OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES

AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL

AREA DE ARCHIVO DIGITAL

MUNICIPIO DE VILLALBA
AUDITORIA 2003-2004

30 DE JUNIO DE 2004

Cont Hor-5575-3

MUNICIPALITY OF VILLALBA, PUERTO RICO

Basic Financial Statements and Single Audit Reports

For the year ended June 30, 2004

Municipality of Villalba

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For the year ended June 30, 2004

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Municipality of Villalba

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ROSALY, OCASIO
AUDIT AND CONSULTING

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

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Villalba, Puerto Rico ("the Municipality"), as of and for the year ended June 30, 2004, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Villalba, as of June 30, 2004, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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As described in Note 1 to the basic financial statements, the Municipality of Villalba has implemented a new financial reporting model, as required by the provisions of the Governmental Accounting Standards Board ("GASB") Statement No. 34, Basic Financial Statements and Management's Discussion and Analysis - for State and Local Government; as of June 30, 2004.

The Management's Discussion and Analysis on pages I through X and the Budgetary Comparison Schedule – General Fund and the Budgetary Comparison Schedule – Debt Service Fund on pages 36 and 37 respectively, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with Government Auditing Standards, we have also issued our report dated March 18, 2005, on our consideration of the Municipality's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

To the Honorable Mayor
and Members of the Municipal Legislature
Municipality of Villalba
Villalba, Puerto Rico
Page # 3

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, Audit of States, Local Government, and Non-Profit Organizations, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects in relation to the basic financial statements taken as a whole.

Rosaly, Ocasio
Auditing & Consulting Group, PSC

License No. 74
Expires December 1, 2007

March 18, 2005

ROSALY, OCASIO AUDITING & CONSULTING GROUP, P.S.C.
PUERTO RICO
CERTIFIED PUBLIC ACCOUNTANTS
Lic# 74

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VILLALBA
FOR THE YEAR ENDED JUNE 30, 2004

MUNICIPALITY OF VILLALBA'S BASIC FINANCIAL SATATEMENTS
MANAGEMENT DISCUSSION AND ANALYSIS

HONORABLE WALDEMAR RIVERA TORRES
MAYOR

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Municipal Administration ("Management") of the Municipality of Villalba, in order to comply with the requirements of the Governmental Accounting Standards Board (GASB) Statement Number 34, ***"Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments"***, implemented the statement for the fiscal year ended on June 30, 2004 for the first time. This ***Management's Discussion and Analysis (MD&A)*** is focus on the current year activities and it should be read it in conjunction with the Municipality's Basic Financial Statement. This analysis present an overview of the financial performance of the Municipality of Villalba, and it's directed to provide a more specific understanding of the financial activities that will give the reader a precise and an objective idea, regarding the financial activities of the Municipality of Villalba for the fiscal year ended on June 30, 2004.

FINANCIAL HIGHLIGHTS

- The Municipality's Net Assets were ***$7,530,921.00*** at the end of the fiscal year.
- The Municipality's Fund Financial Statements show that Governmental Activities Revenues were ***$12,485,664.00*** for the fiscal year ended on June 30, 2004.
- The General fund showed an excess of Revenues over Expenditures of ***$392,327.00*** during the course of this year.
- The Governmental Activities Expenditures were ***$13,392,508.00*** for the fiscal year ended on June 30, 2004.
- The General Fund total expenditures for the fiscal showed an increase of ***$332,125.00*** or ***(4%)*** with last year's balances.
- The Municipality's Governmental Funds reported an ending Fund Balance of ***$428,208.00***, changing it from a Deficit to a Fund Balance.
- The Accumulated Deficit of the Administration decreased by ***$169,135.00*** or ***(100%)*** during the period ended on June 30, 2004 eliminating the entire Accumulated Deficit.

USING THIS FINANCIAL REPORT

This Financial Report will show both of the perspectives that are allowed to users, in order to address certain relevant questions, data and information that is capable of being

USING THIS FINANCIAL REPORT *(Continue)*

the basis for comparison, between more than one fiscal year. Also, this Financial Report will enhance the Municipality's accountability. This report is complimented of a new model of basic financial statements that provide both, ***Government – Wide and Fund – Type*** overview, of the Municipality's Financial Structure.

BRIEF DISCUSSION OF THE BASIC FINANCIAL STATEMENTS

The basic financial statements of the Municipality of Villalba consist of ***Government-Wide Financial Statements and Fund- Type Financial Statements***, as well as ***Notes to the Financial Statements.*** The Municipality of Villalba's Basic Financial Statements includes two new Government- Wide Financial Statements: ***The Statement of Net Assets and the Statement of Activities.*** Both ***Government- Wide Financial Statements*** distinguish governmental activities from business- type activities. The Municipality's governmental activities are supported, principally by the Intergovernmental revenues. The Municipality's ***Government- Wide Financial Statements*** are composed of only Governmental Activities, because no Business- Type Activities were made during the Fiscal year ended on June 30, 2004.

GOVERNMENT- WIDE FINANCIAL STATEMENTS

The Statement of Net Assets, one of the two new ***Government- Wide Financial Statements***, presents the information on all of the Municipality's assets and liabilities with the difference between both, reported as ***Net Assets***. This will become very useful overtime, because it will indicate the financial position of the Municipality, as to be improving or deteriorating.

The Statement of Activities, the other new ***Government- Wide Financial Statement***, will report how the Municipality's Net Assets changed during the course of the fiscal year. In this statement, all revenues and expenses are included regardless of when cash was paid or received. This Statement is focused on the gross and net costs of various activities and is intended to summarize and simplify the user's analysis of cost of the multiple governmental services.

The Government- Wide Financial Statements are presented on pages ***4*** to ***5*** of the Municipality of Villalba's Financial Statements.

FUND- TYPE FINANCIAL STATEMENTS

The Fund- Type Financial Statements will focus on the Municipality's Major Funds, which will be reported separately from all of the other funds. ***The Fund- Type Financial Statements*** provide detailed information about the Municipality's most significant Funds, not the Municipality as a whole. Unlike ***The Government- Wide Financial Statements, Fund- Type 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. Because the focus of Governmental Funds is narrower than that of the ***Government-Wide Financial Statements,*** it is recommended to compare the information presented for Governmental Funds, with comparable information presented, for Governmental Activities in the ***Government- Wide Financial Statements. The Fund- Type Financial Statements*** are composed of both, the Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances. These Statements will provide the user of this information a better comparison between Governmental Funds and Governmental Activities.

The Municipality's ***Fund- Type Financial Statements*** are presented on pages ***6*** to ***8*** of the Municipality of Villalba's Financial Statements.

NOTES TO THE FINANCIAL STATEMENTS

The Basic Financial Statements of the Municipality of Villalba also includes Notes to the Financial Statements. These Notes accompanied the Basic Financial Statements and they'll help to get a full understanding of the ***Government- Wide and Fund- Type Financial Statements.***

The ***Notes to the Financial Statements*** are presented on page ***9*** to ***35*** of the Municipality of Villalba's Financial Statements.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

The Municipality of Villalba implemented this new financial reporting model in the current fiscal year that ends on June 30, 2004. Every year, new financial information will be accumulated on a consistent basis, which will cause changes in Net Assets that should be observed and used, to discuss or compare the changing Financial Position of the Municipality as a whole.

NET ASSETS

The ***Net Assets*** are the excess of assets over liabilities. The ***Net Assets*** may serve as an indicator of the Municipality's Financial Position. The Municipality's Net Assets at fiscal year end are ***$7,530,921.00***. The following table provides a summary of the Municipality's Net Assets:

Municipality of Villalba
Summary of Net Assets
June 30, 2004

		Governmental Activities
Assets:		
Current Assets and Other Assets	$	6,271,516.00
Capital Assets		10,077,229.00
Total Assets		16,348,745.00
Liabilities:		
Current liabilities		3,013,638.00
Non current liabilities		478,049.00
Long- Term liabilities		5,326,137.00
Total liabilities		8,817,824.00
Net Assets:		
Invested in Capital Assets, Net of Debt		7,582,229.00
Restricted		2,964,078.00
Unrestricted		*(3,015,386.00)*
Total of Net Assets	$	7,530,921.00

Approximately ***62%*** of the Governmental Activities' Total Assets is Capital. The Municipality uses these Capital Assets to provide services to its citizens.

Current Ratio

Governmental Activities:

Current Assets / Current Liabilities ***$5,597,411.00 / $3,013,638.00***

The Current Ratio for the Municipality of Villalba is **1.85**

NET ASSETS *(Continue)*

The Municipality of Villalba has a positive Current ratio. The Current ratio indicates the ability of the Municipality to pay Current Obligations.

Comparative data cannot be presented, because this is the first year in which ***Government- Wide*** information is available. However, in future years an analysis of Comparative data will be possible, because of the accumulation of data gathered during the course of subsequent years.

CHANGES IN NET ASSETS

This Municipality is strongly supported by the Intergovernmental Revenues for the operations of this government. In the other hand, the Municipality's Expenses covered a range of activities, from which the largest expensed activity was General Government, followed by Health and Welfare, Public Works, Culture and Recreation, Community Development and last but not least, Public Safety. The following table will show a summary of the Municipality's Changes in Net Assets:

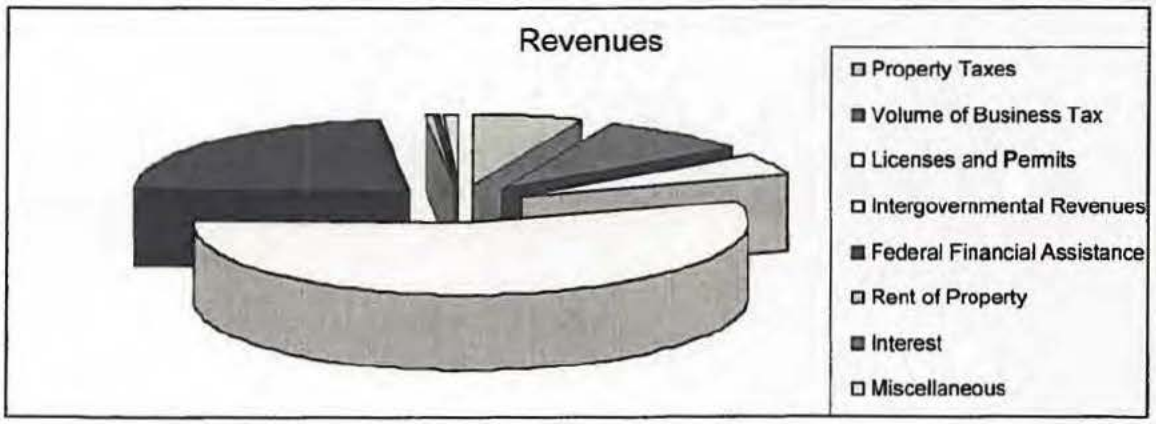
Municipality of Villalba
Summary of Changes in Net Assets
June 30, 2004

	Governmental Activities
Revenues:	
Program:	
Property Taxes	$ 793,078.00
Volume of Business Tax	1,113,495.00
Licenses and Permits	626,125.00
Intergovernmental Revenues	6,917,113.00
Federal Financial Assistance	2,840,307.00
Rent of Property	51,820.00
Interest	23,614.00
Miscellaneous	120,110.00
Total Revenues	12,485,662.00
Expenses:	
Program:	
General Administration	6,342,501.00
Public Safety	635,776.00
Public Works	1,211,429.00
Culture and Recreation	440,683.00

Environmental Control		38,515.00
Health and Welfare		771,085.00
Community and Economic Development		3,200,878.00
Payment of Principal ***(Debt Service)***		459,971.00
Interest		291,670.00
Total Expenses		13,392,508.00
Change in Net Assets		*(906,846.00)*
Beginning Net Assets		8,437,767.00
Ending Net Assets	$	7,530,921.00

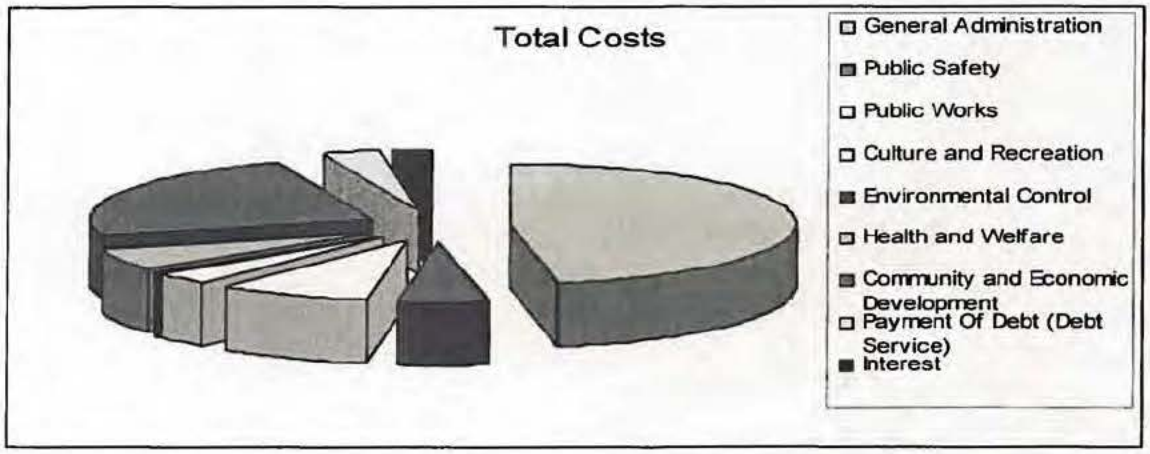
Intergovernmental Revenues provided ***55.4%*** of the Total Revenues for fiscal year 2004 and Federal Financial Assistance was ***22.7%*** of Total Revenues for the fiscal year ended on June 30, 2004.

