Progress	6,622,304	553,148	-	-	7,175,452	
Total Non-Depreciable Capital Assets	72,273,056	553,148	-	-	72,826,204	
Depreciable Capital Assets:						
Buildings and Buildings Improvements	30,422,254	-	-	-	30,422,254	
Equipment and Vehicles	2,419,621	-	-	-	2,419,621	
Furniture and Fixtures	2,205,542	-	-	-	2,205,542	
Infrastructure	66,691,389	-	-	-	66,691,389	
Total Depreciable Capital Assets	101,738,806	-	-	-	101,738,806	
Less Accumulated Depreciation:						
Buildings and Buildings Improvements	(13,184,945)	(608,445)	-	-	(13,793,390)	
Equipment and Vehicles	(2,040,766)	(120,981)	-	-	(2,161,747)	
Furniture and Fixtures	(2,213,437)	7,895	-	-	(2,205,542)	
Infrastructure	(26,878,288)	(1,333,828)	-	-	(28,212,116)	
Total Accumulated Depreciation	(44,317,436)	(2,055,359)	-	-	(46,372,795)	
Total Depreciable Capital Assets (Net)	57,421,370	(2,055,359)	-	-	55,366,011	
CAPITAL ASSETS, NET	\$ 129,694,426	\$ (1,502,211)	\$ -	\$ -	\$ 128,192,215	

9. CAPITAL ASSETS – continuation

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

	AMOUNT
General Government	\$ 129,487
Mayor and Municipal Legislature	616,608
Public Safety	246,643
Public Works and Transportation	513,840
Culture and Recreation	164,429
Health and Sanitation	267,197
Urban Development	117,155
Total Depreciation Expenses	\$ 2,055,359

10. NONCURRENT LIABILITIES

A. General Obligations Bonds and Special Obligations Bonds

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

The following is a summary of general and special obligation bonds of the **Municipality** as of June 30, 2014:

Type of Obligation and Purpose	Issue Date	Original Borrowing	Maturity Date	Interest Rate	Balance Amount
General Obligation Bonds:					
Property Taxes Income:					
Acquisition of Building	1999	\$ 720,000	2023	4.86 to 6.50%	\$ 440,000
General Construction	2002	655,000	2026	2.70 to 5.60%	455,000
Purchase of Land	2007	290,000	2031	6.60 to 7.50%	255,000
General Construction	2007	1,135,000	2032	3.93 to 7.50%	1,015,000
General Construction	2011	1,080,000	2030	6.00 to 7.50%	1,005,000
General Construction	2012	2,190,000	2034	6.00 to 7.00%	2,105,000
Operational Purpose	2012	385,000	2038	6.00 to 7.00%	380,000
Total General Obligation Bonds					5,655,000
Special Obligation Bonds:					
General Revenues:					
Operational Purpose	2002	837,000	2026	5.00 to 6.00%	588,900
Operational Purpose	2003	380,000	2029	5.00 to 6.00%	285,000
Operational Purpose	2008	2,222,000	2027	3.93 to 7.50%	1,771,000
General Construction	2009	315,000	2018	5.40 to 7.50%	185,000
General Construction	2009	3,240,000	2033	2.43 to 7.00%	2,945,000
Purchase of Equipment	2010	85,000	2016	1.60 to 6.00%	45,000
Operational Purpose	2012	291,000	2018	6.00 to 7.00%	221,500
Total Special Obligation Bonds					6,041,400
Total General and Special Obligation Bonds					\$ 11,696,400

10. NONCURRENT LIABILITIES - continuation

Variable interest rates on bonds are reviewed periodically by GDB and are based on the fluctuation of GDB's weighted average rate for its commercial paper program. Under this program, GDB issues commercial paper: (1) in the taxable and tax-exempt markets of the USA, and (2) to corporations having tax exemptions under the Puerto Rico Industrial Incentives Acts and, which qualify for benefits provided by the former Section 936 of the US Internal Revenue Code.

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, 2014, 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 Noncurrent Liabilities

Following are the other noncurrent liabilities as of June 30, 2014 and corresponding change during the fiscal

DESCRIPTION	BALANCE		RETIREMENTS AND ADJUSTMENTS	BALANCE		AMOUNTS	
	JULY 1, 2013	NEW ISSUES		JUNE 30, 2014	DUE WITHIN ONE YEAR	DUE AFTER NEXT YEAR	
Law Number 42 – MRCC	\$ 2,151,710	\$ -	\$ (59,260)	\$ 2,092,450	\$ 62,984	\$ 2,029,466	
Law Number 146 – MRCC	68,228	-	(3,590)	64,638	3,590	61,048	
Dept of Labor and Human Resources	358,315	-	(164,623)	193,692	164,623	29,069	
Puerto Rico Aqueduct and Sewer Authority	-	58,000	-	58,000	34,800	23,200	
Claims and Judgements	68,027	-	-	68,027	-	68,027	
Christmas Bonus	177,444	166,015	(177,444)	166,015	166,015	-	
Compensated Absences	1,359,060	358,175	(98,083)	1,619,152	1,080,296	538,856	
TOTAL	\$ 4,182,784	\$ 582,190	\$ (503,000)	\$ 4,261,974	\$ 1,512,308	\$ 2,749,666	

year:

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 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%.

10. NONCURRENT LIABILITIES – continuation

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.

Claims and Judgments

This amount represents the amount accrued for possible claims arising from litigations as recommended by the Municipality's attorneys and classified as due after one year. Only claims is presented as due within one year when the Municipal Legislature approved it in the next fiscal year budget.

Christmas Bonus

This amount represents the estimated accrued Christmas bonus accumulated as of June 30, 2014 and payroll related benefits, representing the benefit to employees to be paid during the first week of December 2014.

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.

D. Changes in General Long-Term Debts

The following is a summary of changes in long-term debts for the year ended June 30, 2014:

DESCRIPTION	BALANCE JULY 1, 2013	NEW ISSUES	RETIREMENTS AND ADJUSTMENTS	BALANCE JUNE 30, 2014	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER NEXT YEAR
General Obligation Bonds	\$ 5,925,000	\$ -	\$ (270,000)	\$ 5,655,000	\$ 165,000	\$ 5,490,000
Special Obligation Bonds	6,300,200	-	(258,800)	6,041,400	290,240	5,751,160
Other Obligations	4,182,784	582,190	(503,000)	4,261,974	1,512,308	2,749,666
TOTAL	\$ 16,407,984	\$ 582,190	\$ (1,031,800)	\$ 15,958,374	\$ 1,967,548	\$ 13,990,826

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.

10. NONCURRENT LIABILITIES - continuation

The annual requirements to amortize the general long-term debts outstanding as of June 30, 2014 are as follows:

YEAR ENDING JUNE 30,	General Obligation Bonds		Special Obligation Bonds		Other Noncurrent Obligations		TOTAL	
	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL	INTEREST
Governmental Funds:								
2014	\$ 165,000	276,813	\$ 290,240	249,500	\$ 1,512,308	\$ 129,233	\$ 1,967,548	\$ 655,546
2015	185,000	375,207	306,800	373,153	122,801	135,599	614,601	883,959
2016	195,000	367,108	323,400	351,146	74,737	121,786	593,137	840,040
2017	215,000	353,164	337,400	328,096	79,208	117,225	631,608	798,485
2018	225,000	338,163	361,900	303,783	83,958	112,384	670,858	754,330
2020-2024	1,335,000	1,396,092	1,656,760	1,242,607	502,192	478,176	3,493,952	3,116,875
2025-2029	1,575,000	895,735	1,619,900	642,500	674,677	303,447	3,869,577	1,841,682
2030-2034	1,460,000	340,138	1,145,000	211,925	605,210	76,340	3,210,210	628,403
2035-2039	300,000	23,800	-	-	-	-	300,000	23,800
UNMATURED	-	-	-	-	606,883	-	606,883	-
TOTAL	\$ 5,655,000	\$ 4,366,220	\$ 6,041,400	\$ 3,702,710	\$ 4,261,974	\$ 1,474,190	\$ 15,958,374	\$ 9,543,120

11. 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 12).

These property taxes are accumulated by the Municipal Revenue Collection Center in costs of the general obligations bonds issued by the Municipality (See Note 10). 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.

As per Act Number 18 of 2014 was created the "Law of Municipal Administration Fund (MAF)" to establish a special fund called the Municipal Administration, authorize municipalities to pledge the funds deposited in the Local Government Fund to which they are to secure the repayment of any loan, bond, note or other evidence of indebtedness, which are the source of repayment funds deposited in the Special Fund and to meet any expenditure budget of the Municipality and the Municipality any activity or project, authorize the Government Development Bank for Puerto Rico to make disbursements for purposes set out in this Act.

This measure is intended, first, to strengthen the financial capacity of the Corporation Tax Fund of Puerto Rico (COFINA, by Spanish acronyms), established under Law No. 91-2006, as amended, known as the "Law Fund of Sales and Usage Taxes", adjusting the sales and usage taxes (SUT) by increasing the state portion to 6.0% while the municipal SUT is reduced to 1.0%, effective February 1, 2014.

Through this legislation a mechanism under which the SUT collections entitled to receive the Commonwealth of Puerto Rico each fiscal year, after complying with the deposits in the Tax Fund requires by Act No. 91-2006, shall be deposited in a special fund created for the benefit of, and assigned to the municipalities. This special fund is called the "Local Government Fund" ("LGF"), which will be guarded by the Government Development Bank of Puerto Rico.

