

**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES  
ÁREA DE ASESORAMIENTO, REGLAMENTACIÓN E INTERVENCIÓN FISCAL  
ÁREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE YABUCOA  
AUDITORÍA 2012-2013  
30 DE JUNIO DE 2013**

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF YABUCOA**

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**BASIC FINANCIAL STATEMENTS  
WITH ADDITIONAL REPORTS AND INFORMATION  
REQUIRED BY THE SINGLE AUDIT ACT**

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**Year Ended June 30, 2013**

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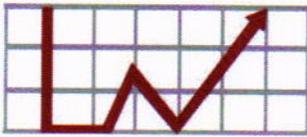
Municipality of Yabucoa, PO Box 97 Yabucoa P.R. 00767-0097  
Hon. Rafael Surillo Ruiz

CONTENTS

	Page
<b><u>BASIC FINANCIAL STATEMENTS</u></b>	
Independent Auditors' Report	1-4
Required Supplementary Information (Part 1) Management's Discussion and Analysis	5-14
Government-Wide Financial Statements:	
Statement of Net Position	15
Statement of Activities	16
Fund Financial Statements:	
Governmental Funds:	
Balance Sheet	17
Statement of Revenues, Expenditures and Changes in Fund Balances	18
Reconciliation of the Balance Sheet- Governmental Funds to Statement of Net Position	19
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities	20
Notes to Basic Financial Statements	21-52
<b><u>SUPPLEMENTARY INFORMATION</u></b>	
Required Supplementary Information (Part II):	
Budgetary Comparison Schedule-General Fund	53
Notes to Budgetary Comparison Schedule-General Fund	54
Schedule of Expenditures of Federal Awards	55-56
Notes to the Schedule of Federal Awards	57

CONTENTS

	Page
<b><u>INTERNAL CONTROL AND COMPLIANCE WITH LAWS AND REGULATIONS</u></b>	
Independent Auditor's Report on internal control over financial reporting and on compliance and other matters based on an audit of financial statements performed in accordance with <i>Government Auditing Standards</i>	58-59
Independent Auditor's Report on compliance for each major program and on internal control over compliance required by OMB Circular A-133	60-62
<b><u>FINDINGS AND QUESTIONED COSTS</u></b>	
Schedule of Findings and Questioned Costs	63-79
Summary Schedule of Prior Year's Audit Findings	80



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Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

## INDEPENDENT AUDITORS' REPORT

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

### **Report on the Financial Statements**

We were engaged to audit the accompanying basic financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Yabucoa**, Puerto Rico, as of and for the year ended June 30, 2013, and the related notes to the basic financial statements, which collectively comprise the Municipality's basic financial statements as listed in the table of contents.

### **Management's Responsibility for the Financial Statements**

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

### **Auditor's Responsibility**

Our responsibility is to express opinions on these basic financial statements based on conducting the audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. Because of the matters described in the Basis of Disclaimer of Opinion paragraphs, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

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

## INDEPENDENT AUDITORS' REPORT (CONTINUED)

### Basis for Disclaimer of Opinion

The Municipality does not have adequate and effective internal controls to ensure that all the required financial and budgetary information was recognized and reported in the proper accounting period. As a result, we were unable to confirm or validate by alternative means accounts receivable, accounts payable and interfund loans included in the balance sheet at a total amount of \$3,108,930, \$4,881,608 and \$4,641,500, respectively, at June 30, 2013. Also, we were not able to obtain sufficient audit evidence to support and assess the reasonableness of the amounts reported in the "Final Budget and Actual Amounts" (Budgetary Basis) columns of the Budgetary Comparison Schedule for the fiscal year ended June 30, 2013.

In addition, the capital assets of governmental activities reported in the statement of net position at a total amount of \$44,877,305, net of accumulated depreciation of \$20,418, could be materially misstated since we were unable to ascertain by other audit procedures the completeness of the balances reported.

Also, the Municipality did not comply with the requirements established by Statement No. 18, "Accounting for Municipal Solid Waste Landfill Closure and Post Closure Care Costs", issued by the Governmental Accounting Standards Board and the regulations set forth by the U.S. Environmental Protection Agency (EPA). At June 30, 2013, the accompanying statement of net position presents a liability for post-closure care costs of the Municipality's solid waste landfill of \$3,563,314. However, this estimate has not been made based a study in conformity with the regulatory requirements established by the EPA "Solid Waste Disposal Facility Criteria". The amount by which departure would affect the liabilities, net position and expenses of the governmental activities is not reasonably determinable.

As a result of these matters, we were unable to determine whether any audit adjustments might have been found necessary in respect of recorded or unrecorded accounts receivable, accounts payable, interfund loans, capital assets and liability for post-closure care costs, the elements making up the Statement the Statement of Revenues, Expenditures and Changes in Fund Balance and Statement of Activities, and finally, of the transactions reported in the Budgetary Comparison Schedule.