Exhibit I



The Costs of all Activities during this fiscal year was ***$13,392,508.00*** with ***47.3%*** of the Total Costs being assigned to General Administration and ***23.9%*** to Community and Economic Development.

Exhibit II



FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

The Municipality uses fund accounting to ensure and demonstrate compliance with finance related legal requirements.

GOVERNMENTAL FUNDS

The ***Municipality's Governmental Funds*** Information is useful in assessing the Municipality's financial requirements. At the end of the fiscal year any resource available for spending should be measured by the unreserved fund balance. In the current fiscal year, the ***Municipality's Governmental funds*** reported a Total Fund Balance of ***$3,306,432.00,*** an excess of revenues over expenditures of *($597,343.00)* during this fiscal year was shown. There are reservations of Fund Balance up to ***$3,048,973.00.*** This reserved Fund Balance is committed to cover balances shown as follows:

- ***$84,894.00 is reserved to cover purchase orders of prior fiscal years.***
- ***$498,519.00 is to pay Debt Service.***
- ***$85,854.00 is reserved to pay for Capital Projects.***
- ***$2,379,705.00 is reserved for HUD Programs, for Legislative Resolutions and for other Governmental purposes.***

The ***Municipality's Governmental Funds*** includes the ***General Fund*** which is the Major Operating Fund of the Municipality and as of June 30, 2004, it showed a ***Fund Balance*** of ***$428,208.00.***

GENERAL FUND BUDGETARY HIGHLIGHTS

During the course of this fiscal year 2003-2004, there were no increases in revenues identified that could affect the Municipality's finances. Therefore, if no revenues were added, no expenditures were added neither in order to balance the budget.

CAPITAL ASSETS AND DEBT ADMINISTRATION

The Municipality's investment in capital assets as of June 30, 2004 is ***$13,091,825.00***, net of Accumulated Depreciation of *($3,014,596.00)* , leaving a Net Book Value of ***$10,077,229.00.*** The investment in capital assets includes land, buildings improvement, equipment and construction in progress.

The total increase in the Municipality's investment in capital assets for the current fiscal year was ***$1,470,166.00*** in terms of Net Book Value. Depreciation charges for the year totaled ***$457,664.00.***

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

DEBT ADMINISTRATION

The Puerto Rico Legislature has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each Municipality may be pledged.

The Law requires that in order for a Municipality to be able to issue additional general obligations bonds and notes, such Municipality must have sufficient *"Payment Capacity"*. The *"Payment Capacity"* is determine with the moneys deposits in the Redemption Fund of the Municipality and the amounts collected with respect to the Municipality's Special Additional Tax, as projected by the ***Government Development Bank (GDB)*** be enough to fulfill the general and the proposed additional general obligation. For a Municipality to incur additional general obligation debt it must be sufficient to service to maturity, the Municipality's outstanding general obligation debt and the additional proposed general obligation debt.

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of an interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly,

DEBT ADMINISTRATION ***(Continue)***

the Municipality's Basic Tax revenues would be available to make Debt Service payments on general obligation municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, are not sufficient to cover such Debt Service. It has never been necessary to apply Basic Taxes to pay Debt Service on general obligation debt for the Municipality.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on Intergovernmental Revenues as well as Federal Financial Assistance to carry out the governmental activities. Historically, these amounts have been predictable for every fiscal year, providing the Municipality with increases of approximately five percent. Federal Financial Assistance may vary if new grants are available but the revenue is also predictable.

Those factors were considered when preparing the Municipality's Budget for the fiscal year 2005-2006.

FINANCIAL CONTACT

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

MUNICIPALITY OF VILLALBA, PUERTO RICO
STATEMENT OF NET ASSETS
June 30, 2004

	Governmental Activities
ASSETS	
Cash and cash equivalents	
(includes $1,030,857 in certificate of deposit)	$ 4,918,234
Cash held with fiscal agent	679,177
Accounts receivable:	
Due from other governmental entities	674,105
Capital assets, net of related depreciation	10,077,229
Total assets	**16,348,745**
LIABILITIES	
Accounts payable and accrued liabilities	1,443,154
Due to other governmental entities	190,723
Deferred volume of business tax	1,200,437
Defered federal financial assistance revenue	28,066
Accrued interest	151,258
Non current liabilities:	
Due withing one year	478,049
Due in more than one year	5,326,137
Total liabilities	**8,817,824**
NET ASSETS	
Invested in capital assets, net of related debt	7,582,229
Restricted for:	
Debt service	498,519
Capital projects	85,854
Federal programs and state statutes	2,379,705
Unrestricted (deficit)	(3,015,386)
Total net assets	**$ 7,530,921**

See accompanying notes to basic financial statements.

MUNICIPALITY OF VILLALBA, PUERTO RICO
STATEMENT OF ACTIVITIES
For the year ended June 30, 2004

Governmental Activities Functions/Programs	Expenses	Program Revenue: Operating Grants and Contributions	Program Revenue: Capital Grants and Contributions	Net (Expenses) Revenues and Changes in Net Assets
General Administration	$ 6,429,264	$ 712,227	$ 2,108	$ (5,714,929)
Public Safety	660,383	-	-	(660,383)
Public Works	1,363,263	61,093	-	(1,302,170)
Culture and Recreation	629,133	-	-	(629,133)
Enviromental Control	38,515	-	-	(38,515)
Health	283,452	-	-	(283,452)
Welfare	490,638	417,091	-	(73,547)
Community and Economic Development	1,454,890	884,138	839,460	268,708
Interest	340,226	-	-	(340,226)
Total governmental activities	**$ 11,689,764**	**$ 2,074,549**	**$ 841,568**	**(8,773,647)**

General revenues:	
Property taxes	793,078
Volume of business tax	1,113,495
Licenses and permits	626,125
Intergovernmental revenues	6,681,581
Grants and contiributions not restricted to specific programs	159,723
Rent of property	51,820
Interest	23,615
Miscellaneous	188,924
Total general revenues	9,638,361
Change in Net Assets	864,714
Net Assets - Beginning of Year	**5,726,144**
Prior Period Adjustment	**940,063**
Net Assets - Beginning of Year, as restated	**6,666,207**
Net Assets - End of Year	**$ 7,530,921**

See accompanying notes to basic financial statements.

MUNICIPALITY OF VILLALBA, PUERTO RICO
BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2004

	General Fund	HUD Programs	Legislative Resolutions	Debt Service Fund	Agro-Industrial Building Project	Other Governmental Funds	Total Governmental Funds
ASSETS							
Cash and cash equivalents							
(includes $1,013,840 in certificates of deposits)	$ 1,967,827	$ 242,855	$ 655,691	$ -	$ 231,431	$ 1,820,430	$ 4,918,234
Cash held with fiscal agent	85,854	-	-	498,519	-	94,804	679,177
Accounts receivable:							
Due from other funds	1,779,263	24,849	818,061	-	-	780,225	3,402,398
Due from other governmental entities	103,296	375,301	-	-	79,479	116,029	674,105
Total assets	3,936,240	643,005	1,473,752	498,519	310,910	2,811,488	9,673,914
LIABILITIES AND FUND BALANCE							
Liabilities:							
Accounts payable and accrued liabilities	541,516	246,274	222,535	-	310,910	121,919	1,443,154
Due to other funds	1,575,356	177,402	30,150	-	-	1,619,490	3,402,398
Due to other governmental entities	190,723	-	-	-	-	-	190,723
Deferred volume of business tax	1,200,437	-	-	-	-	-	1,200,437
Defered federal financial assistance revenue	-	28,066	-	-	-	-	28,066
Accrued interest	-	-	-	-	-	102,704	102,704
Total liabilities	3,508,032	451,742	252,685	-	310,910	1,844,113	6,367,482
Fund balance:							
Fund equity:							
Reserved for encumbrances	84,894	-	-	-	-	-	84,894
Reserved for debt service	-	-	-	498,519	-	-	498,519
Reserved for capital projects	85,854	-	-	-	-	-	85,854
Reserved for federal programs and state statutes	-	191,263	1,221,067	-	-	967,375	2,379,705
Unreserved fund balance	257,460	-	-	-	-	-	257,460
Total fund balance	428,208	191,263	1,221,067	498,519	-	967,375	3,306,432
Total liabilities and fund balance	$ 3,936,240	$ 643,005	$ 1,473,752	$ 498,519	$ 310,910	$ 2,811,488	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	10,077,229
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds.	(5,852,740)
Net assets of governmental activities	$ 7,530,921

See accompanying notes to basic financial statements.

MUNICIPALITY OF VILLALBA, PUERTO RICO
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
For the year ended June 30, 2004

	General Fund	HUD Programs	Legislative Resolutions	Debt Service Fund	Agro-Industrial Building Project	Other Governmental Funds	Total Governmental Funds
REVENUES							
Property taxes	$ 567,679	$ -	$ -	$ 225,399	$ -	$ -	$ 793,078
Volume of business tax	1,113,495	-		-	-	-	1,113,495
Licenses and permits	626,125	-	-	-	-	-	626,125
Intergovernmental revenues	5,815,791	-	235,532	-	-	865,790	6,917,113
Federal financial assistance	-	1,839,016	-		841,568	159,723	2,840,307
Rent of property	51,820	-	-	-	-	-	51,820
Interest	19,731	201	-	3,433	103	146	23,614
Miscellaneous	120,110	-	-	-	-	-	120,110
Total revenues	8,314,751	1,839,217	235,532	228,832	841,671	1,025,659	12,485,662
EXPENDITURES							
General Administration	5,030,921	679,558	9,252	-	2,900	619,870	6,342,501
Public Safety	575,743	-	-	-	-	60,033	635,776
Public Works	1,090,181	38,499	82,749	-	-	-	1,211,429
Culture and Recreation	413,917	-	-	-	-	26,766	440,683
Enviromental Control	38,515	-	-	-	-	-	38,515
Health	271,904	-	-	-	-	-	271,904
Welfare	6,309	399,268	-	-	-	93,604	499,181
Community and Economic Development	31,928	643,107	841,626	-	1,154,834	529,383	3,200,878
Debt Service:							
Payment of principal	282,971	-	-	177,000	-	-	459,971
Interest	180,035	-	-	53,025	-	58,610	291,670
Total expenditures	7,922,424	1,760,432	933,627	230,025	1,157,734	1,388,266	13,392,508
Excess (deficiency) of revenues over expenditures	392,327	78,785	(698,095)	(1,193)	(316,063)	(362,607)	(906,846)
OTHER FINANCIAL SOURCES (USES):							
Operating transfers from other funds	3,612	-	-	-	-	-	3,612
Operating transfers to other funds	-	-	-	(3,612)	-	-	(3,612)
Refinancing of debt with AAA	201,404	-	-	-	-	-	201,404
Advances received from USDA - RD	-	-	-	-	-	130,940	130,940
Net other financing sources (uses)	205,016	-	-	(3,612)	-	130,940	332,344
EXCESS (DEFICIENCY) OF REVENUES AND OTHER SOURCES OVER EXPENDITURES AND OTHER USES	597,343	78,785	(698,095)	(4,805)	(316,063)	(231,667)	(574,502)
FUND BALANCE (DEFICIT) AT BEGINNING OF YEAR, AS PREVIOUSLY REPORTED	(169,135)	112,478	1,919,162	312,524	316,063	1,199,042	3,690,134
PRIOR PERIOD ADJUSTMENT	-	-	-	190,800	-	-	190,800
FUND BALANCE (DEFICIT) AT BEGINNING OF YEAR, AS RESTATED	(169,135)	112,478	1,919,162	503,324	316,063	1,199,042	3,880,934
FUND BALANCE AT END OF YEAR	$ 428,208	$ 191,263	$ 1,221,067	$ 498,519	$ -	$ 967,375	$ 3,306,432

See accompanying notes to basic financial statements.