Also, on February 1, 2014 was enacted the Act No. 19 that creates the Municipal Financing Corporation (COFIM, by Spanish acronyms). The COFIM, attached to the Government Development Bank (GDB), with the power to issue bonds or use other mechanisms to pay or refinance debt incurred by municipalities, the payment of principal and interest is backed by the municipal SUT.

11. DEBT RETIREMENT – continuation

In addition, create the Redemption Fund of COFIM, to which the resources of the existing Municipal Fund Redemption will be transferred effective February 1, 2014, and facilitated the distribution of funds from the Municipal Redemption Fund, the Municipal Development Fund and the Municipal Improvement Fund. Provides that the first proceeds of the municipal SUT of 1% shall be collected by the Treasury Department and deposited directly into the Redemption Fund of COFIM. Provides that bonds and notes issued by the COFIM be payable and secured by the pledge of a fixed amount, or municipal SUT corresponding to a fixed rate of 0.3% has been collected during the previous fiscal year, whichever is greater.

12. 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 1st 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. Real property taxes are assessed by the MRCC as January 1st of each year.

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 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 difference between the advances and the final settlement from MRCC for the fiscal year 2014 resulted in a receivable of \$8,220 for the Debt Service Fund. At the time of the preparation of the financial statement, the difference between the advances and the final settlement to the General Fund is pending of final determination.

The tax rate for fiscal year 2014 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.

12. PROPERTY TAXES – continuation

As previously mentioned, on March 9, 2009, the Commonwealth of Puerto Rico approves Act Number 7 that provides for revision of the valuation of property subject to taxation and imposes special property taxes for the Commonwealth. The effect of this Law was an increase in the valuation of the real properties and in the exemption granted for the residential units occupied by their owners by multiply both amount by ten. Accordingly, the residential units occupied by their owners are exempt from real property taxes on the first \$150,000 assessed value. For such exempted amounts, the Puerto Rico Secretary of the Treasury assumes payment of the basic tax to the Municipality (6.00%), except for residential units assessed at less than \$35,000 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 Secretary of the Treasury to the Municipality was frozen as of January 1, 1992. The Municipal Revenue Collection Center, instead of the property taxpayer, becomes the source of payment in these cases.

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.

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.

The fiscal impact for the future years has not been determined by the Municipality's management.

13. 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, 2013, the tax rates were as follows:

- a. Financial institutions and savings and loan associations – 1.50%
- b. Other organizations – 0.50%

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, the taxpayer is granted a 5% of discount. Collections of taxes during current fiscal year, applicable to the next fiscal year, are recorded as unearned revenues in the General Fund.

14. 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 Usage Tax Return Form, no later than the 10th 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.

14. SALES AND USAGE TAXES – continuation

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, 2014, but pertaining to the current year period.

As per Act Number 18 of 2014 was created the "Law of Municipal Administration Fund (MAF)" to establish a special fund called the Municipal Administration, authorize municipalities to pledge the funds deposited in the Local Government Fund to which they are to secure the repayment of any loan, bond, note or other evidence of indebtedness, which are the source of repayment funds deposited in the Special Fund and to meet any expenditure budget of the municipality and the municipality any activity or project, authorize the Government Development Bank for Puerto Rico to make disbursements for purposes set out in this Act.

This measure is intended, first, to strengthen the financial capacity of the Corporation Tax Fund of Puerto Rico (COFINA, by Spanish acronyms), established under Law No. 91-2006, as amended, known as the "Law Fund of Sales and Usage Taxes", adjusting the sales and usage taxes (SUT) by increasing the state portion to 6.0% while the municipal SUT is reduced to 1.0%, effective February 1, 2014.

Through this legislation a mechanism under which the SUT collections entitled to receive the Commonwealth of Puerto Rico each fiscal year, after complying with the deposits in the Tax Fund requires by Act No. 91-2006, shall be deposited in a special fund created for the benefit of, and assigned to the municipalities. This special fund is called the "Local Government Fund" ("LGF"), which will be guarded by the Government Development Bank of Puerto Rico.

Also, on February 1, 2014 was enacted the Act No. 19 that creates the Municipal Financing Corporation (COFIM, by Spanish acronyms). The COFIM, attached to the Government Development Bank (GDB), with the power to issue bonds or use other mechanisms to pay or refinance debt incurred by municipalities, the payment of principal and interest is backed by the municipal SUT.

In addition, create the Redemption Fund of COFIM, to which the resources of the existing Municipal Fund Redemption will be transferred effective February 1, 2014, and facilitated the distribution of funds from the Municipal Redemption Fund, the Municipal Development Fund and the Municipal Improvement Fund. Provides that the first proceeds of the municipal SUT of 1% shall be collected by the Puerto Rico Treasury Department and deposited directly into the Redemption Fund of COFIM. Provides that bonds and notes issued by the COFIM be payable and secured by the pledge of a fixed amount, or municipal SUT corresponding to a fixed rate of 0.3% has been collected during the previous fiscal year, whichever is greater.

15. 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 and fixtures, and other types of construction-related activities.

15. 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.

16. 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.

17. PENSION PLAN

Description of the Plan

Employees of the **Municipality** participate in the Employee's Retirement System of the Government of the Commonwealth of Puerto Rico (ERS) administered by the Puerto Rico Government Employees and Judiciary Retirement Systems Administration. The ERS is cost-sharing multiple-employer defined benefit pension plan sponsored by the Commonwealth under the Act No. 447, approved on May 15, 1951, as amended. The ERS is a pension trust of the Commonwealth. ERS covers all regular employees of the Commonwealth and its instrumentalities and of certain municipalities and components units not covered by their own retirement systems. The ERS, as a governmental retirement plan, is excluded from the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

As of June 30, 2013, the ERS has an unfunded actuarial accrued liability (UAAL) of approximately \$22,981 million, representing a 3.1% funding ratio. In the opinion of management and based on information prepared by consulting actuaries, it is estimated that starting in fiscal year 2015, the ERS's assets will be less than its obligations (including bonds payable but excluding its UAAL) resulting in a deficit net position. In addition, annual cash flow estimates for the foreseeable future are presently estimated to continue to reduce the net position unless other measures are taken.

The estimate of when the ERS's net position will become a deficit and when its assets would be exhausted is based on significant assumptions, including the rate of return on investments, the amount and timing of collections from the Commonwealth for the member, employer contributions and the employer additional contribution (Act No. 32), which as discussed below, was estimated in \$120.0 million annually, as well as the estimated participant benefits and the ERS's administrative expenses to be paid each year.

To improve the liquidity and solvency of the ERS, the Commonwealth enacted Act No. 32 of June 25, 2013, which provides for incremental annual contributions from the Commonwealth General Fund beginning in fiscal year 2014 and up to the fiscal year 2033. This additional contribution will be determined annually based on actuarial studies to be performed by the ERS's actuaries. An appropriation for such additional contribution of approximately \$120 million was included in the Commonwealth's budget for the fiscal year 2014. However, as a result of budgetary constraints at the present time management believes that approximately \$90 million of this amount will not be collected as expected during fiscal year 2014. Further, this additional contribution was reduced to \$28.2 million for the Commonwealth's proposed budget for the fiscal year 2015.

If the Commonwealth's financial condition does not improve as a result of fiscal and budgetary measures it is taking, its ability to repay its obligations, including its regular employer contributions to the ERS and its additional contribution as provided by Act No. 32, for the upcoming years, may continue to be adversely affected, and could also affect the payment of benefits and the repayment of the ERS's bond payable.

Act No. 70 established a program that provides benefits for early retirement or economic incentives for voluntary employment termination to eligible employees, as defined. Act No. 70 also establishes that early retirement benefits will be provided to eligible employees that have completed between 15 to 29 years of creditable services and will consist of monthly benefits ranging from 37.5% to 50% of each employees' monthly salary. Benefits under this program will be paid by the General Fund of the Commonwealth and by the public corporations, covering their respective employees until the plan member reaches the later of age 55 for members under Act No. 447 or age 65 for members under Act 1, or the date the plan member would have completed 30 years of service had the member continued its employment. The ERS will be responsible for benefit payments afterwards. In addition, the General Fund and the public corporations will also be required to make the required contributions to the ERS. As of June 30, 2013, the ERS has recorded a liability of approximately \$16 million for its responsibility as an employer under Act No. 70.

17. PENSION PLAN – continuation

Furthermore, Act No. 3 was enacted on April 4, 2013, amended the Act No. 447 for the purpose of establishing a major reform of the ERS effective on July 1, 2013. Employees participating in the current system (ERS) should be retired as of June 30 2013 in order to obtain the current benefits. Also, Act No. 3 amended the Act No. 305 of September 24, 1999 that's created a Defined Contribution Hybrid Program known as System 2000, incorporating the provisions of the system to Chapter 5 of the ERS. The System 2000 applied to employees joining the ERS on or after January 1, 2000.

Follow are the principal amendment of Act No. 447 by Act No. 3:

Chapter 3 of the Act No. 447, established the following date of retirement:

- (a) General Rule – The first day of the month that coincides with or is subsequent to the date that the participant of the program reaches the age of sixty (60), except as provided in clause (b) of this subsection.
- (b) Public Officers in High-Risk Positions- In the case of Public Officers in High-Risk Positions, it shall mean the first day of the month that coincides with or is subsequent to the date that the Participant reaches the age of fifty-five (55) years. (Public Officers in High-Risk Positions shall mean the Commonwealth of Puerto Rico Police, the Municipal Police, the Commonwealth Firefighter Corps, the Municipal Firefighter Corps, and the Custody Officers Corps.)
- (c) Effectiveness of these provisions: the normal date of retirement established in subsections (a) and (b) of this definition shall be in force until June 30, 2013.