### Disclaimer of Opinion

Because of the significance of the matters described in the *Basis for Disclaimer Opinion* paragraphs, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for our audit opinion and accordingly, we do not express an opinion on the basic financial statements of the **Municipality of Yabucoa**, Puerto Rico, as of June 30, 2013, as to whether they have been properly prepared, in all material respects, in accordance with accounting principles generally accepted in the United States of America.



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## INDEPENDENT AUDITORS' REPORT (CONTINUED)

### Other Matters

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 4 through 14 and 53 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with the auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

#### *Other Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the **Municipality of Yabucoa's** basic financial statements. The accompanying supplementary information – Schedule of Expenditures of Federal Awards shown in pages 55 and 56 is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements.

The Schedule of Expenditures of Federal Awards is the responsibility of management and was derived from and related directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other procedures in accordance with auditing standards generally accepted in the United States of America. Because of the significance of the matters disclosed in the "Basis for Disclaimer of Opinion" section of the auditor's report it is inappropriate to and therefore, we do not express an opinion on the Schedule of Expenditures of Federal Awards.

We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion of or provide us any assurance. Also, due to the significance of the matters disclosed in the "Basis for Disclaimer of Opinion" section of the auditor's report we find it inappropriate and therefore we do not express an opinion on the Schedule of Expenditures of Federal Awards.



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## INDEPENDENT AUDITORS' REPORT (CONTINUED)

### Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated July 15, 2014, on our consideration of **Municipality of Yabucoa's** internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of this report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering **Municipality of Yabucoa's** internal control over financial reporting and compliance.

  
LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico  
July 15, 2014  
Stamp No. 2675843 of the Puerto Rico  
Society of Certified Public Accountants  
was affixed to the record copy of this report.



*López-Vega, CPA, PSC*

Certified Public Accountants / Management Advisors

This discussion and analysis of the **Municipality of Yabucoa's** (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2013. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. This document also includes comparative data with prior year as this information was available for the fiscal year ended on June 30, 2012. This MD&A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

1. A broader basis in focusing important issues;
2. acknowledgement of an overview of the Municipality's financial activities;
3. an evaluation of its financial condition as of the end of fiscal year 2012-2013 compared with prior year results;
4. identification of uses of funds in the financing of the Municipality's services, construction programs and other activities; and
5. a basis to assess Management's ability to handle budgetary functions.

#### FINANCIAL HIGHLIGHTS

During the fiscal year 2012-2013, the economic environment of the Commonwealth of Puerto Rico continued to suffer the adverse results of a recession that, has deeply hurt the local economy during the past 8 years. Considering this economic reality, the financial position and results of operations as reflected in the financial statements prepared for fiscal year 2013, reflects the continued decreasing trend of the Municipality's economic strength during the last three years.

1. Total net position of the Municipality as of the end of fiscal year 2013 amounted to \$16,418,528, or thirty percent (30%) of total assets, as restated.
2. The Municipality's total net position at the end of the year decreased by \$4,828,632, or a 23% reduction when compared with the prior fiscal year 2012, as restated. Such decrease is mainly attributable to the increase of total liabilities and a decrease of the net investment in capital assets.
3. As of the end of fiscal year 2012-2013, the Municipality's Governmental Funds Balance Sheet reflected a combined ending fund balances of \$(2,164,652) which represents a decrease of \$4,705,435 when compared with the corresponding figures for the previous fiscal year 2011-2012, as restated.
4. As of the end of the fiscal year 2012-2013, the deficit of the Municipality's General Fund amounted to \$(7,346,749), reflecting an increase of \$5,352,686 when compared to the prior year's reported deficit, as restated.

### FINANCIAL HIGHLIGHTS (CONTINUED)

Although such balance is partially explained by the prevailing economic constraints, Management is aware that in order to improve the Municipality's rate of return, drastic measures must be implemented to increase revenues and reduce current expenditures. Management is aware that these corrective actions will encounter several difficulties since further increases in statutory expenditures are expected such as contributions to the Commonwealth Government Pension Funds, certain limitations imposed by law in budget management and restrictions in projects financing due to credit downgrading imposed by rating agencies.

5. As indicated in the accompanying General Fund Budgetary Comparison Schedule, as of June 30, 2013, the actual budgetary activities resulted in a deficiency of revenues and other financing sources under expenditures, encumbrances and other financing uses of \$747,604. Such balance is mainly attributable to a significant negative variance in the actual revenues derived from municipal license taxes, licenses, permits and other local taxes and miscellaneous revenues, in the total amount of \$4,472,389.
6. At the end of fiscal year 2013, total government-wide liabilities amounted to \$37,472,524. Out of the said amount, \$25,563,874 corresponds to long-term liabilities of which \$17,767,300 represents the outstanding balance of bonds issued. The Municipality continued to meet all debt service requirements, most of which were paid from self-generated revenues.

### FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2013. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

Under the aforementioned approach, assets and liabilities are recognized using the accrual basis of accounting which is similar to the method used by most private enterprises. This means that current year's revenues and expenses are accounted for regardless of when cash is received or paid.