MUNICIPALITY OF VILLALBA, PUERTO RICO
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
For the year ended June 30, 2004

Net change in fund balances - total governmental funds	$	(574,502)
Amounts reported in the statement of activities are different because:		
Gorvernmental funds report capital adquisitions as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in t		1,859,016
Depreciation expense on capital assets is reported in the statement of activities, but they do not require the use of current financial resources. Therefore, depreciation expense in not reported as expenditures in governmental funds.		(457,664)
Capital assets donated during the year are not current financial resources and therefore are not reported as revenues in the funds.		68,814
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 the governmental funds.		(158,577)
The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes current financial resources. This is the amount by which debt proceeds (exceed) or are below debt servi		127,627
Change in net assets of governmental activities	$	864,714

See accompanying notes to basic financial statements.

Municipality of Villalba

Notes to Basic Financial Statements

For the year ended June 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION:

The Municipality of Villalba, Puerto Rico ("the Municipality") was founded in 1917. The Municipality's governmental system consists of an executive and a legislative body. It is governed by a Mayor and fourteen members Municipal Legislature who are elected for four years terms through the Commonwealth of Puerto Rico general elections.

The Municipality provides general and administrative services, public safety, public work, culture and recreation, environmental control, health, education, housing and urban development, welfare and other miscellaneous services.

Since 1995, the Municipality is member of Consorcio de la Montaña, a local workforce investment area according to Section 116 (A) of Public Law 105-220 known as Workforce Investment Act of 1998 (WIA). The purpose of the Consorcio is to provide One-Stop service delivery area to administer federal programs and services pursuant to the Workforce Investment Act. The Mayor is member of the Board of Mayors which is responsible for the operations and decisions of the Consorcio.

ADOPTION OF NEW ACCOUNTING STANDARD:

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

In June 1999, the GASB issued Statement No. 34, Basic Financial Statements - Management's Discussion and Analysis - for State and Local Governments. This Statement establishes new financial reporting requirements for state and local governments.

It requires new information and restructures much of the information that governments have reported in the past. Comparability with reports issued in prior years is affected. In June 2001, the GASB issued Statement No. 37, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments Omnibus, which in part addressed the Management's Discussion and Analysis and Major Fund criteria requirements in the reporting model in Statement No. 34.

The Municipality implemented these Standards for the fiscal year ended June 30, 2004.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

A. THE FINANCIAL REPORTING ENTITY

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

Based on these criteria, at June 30, 2004, there are no potential component units for which the Municipality exercises oversight responsibility. Therefore, the reporting entity is limited to those departments, which comprise the Municipality's primary government.

B. GOVERNMENT-WIDE AND FUND FINANCIAL SATEMENTS

The government-wide financial statements (the statement of net assets and the statement of activities) report information of all the activities of the primary government and its component units, if any. For the most part, the effect of inter-fund activity has been removed from these government-wide financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, if any, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component units, if any, for which the primary government is financially accountable.

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

The fund financial statements segregate transactions related to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. These statements present each major fund as a separate column on the fund financial

statements; all non-major funds are aggregated and presented in a single column.

C. MEASUREMENT FOCUS, BASIS OF ACCOUNTING, AND FIANANCIAL STATEMENT PRESENTATION

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

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. Modification to the accrual basis of accounting includes;

1. Employees' vested annual leave is recorded as expenditure when utilized. The amount of accumulated annual leave unpaid at June 30, 2004, has been reported only in the government-wide financial statements.
2. Interest on general long-term obligations is recognized when paid.
3. Executory purchase orders and contracts are recorded as a reservation of fund balance.

4. Debt service expenditures and claims and judgments are recorded only when payment is due.
5. Capital assets acquisitions are reported as expenditure in governmental funds.
6. Proceeds from issuance of general long-term debt are reported as other financing sources.

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

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business type activities and enterprise funds, subject to this same limitation. The Municipality has elected not to follow subsequent private-sector guidance.

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

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

C. FUND ACCOUNTING

The financial activities of the Municipality are recorded in individual funds, each of which is deemed to be a separate accounting entity. The Municipality uses fund accounting to report on its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The financial activities of the Municipality that are reported in the accompanying financial statements have been classified into the following major governmental funds:

General Fund - This is the general operating fund of the Municipality and accounts for all financial transactions, except those required to be accounted for in another fund.

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

Legislative Resolutions - This fund accounts for the revenues derived from the Legislature of the Commonwealth of Puerto Rico which are earmarked for specific purposes.

Debt Service Fund – This fund is used to account for the accumulation of resources for and the payment of principal and interest on, the Municipality's general long-term debt obligations of governmental funds.

Agro-Industrial Building Project - This fund accounts for the proceeds of federal grant from the Department of Commerce which is earmarked for an Agro-Industrial Project.

D. CASH, CASH EQUIVALENTS AND CASH HELD WITH FISCAL AGENT

The Municipality's Finance Director is responsible for investing available resources. The Municipality is restricted by law to invest only in savings account and certificates of deposit with banks qualified as a depository of public funds by the Puerto Rico Treasury Department (PRTD) or in instruments of the Government Development Bank for Puerto Rico (GDB). The Municipality's policy is to invest any excess cash in certificates of deposit with institutions qualified by the PRTD. Earnings from these funds are recorded in the corresponding fund.

Cash held with fiscal agent in the general fund consists of unused loan proceeds from GDB for the payment of certain capital projects. Cash with fiscal agent in the debt service fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law.

The Municipality considers all investments with an original maturity of three months or less to be cash equivalents.

E. RECEIVABLES

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables in the general fund represent mostly contributions from the Puerto Rico Electric Power Authority, which contribute a specific percentage of their revenues as payment in lieu of taxes.

F. INTERFUND RECEIVABLES AND PAYABLES

The general fund provides services at cost to other funds. The amounts charged to these funds for the services provided are treated as a reduction of expenditures in the respective funds. Activities 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. Advances 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.

During the fiscal year ended June 30, 2004, the Debt Service Fund transferred to the General Fund a total of $3,612 representing interest earned on deposits held on behalf of the Municipality by the Government Development bank of Puerto Rico.

G. CAPITAL ASSETS

Capital assets, which include property, plant, equipment, and infrastructure (which is normally immovable and of value only to the Municipality, such as roads, bridges, streets sidewalks, and similar items), are reported in the governmental activities column in the government-wide financial statements. The Municipality defines capital assets as assets

with an initial, individual cost of more than $500 and an estimated useful life in excess of one year. Purchased capital assets are carried at historical cost or estimated historical cost. Donated capital assets are recorded at fair market value at the date of donation.

Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Others costs incurred for repairs and maintenance are expensed as incurred.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements.

Capital assets of the primary government are depreciated on the straight-line method over the assets' estimated useful life. Generally, estimated useful lives are as follows:

Description	Useful Life
Building and building improvements	30 years
Machinery and equipment	3-10 years
Recreation facilities	15-20 years
Vehicles	5-10 years

H. ENCUMBRANCES

Encumbrances accounting are used in all governmental funds. Under the encumbrances system all purchased orders, contracts and other commitments for expenditures of resources are recorded to reserve the portion of applicable appropriation for future obligations. Open encumbrances at year-end are reported as a reserve of fund balance since they do not constitute expenditures or liabilities. Encumbrances do not lapse at the close of the fiscal year but are carried forward as a reserve of fund balance until liquidated.

I. RESERVATIONS OF FUND BALANCE

Reservations of funds balance in the fund financial statements represent those portions of fund balances that are not appropriable for expenditure or that are legally segregated for a specific future use. The Municipality has the following reservations of fund balance:

- Encumbrances – represent future expenditures under purchase orders, contracts and other commitments. Generally these committed amounts will become liabilities in future periods as the goods or services are received or performed.

- Federal Programs – represents the reservations of amounts available for specific use under federal grant programs.

- Debt Service – represent net assets available to finance future debt service payments.

- Capital Projects – represents the reservation of amounts to be used for future expenditures for capital projects under contract or other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.

J. RISK FINANCING

The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. The Puerto Rico Treasury Department negotiates insurance policies and costs are allocated among all the municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2004 amounted to approximately $92,485. The CRIM also deducted

$181,867 for workers compensation insurance covering all municipal employees.

K. COMPENSATED ABSENCES

Employees accumulate vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work.

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the then current rate, if the employee has at least 10 years of service of the Municipality.

L. USE OF ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

2. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. BUDGETARY CONTROL

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

Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

The Municipality prepares its annual budget including the operations of the general and the debt service funds. Certain other budget are prepared on a grant or project basis, including the activities programmed under the Community Development Block Grant/State's Program (CDBG), however these are not legally enacted.

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

See required supplementary information on pages 36 thru 38.

B. LEGAL COMPLIANCE

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

3. PROPERTY TAXES

The personal property tax is self assessed by the taxpayer on a return which is to be filed by May 15 of each year with the Municipal Revenue Collection Center (CRIM), a governmental entity created by the government of Puerto Rico as part of the Municipal

Governmental Autonomy Law of August 30, 1991. Since July 1, 1993, real property tax is assessed by the CRIM on each piece of real estate and on each building.

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amount advances 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 the year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. Total advances from CRIM as of June 30, 2004 presented as non current liabilities in the government-wide financial statements amounted to $1,932,607 (see note 10).

Based on the final settlement, during the year ended June 30, 2004, the amount received in advances from CRIM exceeded the amount collected from taxpayers and charges by CRIM for the same period by $31,820. Such amount is presented as due to other governmental entities in the basic financial statements.

In accordance with Public Law 190 enacted on July 30, 1999 the Municipality was entitle to a moratorium on the payment of any debt to CRIM arising from the final settlements of advances vs. actual collections through fiscal year 1998-99. Such moratorium was due to expire on June 30, 2001 after which date the Municipality has the right to request a payment plan for a period of up to five years, in accordance with Public

Law 234, enacted on August 12, 1998. However, on January 26, 2000, Public law 42 was enacted which revoked laws 190 and 234, and which authorized the CRIM to obtain a loan up to $200 million, and for a term not exceeding 10 years, to allow for the financing of the debt that the Municipalities have with the CRIM arising from final settlements of property tax advances vs. actual collections through fiscal year 1999-2000. The amounts that the Municipalities will collect from the additional property taxes resulting from the increase in the subsidy from the Central Government to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of Public Law 238, enacted on August 15, 1999. In addition, Public Law 146 of October 11, 2001, as amended, amends law 42 to extent the term of the financing from 10 years to 30 years. Subsequently, on August 11, 2002 Public Law 172 was enacted which amends law 42, and which authorized the financing of debt that the Municipalities have with the CRIM arising from final settlements of property tax advances vs. actual collections through fiscal year 2000-2001.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first $15,000 of the assessed value. For such exempted amounts, the Puerto Rico Treasury Department assumes payment of the basic tax to the Municipalities, except for property assessed at less than $3,500 for which no payment is made. As part of the Municipal Autonomous Law of 1991, the exempt amount to be paid by the Puerto Rico Treasury Department to the Municipalities was frozen as of January 1, 1992. In addition, the law grants a tax exemption from the payment of personal property taxes of up to $50,000 of the assessed value to retailers having annual net sales of less than $150,000.

The annual tax rate for fiscal year 2003-04 is 8.58% for real property and 6.58% for personal property of which 1.03% of both tax rates is for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 6.0% and 4.0%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in 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. From such fund, a distribution is made to all

municipalities; (b) 1.75% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund. The Commonwealth also contributes an annual tax rate of 0.2% of the property tax collected and such amount is accounted for similar to item (a) above.

4. DEPOSITS

Under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

The Municipality's bank balances in commercial banks of approximately $5,147,873 were fully collaterized at June 30, 2004.

The deposits at GDB of approximately $180,659 that is restricted principally for capital projects and the $498,519 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

As of June 30, 2004, the Municipality's cash and cash equivalents are classified by credit risk category as shown below:

			Credit Risk Category		
Description	Carrying Amount	Bank Balance	1	2	3
Cash	$4,566,554	$4,117,016	$3,437,839	$ --	$ 679,177
Certificate of deposit	1,030,857	1,030,857	--	1,030,857	--
Total	$5,597,411	$5,147,873	$3,437,839	$1,030,857	$679,177

The cash classified in category 3 at June 30, 2004 correspond to interest bearing account and deposits maintained in the Government Development Bank for Puerto Rico.