Retirement age for participants who joined public service after June 30, 2013. The retirement age shall be 67 years, except in the case of Public Officers in High-Risk Positions, for whom it shall be fifty eight (58) years.

Participant of the Program

Shall mean, until June 30, 2013, every person for whom the Administrator maintains an account under the Retirement Savings Account Program pursuant to the provisions of Chapter 3 of Act No. 447. Beginning on July 1, 2013, it shall mean every person for whom the Administrator maintains an account under the Defined Contribution Hybrid Program pursuant to the provisions of Chapter 5 of this Act.

The membership of the System shall be constituted by every person who holds a regular position as a career, trust, temporary employee or with probationary personnel status in any executive department, agency, administration, board, commission, office, or instrumentality of the Executive Branch, by the Justices of the Peace, the regular employees and officials of the Judiciary Branch, and by all regular officials and employees of the municipalities, including the mayors. Temporary municipal employees shall not participate in the Retirement System.

Membership in the Retirement System shall be optional for the Governor of Puerto Rico, for all the Secretaries of Government, heads of public agencies and instrumentalities, the Governor's aides, the members of commissions and boards appointed by the Governor, the members of the Legislative Assembly of Puerto Rico, for the employees and officials of the Legislative Assembly of Puerto Rico, the Office of Legislative Services and the office of the Superintendent of the Capitol, and the Comptroller of Puerto Rico. These officials may, at any time, request to be discharged from, or readmitted into the System. The period of services rendered to the Government while separated from the System, shall be credited as creditable service, provided said officials pay the individual and employer contributions, plus interest, that correspond to the period of separation, to the system.

17. PENSION PLAN – continuation

As of July 1, 2013, every employee who is a participant of the System, including mayors, regardless of the date when he/she was first appointed to the Government of the Commonwealth of Puerto Rico, its instrumentalities, municipalities or participating employers of the System, shall become part of the Defined Contribution Hybrid Program.

Notwithstanding the fact that a superannuation retirement annuity is payable for life, if annuitants return to the service, the payment of their annuity shall be suspended. After an annuitant separates from service, payment of the suspended annuity shall resume and he/she shall also have the option to withdraw the contributions made since the date he/she returned to service up until he/she separates from service if, after returning to service, he/she worked less than five (5) years or accrued contributions for less than ten thousand dollars (\$10,000). In the event the annuitant worked five (5) years or more and contributed ten thousand dollars (\$10,000) or more, after returning to service, he/she shall be entitled, after his/her separation from service and after reaching the age established in Section 5-110 of Act No. 447, to receive an additional annuity computed pursuant to Section 5-110 of this Act, on the basis of the contributions made since the date said annuitant returned to service until his/her separation from it.

Annuity for Years of Service

As per Act No. 3, retirement shall be optional for new participants joining the System for the first time after April 1, 1990, as of the date in which they reach the age of sixty-five (65), have completed a minimum of ten (10) years of accredited services and have not requested or received the reimbursement from the accrued contributions. The amount of the annuity shall be one point five percent (1.5%) of the average compensation multiplied by the years of accredited services. However, a minimum pension of five hundred dollars (\$500) per month, effective July 1, 2013, is hereby fixed for those participants who retired in accordance with the provisions of this Chapter 2. Every pensioner who receives a pension of less than five hundred dollars (\$500) per month shall receive, effective July 1, 2013, the increase required for his/her pension to be five hundred dollars (\$500).

Public Officers in High-Risk Positions may voluntarily opt to retire after reaching the age of fifty-five (55) and thirty (30) years of service. Retirement shall be mandatory on the date the participant reaches both thirty (30) years of service and the age of fifty-eight (58). Provided, that the Superintendent of the Puerto Rico Police, the Chief of the Firefighter Corps or the corresponding appointing authority may grant dispensations authorizing members of this group to work for an additional maximum period of two (2) years performing the functions assigned to them; provided that their health and safety are not compromised. Such a request for dispensation shall be made by the member, not later than ninety (90) days before his/her retirement date. It is hereby provided that the Superintendent of the Puerto Rico Police, the Chief of the Firefighter Corps or the corresponding appointing authority shall make the necessary regulatory provisions to comply with this Act.

Retirement shall be optional for the members of the System in active service, on and after the date they have attained the age of fifty-five (55) years and have completed at least twenty-five (25) years of creditable service; and for members of the System who having reached the age of fifty-eight (58) years, and have completed at least ten (10) years of creditable service. The members of the Police Corps or the Firefighting Corps shall also have the option to avail themselves of a retirement annuity on and after the date on which they have attained the age of fifty (50) years and have completed at least twenty-five (25) years of creditable service.

Any participant whose separation from the service occurs prior to having attained the age of fifty-eight (58) years, who shall have completed at least ten (10) years of creditable service, and who shall have not applied for, nor received reimbursement of accumulated contributions shall be entitled to receive a deferred retirement annuity. Said participants shall receive a deferred retirement annuity which shall commence upon attaining the age of fifty eight (58) years or after attaining the age of fifty (50) years in the case of policemen or firemen, and fifty-five (55) years in the case of the other participants, if they have completed at least twenty-five (25) years of service in one case or the other.

17. PENSION PLAN – continuation

The amount of the annuity shall be one and one-half percent (1.50%) of the average compensation multiplied by the number of years of creditable service up to twenty (20) years, plus two percent (2%) of the average compensation multiplied by the number of years of creditable service in excess of twenty (20) years. Said annuity shall be payable in full to the members who retire at the age of fifty-eight (58) years or more, and to the members of the Police Corps [or] the Firefighting Corps who retire at the age of fifty (50) years or more and who have completed at least twenty-five (25) years of creditable service. The maximum retirement annuity (as of June 30, 2013) for the participants shall be seventy-five percent (75%) of the average compensation.

Merit Annuity – Plan members are eligible for merit annuity with a minimum of 30 years or more of credited service. The annuity for which the plan member is eligible is limited to a minimum of 65% and a maximum of 75% of the average compensation. As a result of the enactment of Act No. 3 of April 4, 2013, effective July 1, 2013, merit annuities will no longer be available to participants who joined the ERS after April 1, 1990.

Deferred Retirement Annuity – A participating employee who ceases to be an employee of the Commonwealth after having accumulated a minimum of 10 years of credited service qualifies for retirement benefits provided his/her contributions to the ERS are left within the ERS until attainment of 58 years of age.

The amount of the superannuation retirement annuity of mayors who are participants of the System shall be computed on the basis of the highest salary he/she may have received while discharging his/her government duties in the following manner:

- (1) For services performed as mayor, five percent (5%) of said salary for each year of creditable service up to a maximum of ten (10) years or fifty percent (50%), plus
- (2) For other services performed not included in the above computation, one and one half percent (1.50%) of said salary multiplied by the number of years of such other creditable services up to twenty (20) years, or two percent (2%) of said salary multiplied by the number of years of such other creditable services in excess of twenty (20) years.

The maximum superannuation retirement annuity to be granted under this subsection shall be ninety percent (90%) of the highest salary that the mayor may have received. The payments of the retirement annuity shall begin on and after the date of separation from service, but never before the mayor has attained fifty (50) years of age.

Retirement shall be optional for any participant of the System in active service who shall have completed at least thirty (30) years of creditable service. Said participant shall be entitled to receive the Merit Annuity for thirty (30) years or more of service in accordance with subsections (b) and (c) of this section thereof. Participants of the System under the Coordinating Plan and receiving Social Security benefits, who have not attained sixty-five (65) years of age, shall receive a merit annuity to be computed as provided for hereinafter:

- (1) For those participants who have completed thirty (30) years or more of creditable services and have not attained fifty-five (55) years of age or more, sixty-five percent (65%) of the average compensation.
- (2) For those who have completed thirty (30) years or more of creditable services and have attained fifty-five (55) years of age or more, seventy-five (75%) of the average compensation.
- (3) Years in excess of thirty (30) may only serve as basis to calculate the average compensation

As per Act No. 447 the following provisions shall apply to employees who participate in the System that (i) began to work before January 1, 2000, (ii) as of June 30, 2013, are not participants of the Retirement Savings Account Program established in Chapter 3 of this Act and (iii) as of June 30, 2013, do not meet the requirements of years of service and age to retire that are required in Chapter 2 of this Act:

17. PENSION PLAN – continuation

- (1) New Retirement Age for participants who joined the System for the first time before April 1, 1990. For those participants who, as of June 30, 2013, have not reached the age of 58 and completed at least 10 years of service, or have not reached the age of 55 and completed at least 25 years of service, retirement shall be optional when they meet the following age and service requirements:
 - (i) If, as of June 30, 2013, the participant is 57 years of age, the retirement will be optional when he/she reaches 59 years of age and has completed at least 10 years of service.
 - (ii) If, as of June 30, 2013, the participant is 56 years of age, the retirement will be optional when he/she reaches 60 years of age and has completed at least 10 years of service.
 - (iii) If, as of June 30, 2013, the participant is 55 years of age or less, the retirement will be optional when he/she reaches 61 years of age and has completed at least 10 years of service.
- (2) Retirement Age for participants who joined the System for the first time between April 1, 1990, and December 31, 1999 – For participants who, as of June 30, 2013, have not reached the age of 65 and completed at least 10 years of service, retirement shall be optional when the participant reaches 65 years of age and has completed 10 years of service.
- (3) For Public Officers in High-Risk Positions who began to work before April 1, 1990 and who, as of June 30, 2013, have not reached the age of 50 and completed at least 25 years of service, or who have not completed 30 years of service, regardless of their age, retirement shall be optional when they reach 55 years of age and have completed 30 years of service.
- (4) For Public Officers in High-Risk Positions who began to work between April 1, 1990, and December 31, 1999, and who, as of June 30, 2013, are not 55 years old and have completed 25 years of service, or who have not completed 30 years of service, regardless of their age, retirement shall be optional when they reach 55 years of age and have completed 30 years of service.
- (5) Public Officers in High-Risk Positions who separate from active service before meeting the requirements of age and service provided in subsection (a)(3) or (a)(4) of this Section may only receive their accrued pension when they meet the following age and service requirements:
 - (i) If the participant joined the System for the first time before April 1, 1990, after he/she meets the age and service requirements established in subsection (a) 1 of this Section.
 - (ii) If the participant joined the System for the first time between April 1, 1990, and December 31, 1999, after he/she meets the age and service requirements established in subsection (a) 2 of this Section.

Pension Computation

When the participant meets the age and service requirements established above, he/she shall be entitled to receive an annuity computed on the basis of years of service accrued as of June 30, 2013, in accordance with the following rules:

- (i) The average salary of employees who began to work before April 1, 1990, shall be the one established in definition number 15 of Section 1-104 of Act No 447.
- (ii) The average salary of employees who began to work between April 1, 1990, and December 31, 1999, shall be the one established in Section 1-108 of this Act.

17. PENSION PLAN – continuation

- (iii) The pension computation of employees who began to work before April 1, 1990, shall be made on the basis of one and one half percent (1.5%) of the average salary, multiplied by the number of years of creditable service up to twenty (20) years, plus two percent (2.0%) of the average salary, multiplied by the number of years of creditable service in excess of twenty years, in each case up to June 30, 2013.
- (iv) The pension computation of employees who began to work between April 1, 1990 and December 31, 1999, shall be made on the basis of one and one half percent (1.5%) of the average salary, multiplied by the number of years of creditable service up to June 30, 2013.
- (v) Participants of the System who, as of June 30, 2013, have availed themselves to the Coordinating Plan and are receiving Social Security benefits will have their annuities adjusted in accordance with the provisions of subsection (e) of Section 2-101 of this Act. Provided that until the participant is entitled to receive the Social Security benefits, he/she may receive an annuity in accordance with Section 5-103 of this Act.
- (vi) This pension shall be received together with the annuity accrued by a participant under Section 5-110 of this Act.

Beginning on July 1, 2013, participants shall not accrue any more years of service for the determination of the average salary and computation of a pension under Section 5-103(a)(4). In addition, participants may not have services not credited recognized, contributions transferred or returned for periods worked before June 30, 2013, except for those exceptions specifically established in Act No 447.

Those participants who began to work on or after January 1, 2000, or those who as of June 30, 2013, were participants in the Retirement Savings Program and who as of June 30, 2013, could retire from service because they are sixty (60) years old, may retire on any later date and they shall be entitled to receive the annuity that could be acquired with the balance of the contributions under the Retirement Savings Account Program and those accrued under the Defined Contribution Hybrid Program.

The savings accounts under the Retirement Savings Account Program of employees who joined the System for the first time on or after January 1, 2000, shall be rolled over to the Defined Contribution Hybrid Program. Be it provided that if, as of June 30, 2013, the employees have not reached the age of sixty (60), they shall be entitled to the annuity established in Section 5-110 of Act No. 447 when they meet the following age requirements:

- (i) If, as of June 30, 2013, the participant is 59 years old, the retirement will be optional when he/she has reached 61 years of age.
- (ii) If, as of June 30, 2013, the participant is 58 years old, the retirement will be optional when he/she has reached 62 years of age.
- (iii) If, as of June 30, 2013, the participant is 57 years old, the retirement will be optional when he/she has reached 63 years of age.
- (iv) If, as of June 30, 2013, the participant is 56 years old, the retirement will be optional when he/she has reached 64 years of age.
- (v) If, as of June 30, 2013, the participant is 55 years old or less, the retirement will be optional when he/she has reached 65 years of age.

For Public Officers in High-Risk Positions who began to work after December 31, 1999, and who, as of June 30, 2013, are not 55 years old, retirement shall be optional when they reach 55 years of age.

17. PENSION PLAN – continuation

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.

Contributions of Participants of Defined Benefit Program

Contribution requirements are established by law and are as follows:

Coordinated Plan – Prior to July 1, 2013 on the coordinated plan, the participating employee contributes 5.775% for the first \$6,600 of salary plus 8.275% for the excess over \$6,600. For fiscal 2013-2014 the contribution was 7.00% for the first \$6,600 of salary plus 10.00% for the excess over \$6,600. For fiscal 2014-2015 the contribution was 8.50% for the first \$6,600 of salary plus 10.00% for the excess over \$6,600. After July 1, 2015 the contribution was 10.00% of salary. By the time the employee reaches 65 years old and begins to receive social security benefits, the pension benefits are reduced by the following:

- \$165 per month if retired with 55 years of age and 30 years of credited service.
- \$110 per month if retired with less than 55 years of age and 30 years of credited service.
- All other between \$82 and \$100 per month.
- Disability annuities under the coordinated plan are also adjusted at age 65 and in some cases can be reduced over \$165 per month.

Non-Coordinated Plan (Supplementation Plan) – Prior to July 1, 2013 on the non-coordinated plan, the participating employee contributes 8.275% of the monthly salary and does not have any change on the pension benefits upon receiving social security benefits. After July 1, 2015 the contribution was 10.00% of salary.

Contributions of Participants of Hybrid Program

Contribution requirements are established by law and are as follows:

- (a) Every participant of the Hybrid Program shall compulsorily have to contribute ten percent (10%) of his/her salary while he/she is an employee.
- (b) Contributions under the Plan of Coordination with Social Security benefits – The participants of the System who, as of June 30, 2013, have availed themselves to the Plan of Coordination with Social Security benefits shall contribute to the Hybrid Program:
 - (1) Effective July 1, 2013, shall contribute seven percent (7%) of their monthly salaries up to five-hundred fifty dollars (\$550) and ten percent (10%) of their monthly salaries in excess of said amount.
 - (2) Effective July 1, 2014, shall contribute eight point five percent (8.5%) of their monthly salaries up to five-hundred fifty dollars (\$550) and ten percent (10%) of their monthly salaries in excess of said amount.
 - (3) Effective July 1, 2015, shall contribute ten percent (10%) of their full monthly salaries.

The participants of the Program under subsections (a) and (b) of this Section may voluntarily contribute to their account an amount in addition to the one established here. These contributions shall be credited to the contribution account of each participant of the Hybrid Program. The Administrator shall establish the way in which the participants may make additional contributions.

17. PENSION PLAN – continuation

- (c) Mandatory Contribution for the Purchase of Disability Insurance – Every participant of the Hybrid Program shall mandatorily contribute to the disability insurance established in Section 5-112 of Chapter 5 of Act No. 447, for which he/she shall have to contribute such sums, fixed in dollars or a percent of the salary, that the Administrator, with the approval of the Board, determines that are needed to provide the disability benefit, provided the contribution required by the Administrator is equal to or less than point twenty five percent (0.25%) of the participant's salary. The contributions made pursuant to this subsection may be credited against and will reduce the contributions that the participant of the Program is bound to pay to the Commonwealth of Puerto Rico Employees Association as provided in Section 8 of Act No. 133 of June 28, 1966, as amended. The contributions made under this subsection shall not be credited to the participant's account.

Employer Contributions to the System (ERS and Hybrid Program)

On July 6, 2011, the Commonwealth enacted Act No. 116, increasing the employers' contributions rate from 9.275% to 10.275% of employee compensation for fiscal year 2011-2012, an additional 1% annually for each of the next four years, and 1.25% annually for each of the five years thereafter, reaching an aggregate contribution rate of 20.525% effective July 1, 2020.

Every employer, beginning on July 1, 2013, shall mandatorily contribute to the System the following:

July 1, 2013	Twelve point two hundred seventy-five percent (12.275%) of the salary of each participant
July 1, 2014	Thirteen point two hundred seventy-five percent (13.275%) of the salary of each participant
July 1, 2015	Fourteen point two hundred seventy-five percent (14.275%) of the salary of each participant
July 1, 2016	Fifteen point five hundred twenty-five percent (15.525%) of the salary of each participant
July 1, 2017	Sixteen point seventy hundred seventy-five percent (16.775%) of the salary of each participant
July 1, 2018	Eighteen point twenty-five percent (18.025%) of the salary of each participant
July 1, 2019	Nineteen point two hundred seventy-five percent (19.275%) of the salary of each participant
July 1, 2020	Twenty point five hundred twenty-five percent (20.525%) of the salary of each participant

It is provided that the established increases applicable to the municipalities for fiscal years 2012-2013 and 2013-2014, shall be included in the budget petition submitted by the Office of Management and Budget to the Legislative Assembly.