### FINANCIAL STATEMENTS COMPONENTS

The basic financial statements consist of the government-wide financial statements, the major funds financial statements and the notes to the financial statements which provide details, disclosure and description of the most important items included in said statements. The Statement of Net Position reflects information of the Municipality as a whole on a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year.

Such financial level is measured as the difference between total assets and liabilities, with the difference between both items reported as net position as previously mentioned. In the particular case of the **Municipality of Yabucoa**, as of June 30, 2013, such figure amounted to \$16,418,528, a decrease of \$4,828,632 over previous year 2012, as restated, and represents thirty percent (30%) of the total assets. Such decrease is due to the reasons previously stated, especially those related to limited borrowing opportunities to finance the Municipality's improvement program and to the lack of General Fund contributions to afford the cost of such program.

## FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

It is important to note that, although municipalities as governmental public entities were not created to operate under a profit motive framework, the return on assets performance plays an important role in their financial operations.

The higher the increments achieved in net revenues, the higher the capacity to increase the net position figure either through additional borrowings or through internally generated funds. This in turn will benefit the welfare of Yabucoa constituents.

The Statement of Activities is focused on both gross and net cost of the various activities of the Municipality. It presents information which shows the changes in the Municipality's net position at the most recent fiscal year. Based on the use of the accrual basis of accounting, changes are reported as soon as the underlying event occurs, regardless of the timing of the related cash flows. Under said approach, revenues and expenses are reported in the Statement of Activities based on the theory that it will result in cash flows to be realized in future periods.

A brief review of The Statements of Activities of the Municipality at June 30, 2013, shows total expenses incurred to afford the cost of all functions and programs amounted to \$30,045,985. Upon examining the sources of revenues for the financing of said programs, the Statement reflects that the amount of \$9,403,982 was derived from the following sources: \$284,838 charges for services; \$5,843,010 from operating grants and contributions; and \$3,276,134 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$15,813,371. When such figure is added to the \$9,403,982 previously mentioned, total revenues available for the financing of activities amounted to \$25,217,353. There was a deficiency of revenues over expenses in the amount of \$4,828,632. The main causes of this deficiency have been previously explained.

The Fund Financial Statements are another important component of the Municipality's financial statements. A fund is a grouping of related accounts that are used to maintain accountability and controls over economic resources of the Municipality that have been segregated for specific activities. The municipal fund-type accounting is used to demonstrate compliance with related legal requirements. Information offered through these Statements is limited to the Municipality most significant funds and is particularly related to the local government only, instead of the government as a whole.

Government funds are used to account for essentially the same functions as those reported as governmental activities. The funds are reported using an accounting method known as modified-accrual basis of accounting which measures cash and all other financial assets that can be readily converted into cash.

The fund statement approach gives the user a short term view of the Municipality's government operations and the basic services it provides. Since the focus of government funds is narrower than that of the financial statements as a whole, it also helps the user with comparable information presented in the governmental activities report. By doing so, readers of the basic financial statements may understand better the long-term effect of the Municipality's short-term financial decisions.

## CAPITAL ASSETS - INFRASTRUCTURE

Historically, capital assets such as roads, bridges, traffic signals, underground pipes not associated with utilities, have not been recognized nor depreciated in the accounting records of the Municipality. GASB 34 requires that such type of assets be inventoried, valued and reported under the governmental column of the government-wide Statement of Net Position. During the previous fiscal years, the Municipality reported historical costs of infrastructure assets of \$33,663,415, with an accumulated depreciation of \$12,158,394. This year, capital additions totaled \$453,255, of which \$232,172 corresponds to infrastructure. Total depreciation expense for the fiscal year amounted to \$20,418, of which \$4,594 pertains to this category of capital assets. The net value of infrastructure capital assets as of June 30, 2013 amounts to \$21,732,599, which represents 48% of total net capital assets.

According to the requirements of GASB 34, the government must elect to either (a) depreciate the aforementioned assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery to near perpetuity. If the government develops the asset management system, (the modified approach) which periodically (at least every three years), by category, measures and demonstrate its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. In this particular respect, the Municipality has elected the use of recognizing depreciation under the useful life method and it contemplates to continue this treatment on said basis.