The following is a description of the categories of credit risk:

Category	Description
1	The deposits are insured or collaterized with securities held by the Municipality or by its agent in the Municipality's name.
2	The deposits are collateralized with securities held by the financial institution's trust department or its agent in the Municipality's name.
3	The deposits are uninsured and uncollaterized.

5. MUNICIPAL LICENSE TAX

The Municipality imposes a municipal license tax on all business that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the prior year's gross sales. Entities with sales volume of $1 million or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2004, tax rates were as follows:

- Financial business - 1.50% of gross revenues
- Other organizations - .50% of gross revenues

All taxpayers are required to file their declaration five days after April 15 of each year. This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before five days after April 15 of each year.

Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year is recorded as deferred revenues.

6. INTERGOVERNMENTAL REVENUES

Intergovernmental revenues in the general fund consist mainly of collections from the Commonwealth of Puerto Rico and payments in lieu of taxes from certain public corporations, principally the Puerto Rico Electric Power Authority.

Following is detail of the principal intergovernmental revenue:

Puerto Rico Electric Power Authority	$ 614,008
Property Taxes – basic	5,036,705
Reimbursement from the Commonwealth of Puerto Rico for Christmas bonus expenditures	128,997
Total	$ 5,779,710

7. DUE TO OTHER GOVERNMENTAL ENTITIES

Current liabilities with other governmental entities at June 30, 2004 are as follows:

	Due to
Puerto Rico Aqueducts and Sewer Authority	$ 93,226
Municipal Revenues Collection Center (CRIM)	31,821
Retirement System Administration	43,280
Puerto Rico Telephone Company	7,028
Department of Labor	13,130
General Services Administration	2,238
Total	$ 190,723

8. DEFERRED REVENUES

Municipal License Tax

The deferred revenues of approximately $1,200,437 in the general fund relates to municipal license tax collect in fiscal year 2003-04 that will be earned in fiscal year 2004-05.

Federal Government

The deferred revenues presented in the special revenue funds represent the portion of federal grants received for which qualifying expenditures have not been incurred. The amount was determined taking into consideration the specific years of the grant.

9. CAPITAL ASSETS

Capital assets activity during the year ended June 30, 2004 was as follows:

	Balance June 30, 2003	Increases	Decreases	Balance June 30, 2004
Governmental activities:				
Capital assets, not being depreciated:				
Land	$ 935,362	$ --	$ --	$ 935,362
Construction in progress	1,704,845	1,157,734	--	2,862,579
Total capital assets, not being depreciated	2,640,207	1,157,734	--	3,797,941
Capital assets, being depreciated:				
Building and building improvements	3,942,698	102,262	--	4,044,960
Machinery and equipment	204,762	68,957	--	273,719
Recreation facilities	2,978,618	457,938	--	3,436,556
Vehicles	1,397,710	140,939	--	1,538,649
Total capital assets, being depreciated	8,523,788	770,096	--	9,293,884
Less accumulated depreciation for:				
Building and building improvements	530,917	132,411	--	663,328
Machinery and equipment	71,744	39,976	--	111,720
Recreation facilities	1,455,099	113,419	--	1,568,518
Vehicles	499,172	171,858	--	671,030
Total accumulated depreciation	2,556,932	457,664	--	3,014,596
Total capital assets, being depreciated, net	5,966,856	312,432	--	6,279,288
Governmental activities capital assets, net	$ 8,607,063	$1,470,166	$ --	$ 10,077,229

Depreciation expense was charged to functions/programs of the Municipality as follows:

General administration	$ 35,230
Public Safety	38,798
Public Work	183,637
Culture and Recreation	188,451
Health	11,548
Total depreciation expense	$ 457,664

10. LONG-TERM DEBT

Changes in long-term debt are summarized as follows:

	Balance at July 1, 2003	Borrowings O r Additions	Payments or Deductions	Balance at June 30, 2004	Due Within One Year
General obligations	$ 1,352,000	$ 1,320,000	$ 177,000	$ 2,495,000	$ 222,000
Advances from PRTD	204,911	--	81,600	123,311	81,600
Advance from CRIM (Note 3)	1,968,585	--	35,978	1,932,607	27,358
Long-term agreement with GDB	6,231	--	2,991	3,240	2,991
Community Facilities Loans and Grants – Direct Loan	1,189,060	130,940	1,320,000	--	--
Accrued vacations and sick leave	860,226	110,024	--	970,250	100,000
P.R. Department of Labor and Human Resources	111,676	--	111,676	--	--
Puerto Rico Aqueducts and Sewer Authority	--	201,403	50,725	150,678	44,100
Payment of claims and Judgments	878,363	-	749,263	129,100	-
Total	$ 6,571,052	$ 1,762,367	$ 2,529,233	$ 5,804,186	$ 478,049

General obligations at June 30, 2004, consist of bonds and notes as follows:

• 1992 public improvements bonds due in annual installments of $10,000 to $31,000, through January 1, 2016, with interest at 5%.	$ 280,000
• 1998 general obligations note due in annual installments of $25,000 to $45,000, through July 1, 2004; with interest ranging from 4.865% to 6.710%.	45,000
• 1998 general obligation note due in annual installments of $20,000 to $35,000, through July 1, 2005; with interest ranging from 4.865% to 6.310%.	65,000
• 2000 general obligation note due in annual installments of $35,000 to $50,000, through July 1, 2007; with interest ranging from 5% to 8%.	185,000
• 2001 general obligation bond due in annual installments of $5,000 to $30,000, through July 1, 2025; with interest ranging from 5% to 8%.	280,000
• 2002 general obligation note due in annual installments of $15,000 to $25,000, through July 1, 2008; with interest ranging from 5% to 7%.	115,000
• 2003 general obligation note due in annual installments of $25,000 to $40,000, through July 1, 2009; with interest ranging from 5% to 6.5%.	205,000
• 2001 general obligation bond due in annual installments of $34,000 to $94,000, through January 1, 2026; with interest at 4.75%.	1,320,000
Total general long-term debt obligations	$ 2,495,000

These notes and bonds are payable from the additional property tax of 1.75% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes (see Note 3).

The annual requirement for the amortization of general obligations outstanding as of June 30, 2004, is as follow:

Year ended June 30,	Principal	Interest
2005	$ 222,000	$ 103,460
2006	189,000	104,955
2007	172,000	98,301
2008	176,000	90,571
2009	129,000	83,350
Next five years	455,000	348,021
Thereafter	1,152,000	374,680
Total	$ 2,495,000	$ 1,203,338

Advances from PRTD

On November 6, 2000, a formal agreement for the payment of property tax advances to the Puerto Rico Treasury Department was signed. The agreement consists in 59 monthly installments of $6,800 and a final installment of $7,711, starting January 1, 2001 through December 2005. All the payments will be made through retention from the monthly remittance from CRIM.

Advances from CRIM

This amount represents the balance owed to CRIM at June 30, 2004 as described in note 3, and that is being repaid through a financing obtained by the CRIM, as authorized by law and as explained in that note 3.

Long-term debt with GDB

In December 8, 2000 the Municipality received an operational loan from Government Development Bank for Puerto Rico of $385,000 for the payment of statutory debt. Since the monies were never used, in June 21, 2001 the Municipality requested the

cancellation of that loan. As of June 1, 2001 interest on the loan stop to accrue and a formal payment plan was agreed. The payment plan is for 48 monthly installments of $249 from August 1, 2001 through July 1, 2005. All the payments will be made through retention from the monthly remittance from CRIM.

At June 30, 2004 the Municipality issued a special obligation note from Government Development Bank for Puerto Rico for $470,000 for the purchase of equipment. Principal is due in annual installments of $55,000 to $80,000 through July 1, 2011, with interest ranging from 5% to 6%. GDB disbursed the note on July 1, 2004.

Community Facilities Loans and Grants – Direct Loan

In July 2, 2001 the Municipality obtained a direct loan from USDA – Rural Development of $1,320,000 for the final construction of a municipal theater. In June 19, 2002, the Municipality received the first advance of $375,013. During the fiscal year 2002-2003 the Municipality received other advances totaling $814,047. All advances will be annotated into the "Payment Register of the Promissory Note in Advance of Global Bonds" until total loan amount is reach. Then a bond will be issued by GDB substituting the Global Note. During the fiscal year 2003-2004 the Municipality received final advance in the amount of $130,940. Accordingly, on February 25, 2004 a general bond obligation was issued to substitute the Global Note.

Long-term debt with PRDOL

In March 8, 2001 the Municipality refinanced a liability amounting to $300,444, with the Puerto Rico Department of Labor. The agreement is for 36 monthly installments of $9,889 including interest at approximately 11.4%. All the payments will be made directly from the Municipality.

Long-term debt with Puerto Rico Aqueducts and Sewer Authority

In November 21, 2003 the Municipality refinanced a liability amounting to $201,404, with the Puerto Rico Aqueducts and Sewer Authority. The agreement is for 48

monthly installments of $3,675 without interest. All the payments will be made directly from the Municipality.

The Municipality is subjected to a legal debt margin requirement, which is equal to 10% of the total assessment of property located within the Municipality. In addition, before any new bonds or notes are issued, the revenues of the debt service fund should be sufficient to cover the project debt service requirement. Total property assessed value at June 30, 2004 amounted to $32,828,015. Long-term debt, except for the general obligations and advances from CRIM, is paid with unrestricted

11. PRIOR PERIOD ADJUSTMENT

During this year, as part of the conversion process, as required by GASB Statement No. 34, the Municipality reclassify prior year presentation related to general long-term debt obligations in which principal and interest due on July 1 of the following fiscal year were previously accounted for as a debt service fund liability ($190,800), instead of the general long-term account group. In addition, the Municipality adjusts its beginning net assets for an overstatement in its reserve for claims and judgments for $749,263.

12. PENSION PLAN

The Employees' Retirement System of the Commonwealth and its Instrumentality's (the Retirement System) is a cost-sharing multiple-employer defined benefit pension plan sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Municipality under 55 years of age at the date of employment become members of the Retirement System as a condition to their employment.

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

Members who have attained 55 years of age and have completed at least 25 years of creditable service or members who have attained 58 years of age and have not completed ten years creditable service are entitled to an annual benefit payable in monthly for life.

The amount of the annuity shall be one and one-half percent of the average compensation, as define, multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation, as define, and multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than $200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65 percent of the average compensation, as defined; otherwise they will receive 75 percent of the average compensation, as defined. No benefits are payable if the participant receives a refund of his/her accumulated contributions.

Commonwealth legislation requires employees to contribute 5.775% for the first $550 of their monthly gross salary and 8.275% for the excess over $550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total employee and employer contributions during the year ended June 30, 2004 amounted to approximately $185,122 and $207,488, respectively.

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

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

13. CONTINGENCIES

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions. It is management's opinion, based on the advice of the legal counsels, that the potential claims against Municipality not covered by insurance will not materially affect the financial condition of the Municipality.

The Municipality participates in a number of federal financial assistance programs funded by the Federal Government. Expenditures financed by these programs are subjected to financial and compliance audits by the appropriate grantor or sub-grantor. The "Reports on Compliance and Internal Control in accordance with Government Auditing Standards and the Requirements of OMB Circular A-133" - for the year ended June 30, 2004 disclosed several instances of noncompliance with applicable laws and regulations and with internal accounting and administrative controls.

If expenditures are disallowed due to noncompliance with grant programs regulations, the Municipality may be required to reimburse to the grantor. Management believes that the Municipality will be able to comply with the terms of corrective action plans that may be requested by the federal grantors. Management has provided in the general long-term debt account group an estimated liability for the total exposure for claims and judgments arising from lawsuits and federal actions.

14. SUBSEQUENT EVENTS

During August 2004 the Municipality authorized through ordinance number 20, series 2004-2005, the issuance of $505,000 municipal general obligation bonds for the acquisition of a building and related financing costs.

During December 2004 the Municipality authorized through resolution number 27, series 2004-2005, the issuance of $555,000 special obligation note for the acquisition of equipment and related financing costs.