17. PENSION PLAN - continuation

Death, Disability or Terminal Illness Benefits

Death of a Participant in Active Service

Upon death of any person who is rendering services and who had contributions accrued in the Hybrid Program, these contributions shall be reimbursed to the person or persons the participant had designated through written order duly acknowledged and submitted to the Administrator, or to his/her heirs, in the event such designation had not been made. The reimbursement shall be equal to the sum of the contributions and the investment yields up to the date of the demise of the participant. The Administrator shall collect from the contributions any debt the participant may have with the System.

Death of a Pensioner

If a pensioner dies without having consumed all of his/her pension payment contributions, his/her designated beneficiaries or, absent such designation, his/her heirs, shall continue receiving the monthly pension payments until the contributions of the participant are completely consumed.

Separation from Service for Disability or Terminal Illness

The balance in the contribution account of every participant of the Hybrid Program who is permanently separated from service due to total and permanent disability, due to disability pursuant to Act No. 127 of June 27, 1958, as amended, or due to terminal illness, as determined by the Administrator, shall be distributed to the participant by the Administrator in a lump sum, or through the grant of an annuity, or any other optional form of payment pursuant to Section 5-110 of Act No. 447, at the option of the participant.

Beginning on June 30, 2013, no disability pensions shall be awarded pursuant to Sections 2-107 thru 2-111 of Act No. 447.

Disability Insurance

The Administrator, with the approval of the Board, shall establish a disability benefits program, which shall provide a temporary annuity in the event of total and permanent disability. Disability benefits may be provided through one or more disability insurance contracts with one or more insurance companies authorized by the Insurance Commissioner of Puerto Rico to conduct business in Puerto Rico. The determination as to whether a person is partially or totally and permanently disabled, shall be made by the insurance company that issues the insurance policy covering the person. All the participants of the Program who are employees shall avail themselves to the disability benefits program in the manner and form established by the Administrator.

Additional Benefits Program

The Additional Benefits Program is established for pensioners of the ERS; said benefits are separate and shall not form part of the pension or annuity.

Except for those persons who retire under Chapter 5 of Act No. 447 of May 15, 1951, as amended, every person who was receiving a pension or benefit under Act No. 447, or the pension plans superseded by it, or any other law administered by the Administrator of the ERS, excluding any person who is receiving a pension or benefit under Act No. 12 of October 19, 1954, as amended, shall be entitled to receive the following benefits:

- (a) A Medication Bonus equal to one hundred (\$100), which shall be paid no later than July 15 of each year;

17. PENSION PLAN – continuation

- (b) A Christmas Bonus equal to two hundred dollars (\$200), which shall be paid no later than December 20 of each year; and
- (c) A Government contribution for health benefits for employees covered by health benefit plans under Act No. 95 of June 29, 1963, as amended, of one hundred dollars (\$100) monthly for pensioners of the Employees Retirement System of the Government of the Commonwealth of Puerto Rico, but it shall not exceed the total amount of the corresponding fee to be paid to any employee.

In order to fund the Additional Benefits Program and the ERS, beginning on fiscal year 2013-2014 and every subsequent fiscal year, the ERS shall receive a contribution equal to two thousand dollars (\$2,000) as of July 1 of every year for every pensioner of the ERS who began to work in the Public Service on or before of December 31, 1999.

The Administration of the ERS shall determine the total amount of the special additional contribution provided in the above paragraph and shall send a certification to the Director of the Office of Management and Budget and to each public corporation and municipality whose employees are retired under the ERS, informing them the amount corresponding to the special additional contribution.

The funds to cover the contribution described above, with respect to pensioners of the Central Government, shall be allocated in the Budget of Expenses of the Government of the Commonwealth of Puerto Rico. Public corporations and municipalities whose employees are covered under this Act shall provide the funds to cover the contribution described in Section 2 with respect to their pensioners.

The persons who retire under the provisions of Act 305-1999, known as 'Retirement Savings Accounts Program', and under Chapter 5 of Act No. 447 of May 15, 1951, as amended, shall be excluded from receiving the benefits granted under Act.

Annual Contribution

The Municipality's contributions during those years are recognized as total pension expenditures/expenses in the category of administration as follow:

FISCAL YEAR	DEFINED BENEFIT	HYBRID PROGRAM	ACT NO. 3
2014	\$ 8,772	\$ 21,378	\$ 323,535
2013	113,654	216,747	
2012	154,757	191,559	

Total employee contributions to the above-mentioned plans during the year ended June 30, 2014, 2013 and 2012 amounted to approximately \$990,602.

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 the Commonwealth of Puerto Rico provides additional information of the Defined Benefit Program and Hybrid Program. They issue a publicly available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Commonwealth. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, PR 00940-2003.

18. HEALTHCARE COSTS

During the year ended June 30, 2000 the Governor of the Commonwealth of Puerto Rico required to the municipalities of Puerto Rico an annual contribution to subsidize the cost of the implementation and administration of the Healthcare Reform. Such contributions are required to be disbursed from general fund operating budget. Total contributions made by the Municipality amounted to approximately \$396,321 for the fiscal year ended June 30, 2014.

19. 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 that an opinion cannot be formed as to the probable outcome, with the exception of various uninsured lawsuits for which our legal counsel estimate in \$68,027 the probable unfavorable 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.

20. COMMITMENTS

A. Operating Leases

The Municipality leases equipment under various operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same term. Rental expenditures/expenses recorded in the general fund for the year ended June 30, 2014, amounted to approximately \$39,000. Management believes that the summary of the future minimum rental commitments under noncancelable equipment lease with terms exceeding one year is not material to the basic financial statements taken as a whole.

21. FUND BALANCES RESTATEMENTS

Fund Balance

The following reconciles the June 30, 2013 Fund Balance, as previously reported to Beginning Fund Balance, as restated, July 1, 2013 for the various funds:

	GENERAL FUND	STATE ASSIGNMENT FUND
Fund Balance (Deficit), as Previously Reported, At June 30, 2013	\$ (6,387,348)	\$ 6,073,846
Adjustment to Interfund Debt	2,735,723	(2,735,723)
Reclassification according to GASB 54	<u>3,338,123</u>	<u>(3,338,123)</u>
Beginning Fund Balance (Deficit), As Restated, At July 1, 2013	<u>\$ (313,502)</u>	<u>\$ -</u>

This reclassification did not constitute a change in accounting principle.

22. NEW ACCOUNTING STANDARDS

The provisions of the following Governmental Accounting Standards Board (GASB) Statement have been implemented for the year ended June 30, 2014:

GASB Statement No. 67, *Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25*. The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. This Statement replaces the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures*, as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements No. 25 and No. 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement, and to defined contribution plans that provide postemployment benefits other than pensions.

The major fundamental change, among others related to the application and determination of certain measurement assumptions in valuing pension plans, is switching from the existing “funding-based” accounting model, where currently the Annual Required Contribution (ARC) is compared to the actual payments made and that difference determines the Net Pension Obligation; to an “accrual basis” model similar to current FASB standards, where the Total Pension Obligation (Actuarially determined) is compared to the Net Plan Position (or assets) and the difference represents the Net Pension Liability. This particular Statement will be applicable to the three Retirement Systems of the Commonwealth of Puerto Rico, not to the rest of the Commonwealth’s agencies or any of the Commonwealth’s component units. The impact of this Statement will be establishing its new net pension liability for the Commonwealth to an amount resembling the existing actuarial deficiency in the aforementioned Retirement Systems which at June 30, 2013 amounted to approximately \$34 billion.

22. NEW ACCOUNTING STANDARDS – continuation

GASB Statement No. 70 ("GASB 70"), *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, requires a state or local government guarantor that offers a nonexchange financial guarantee to another organization or government to recognize a liability on its financial statements when it is more likely than not that the guarantor will be required to make a payment to the obligation holders under the agreement.

A nonexchange financial guarantee is a credit enhancement or assurance offered by a guarantor without receiving equal or approximately equal value in exchange. The guarantor agrees to pay an obligation holder in the event that the issuer of the obligation is not able to make its required payments to the obligation holder. Nonexchange financial guarantees can include guarantees by a state for bonds issued by local governments within that state or guarantees of mortgage loans to individuals, if equal or approximately equal value is not received in exchange.

GASB 70 does not have any impact on the Municipality's financial statements.

23. SUBSEQUENT EVENT

In preparing these financial statements, the Municipality has evaluated significant transactions for potential recognition or disclosure through March 25, 2015, the date the financial statements were issued. Based on such analysis, no additional transaction need to be recorded or disclosed.