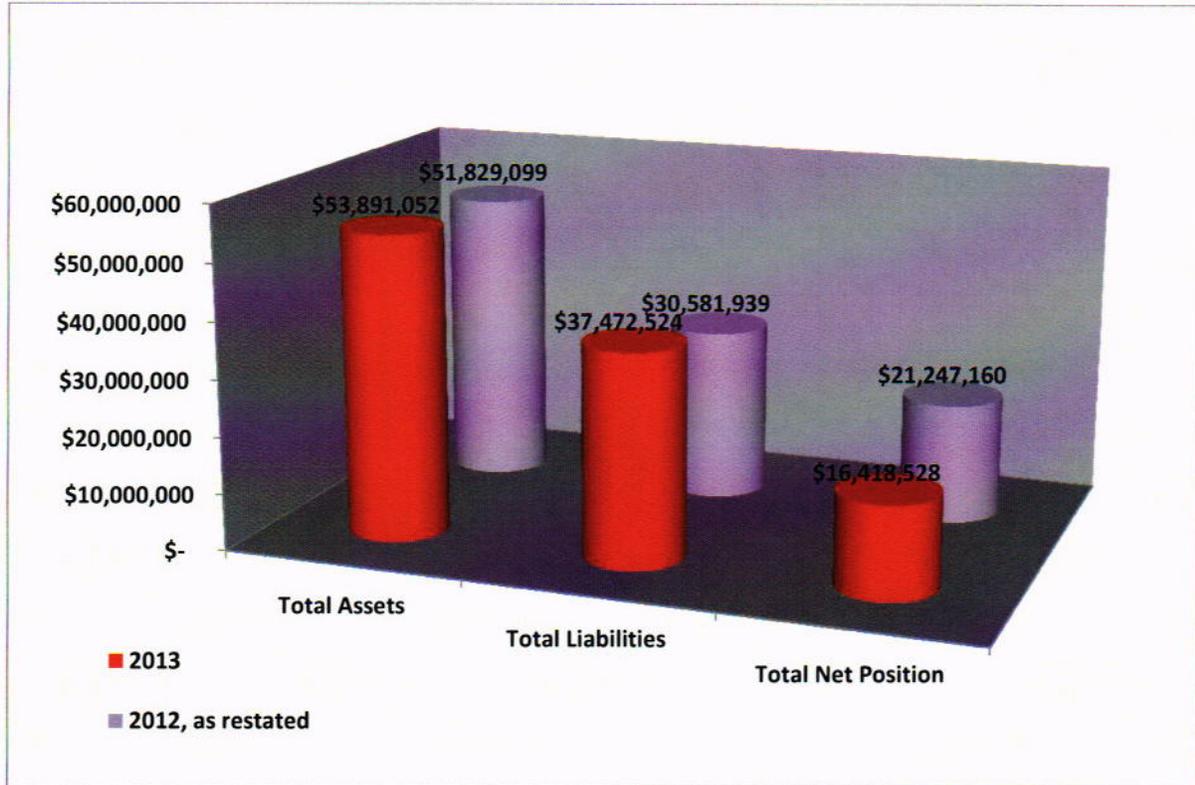
## FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

### Net position

The Statement of Net Position serves as an important indicator of the Municipality's financial position at the end of the fiscal year. In the case of the **Municipality of Yabucoa**, primary government assets exceeded total liabilities by \$16,418,528 at the end of 2013, and, when compared with the prior year balance of \$21,247,160, as restated, it reflects a decrease of \$4,828,632. The following condensed Statement of Net Position of the Primary Government shows on a comparative basis the most important components of the \$(4,828,632) decrease reflected in the net position figure.

<i>Condensed Statements of Net Position, as of June 30,</i>				
	<b>2013</b>	<b>2012, as restated</b>	<b>Increase (Decrease)</b>	<b>%</b>
Current assets	\$ 9,013,747	\$ 8,015,339	\$ 998,408	12%
Capital assets, net	44,877,305	43,813,760	1,063,545	2%
<b>Total assets</b>	<b>\$ 53,891,052</b>	<b>\$ 51,829,099</b>	<b>\$ 2,061,953</b>	<b>4%</b>
Current liabilities	\$ 11,908,650	\$ 5,474,556	\$ 6,434,094	118%
Noncurrent liabilities	25,563,874	25,107,383	456,491	2%
<b>Total liabilities</b>	<b>\$ 37,472,524</b>	<b>\$ 30,581,939</b>	<b>\$ 6,890,585</b>	<b>23%</b>
Net investment in capital assets	\$ 29,715,005	\$ 33,587,188	\$ (3,872,183)	-12%
Restricted	5,182,097	4,534,846	647,251	14%
Unrestricted deficit	(18,478,574)	(16,874,874)	(1,603,700)	-10%
<b>Total net position</b>	<b>\$ 16,418,528</b>	<b>\$ 21,247,160</b>	<b>\$ (4,828,632)</b>	<b>-23%</b>

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)



**Changes in Net Position**

The Statement of Activities reflects that for fiscal year 2013, the net effect of the revenues derived from several programs plus current operating expenses, amounted to a deficit of \$4,828,632. As previously stated, such amount constituted a decrease in the Municipality's net position. Approximately thirty one percent (31%) of the Municipality's total revenue came from taxes, while sixty six percent (66%) resulted from grants and contributions, including federal aid. Charges for services provided one percent (1%) and interest and investment earnings represented less than one percent (.5%) of total revenues. The Municipality's largest expenses included items such as general government, health and welfare services, public works, community development, public safety, and waste disposal. The following table and graphic presentation includes in absolute and relative terms, the composition of revenues and expenses for the fiscal years ended on June 30, 2013 and 2012, as restated. Such analysis helps the reader to evaluate the Municipal administration performance in the administration of its current financial operations.