MUNICIPALITY OF VILLALBA, PUERTO RICO
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
For the year ended June 30, 2004

	Budgeted Amounts		Actual Amounts Budgetary Basis	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES AND OTHER FINANCING SOURCES:				
Property taxes	$ 899,344	$ 899,344	$ 567,679	$ (331,665)
Volume of business tax	1,107,000	1,107,000	1,102,271	(4,729)
Licenses and permits	998,303	998,303	626,125	(372,178)
Intergovernmental revenues	5,178,662	5,178,662	5,781,619	602,957
Rent of property	30,000	30,000	51,820	21,820
Interest	12,000	12,000	19,729	7,729
Miscellaneous	96,000	96,000	19,731	(76,269)
Operating transfer from other fund	-	-	3,612	3,612
Total revenues and other financing sources	**8,321,309**	**8,321,309**	**8,172,586**	**(148,723)**
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
General Administration	5,528,453	5,836,042	4,837,476	998,566
Public Safety	673,988	578,225	569,994	8,231
Public Works	1,202,792	1,137,680	998,205	139,475
Culture and Recreation	451,892	394,515	396,192	(1,677)
Enviromental Control	38,000	34,710	31,686	3,024
Health	355,884	270,877	271,904	(1,027)
Welfare	8,300	7,460	6,309	1,151
Community and Economic Development	3,000	2,800	2,787	13
Debt Service:				-
Payment of principal	-	-	282,971	(282,971)
Interest	-	-	180,036	(180,036)
Operating transfer to other fund	59,000	59,000	-	59,000
Total expenditures, encumbrances and other financing uses	**8,321,309**	**8,321,309**	**7,577,560**	**743,749**
Excess of revenues and other financing sources over expenditures, encumbrances and other financing uses	**$ -**	**$ 0**	**$ 595,026**	**$ 595,026**

See accompanying notes to basic financial statements.

MUNICIPALITY OF VILLALBA, PUERTO RICO
BUDGETARY COMPARISON SCHEDULE - DEBT SERVICE FUND
For the year ended June 30, 2004

	Budgeted Amounts		Actual Amounts Budgetary Basis	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES AND OTHER FINANCING SOURCES:				
Property taxes	$ 258,553	$ 258,553	$ 225,399	$ (33,154)
Interest	-	-	3,433	3,433
Total revenues and other financing sources	**258,553**	**258,553**	**228,832**	**(29,721)**
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Debt Service:				
Payment of principal	157,000	157,000	177,000	(20,000)
Interest	44,280	44,280	53,025	(8,745)
Operating transfer to other fund	-	-	3,612	(3,612)
Total expenditures, encumbrances and other financing uses	**201,280**	**201,280**	**233,637**	**(32,357)**
Excess (deficiency) of revenues and other financing sources over expenditures, encumbrances and other financing uses	**$ 57,273**	**$ 57,273**	**$ (4,805)**	**$ (62,078)**

See accompanying notes to basic financial statements.

Municipality of Villalba

Notes to Required Supplementary Information – Budgetary Comparison Schedules

For the year ended June 30, 2004

The Budgetary Comparison Schedules (NON-GAAP Budgetary Basis), where prepare only for the operations of the general and the debt service funds. The annual budget as presented in the Budgetary Comparison Schedules (NON-GAAP Budgetary Basis) is the budget ordinance to June 30, 2004 representing the original budget adjusted by various Mayor's Resolutions and Municipal Legislature Ordinances.

BUDGETARY DATA RECONCILIATION

The following schedule presents comparisons of the legally adopted budget with actual data on a budget basis. Because accounting principles applied for purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP (see note 2 to basic financial statements), a reconciliation of entity and timing differences in the excess of revenues and other financing sources over expenditures and other financing uses for the year ended June 30, 2004 is presented below for the general, and debt service funds:

General Fund:		
Accounting basis per Statement of Revenues, Expenditures and Changes in Fund Balance (Deficit)	$ 8,314,751	$ 7,922,424
Timing differences:		
Add:		
Current year encumbrances recorded as expenditures for budgetary basis		84,894
Deduct:		
Prior year encumbrances recorded as current year expenditures for GAAP basis		(147,561)
Deduct:		
Non-budgetary items	(142,165)	(18,174)
Payment of "Resultas"	--	(264,023)
Budgetary basis per Budgetary Comparison Schedule – General Fund	$ 8,172,586	$ 7,577,560

MUNICIPALITY OF VILLALBA, PUERTO RICO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the year ended June 30, 2004

Federal Grantor Pass-Trough Grantor Program Title	Federal CFDA Number	Pass-Trough Grantor Number	Federal Expenditures
U.S. Department of Housing and Urban Development			
Direct Program:			
Section 8 Housing Choice Vouchers	14.871	RQ-049-VO	$480,148
Passed through the Puerto Rico Office of Commissioner of Municipal Affairs:			
Community Development Block Grant / State's Program			
	14.228	B-98-CD-72-0001	214,252
	14.228	B-99-CD-72-0001	173,962
	14.228	B-00-CD-72-0001	20,190
	14.228	B-01-CD-72-0001	257,515
	14.228	B-02-CD-72-0001	326,382
	14.228	B-03-CD-72-0001	299,081
			1,291,382
Total U.S. Department of Housing and Urban Development			1,771,530

See notes to Schedule of Expenditures of Federal Awards.

MUNICIPALITY OF VILLALBA, PUERTO RICO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the year ended June 30, 2004

Federal Grantor Pass-Trough Grantor Program Title	Federal CFDA Number	Pass-Trough Grantor Number	Federal Expenditures
U.S. Department of Justice			
Pass-through Puerto Rico Department of Justice:			
Crime Victims Assistance	N/A	00-VA-VCV-01	10,752
Local Law Enforcement Block Grant	N/A	2001-LB-BX-2794	15,924
		2002-LB-BX-2449	60,000
Total U.S. Department of Justice			86,676
Federal Emergency Management Agency			
Pass-through GAR Disaster Assistance:			
FEMA 1277	83.544		35,459
Department of Commerce			
Grants For Public Works and Economic Development Facilities	11.300	01-01-07587	1,157,734

See notes to Schedule of Expenditures of Federal Awards.

MUNICIPALITY OF VILLALBA, PUERTO RICO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the year ended June 30, 2004

Federal Grantor Pass-Trough Grantor Program Title	Federal CFDA Number	Pass-Trough Grantor Number	Federal Expenditures
U.S. Department of Health and Human Services			
Pass-through Puerto Rico Department of Family:			
Child Care and Development Block Grant	93.575		68,525
Special Programs for the Aging – Title III, Part C- Nutrition	93.045		68,145
Total U.S. Department of Health and Human Services			136,670
U.S. Department of Agriculture			
Passed through the Government Development Bank of Puerto Rico			
Community Facilities Loans and Grants – Direct Loan	10.766		130,940
Total Federal Financial Assistance			$3,319,009

N/A- Number not available

See notes to Schedule of Expenditures of Federal Awards.

MUNICIPALITY OF VILLALBA, PUERTO RICO

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the year ended June 30, 2004

1. BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards is presented on the modified accrual basis of accounting and was prepared primarily from the Municipality's internal accounting records. The financial statements of the Municipality are presented on the basis of funds and account groups, each of which is considered a separate accounting entity. The operation of each fund is presented in a separate set of self-balancing accounts that comprises its assets, liabilities, fund equity, revenues and expenditures or expenses, as appropriate. Government resources are allocated to and accounted for by individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The accounts and other accounting records of the Municipality were not designed to capture the information required to prepare the basic financial statements, consequently, such information was obtained from different individuals, departments and accounting records or reports which are not integrated into a double entry bookkeeping system. In addition, several departments within the Municipality are responsible for managing federal financial assistance and there is no centralized control for all federal financial assistance programs. The Municipality's reporting entity is defined in Note 1 to the basic financial statements.

2. CATALOG OF FEDERAL DOMESTIC ASSISTANCE ("CFDA")

Catalogs of Federal Domestic Assistance ("CFDA") numbers are presented for programs for which such numbers are available.

MUNICIPALITY OF VILLALBA, PUERTO RICO

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the year ended June 30, 2004

3. RELATIONSHIP TO BASIC FINANCIAL STATEMENTS

Expenditures of the federal awards are included in the Municipality's basic financial statements. The reconciliation between the expenditures in the basic financial statements and expenditures in the Schedule of Expenditures of Federal Awards is as follows:

Expenditures in the basic financial statements:

HUD Programs	$ 1,760,431
Agro-Industrial Building Project	1,157,734
Other Governmental Funds	1,388,266
Sub-total	4,306,431
Plus: advance received from USDA Rural Development	130,940
Less: Local and Legislative grants and other miscellaneous charges	(1,118,362)
Expenditures in the Schedule of Expenditures of Federal Awards	$ 3,319,009

ROSALY, OCASIO
AUDIT AND CONSULTING

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

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

We have audited the basic financial statements of the Municipality of Villalba ("the Municipality") as of and for the year ended June 30, 2004, and have issued our report thereon dated March 18, 2005. 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.

Compliance

As part of obtaining reasonable assurance about whether the Municipality's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items 2004-01 thru 2004-11.

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Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Municipality's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Municipality's ability to record process, summarize and report financial data consistent with the assertions of management in the basic financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 2004-01 thru 2004-11.

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

To the Honorable Mayor
and Members of the Municipal Legislature
Municipality of Villalba
Villalba, Puerto Rico
Page #3

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

Rosaly, Ocasio
Auditing & Consulting Group, PSC

License No. 74
Expires December 1, 2007

March 18, 2005

ROSALY, OCASIO
AUDIT AND CONSULTING

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

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

Compliance

We have audited the compliance of the Municipality of Villalba ("Municipality") with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2004. The Municipality's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grant applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on the Municipality's compliance based on our audit.

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

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As described in item 2004-13 in the accompanying schedule of findings and questioned costs, the Municipality did not comply with requirement regarding Allowable Costs / Cost Principles that is applicable to its Community Development Block Grant. Compliance with such requirement is necessary, in our opinion, for the Municipality to comply with requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2004. The results of our auditing procedures also disclosed other instances of non compliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2004-12 thru 2004-20.

Internal Control Over Compliance

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

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Municipality's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants.

Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 2004-12 thru 2004-20.

A material weakness is a condition in which the design or operations of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclosed all matters in the internal control that may be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider item 2004-13 to be material weakness.

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

Rosaly, Ocasio
Auditing & Consulting Group, PSC

License No. 74
Expires December 1, 2007

March 18, 2005

ROSALY OCASIO AUDITING & CONSULTING GROUP, P.S.C.
CERTIFIED PUBLIC ACCOUNTANTS
PUERTO RICO
Lic# 74

Municipality of Villalba

Schedule of Findings and Questioned Costs

For the year ended June 30, 2004

Section I - Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:	unqualified
Internal control over financial reporting:	
Material weakness (es) identified?	__yes _X_no
Reportable conditions identified that are not considered to be material weakness (es)?	_X_yes ___none reported
Noncompliance material to financial statements noted?	__yes _X_no

Federal Awards

Internal control over major programs:	
Material weakness (es) identified?	_X_yes ___no
Reportable conditions identified that are not considered to be material weakness (es)?	_X_yes ___none reported
Type of auditors' report issued on compliance for major programs:	qualified
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?	_X_yes ___no

Municipality of Villalba

Schedule of Findings and Questioned Costs

For the year ended June 30, 2004

Section I - Summary of Auditors' Results

Identification of major programs:

CFDA Number	Name of Federal Program
14.228	Community Development Block Grants / State's Program
14.871	Section 8 Housing Choice Vouchers
11.300	Grants for Public Works and Economic Development

Dollar threshold used to distinguish between type A and type B programs: $300,000

Auditee qualified as low-risk auditee? __yes _X_no

Municipality of Villalba

Schedule of Findings and Questioned Costs

For the year ended June 30, 2004

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

2004-01 CAPITAL ASSETS

STATEMENT OF CONDITION:

The following deficiencies were noted:

a) There are no adequate internal control procedures to ascertain that all applicable expenditures are properly recorded in the capital assets ledger at the Property Area on a timely basis, as required by Law 81 and the revised Regulation on Basic Standards for the Municipalities of Puerto Rico.

b) The capital assets ledger is not reconciled on a monthly basis with the Municipality's accounting records.

c) The acquisition of capital assets is not always informed to the property custodian for the updating of the capital assets ledger on a timely basis.

d) At June 30, 2004 the Municipality take a physical inventory count of its capital assets, however it was not performed by the Property Area neither it was reconciled with the existence property subsidiary. Based on the physical count, a subsidiary was created on an electronic spreadsheet in order to comply with GASB Statement No. 34.

RECOMMENDATION:

We recommend that the Municipality:

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

a) Establish adequate internal controls procedures to assure that all applicable expenditures are properly recorded in the Municipality's accounting records on a timely basis as required by Law 81 and the revised Regulation on Basic Standards for the Municipalities of Puerto Rico.

b) Compare the physical inventory of all capital assets it with the items recorded in the capital assets ledger. All differences noted should be immediately investigated and resolved. After updating the capital assets ledger, formal procedures should be established to take a physical inventory on a periodic basis.

c) Designed a person to analyze the expenditure accounts to identify and prepare a report of all items that should be included in the property records. This record should be sent to the property custodian to reconcile and update the property ledger on a monthly basis as required by Law 81 and the revised Regulation on Basic Standards for the Municipalities of Puerto Rico.