END OF NOTES

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES, PUERTO RICO
REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

	Budget Amounts		Actual Amounts	Variance with
	Original	Final	(Budgetary Basis) (See Note A)	Final Budget
BUDGETARY FUND BALANCE (DEFICIT), JULY 1, 2013	\$ (5,078,656)	\$ (5,078,656)	\$ (5,078,656)	\$ -
Resources (Inflows):				
Property Taxes	1,037,834	1,037,834	1,037,834	-
Volume of Business Taxes	344,375	344,375	162,848	(181,527)
Intergovernmental Revenues	8,326,136	8,326,136	7,474,088	(852,048)
Construction Excise Taxes	250,000	250,000	360,217	110,217
Sales and Usage Taxes	410,000	410,000	537,876	127,876
Miscellaneous	1,463,345	1,463,345	500,617	(962,728)
Rent	50,000	50,000	9,805	(40,195)
Transfer-In	-	-	546,135	546,135
Total Resources (Inflows)	11,881,690	11,881,690	10,629,420	(1,252,270)
Amounts Available for Appropriation	6,803,034	6,803,034	5,550,764	(1,252,270)
Charges to Appropriations (Outflows):				
Mayor and Municipal Legislature	275,420	287,021	682,339	(395,318)
General Government	7,796,110	7,946,652	5,347,007	2,599,645
Public Safety	1,062,357	935,652	962,869	(27,217)
Public Works	740,004	719,285	653,568	65,717
Culture and Recreation	681,552	669,656	711,900	(42,244)
Health and Sanitation	762,497	758,652	522,042	236,610
Human Services and Welfare	563,750	564,772	642,831	(78,059)
Urban Development	-	-	66,688	(66,688)
Capital Outlays	-	-	30,123	(30,123)
Transfer to Other Funds	-	-	686,509	(686,509)
Total Charges to Appropriations	11,881,690	11,881,690	10,305,876	1,575,814
BUDGETARY FUND BALANCE (DEFICIT), JUNE 30, 2014	\$ (5,078,656)	\$ (5,078,656)	\$ (4,755,112)	\$ 323,544

The accompanying Notes to Budgetary Comparison Schedule - General Fund are an integral part of this statement.

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, 2013

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 construction excise taxes and sales and usage taxes were less than expected. The Municipality's expenditures in General Government function were significantly less than the budgetary amount by \$1,880,916 due to cost cutting adjustments made during the year.

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

	<u>General Fund</u>
Sources/Inflows of Resources:	
Actual Amounts (Budgetary Basis) "Available for Appropriation" from the Budgetary Comparison Schedule (See Page 48)	\$ 5,550,764
Difference – Budget to GAAP:	
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes	(546,135)
The Fund Balance (Deficit) at the Beginning of Year is a budgetary resource but is not a Current-Year Revenue for financial reporting purposes	<u>5,078,656</u>
Total Revenues as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 19)	<u>\$ 10,083,285</u>
Uses/Outflows of Resources:	
Actual Amounts (Budgetary Basis) "Total Charges to Appropriation" from the Budgetary Comparison Schedule (See Page 48)	\$ 10,305,876
Difference – Budget to GAAP:	
Non budgetary expenditures (expenditures reclassification GASB 54)	1,127
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes	(112,331)
Payments of encumbrances of prior year that are expenditures for financial reporting purposes but are not outflows for budgetary purposes	-
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	<u>(686,509)</u>
Total Expenditures as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 19)	<u>\$ 9,508,163</u>

END OF THIS SECTION

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	\$ 572,862
Direct Program:			
Section 8 Housing Choice Voucher	14.871		<u>714,512</u>
Total U.S. Department of Housing and Urban Development .			<u>1,278,374</u>
U.S. Department of Homeland Security: Pass-Through Puerto Rico Office for Public Security:			
Disaster Grants – Public Assistance (Presidentially Declared Disasters)....	97.036		<u>54,445</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$1,332,819</u>

The accompanying Notes to Schedule of Expenditures of Federal Awards are an integral part of this schedule.

1. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the federal grant activities of the Autonomous Municipality of Vieques of the Commonwealth of 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* in the Other Governmental Funds column.

END OF NOTES

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

To the Honorable Mayor and
Municipal Legislature
Municipality of Vieques

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Vieques of the Commonwealth of Puerto Rico, (from now on the Municipality) as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements, and have issued our report thereon dated March 25, 2015. Our report was qualified because the Municipality did not provide a subsidiary of capital assets that agreed with the amounts reported in governmental activities of the Governmental-Wide Financial Statements and, also, the depreciation expense of those assets is not supported. In addition, no construction in progress is reported.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Municipality's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, 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 entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs, as items #14-01, #14-03, #14-04, #14-10, #14-12, #14-13, #14-14, and #14-15 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 #14-02, #14-05, #14-06, #14-07, #14-08, #14-09 and #14-11 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs, as items #14-01 through #14-15.

The Municipality's Response to Findings

The Municipality's responses to the internal control over compliance findings identified are described in a separate document (Corrective Action Plan) prepared by the Municipality. The Municipality's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

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

Carolina, Puerto Rico

March 25, 2015

Stamp #E156295 of the
College of CPA's of
Puerto Rico is affixed
to the original.

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON
INTERNAL CONTROL OVER COMPLIANCE OF FEDERAL AWARDS REQUIRED BY OMB CIRCULAR A-133**

To the Honorable Mayor and
Municipal Legislature
Municipality of Vieques

Report on Compliance for Each Major Federal Program

We have audited the Municipality of Vieques of the Commonwealth of Puerto Rico, (from now on the Municipality) compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of the Municipality's major federal programs for the year ended June 30, 2014. The Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Municipality's major federal programs based on our audit of the types of compliance requirements referred to above. 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 on compliance for each major federal program. However, our audit does not provide a legal determination of the Municipality's compliance.

Basis for Qualified Opinion on Section 8 Housing Choice Voucher Program and the Community Development Block Grant/States Program (SBGP)

As described in the accompanying schedule of findings and questioned costs as items #14-12 through #14-15, the Municipality did not comply with requirements regarding Cash Management and Equipment and Real Property Management that are applicable to the Community Development Block Grant/States Program (SBGP), and the Municipality did not comply with requirements regarding Eligibility and Reporting that are applicable to Section 8 Housing Choice Voucher Program. Compliance with such requirements are necessary, in our opinion, for the Municipality to comply with the requirements applicable to those programs.

Qualified Opinion on Section 8 Housing Choice Voucher Program and the Community Development Block Grant/States Program (SBGP) (Continued)

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion Paragraph, the Municipality complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.

Other Matters

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 item #14-11. Our opinion on each major federal program is not modified with respect to those matters.

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

Report on Internal Control Over Compliance

Management of the Municipality is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Municipality's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, 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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not 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 a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items #14-12 through #14-15 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 item #14-11 to be significant deficiency.

Report on Internal Control Over Compliance (Continued)

The Municipality's responses to the internal control over compliance findings identified are described in a separate document (Corrective Action Plan) prepared by the Municipality. The Municipality's was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the responses.

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

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

Carolina, Puerto Rico

March 25, 2015

Stamp #E156296 of the
College of CPA's of
Puerto Rico is affixed
to the original.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FOR THE YEAR ENDED JUNE 30, 2014

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).

	<u> X </u> yes	_____ no
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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

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	<u> X </u> no
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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

Part II - Findings Related to the Financial Statements:

FINDING NUMBER 14-01: SUPPORTING DOCUMENTS FOR DISBURSEMENT TRANSACTIONS NOT AVAILABLE

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

1. Three (3) disbursements made did not have a certification that merchandise received agrees in terms and quantities with the one specified in the purchase order and
2. Two (2) disbursements did not have an invoice in its supporting documents,

CRITERIA: As an appropriate internal control procedure, quotations should be requested as evidence of protecting municipal interests. Also, to comply with Chapter 4, sections 2, 14 and 15 from the Office of the Commissioner of Municipal Affairs (OCAM) Ruling for Municipal Administration, which states that 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.

CAUSE: The Municipality's internal control procedure to assure that all disbursements prepared have the quotations required by law, receiving reports, invoices and written certifications 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:

1. Chapter 8, Part III, Section 1, of the OCAM Ruling for Municipal Administration,
2. Chapter 4, sections 2, 14 and 15 of the OCAM Ruling for Municipal Administration and,
3. Informative Bulletin for the "Purchase Process of the Government of Puerto Rico" published by Comptroller's Office of Puerto Rico (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, receiving reports, invoices and written certifications. 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

FINDING NUMBER 14-02: SUPPORTING DOCUMENTS WITHOUT SIGNATURE OF MUNICIPAL OFFICIALS

CONDITION: Of a sample of twenty-five (25) disbursements examined, one (1) purchase order did not have the signature of the Agency Director.

CRITERIA: To comply with Chapter 4, Section 2 of OCAM Ruling for Municipal Administration which states all disbursement orders should be authorized by Mayor, Disbursing Officer, Finance Director and Pre-intervention In-charge. It also states that all purchase orders should be authorized by Mayor, Dependency In-charge and Finance Director.

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 Chapter 4, Section 2 of OCAM Ruling for Municipal Administration.

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

MANAGEMENT RESPONSE: See corrective action plan.

FINDING NUMBER 14-03: DISBURSEMENT ORDER MADE AFTER INVOICE DATE

CONDITION: Of a sample of twenty-five (25) disbursements examined, three (3) purchase orders were prepared after the invoice date.

CRITERIA: As an appropriate internal control procedure, a purchase order should be made in order to request a service or purchase goods as evidence of protecting municipal interests. Also, to assure that municipal officials are responsible for the legality, correctness, completeness and propriety of all disbursements authorized for payment.

CAUSE: The Municipality's internal control procedure to assure that all disbursements prepared have the appropriate authorizations from municipal officials and properly reviewed by the pre-intervention officer was not effective enough during this fiscal year.

EFFECT: The Municipality is not in compliance with internal control procedures related to disbursement procedures.

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

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, 2014

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

FINDING NUMBER 14-04: SUPPORTING DOCUMENTS OF DISBURSEMENT TRANSACTIONS INCOMPLETE

CONDITION: Of a sample of twenty-five (25) disbursements examined supporting documents for two (2) disbursements made were not found.