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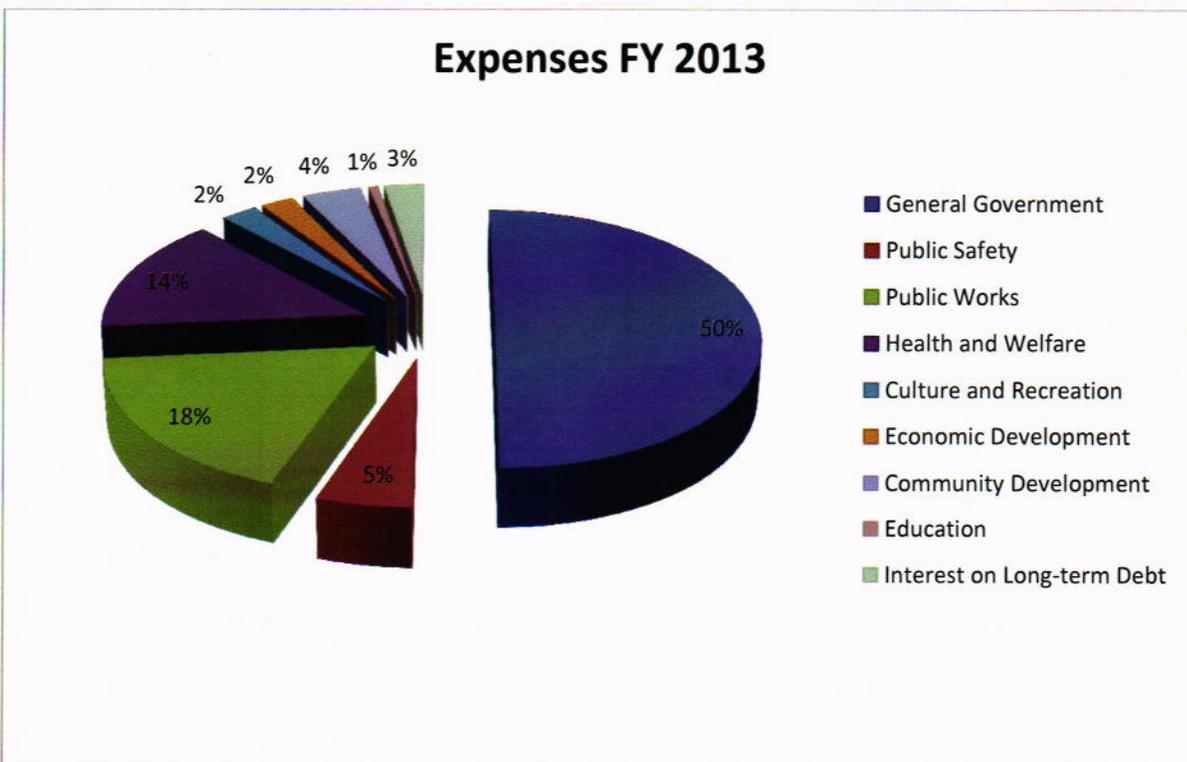
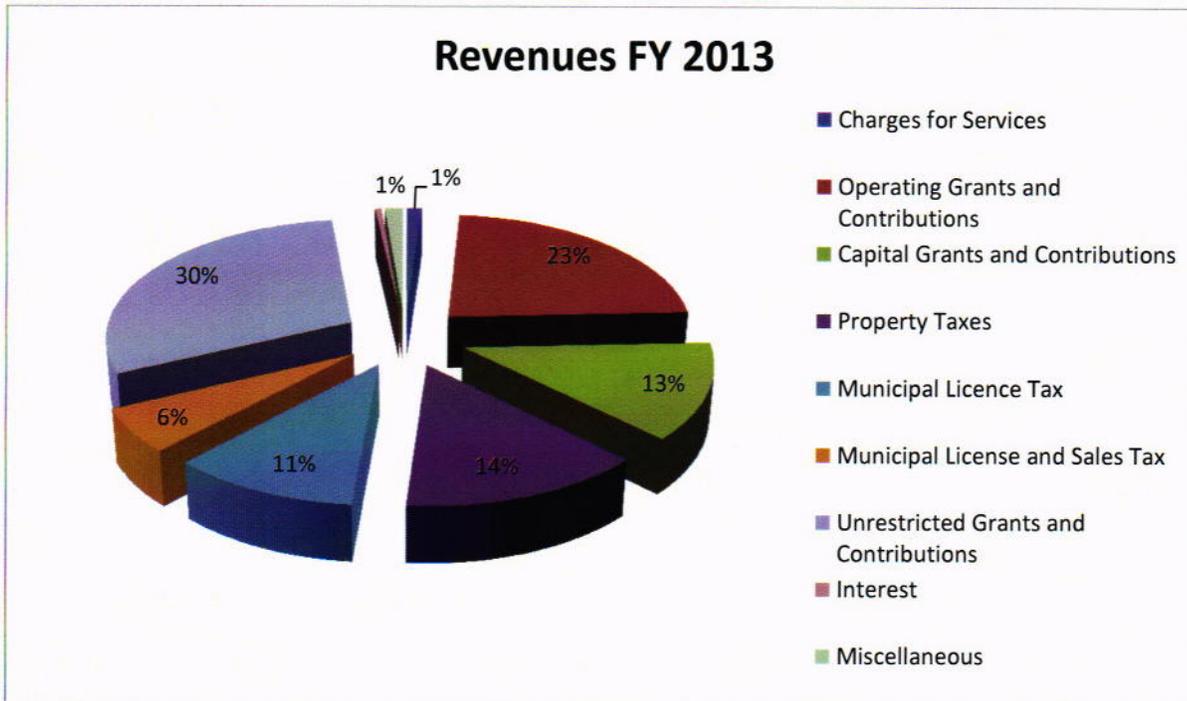
FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