2004-02 ACCOUNTING SYSTEM

STATEMENT OF CONDITION:

The Municipality does not have accounting practices and policies that clearly provide for the preparation on a timely basis of the basic financial statements in accordance with accounting principles generally accepted in the United States of America. The accounting system only provides for the recording of cash receipts and cash disbursements and a limited number of other transactions, therefore, the financial information to prepare the basic financial

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

statement is obtained by management at year-end from various departments and accounting records within the Municipality. In addition, the accounting records are not integrated, and do not follow a double entry system (debits and credits).

The system lacks the necessary supporting records for the preparation of periodic basic financial statements in accordance with accounting principles generally accepted in the United States of America. We noted in the Municipality's accounting records, that certain records in use were not adequately maintained or posted on a timely basis.

RECOMMENDATION:

The Municipality should implement a plan to transform its accounting system to allow for the preparation of monthly and year-end basic financial statements in accordance with accounting principles generally accepted in the United States of America applicable to governmental entities. This plan should provide for:

a) The implementation of a double entry accounting system, the integration of all subsidiary ledgers and the reconciliation with the records maintained for the federal funds,

b) the preparation of the bank reconciliation on a timely monthly basis,

c) recording of all fiscal year transactions in the general ledger,

d) periodic financial reports to the Finance Director, the Mayor and the Municipal Legislature,

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

e) reconciliation of financial records with the reports prepared and submitted to the federal government.

2004-03 CASH AND BANK ACCOUNTS

STATEMENT OF CONDITION:

The Municipality has not established adequate and sufficient controls in the handling of the bank account in the Debt Service Fund to prevent errors and irregularities from being timely detected. The following control deficiencies were noted during our examination:

a) The cash balance shown by the Municipality's Treasury Department for the Debt Service Fund as of June 30, 2004, did not agree with the notification of the Account Activity of the Municipal Revenues Collection Center, known by its Spanish acronym (CRIM). This is due to transactions for various fiscal years, which have not been recorded in the Municipality's books.

b) The year transactions on the escrow accounts resulted from Notes and Bonds Payables were not recorded in the Municipality's books as notified by Government Development Bank for Puerto Rico (GDB).

c) The year transactions on the FEMA - Hurricane Georges account were not recorded in the Municipality's books as notified by Government Development Bank for Puerto Rico (GDB).

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RECOMMENDATION:

We recommend that the transactions affecting funds held by any fiscal agent for the Municipality should be recorded on a timely basis and balances reconciled on a monthly basis.

2004-04 USE OF RESTRICTED FUNDS

STATEMENT OF CONDITION:

As of June 30, 2004, the Municipality used funds arising from legislative resolutions and other grants to finance the operations of the general fund and fulfill its cash needs.

However, such funds were earmarked for specific projects and therefore, should not be commingled with other funds and/or used for other purposes.

RECOMMENDATION:

The general fund should reimburse amounts borrowed from the legislative resolutions and other grants and execute the projects for which they were awarded.

2004-05 INTER-FUNDS TRANSACTIONS

STATEMENT OF CONDITION:

The Municipality does not maintain adequate internal control over inter-funds transactions. Cash transferred between funds is recorded as revenue in the

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

receiving fund and as expenditure in the disbursing fund. Several adjustments were made by the Municipality at year-end to reconcile such inter-funds transactions and properly account for these transfers as inter-funds receivable or payable.

RECOMMENDATION:

We recommend that adequate control procedures be established to assure proper accountability of inter-funds transactions on a timely monthly basis. These procedures should be designed to properly segregate cash transferred on a loan basis from cash that represents revenue to the program since these transactions have different accounting treatment for basic financial statements presentation.

2004-06 PERSONNEL FILES AND PAYROLL RELATED PROCEDURES

STATEMENT OF CONDITION:

As part of our payroll test, we selected a sample of 85 personnel files (60 from payroll checks population and 25 from direct deposit population) (unless otherwise noted percent are based on 77 items since 6 employees came out twice in the sample and 2 files were not available for our examination. The following will summarize the deficiencies noted:

- In 48 (62%) of the items examined, Federal Form I-9 was missing or incomplete.

- In 55 (71%) of the items examined, "Hacienda Form 499/R4" was missing or incomplete.

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- In 6 (8%) of the items examined, copy of the social security card was missing.
- In 46 (60%) of the items examined, the good behavior certificate was missing.
- In 46 (60%) of the items examined, the health certificate requirement was missing.
- In 31 (40%) of the items examined, personal history was missing.
- In 5 (6%) of the items examined, birth certificate was missing.
- In 63 (82%) of the items examined, Drug & Alcohol Policy Certificate was missing.
- In 43 (56%) of the items examined, the OP-15 Form was missing.
- In 6 (8%) of the items examined, the employee photo was missing.
- In 73 (95%) of the items examined, the Doping (Drug Free Act) Certification was missing.
- In 26 (34%) of the items examined; the ASUME Certification Form was missing.
- In 22 (29%) of the items examined, the Employee Application Form was missing.

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- In 20 (26%) of the items examined, the Job Appointment Letter was missing.
- In 66 (86%) of the items examined, the Job Description Letter was missing.
- In 25 (32%) of the items examined, the Academic Credential was missing.
- In 63 (82%) of the items examined, the income tax filing and debt certificate was missing
- In 57 (74%) of the items examined, the Evaluation Report was missing.
- In 1 out of 43 (3%) time cards examined, the supervisor signature was missing from the time card.
- In 2 out of 77 (3%) personnel files selected, the file was not available for examination.

RECOMMENDATION:

The Municipality should implement a checklist to be used for each employee to assure completeness of the required documentation and perform periodic follow-up procedures in order to update such files.

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2004-07 LONG-TERM DEBT

STATEMENT OF CONDITION:

The Municipality does not maintain adequate records of its outstanding long-term obligations, and consequently, solely relies on the notification from the Government Development Bank for Puerto Rico, the Puerto Rico Treasury Department and others to acknowledge and record the balance of the outstanding debt and the amounts needed to fund its debt service.

RECOMMENDATION:

The Municipality should design a system and establish adequate procedures to maintain accounting records of its outstanding long-term obligations. These records will be used to verify the correctness of the amounts informed by third parties and the outstanding balance of the long-term debt.

2004-08 ACCOUNTS PAYABLE AND ENCUMBRANCES

STATEMENT OF CONDITION:

Under the Municipality's current accounting system, there is no adequate segregation between items representing actual accounts payable and those representing encumbrances due to the fact that the liability is recognized when the purchase order is issued.

RECOMMENDATION:

The Municipality should establish procedures to clearly distinguish between encumbrances and amounts actually owned for goods and services

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received at year-end. Generally accepted accounting principles in the United States of America for governments, require that purchase orders issued for which the goods or services have not been received at year end be reported as encumbrance, while the goods or services received but not paid at year end be recorded as a liability.

2004-09 BIDDING PROCEDURES

STATEMENT OF CONDITION:

As part of our procurement procedures test, we selected six auction files out of ten bids adjudicated during the fiscal year. The following summarize the exceptions noted (exceptions and percents are based on fifteen bids, since are based on specific items within each bid):

STATEMENT OF CONDITION:

- In 6 out of 15 (40%) auction files examined, a particular citizen was not present (or excused) as member of the Bid Board.
- In 12 out of 15 (80%) auction files examined, the Bidder Register Certification was not included in the file.
- In 5 out of 15 (33%) auction files examined, purchase order was issued before 20 days after the bid award notification.
- In 7 out of 15 (47%) auction files examined, no reason for bid adjudication was documented the file.

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- In 1 out of 15 (7%) auction files selected, a construction project was adjudicated through quotations since it no not reach the $40,000 limit for public bid. However, the file which should include the quotations and the authorization for the construction where not available for our examination.

CRITERIA:

Law 81 of August 30, 1991, chapter X, Article 10.005 states that "the Board will establish the rules and procedures for their internal function and to perform all the function and responsibilities that are stated in this law".

Law 81 of August 30, 1991, chapter X, Article 10.004 states "all municipalities will have one Bid Board with five (5) members. Three (3) of the members are municipal officers nominated by the Mayor and confirmed by the Municipal Legislature. The fourth member will be the Mayor, and will be the President of the Board. The fifth member will be a particular citizen with proven moral reputation, who will be nominated by the Mayor and confirmed by the Municipal Legislature, and whom should not have any contractual contract with the Municipality.

The Bid Board Regulation as approved on August 19, 2003 also states dispositions regarding these conditions.

RECOMMENDATION:

The Municipality of Villalba should take the proper action in order for the Bid Board to enforce the occurrence of the regulation and procedures established through the Bid Board Regulation and Law 81.

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

The Municipality of Villalba should name a particular citizen that will fulfill the responsibilities as the fifth member of the Bid Board.

The Municipality of Villalba should implement and use a Bidder Register, or may use the one provided by Commonwealth of Puerto Rico General Administration Services.

2004-10 CASH DISBURSEMENTS-GENERAL ACCOUNT

STATEMENT OF CONDITION:

As part of our test of cash disbursements during the year, we selected a sample of 60 checks from the general account out of 2,041 (unless otherwise noted percent are based on 54 items since 6 payment vouchers were not available for our examination). The following exceptions were noted:

- In 6 (10%) of the sample selected, the payment vouchers were not available for our examination.
- Twenty one (21) items of the sample examined require bids or quotes. In 9 (43%) of them no bid or quote were available on the files.
- In 1 (2%) of the items examined, the authorized requisition form was made for less than the amount of payment.
- In 1 (2%) of the items examined, the authorized purchase order was dated after the goods were bought.

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- In 1 (2%) of the items examined, the invoices do not appear as part of the disbursement voucher.

- In 29 (54%) of the items examined, the cancelled check was not available for our examination.

- In 4 (8%) of the items examined, the required vendor certification do not appear as part of the disbursement voucher.

- In 12 (23%) of the items examined, one or more signatures were missing from the disbursement voucher or the dates do not follow the required sequences.

- In 1 (2%) of the items examined, the certification of availability of credit does not appear as part of the disbursement voucher.

CRITERIA:

According to the revised Regulation on Basic Standards for the Municipalities of Puerto Rico, the pre-auditing unit should verify the documents correctness in all of its parts and that the transaction is in order pursuant to the correct legislation, ordinances, resolutions, contracts and regulations. Once everything is found to be in order, the document shall be certified as pre-audited and shall be sent for the approval of the Finance Director. In addition, of the aforementioned regulation, the vouchers, all cancelled checks and any other document, that justifies a payment, shall be filed by the Finance Director to be audited by the Puerto Rico Comptroller's Office or any other agency as required by law.

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RECOMMENDATION:

The Municipality should improve the pre-audit procedures of the disbursement vouchers to assure compliance with the prescribed procedures. In addition, the Municipality should follow the prescribed procedures outline in the municipal purchasing manual for the acquisition of goods and services.

The Municipality should enforce strict compliance with the procedures prescribed by the revised regulations on Basic Standards for the Municipalities of Puerto Rico during the process of acquisition of materials and supplies, equipment, and construction and service contracts.

2004-11 CASH DISBURSEMENTS-SPECIAL ACCOUNTS

STATEMENT OF CONDITION:

As part of our test of cash disbursements during the year, we selected a sample from all others accounts. The following exceptions were noted:

- Resoluciones Conjuntas (account number 127-013458) (State Funds) (25 disbursement selected out of 196)

  In 1 (4%) of the items selected, the voucher was not available for our examination.

  In 1 (5%) of the items tested, the vendor's invoice was missing.

  In 1 (5%) of the items tested, the employee certification was missing.

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In 3 (13%) of the items tested, the vendor's certification was missing.

In 1 (5%) of the items tested, the date and signature of official payer was missing.

- Manejo de Emergencias (account number 127-013873) (Federal Funds) (2 disbursements selected out of 12)

  In 1 (50%) of the items examined, the required employee certification was missing.

  In 1 (50%) of the items tested, the vendor's certification was missing.

- Local Law Enforcement (account number 127-013679) (Federal Funds) (4 disbursements selected out of 11)

  In 1 (25%) of the items examined, the lower quotation was not chosen without any documentation for reason.

  In 1 (25%) of the items examined, the date and signature of official payer was missing.

- Centro de Envejecientes (account number 127-013865) (Federal Funds) (10 disbursements selected out of 34)

  In 1 (10%) of the items tested, the quotations were missing.

  In 1 (10%) of the items examined, the dates in the disbursement voucher

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

do not follow the required sequences.