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.

CAUSE: The Municipality's internal control procedure to assure that all disbursements prepared were filled with all supporting documents as the quotations required by law, invoice, disbursement voucher 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:

Instance:

1. Chapter 8, Part III, Section 1, of the OCAM Ruling for Municipal Administration,
2. Chapter 4, Section 2(a), of the OCAM Ruling for Municipal Administration,
3. Chapter 4, Section 15 of the OCAM Ruling for Municipal Administration and
4. Chapter 4, Section 15 of the OCAM Ruling for Municipal Administration.

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 14-05: REQUIRED CLAUSES NOT INCLUDED ON CONTRACTS

CONDITION: We selected ten (10) contracts for examination. We noted the following required clauses were not included, stating the following:

1. That the Municipality may cancel the contract immediately in case of negligence, abandonment of duty or noncompliance from contract party (1 Contract), and

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

FINDING NUMBER 14-05: REQUIRED CLAUSES NOT INCLUDED ON CONTRACTS (CONTINUED)

2. That a 10% will be retained from every partial payment until completion of the project (1 Contract).

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 5, M, Law No. 237 of August 31, 2004, and
Memorandum No. 07-93 from the Office of the Governor of Puerto Rico

Instance 2 -

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.

MANAGEMENT RESPONSE: See corrective action plan.

FINDING NUMBER 14-06: CERTIFICATIONS NOT INCLUDED AS PART OF CONTRACT

CONDITION: We selected ten (10) 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 CPR for taxes or is under a payment plan (2 Contracts),

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

FINDING NUMBER 14-06: CERTIFICATIONS NOT INCLUDED AS PART OF CONTRACT(CONTINUED)

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, (1 Contract), and
3. Certification from the Department of Labor and Human Resources that no debt is outstanding for Unemployment and Disability taxes (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 3 –

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.

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.

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, 2014

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

FINDING NUMBER 14-07: EVIDENCE OF CONTRACT SUBMITTED TO THE COMPTROLLER OFFICE

CONDITION: Eight (8) contracts of a sample of ten (10) examined were not submitted to the Comptroller's Office of Puerto Rico, as required by Ruling #33, dated September 15, 2009, as amended.

CRITERIA: To comply with Ruling #33 from Comptroller's Office, Article 8(b) and as an appropriate internal control procedure, all contracts must be submitted to the Comptroller's Office within fifteen (15) days after awarded or after amended.

CAUSE: Municipality's internal control procedure to assure that all contracts were send to the Comptroller's Office within the period of time required, was not effective enough during this fiscal year.

EFFECT: The Municipality is not in compliance with the Ruling #33 from Comptroller's Office.

RECOMMENDATION: To implement a control procedures in order to send contracts to the Comptroller's Office within fifteen labor days after signed by parties, or after amended, as required by law.

MANAGEMENT RESPONSE: See corrective action plan.

FINDING NUMBER 14-08: 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. Performance Bond and Payment Bond Evidence,	1
2. No Legal Cases against the Municipality Certification	1
3. Certification of no Debt from the Department of Labor,	1

CRITERIA: To comply with OCAM Ruling for Municipal Administration, Chapter VIII, Part II, Sections 5, 10, 11 and 13.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

FINDING NUMBER 14-08: BIDS FILES INCOMPLETE (CONTINUED)

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

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 14-09: DOCUMENTS NOT AVAILABLE ON MUNICIPAL EMPLOYEE FILES

CONDITION: We selected twenty (20) employee files for examination. We noted the following documents were either not included or not appropriately filed:

1. Employee did not signed Section 1 of Form I-9 "Employment Eligibility Verification" from the Department of Homeland Security, U.S. Citizenship and Immigration Services (1 Employee file),
2. Employer did not sign and date the certification in section 2 of Form I-9 (1 Employee file),
3. Form 499 R-4.1 was not signed by employee (3 Employee files),
4. Documentation in employee file incomplete for one or more of the following:
 - a. Transcription of studies, diploma or any academic evidence (1 Employee file), and
 - b. ID with photo (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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

FINDING NUMBER 14-09: DOCUMENTS NOT AVAILABLE ON MUNICIPAL EMPLOYEE FILES (CONTINUED)

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 Internal Revenue Code of Puerto Rico (Code).

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: 14-10: 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

FINDING NUMBER: 14-10: LANDFILL CLOSURE AND POST-CLOSURE CARE COSTS NOT ACCUMULATED (CONTINUED)

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 years ended June 30, 2013, 2012 and 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 14-11: DISBURSEMENT ORDERS NOT AVAILABLE

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

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

- ✓ Seven (7) disbursements for a transaction under \$10,000 did not include a purchase order as part of the supporting evidence for the disbursements.

CRITERIA: As appropriate internal control procedure disbursements should be supported by appropriate documentation, which includes purchase order. This procedure will help 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, 2014

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

A - Activities Allowed or Unallowed

FINDING NUMBER 14-11: DISBURSEMENT ORDER NOT AVAILABLE (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. Condition represents 10% of the sample selected.

CONTEXT: We selected ten (10) disbursements made, under both federal awards, during the fiscal year 2013-2014 and verified their related supporting documents available.

CAUSE: The internal control procedures implemented by the Federal Awards Department of the Municipality to assure that all disbursements prepared have appropriate supporting documentation, 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: Disbursements under federal awards are not properly documented and 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: None

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, 2014

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

C - Cash Management

FINDING NUMBER: 14-12: FEDERAL ASSISTANCE NOT USED TO COVER IMMEDIATE EXPENDITURES

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

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 eight (8) labor days to disburse the amounts requested.

Federal Awards Receipt Date	Date Awards Were Used	Lapse of Time Between Receipt and Use of Awards	Deposit Amount
Program: SBGP			
8/08/2013	8/12/2013	4	\$ 51,902
5/13/14	5/21/14	8	39,175

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.

CONTEXT: We selected two 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 2013-14.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

C - Cash Management (Continued)

FINDING NUMBER: 14-12: FEDERAL ASSISTANCE NOT USED TO COVER IMMEDIATE EXPENDITURES (CONTINUED)

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

No Conditions Detected.

E - Eligibility

FINDING NUMBER 14-13: TENANTS'S FILES INCOMPLETE

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

CONDITION: Twelve (12) tenants' files observed did not include the following documents:

- Form HUD 9886 Privacy Authorization was not signed by all family members over 18 years old, and
- Form 52656 for the Initial Voucher was not included in the tenant file.

CRITERIA: Title 24 Housing and Urban Development, Volume 4, Code of Federal Regulations, Section 982.553 requires the Public Housing Administration (PHA) to deny admission of persons engaged in drug-related, violent or any other criminal activity which may threaten the health and safety of the premises by other residents. A criminal background check is necessary to document proper verification and determination of eligibility of tenants. Regarding unit's inspections, Title 24 of CFR section 982.404 requires the owner to correct defects identified within a 30-day period. In any case where the owner fails to correct such deficiencies, the PHA must stop HAP payments to the owner.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

E – Eligibility (Continued)

FINDING NUMBER 14-13: TENANTS'S FILES INCOMPLETE (CONTINUED)

CONTEXT: We selected twelve (12) tenant's files for Section 8 program 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 14-14: PROPERTY RECORDS OF FEDERAL AWARD (Finding Also Applies to the Financial Statements)

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

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

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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

F - Equipment and Real Property Management (Continued)

FINDING NUMBER 14-14: PROPERTY RECORDS OF ALL FEDERAL AWARD (Finding Also Applies to the Financial Statements) (CONTINUED)

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, 2014. 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, 2014.

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.

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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

I - Procurement and Suspension and Debarment

No Conditions Detected.

J - Program Income

No Conditions Detected.

K - Real Property Acquisition and Relocation Assistance

N/A.

L - Reporting

FINDING NUMBER: 14-15 SUBMISSION OF SECTION 8 FINANCIAL REPORTS TO THE REAL ESTATE ASSESSMENT CENTER'S (REAC)

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

CONDITION: The financial reports for the fiscal years 2012-2013 and 2013-2014 has not been transmitted to the REAC System as required by The Public Housing Agency.

CRITERIA: As required by The U.S. Department of Housing and Urban Development (HUD) created the Real Estate Assessment Center (PIH-REAC) to centralize and standardize the way HUD monitors and evaluates HUD developments and programs. Each Public Housing Agencies is responsible for submitting financial information to PIH-REAC/HUD for analysis.

CONTEXT: We request the financial report submitted to the REAC System and the report has not been submitted as of audit report date.

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 years 2012-2013 and 2013-2014.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2014

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

L - Reporting (Continued)

FINDING NUMBER: 14-15 SUBMISSION OF SECTION 8 FINANCIAL REPORTS TO THE REAL ESTATE ASSESSMENT CENTER'S (REAC) (CONTINUED)

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. 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.

QUESTIONED COSTS: None.

MANAGEMENT RESPONSE: See corrective action plan.

M - Subrecipient Monitoring

N/A

N - Special Tests and Provisions

No Conditions Detected.

(1) Audit Findings that have been Fully Corrected:

Finding Number	13-23 10-15	Reporting Late submission of Single Audit Report Package
CFDA Number	14.228, 14.871	
Questioned Cost	None	
Status	Corrected	
Finding Number	13-21 12-19 11-15 10-16 09-02 08-02	Reporting Submission of SBGP Financial Reports to OCAM.
CFDA Number	14.228	
Status	Corrected	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	13-17 12-16 11-11 10-11 09-01 08-01 07-02	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.	