*Condensed Statements of Activities, for the fiscal year ended on June 30,*

	<u>2013</u>	<u>2012, as restated</u>	<u>Increase (Decrease)</u>	<u>%</u>
<b>Program revenues:</b>				
Charges for services	\$ 284,838	\$ 156,427	\$ 128,411	82%
Operating grants and contributions	5,843,010	4,671,152	1,171,858	25%
Capital grants and contributions	3,276,134	5,527,589	(2,251,455)	-41%
<b>General revenues:</b>				
Property taxes	3,528,129	7,552,484	(4,024,355)	-53%
Municipal license tax	2,712,572	4,429,060	(1,716,488)	39%
Municipal sales and use tax	1,485,310	844,054	641,256	76%
Other local taxes	-	492,800	(492,800)	100%
Grants and contributions not restricted to specific programs	7,620,955	2,561,878	5,059,077	197%
Interest and investment earnings	122,722	45,155	77,567	172%
Miscellaneous	343,683	2,293,939	(1,950,256)	-85%
<b>Total revenues</b>	<u>25,217,353</u>	<u>28,574,538</u>	<u>(3,357,185)</u>	-12%
<b>Expenses:</b>				
General government	15,062,404	3,738,804	11,323,600	303%
Public safety	1,552,748	3,288,257	(1,735,509)	-53%
Public works	5,481,043	8,828,734	(3,347,691)	-38%
Health and welfare	4,336,308	7,717,047	(3,380,739)	-44%
Culture and recreation	739,839	2,751,563	(2,011,724)	-73%
Economic Development	671,428	-	671,428	100%
Community development	1,202,368	-	1,202,368	100%
Education	186,474	-	186,474	100%
Interest on long-term debt	813,373	578,034	235,339	41%
<b>Total expenses</b>	<u>30,045,985</u>	<u>26,902,439</u>	<u>3,143,546</u>	12%
Change in net position	(4,828,632)	1,672,099	(6,500,731)	-389%
Net position, beginning of year, as restated	<u>21,247,160</u>	<u>19,575,061</u>	<u>1,672,099</u>	-9%
Net position, end of year, as restated	<u>\$ 16,418,528</u>	<u>\$ 21,247,160</u>	<u>\$(4,828,632)</u>	-23%

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FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)



## FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

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

### Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balance amounting to \$(2,164,652), which represents a decrease of \$4,705,435 when compared with the prior year, as restated. Such decrease is mainly attributable to the increase in total liabilities. Total restricted fund balances amount to \$5,182,097. This is the portion of fund balance that reflects resources that are subject to externally enforceable legal restrictions such as the following: 1) to pay for specific program purposes (\$1,240,933); 2) to pay for capital projects (\$1,365,276); and 3) for debt service payments (\$2,575,888). Assigned fund balances for current year encumbrances totaled \$68,025.

As of June 30, 2013, the General Fund, which is the main operating fund of the Municipality, reflected an unassigned fund deficit of \$(7,414,774). As previously mentioned, Management is in the process of reviewing this negative financial situation through the design and enforcement of those measures that will contribute to reverse the declining trend of the Municipality's profitability. Some of these measures already implemented have produced positive results as reflected from the comparison of certain current expense items for the years 2011-2012 and 2012-2013.

### GENERAL FUND BUDGETARY HIGHLIGHTS

For the fiscal year ended June 30, 2013, significant negative variances in the actual revenues of the following revenue categories were detected: municipal license tax (\$1,932,251); licenses, permits and local taxes (\$1,641,283); and miscellaneous revenues (\$898,855). These negative variances were offset by positive variances in the following expenditure functions: health and welfare (\$1,228,939) and public works (\$2,136,071). The net effect of these variances was a deficiency of revenues and other financing sources under expenditures, encumbrances and other financing uses of \$747,604.

### CAPITAL ASSETS AND DEBT ADMINISTRATION

#### Capital Assets

The Municipality's investment in capital assets as of June 30, 2013, amounted to \$71,816,383 which upon deduction of accumulated depreciation in the amount of \$26,939,078 produced a net book value attributable to capital assets in the amount of \$44,877,305. Said investment includes land, construction work in progress, buildings, improvements, equipment, infrastructure, furnishing, computers and vehicles. Infrastructure assets are composed of items such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

## CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)

The total increase in the Municipality's investment in capital assets for the current fiscal year represented approximately two percent (2%) of net book value. This increase was due to an aggressive construction and improvement of public facilities plan. Depreciation charges for the year totaled \$20,418.