- Comunidades Especiales (account number 127-013474) (State Funds) (4 disbursement selected out of 14)

  In 1 (25%) of the items examined, the purchase of concrete was made to a vendor without a required contract.

- Campamento de Verano (account number 127-013253) (State Funds) (1disbursement selected out of 1)

  In 1 (100%) of the item tested, the pre-authorized audit form was missing.

  In 1 (100%) of the item tested, the vendor's certification was missing.

  In 1 (100%) of the item tested, the dates in the disbursement voucher do not follow the required sequences.

- Teatro Municipal (account number 127-013520) (Federal Funds) (1 disbursement selected out of 1)

  In 1 (100%) of the item examined, the general ledger account number do not appear on the voucher.

- Crime Victims (account number 127-010904) (Federal Funds) (2 disbursement selected out of 9)

  In 1 (50%) of the items examined, the general ledger account number do not appear on the voucher.

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In 1 (50%) of the items examined, one or more signatures were missing from the disbursement voucher or the dates do not follow the required sequences.

In 1 (50%) of the items examined, the certification of availability of credit do not appear as part of the disbursement voucher.

- UMTA (account number 127-010246) (Federal Funds) (1 disbursement selected out of 1)

  In 1 (100%) of the item examined, the general ledger account number do not appear on the voucher.

  In 1 (100%) of the items examined, the dates in the disbursement voucher do not follow the required sequences.

- Section 8 (account number 127-831223) (Federal Funds) (40 disbursements selected out of 1,407)

  In 1 (3%) of the items examined, the dates in the disbursement voucher do not follow the required sequences.

  In 2 (6%) of the items examined, the vouchers were not stamped as cancelled.

CRITERIA:

According to the revised Regulation on Basic Standards for the

Section II - Findings related to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards of the United States of America (GAGAS)

Municipalities of Puerto Rico, the pre-auditing unit should verify the documents correctness in all of its parts and that the transaction is in order pursuant to the correct legislation, ordinances, resolutions, contracts and regulations. Once everything is found to be in order, the document shall be certified as pre-audited and shall be sent for the approval of the Finance Director. In addition, of the aforementioned regulation, the vouchers, all cancelled checks and any other document, that justifies a payment, shall be filed by the Finance Director to be audited by the Puerto Rico Comptroller's Office or any other agency as required by law.

OMB Circular A-87 states that proper documentation of disbursements is necessary to support its allowability and accounting distribution.

RECOMMENDATION:

The Municipality should improve the pre-audit procedures of the disbursement vouchers to assure compliance with the prescribed procedures. In addition, the Municipality should follow the prescribed procedures outline in the municipal purchasing manual for the acquisition of goods and services.

The Municipality should improve its file management and documentation procedures in order to comply with state and federal regulations.

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	All of the following findings are considered reportable conditions. The letter inserted at the end of the finding name, refers to the type of compliance requirement as per OMB Circular A-133 Compliance Supplement.	
All Major Programs	**2004-12 EQUIPMENT AND REAL PROPERTY MANAGEMENT (F)**	
	STATEMENT OF CONDITION:	
	The Municipality is not maintaining adequate property records that provide all the information required by the federal regulations. Property records maintained by the federal programs only included limited information, if any.	
	The capital assets ledger is not reconciled on a monthly basis with the Municipality's accounting records.	
	At June 30, 2004 the Municipality take a physical inventory count of its capital assets, however it was not performed by the Property Area neither it was reconciled with the existence property subsidiary. Based on the physical count, a subsidiary was created on an electronic spreadsheet in order to comply with GASB Statement No. 34.	

Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs

CRITERIA:

OMB Circular A-102 (§___.32), states that:

1. Equipment records shall be maintained accurately and shall include the following information.
   a) A description of the equipment.
   b) Manufacturer's serial number, model number, Federal stock number, national stock number, or other identification number.
   c) Source of the equipment, including the award number.
   d) Whether title vests in the recipient or the Federal Government.
   e) Acquisition date (or date received, if the equipment was furnished by the Federal Government) and cost.

Information from which one can calculate the percentage of Federal participation in the cost of the equipment (not applicable to equipment furnished by the Federal Government).

The Common Rule, 45 CFR Part 92, Subpart C, requires that property records shall include, the source of property, acquisition date, percentage of federal participation in the property and any disposition data, including the date of disposal and sale price.

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Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	CAUSE: The Municipality is not monitoring compliance with federal regulations regarding property management. EFFECT: Incomplete and/or not accurate equipment records may cause misuse, misplace and/or lost and/or wrong disposal of equipment. The Municipality may not be adequately safeguarding or using for authorized purposes property acquired with federal funds. RECOMMENDATION: The federal programs should include all required information on property records to adequately safeguard all property and must assure that it is used solely for authorized purposes. Then, the Municipality should strength its monitoring procedures in order to ascertain compliance with federal regulations regarding property management. (See finding no. 2004-01 of the Section II of the Schedules of Findings and Questioned Costs)	

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Schedule of Findings and Questioned Costs

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
Community Development Block Grant CFDA 14.228	**2004-13 ALLOWABLE COSTS / COST PRINCIPLES (B)**	
	STATEMENT OF CONDITION:	
	As part of our test of cash disbursements during the year, we selected a sample of 36 disbursements out of 143. The following instances related to the adequacy of supporting documents were noted:	
	In 14 (39%) of the items tested, payments for the purchase of concrete were done to a vendor without the required contract. The bid adjudication for the purchase of concrete and related contract was done to a different vendor.	$ 94,137
	In 1 (3%) of the items tested, for the payment of ten invoices there where only four of these as part of the disbursement voucher.	
	In 1 (3%) of the items tested, for the reimbursement of three payrolls to the general fund there where only two of these as part of the disbursement voucher.	
	In 3 (8%) of the items tested, the authorized requisition form was not included as part of the disbursement voucher.	

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	In 1 (3%) of the items tested, the quotations where not included as part of the disbursement voucher.	
	In 13 (36%) of the items tested, one or more signatures were missing from the disbursement voucher or the dates do not follow the required sequences.	
	CRITERIA:	
	OMB Circular A-102 Subpart C, Section 20 (2), requires that grantees and sub-grantees must maintain records, which adequately identify the source and application of funds provided for financially assisted activities. These records must contain information pertaining to the grant or sub-grant awards and authorizations, obligations, not obligated balances, assets, liabilities, outlays or expenditures, and income. Accounting records must be supported by such source documentation as cancelled invoices, pre-audited invoices, paid bills, payrolls, time and attendance records, etc. Except as otherwise provided, records must be retained for three years.	
	OMB Circular A-87 states that proper documentation of disbursements is necessary to support its allowability and accounting distribution.	

Municipality of Villalba

Schedule of Findings and Questioned Costs

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	CAUSE: The Municipality has not implemented adequate internal controls to provide reasonable assurance that only documented, authorized and allowable costs are charge to federal programs. EFFECT: Inadequate documentation could lead to unauthorized or unallowable payments. RECOMMENDATION: The Municipality should improve its file management and documentation procedures in order to comply with state and federal regulations. The Municipality should enhance its procedures related to disbursements process in order to ascertain that cash disbursements are made only after properly documented and organized supporting documentation is reviewed.	

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
Community Development Block Grant CFDA 14.228	**2004-14 CASH MANAGEMENT (C)**	

STATEMENT OF CONDITION:

As part of our test of cash management during the year, we selected a sample of 36 disbursements out of 143. The following instances related to the adequacy of cash management procedures were noted:

In 5 (14%) of the items selected, the date of request for payment was not available.

In 4 (11%) the days between the day funds were received and the day of payment was more than 7 days.

CRITERIA:

The OMB requires that grantee's cash management system should include administrative procedures to minimize the elapsing time between the transfer of federal funds and their related disbursement.

Federal Regulation requires that grantees shall conform to the standards of timing and amounts as applicable to advances by federal agencies. Amounts requested should be limited to the Program's immediate cash needs.

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	CAUSE: The procedures related to cash management were not properly followed in order to ascertain that the time elapsing between the transfer of funds from OCAM and the disbursement of funds were less than seven (7) days. EFFECT: The Municipality did not comply adequately with cash management requirement for disbursing these drawdowns. RECOMMENDATION: The Municipality should strengthen its procedures related to cash management in order to ascertain that the time elapsing between the transfer of federal funds and the pay out of funds do not exceed established number of days. In accordance with Federal Regulations, the Municipality should estimate the use of federal funds as closely as possible to the actual disbursements.	

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
Section 8 Housing Choice Vouchers CFDA 14.871	**2004-15 ELEGIBILITY (E)**	
	STATEMENT OF CONDITION:	
	The following instances were noted in which required supporting documents were not available in tenants files, 43 files were tested:	
	Signed application form filled out during an interview, not signed or not in file	2
	Form HUD-9886 not signed, dated or missing from tenant's file	4
	Income Eligibility Verification	2
	Reported family annual income	2
	Determine income eligibility and calculate the tenant's rent payment using the documentation from third party verification	2
	Reexamine family income and composition at least once every 12 months	2
	Certificate of birth	3
	Marriage certificate or divorce decree or status affidavit	5

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	Social Security card copy missing	2
	Police record certificate	4

CRITERIA:

The 24 CFR §5.230, §5.609 and §982.516 established that as a condition of admission or continued occupancy the tenant must provide necessary information, documentation and releases to verify income eligibility.

CAUSE:

The Municipality did not maintain adequately supported and organized files or may not be obtaining the required documentation to adequately validate the participant's eligibility.

EFFECT:

The Municipality may be qualifying tenants that do not qualify with eligibility requirements.

RECOMMENDATION:

The Municipality should designed and implement adequate checklist procedures to ascertain compliance with

Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	federal regulations regarding eligibility requirements. The Municipality should also adopt uniform procedures to file such documents in the participant's files.	
Section 8 Housing Choice Vouchers CFDA 14.871	**2004-16 REPORTING (L) FORM HUD-50058**	
	STATEMENT OF CONDITION:	
	As part of our test for special reporting, we examined a sample of 43 family reports (Form HUD-50058). The following instances related to various critical lines were noted:	
	Annual reexamination was due and not done during fiscal year	2
	CRITERIA:	
	The 24 CFR part 908 and 24 CFR section 982.158 states: "the PHA is required to submit this form electronically to HUD each time the PHA completes an admission, annual reexamination, interim reexamination, portability move-in, or other change of unit for a family. The PHA must also submit the Family Report when a family ends participation in the program or moves out of the PHA's jurisdiction under portability".	

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	CAUSE: The Municipality did not maintain adequately supported and organized files or may not be obtaining the required documentation to adequately validate the participant's eligibility. EFFECT: The Municipality may be qualifying tenants that do not qualify with eligibility requirements. RECOMMENDATION: The Municipality should designed and implement adequate checklist procedures to ascertain compliance with federal regulations regarding eligibility requirements. The Municipality should also adopt uniform procedures to file such documents in the participant's files.	
Section 8 Housing Choice Vouchers CFDA 14.871	**2004-17 SPECIAL TEST AND PROVISIONS (N) HQSI** STATEMENT OF CONDITION; Annual unit inspection was due and not done during fiscal year	2

Municipality of Villalba

Schedule of Findings and Questioned Costs

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	Annual unit inspection was due and not concluded during the fiscal year	1

CRITERIA:

The 24 CFR sections 982.158(d) and 982.405(b) states: "the PHA must inspect the unit leased to a family at least annually to determine if the unit meets Housing Quality Standards (HQS) and the PHA must conduct quality control reinspections. The PHA must prepare a unit inspection report.

CAUSE:

The Municipality is not monitoring compliance with federal regulations regarding HQSI.

EFFECT:

Non-compliance with federal compliance requirements.

RECOMMENDATION:

The Municipality should establish procedures to ascertain that the unit under contract is inspected at least once a year.

Municipality of Villalba

Schedule of Findings and Questioned Costs

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Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
Grants for Economic Development CFDA 11.300	**2004-18 ALLOWABLE COSTS / COST PRINCIPLES (B)**	

STATEMENT OF CONDITION:

As part of our test of cash disbursements during the year, we selected a sample of 12 disbursements out of 35. The following instances related to the adequacy of supporting documents were noted:

In 1 (8%) of the items tested, the dates in the disbursement vouchers do not follow the required sequences.