(2) Audit Findings not Corrected or Partially Corrected:

FISCAL YEAR 2013

Finding Number	13-11	Activities Allowed or Unallowed Disbursement order without signature of municipal officials.
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	13-12	Activities Allowed or Unallowed Supporting documents not available for disbursement made.
CFDA Number	14.228	
Questioned Cost	\$52,858	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	13-13	Activities Allowed or Unallowed Supporting documents of disbursement transactions were not stamped as cancelled paid.
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development	
Finding Number	13-14	Activities Allowed or Unallowed Quotations not available for purchases made
CFDA Number	14.228	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development	
Finding Number	13-15	Activities Allowed or Unallowed Supporting documents of disbursement transactions incomplete.
CFDA Number	14.228, 14.871	
Questioned Cost	\$34,018	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development	

(2) Audit Findings not Corrected or Partially Corrected:(Continued)

Finding Number	13-16	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	13-18	Eligibility Tenants's files incomplete
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development	
Finding Number	13-19	Eligibility Section 8 program incomplete waiting list
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development	
Finding Number	13-20	Equipment and Real Property Management Property records of all federal awards
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	13-22	Reporting Submission of Section 8 Financial Report 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	

(2) Audit Findings not Corrected or Partially Corrected (Continued):

FISCAL YEAR 2012

Finding Number	12-09	Activities Allowed or Unallowed Disbursement order without signature of Municipal Officials.
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	12-10	Activities Allowed or Unallowed Supporting documents not available for disbursements made.
CFDA Number	14.228	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	12-11	Activities Allowed or Unallowed Supporting documents of disbursement transactions were not stamped as cancelled paid.
CFDA Number	14.228	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	12-13	Activities Allowed or Unallowed Quotations not available for purchase made.
CFDA Number	14.228	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	12-14	Activities Allowed or Unallowed Supporting documents of disbursement transactions incomplete.
CFDA Number	14.228	
Questioned Cost	\$65,456	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	

(2) Audit Findings not Corrected or Partially Corrected (Continued):

Finding Number	12-15	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.	
Number	12-17	Eligibility Tenant's files incomplete.
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	12-18	Equipment and Real Property Management Property records of all federal awards (finding also applies to the Financial Statements).
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.	
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.	

(2) Audit Findings not Corrected or Partially Corrected (Continued):

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.	
Finding Number	11-12	Eligibility
		Tenant's files incomplete.
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	11-13	Eligibility
		Section 8 Programs incomplete waiting list.
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	11-14	Equipment and Real Property Management
		Property records of all federal awards (finding also applies to the Financial Statements).
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 (Continued):

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.	

(2) Audit Findings not Corrected or Partially Corrected (Continued):

Finding Number	10-12	Eligibility Tenant's Files incomplete.
CFDA Number	14.871	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	10-13	Eligibility Section 8 Programs using different incomplete waiting lists.
CFDA Number	14.871, 14.249	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the US Department of Housing and Urban Development.	
Finding Number	10-14	Equipment and Real Property Management Property records of all federal awards.
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	10-17	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	09-3	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.	

(2) Audit Findings not Corrected or Partially Corrected (Continued):

FISCAL YEAR 2008

Finding Number 08-3 **Allowable Cost/Cost Principles**
Missing documentation on disbursement vouchers.

CFDA Number 14.228

Questioned Cost None

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

Finding Number 08-4 **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 2006

Finding Number 06-7 **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 2006

Finding Number 06-7 **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.

(2) Audit Findings not Corrected or Partially Corrected (Continued):

Finding Number	06-9	Eligibility Missing documentation in participants' files.
CFDA Number	14.856	
Questioned Cost	None	
Auditee Comments	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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VIEQUES

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

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	\$ 572,862
Direct Program:			
Section 8 Housing Choice Voucher	14.871		<u>714,512</u>
Total U.S. Department of Housing and Urban Development .			<u>1,278,374</u>
U.S. Department of Homeland Security: Pass-Through Puerto Rico Office for Public Security:			
Disaster Grants – Public Assistance (Presidentially Declared Disasters)....	97.036		<u>54,445</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$1,341,819</u>

The accompanying Notes to Schedule of Expenditures of Federal Awards are an integral part of this schedule.

	CONTRACT	necessary details and information, as required by proper 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 pre-investigator officer to verify all contracts prepared.	certification included to ensure all contracts prepared contains all the necessary certifications.		
#14-07	EVIDENCE OF CONTRACT SUBMITTED TO THE COMPTROLLER OFFICE	During the contract bid, contracts didn't contain the Comptroller's Office Submittal page, so it had to prove that it was submitted.	We always have the submittal sheet attached and its included in the Municipal Secretary Office.	Municipal Secretary	Done
#14-08	BIDS FILES INCOMPLETE	To implement review procedures to assure that all bid files includes all documents required by applicable laws and regulations. An employee independent to the Finance Department and the Bid Board should be designated to oversee the procedure.	We have prepared a checklist with all required documentation that should be included in the bid files.	Municipal Secretary	1-Jul-15
#14-09	DOCUMENTS NOT AVAILABLE ON MUNICIPAL EMPLOYEE FILES	The implementation of an internal control procedure requiring a checklist to be reviewed each time an employee is hired, and when and employee file is updated, to assure all required documents are available. Also, to schedule reviews of employee files for updating procedures.	We are preparing a checklist with all required documentation in the personnel files. This checklist will be signed by an employee who certifies that all documentation is complete. Annually the employee files will be verified to ensure that all certification are on file.	Personnel Director	1-Jul-15
#14-10	LANDFILL CLOSURE AND POST-CLOSURE CARE COSTS NOT ACCUMULATED	We are 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.	We understand the consequences of not have prepared the study to comply with state and federal regulations. The Municipality is in process of securing some state funds in order to begin with the required studies.	Finance Director	1-Jul-15
#14-11	DISBURSEMENT ORDER NOT AVAILABLE	Of a sample of disbursements examined for Section 8 Housing Choice Voucher Program the purchase order was not available in 7 disbursements made.	We are doing a purchase order per disbursement per OCRM instructions.	Finance Director	Done
#14-12	DISBURSEMENT ORDER WITHOUT SIGNATURE OF MUNICIPAL OFFICIALS	To strengthen control procedures to assure all disbursements are properly authorized by municipal officials and filed with all required supporting documents. Four (4) disbursement orders for transactions under \$10,000 did not have the signature of the Mayor (for Section 8 Housing Choice Voucher Program), and Four (4) disbursements did not have its supporting documents stamped and signed as pre-authorized by the Pre-Inspection Officer (For OIGP).	The control exist, we assure that the pre-audit review that all disbursements are properly authorized by municipal officials.	Finance Director	1-Jul-15
#14-13	FEDERAL ASSISTANCE NOT USED TO COVER IMMEDIATE EXPENDITURES	To strengthen the system for requesting federal funds to be adequate enough to easily immediate expenditures incurred by each federal program, and to avoid maintaining		Federal Program	1-Jul-15

PROJECT NUMBER	ACTIONS DESCRIPTION	AUDITOR'S RECOMMENDATION	CORRECTIVE ACTION PLAN	LEAD PERSONS ACCOUNTABLE FOR ACTION ITEM COMPLETION	TARGET COMPLETION DATE
#14-1	SUPPORTING DOCUMENTS FOR EXHIBITMENT CONTRACTS NOT AVAILABLE	<p>1. Items 13, 14 documents made did not have a verification for contract items received in terms and quantities with the date specified in the purchase order.</p> <p>2. Two (2) instruments did not have an action in its supporting documents.</p>	The City staff will ensure that all documents are received and included in its policy contract when the purchase order number distribution is made.	Finance Director	1 Jul 15
#14-2	SUPPORTING DOCUMENTS WITHOUT SIGNATURE OF MUNICIPAL OFFICIALS	To strengthen internal processes in terms of documents and purchase order items, verify signatures by municipal officials and that all required supporting documents are included before being sent for approval.	We advised in an electronic email to verify that all required documents are complete before by municipal officials before being sent for approval.	Finance Director	1 Jul 15
#14-3	EQUIPMENT ORDER MADE AFTER FISCAL DATE	It is a matter of policy that all equipment purchased should be approved and signed by the signature of the Mayor/ Mayor	We advised in an electronic email to ensure that all required documents are complete before by municipal officials before being sent for approval.	Finance Director	1 Jul 15
#14-4	SUPPORTING DOCUMENTS OF DISBURSEMENT INCOMPLETE	To strengthen internal processes in terms of documents and purchase order items, verify signatures by municipal officials and that all required supporting documents are included before being sent for approval.	The City staff will ensure that all documents are received and included in its policy contract when the purchase order number distribution is made.	Finance Director	1 Jul 15
#14-5	REQUIRED SAMPLES NOT INDICATED ON CONTRACTS	To strengthen internal processes in terms of documents and purchase order items, verify signatures by municipal officials and that all required supporting documents are included before being sent for approval.	We advised in an electronic email to ensure that all required documents are complete before by municipal officials before being sent for approval.	Municipal Secretary	Done
#14-6	CERTIFICATIONS NOT INCLUDED AS PART OF	To strengthen internal processes in terms of documents and purchase order items, verify signatures by municipal officials and that all required supporting documents are included before being sent for approval.	We have prepared a checklist with all required	Municipal Secretary	Done