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2013, the Municipality had \$1,365,276 of unexpended proceeds from bond and notes issuances and other restricted assignments that are mainly committed to future construction activities in the Capital Projects Fund- Local, State and Local Grants.

### Debt Administration

The Puerto Rico Legislative Assembly 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 applicable law also requires that in order for a Municipality to be able to issue additional general obligation bonds and notes, such Municipality must have sufficient "payment capacity" as defined in Act No. 64 of July 3, 1996, as amended, also known as Financing Municipal Act. Such Act requires a Municipality must have sufficient "payment capacity" to incur additional general obligation debt if its deposits in the Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, is sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt.

Under prevailing applicable law the Municipality is required to levy a 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 and 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, 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, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. In the particular case of the Autonomous Municipality of Yabucoa, it has never been necessary to apply basic taxes to pay debt service on general obligation debt of the Municipality.

As mentioned in the notes of the Municipality's financial statements attached hereto, during the earlier months of the present year 2014, the Puerto Rico's Legislative Assembly approved Acts number 18 and 19. Through such legislation, the cash flow produced from collections by the Municipalities of the uses and sales taxes is completely restructured to provide additional liquidity to the Puerto Rico Government Development Bank (GDB) weakened cash position. A new created affiliate to GDB will receive those collections and assumed the total indebtedness incurred by municipalities as of June 30, 2014. A portion of total collections will be used for the payment of debt services requirement. The municipalities included in the new arrangement, advances to the municipalities, free of financing charges, equivalent to the monthly collections from the previous year. In the meantime, total liabilities incurred by the municipalities using Municipal Redemption Fund will be refinanced and GDB will recover its borrowed cash. It is anticipated that under the arrangement, the municipalities will recover the total 1% of uses and sales tax and will get the assurance future sources of financing either from GDB, from new created affiliate or private financing institutions.

## ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases not generally exceeding ten percent. State grant revenues may vary if new grants are available, but the revenue can be also predictable. Due to economic and budgetary constriction being faced by the Federal Government, grants available for present and future years could be reduced for states and territories. Although specific reductions are unpredictable, those factors are being considered by the Municipality in the confection of 2013-2014 and subsequent fiscal years budgets.

## FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the **Municipality of Yabucoa**, Finance Department, or call (787) 893-3000.

	<b>Governmental Activities</b>
<b>Assets</b>	
Cash and cash equivalents	\$ 1,871,660
Cash with fiscal agents	4,031,945
Accounts receivable:	
Property tax	1,207,753
Municipal sales and use tax	61,304
Others	8,712
Due from:	
Commonwealth Government	1,017,001
Federal Government	815,372
Capital assets	
Land, improvements, and construction in progress	8,652,411
Other capital assets, net of depreciation	36,224,894
Total capital assets	<u>44,877,305</u>
<b>Total assets</b>	<u>53,891,052</u>
<b>Liabilities</b>	
Accounts payable and accrued liabilities	5,351,140
Due to Commonwealth Government	2,512,035
Unearned revenues:	
Municipal license tax	3,745,486
Federal grants	39,270
Interest payable	260,719
Noncurrent liabilities:	
Due within one year	2,136,565
Due in more than one year	23,427,309
<b>Total liabilities</b>	<u>37,472,524</u>
<b>Net Position</b>	
Net investment in capital assets	29,715,005
Restricted for:	
Capital projects	1,365,276
Debt service	2,575,888
Other purposes	1,240,933
Unrestricted (deficit)	<u>(18,478,574)</u>
<b>Total net position</b>	<u>\$ 16,418,528</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF YABUCOA**

**Statement of Activities  
For the Year Ended June 30, 2013**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Position
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 15,062,404	\$ 274,400	\$ 1,285,028	\$ -	\$ (13,502,976)
Public safety	1,552,748	2,938	1,781	30,244	(1,517,785)
Public works	5,481,043	7,500		3,245,890	(2,227,653)
Health and welfare	4,336,308		1,771,098		(2,565,210)
Culture and recreation	739,839				(739,839)
Economic development	671,428		212,226		(459,202)
Community development	1,202,368		2,572,877		1,370,509
Education	186,474				(186,474)
Interest on long-term debt	813,373				(813,373)
<b>Total governmental activities</b>	<b>\$ 30,045,985</b>	<b>\$ 284,838</b>	<b>\$ 5,843,010</b>	<b>\$ 3,276,134</b>	<b>(20,642,003)</b>

General revenues:

Property taxes	3,528,129
Municipal license tax	2,712,572
Municipal sales and use tax	1,485,310
Grants and contributions not restricted to specific programs	7,620,955
Interest and investment earnings	122,722
Miscellaneous	343,683
<b>Total general revenues</b>	<b>15,813,371</b>
Change in net position	(4,828,632)
Net position - beginning, as restated	21,247,160
Net position - ending	\$ 16,418,528