CRITERIA:

OMB Circular A-102 Subpart C, Section 20 (2), requires that grantees and sub-grantees must maintain records, which adequately identify the source and application of funds provided for financially assisted activities. These records must contain information pertaining to the grant or sub-grant awards and authorizations, obligations, not obligated balances, assets, liabilities, outlays or expenditures, and income. Accounting records must be supported by such source documentation as cancelled invoices, pre-audited invoices, paid bills, payrolls, time and attendance records, etc. Except as otherwise

Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	provided, records must be retained for three years. OMB Circular A-87 states that proper documentation of disbursements is necessary to support its allowability and accounting distribution. CAUSE: The Municipality has not implemented adequate internal controls to provide reasonable assurance that only documented, authorized and allowable costs are charged to federal programs. EFFECT: Inadequate documentation could lead to unauthorized or unallowable payments. RECOMMENDATION: The Municipality should improve its file management and documentation procedures in order to comply with state and federal regulations. The Municipality should enhance its procedures related to disbursements process in order to ascertain that cash disbursements are made only after properly documented and organized supporting documentation is reviewed.	

Municipality of Villalba

Schedule of Findings and Questioned Costs

For the year ended June 30, 2004

Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
Grants for Economic Development CFDA 11.300	**2004-19 CASH MANAGEMENT (C)**	

STATEMENT OF CONDITION:

As part of our test of cash management during the year, we selected a sample of 12 disbursements out of 35. The following instances related to the adequacy of cash management procedures were noted:

In 5 (14%) of the items selected, the date of request for payment was not available.

In 8 (67%) the days between the day funds were received and the day of payment was more than 7 days.

CRITERIA:

The OMB requires that grantee's cash management system should include administrative procedures to minimize the elapsing time between the transfer of federal funds and their related disbursement.

Federal Regulation requires that grantees shall conform to the standards of timing and amounts as applicable to advances by federal agencies. Amounts requested should be limited to the Program's immediate cash needs.

Municipality of Villalba

Schedule of Findings and Questioned Costs

For the year ended June 30, 2004

Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	CAUSE: The procedures related to cash management were not properly followed in order to ascertain that the time elapsing between the transfer of funds and the disbursement of funds was less than 7 days. EFFECT: The Municipality did not comply adequately with cash management requirement for disbursing these drawdowns. RECOMMENDATION: The Municipality should strengthen its procedures related to cash management in order to ascertain that the time elapsing between the transfer of federal funds and the pay out of funds do not exceed established number of days. In accordance with Federal Regulations, the Municipality should estimate the use of federal funds as closely as possible to the actual disbursements.	

Municipality of Villalba

Schedule of Findings and Questioned Costs

For the year ended June 30, 2004

Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
Grants for Economic Development CFDA 11.300	**2004-20 DAVIS-BACON ACT (D)**	

SATEMENT OF CONDITION:

As part of our test for compliance with regulation of Davis-Bacon Act, we requested the principal construction contract with their respective payroll submission. The following instances related to the adequacy of evidence of inclusion of a clause regarding this act were noted:

> The clause indicating the Davis-Bacon Act compliance was not included as part of the contract as well as a copy of the prevailing wages. Certified weekly payrolls are not being submitted to the Municipality.

CRITERIA:

Non-federal entities shall include in their construction contracts subject to Davis-Bacon Act, a requirement that the contractor or subcontractor comply with the requirements of the Davis-Bacon Act and the DOL regulations (29 CFR Part 5, "Labor Standards Provisions Applicable to Contacts Governing Federally Financed and Assisted Construction"). This includes a requirement for the contractor or subcontractor to submit to the non-Federal entity weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance (certified payrolls) (29 CFR

Section III - Federal Award Audit Findings and Questioned Costs

Federal Program	Findings/Non Compliance and Recommendation	Questioned Costs
	sections 5.5 and 5.6). This reporting is often done using Optional Form WH-347 which includes the required statement of compliance (OMB No. 1215-0149).	
	CAUSE:	
	The internal control procedures related to the contracting process for construction fail in maintain a signed copy of the form HUD-5370 as part of the construction contract file.	
	EFFECT:	
	The Municipality has not complied with the requirements for Davis-Bacon Act. These could result in disallowed costs by the federal awarding agency.	
	RECOMMENDATION:	
	The Municipality should strengthen its procedures related to contracting process in order to ascertain the compliance with Davis–Bacon Act. Certified weekly payrolls should be request and examined to assure compliance with labor standards. Also, a pre-construction conference must be held to explain labor standards.	
	Total Questioned Costs	$ 94,137

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VILLALBA
CORRECTIVE ACTION PLANS
SINGLE AUDIT REPORT

Audit Year: June 30, 2004 Date: March 31,2005

FINDING	CORRECTIVE ACTIONS	RESULTS
Finding 2004-01 **Capital Assets**	During the 2003-2004 fiscal year, the Municipality of Villalba, performed a physical inventory of all Capital Assets, and we reconciled it with the accounting record. The Finance Director always informed the adquisition of capital assets to the property custodian.	Partially Accomplished.
Finding 2004-02 **Accounting System.**	The municipality utilizes the mechanized system from OCAM that accomplished The General Accepted Accounting Principles (GAAP) requirements.	Partially Accomplished.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VILLALBA
CORRECTIVE ACTION PLANS
SINGLE AUDIT REPORT

FINDING	CORRECTIVE ACTIONS	RESULTS
Finding 2004-03 **Cash And Bank Accounts.**	The Accounting Head is preparing the bank reconciliations on a monthly basis and is constantly establishing better procedures to accrue the information.	Partially Accomplished.
Finding 2004-04 **Use Of Restricted Funds.**	When we receive funds from Legislative Resolutions, we used them just for the specific project or for the purpose for which they were awarded	Accomplished

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VILLALBA
CORRECTIVE ACTION PLANS
SINGLE AUDIT REPORT

FINDING	CORRECTIVE ACTION	RESULTS
Finding 2004-05 **Interfund Transactions.**	The Finance Director and the Accounting head identified all of the Interfund Transactions.	Accomplished.
Finding 2004-06 **Personnel Files And Payroll Related Procedures.**	The Human Resources Director implemented the recommendations of the Internal Auditor Report, during the year.	Partially Accomplished.
Finding 2004-07 **Long Term Debt.**	The Finance Director and the Accounting head correct the deficiencies founding in the Long Term Debts.	Partially Accomplished.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VILLALBA
CORRECTIVE ACTION PLANS
SINGLE AUDIT REPORT

FINDING	CORRECTIVE ACTIONS	RESULTS
Finding 2004-08 **Accounts Payable And Encumbrances.**	The Accounting Head prepared a report in which it clearly distinguishes between encumbrance and account payable.	Accomplished.
Finding 2004-09 **Bidding Procedure**	The Municipality of Villalba, already name a particular citizen that will fulfill the responsibilities as the fifth member of the Bid Board.	Partially Accomplished. The Bid Board adopted its Regulations.
Finding 2004-10 **Cash Disbursements-General Account**	The Pre-intervention Head and her assistance pre-audit the procedures of Disbursements to assure compliance with Regulations.	Partially Accomplished. The administration implemented adequate Internal Controls.
Finding 2004-11 **Cash Disbursements-Special Accounts**	A control measure was established by pre-intervening every Voucher, before making the appropriate payment.	Partially Accomplished. Every Voucher is Pre- Intervened by the Pre-Intervention Division.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VILLALBA
CORRECTIVE ACTION PLANS
SINGLE AUDIT REPORT

FINDING	CORRECTIVE ACTIONS	RESULTS
Finding 2004-12 **Equipment and Real Property Management**	During the 2003-2004 fiscal year, the Municipality of Villalba, performed a physical inventory of all Capital Assets, and we reconciled it with the accounting record.	Partially Accomplished.
Finding 2004-13 **Allowable Costs/ Cost Principle (B)**	We give instruction to the accountant, in order to correct this situation, and improve the file management and documentation procedure. We do not accept the questioned cost, because the purchase of concrete was made to a company from the same owner who had the adjudication contract, and the Municipality provide to the auditor all the evidence about the cash disbursement, including disbursement voucher and cancelled check.	Accomplished
Finding 2004-14 **Cash Management**	We give instruction to the Federal Department Director in order to improve the procedure related to cash management.	Partially Accomplished

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF VILLALBA

CORRECTIVE ACTION PLANS

SINGLE AUDIT REPORT

FINDING	CORRECTIVE ACTIONS	RESULTS
Finding 2004-15 **Elegibility**	We gave instruction to the Section 8 Coordinator to evaluate the files and correct this finding.	Accomplished. We revised and evaluated all files in order to correct them.
Finding 2004-16 **Reporting Form HUD-50058**	We gave instruction to the Section 8 Coordinator in order to implement adequate checklist procedure to ascertain compliance with federal regulation regarding eligibility requirement.	Accomplished
Finding 2004-17 **Special Test and Provisions**	We gave instruction to the Section 8 Coordinator in order to establish procedure to ascertain that the unit under contract is inspected as least once a year	Accomplished. We already have a procedure to ascertain that the units are inspected. A register of quality control was prepared.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF VILLALBA
CORRECTIVE ACTION PLANS
SINGLE AUDIT REPORT

FINDING	CORRECTIVE ACTIONS	RESULTS
Finding 2004-18 **Allowable Costs/ Cost Principle (B)**	We give instruction to the accountant, in order to correct this situation, and improve the file management and documentation procedure.	Accomplished.
Finding 2004-19 **Cash Management (C)**	We give instruction to the Federal Department Director in order to improve the procedure related to cash management.	Partially Accomplished.
Finding 2004-20 **Davis Bacon Act (D)**	We designate one person of our Federal programs office to be in charge of the revision of the payrolls of all our projects. We improve the procedure by preparing a file to guarantee the access to the payrolls and the compliance of the requirement.	Partially Accomplished.

I certify that the above information is correct:

Hon. Waldemar Rivera Torres
Mayor
Municipality of Villalba

Municipality of Villalba

Summary Schedule of Prior Years Findings and Questioned Costs

June 30, 2004

The following schedule contains the findings number, title and corrective action taken of each of the findings included in the Report on Compliance and on Internal Control over Financial reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standard for the Fiscal Years ended June 30, 2003 and 2002. Under the heading status there will be the following:

FR - Fully resolved (indicating the corrective action was fully implemented).

PR - Partially resolved (indicating the corrective action plan was partially implemented and the finding repeated in fiscal year 2003-2004).

NR - Not resolved yet (finding repeated in fiscal year 2003-2004).

Finding Number	Finding Title	Status
2003-01	General Fixed Assets	PR
2003-02	Accounting System	PR
2003-03	Operating Deficit of General Fund	FR
2003-04	Cash and Bank Accounts	PR
2003-05	Use of Restricted Funds	PR
2003-06	Inter-funds Transactions	PR
2003-07	Personnel Files and Payroll Related Procedures	PR
2003-08	Municipal License Tax	FR
2003-09	Long-term Debt	PR
2003-10	Account Payable and Encumbrances	PR
2003-11	Bidding Procedures	PR

Municipality of Villalba

Summary Schedule of Prior Years Findings and Questioned Costs

June 30, 2004

2003-12	Cash Disbursements-General Account	PR
2003-13	Cash Disbursements-Special Accounts	PR
2003-14	Equipment and Real Property Management	PR
2003-15	Allowable Cost/Cost Principle	FR
2003-16	Eligibility	FR
2003-17	Special Test and Provision	FR
2003-18	Special Test and Provision	FR
2003-19	Special Test and Provision	FR
2003-20	Special Test and Provision	FR
2003-21	Allowable Cost/Cost Principle	FR
2003-22	Cash Management	PR
2003-23	Allowable Cost/Cost Principle	PR
2003-24	Cash Management	PR
2003-25	Davis Bacon Act	PR
2003-26	Allowable Cost/ Cost Principle	PR
2003-27	Davis Bacon Act	PR
2003-28	Davis Bacon Act	PR
2002-01	General Fixed Assets & GASB 34	PR
2002-02	Accounting System	PR
2002-03	Operating Deficit of General Fund	FR

Municipality of Villalba

Summary Schedule of Prior Years Findings and Questioned Costs

June 30, 2004

2002-04	Cash and Bank Accounts	PR
2002-05	Use of Restricted Funds	PR
2002-06	Inter-funds Transactions	PR
2002-08	Personnel Files and Payroll Related Procedures	PR
2002-09	Long-term Debt	PR
2002-10	Account Payable and Encumbrances	PR
2002-11	Bidding Procedures	PR
2002-12	Cash Disbursements-General Account	PR
2002-13	Cash Disbursements-Other Accounts	PR
2002-14	Equipment and Real Property Management	PR
2002-20	Allowable Cost/Cost Principle	FR
2002-21	Cash Management	FR
2002-22	Allowable Cost/Cost Principle	FR
2002-23	Davis Bacon Act	PR
2002-24	Davis Bacon Act	PR
2002-25	Davis Bacon Act	PR
2002-26	Reporting	PR