	General Fund	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
<b>Assets</b>					
Cash and cash equivalents	\$ 540,898	\$ -	\$ -	\$ 1,330,762	\$ 1,871,660
Cash with fiscal agents	119,503	1,474,178	2,438,264		4,031,945
Accounts receivable:					
Property taxes	1,207,753				1,207,753
Municipal sales and use tax	61,304				61,304
Others	8,712				8,712
Due from					
Commonwealth government	558,911		137,624	320,466	1,017,001
Federal government				815,372	815,372
Other funds	1,723,799			1,051,294	2,775,093
<b>Total assets</b>	<b>\$ 4,220,880</b>	<b>\$ 1,474,178</b>	<b>\$ 2,575,888</b>	<b>\$ 3,517,894</b>	<b>\$ 11,788,840</b>
<b>Liabilities and Fund Balances</b>					
Liabilities :					
Accounts payable and accrued liabilities	\$ 4,265,568	\$ 7,700	\$ -	\$ 608,340	4,881,608
Due to:					
Commonwealth government	2,512,035				2,512,035
Other funds	1,044,540	101,202		1,629,351	2,775,093
Unearned revenues:					
Municipal license tax	3,745,486				3,745,486
Federal grants				39,270	39,270
<b>Total liabilities</b>	<b>11,567,629</b>	<b>108,902</b>		<b>2,276,961</b>	<b>13,953,492</b>
Fund (deficit) balances:					
Restricted		1,365,276	2,575,888	1,240,933	5,182,097
Assigned	68,025				68,025
Unassigned	(7,414,774)				(7,414,774)
<b>Total fund balances (deficit)</b>	<b>(7,346,749)</b>	<b>1,365,276</b>	<b>2,575,888</b>	<b>1,240,933</b>	<b>(2,164,652)</b>
<b>Total liabilities and fund balances</b>	<b>\$ 4,220,880</b>	<b>\$ 1,474,178</b>	<b>\$ 2,575,888</b>	<b>\$ 3,517,894</b>	<b>\$ 11,788,840</b>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF YABUCOA**

**Statement of Revenues, Expenditures and Changes  
in Fund Balance (Deficit)-Governmental Funds  
For the Year Ended June 30, 2013**

	General Fund	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
<b>Revenues</b>					
Property taxes	\$ 2,231,015	\$ -	\$ 1,297,114	\$ -	\$ 3,528,129
Municipal license taxes	2,712,572				2,712,572
Municipal sales and use tax	840,795		644,515		1,485,310
Licenses, permits and other local taxes	274,400				274,400
Intergovernmental	7,620,955	3,089,000		3,233,772	13,943,727
Fines and forfeitures	2,938				2,938
Rent of property	7,500				7,500
Interest	157,236				157,236
Federal grants				2,340,209	2,340,209
Miscellaneous	309,169			456,163	765,332
<b>Total revenues</b>	<b>14,156,580</b>	<b>3,089,000</b>	<b>1,941,629</b>	<b>6,030,144</b>	<b>25,217,353</b>
<b>Expenditures</b>					
Current:					
General government	13,895,097			1,507,552	15,402,649
Public safety	1,344,928			212,946	1,557,874
Public works	3,544,341	2,273,382		156,195	5,973,918
Health and welfare	2,691,999			1,581,480	4,273,479
Culture and recreation	523,054	97,888			620,942
Economic development				671,428	671,428
Community development				1,077,369	1,077,369
Education	186,474				186,474
Debt service:					
Principal			1,111,000		1,111,000
Interest			552,655		552,655
<b>Total expenditures</b>	<b>22,185,893</b>	<b>2,371,270</b>	<b>1,663,655</b>	<b>5,206,970</b>	<b>31,427,788</b>
Excess (deficiency) of revenues over (under) expenditures	(8,029,313)	717,730	277,974	823,174	(6,210,435)
<b>Other financing sources (uses)</b>					
Transfers in	1,953,883		304,631	1,223,165	3,481,679
Transfers out	(782,256)	(745,540)		(1,953,883)	(3,481,679)
Proceeds from the issuance fo general obligation debt	1,505,000				1,505,000
<b>Total other financing sources (uses)</b>	<b>2,676,627</b>	<b>(745,540)</b>	<b>304,631</b>	<b>(730,718)</b>	<b>1,505,000</b>
Net change in fund balances (deficit)	(5,352,686)	(27,810)	582,605	92,456	(4,705,435)
Fund balance (deficit), beginning as restated	(1,994,063)	1,393,086	1,993,283	1,148,477	2,540,783
Fund balance (deficit), ending	\$ (7,346,749)	\$ 1,365,276	\$ 2,575,888	\$ 1,240,933	\$ (2,164,652)

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Total Fund Balances (Deficit) - Governmental Funds \$ (2,164,652)

Amounts reported for Governmental Activities in the Statement of Net Position are different because:

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

Non-depreciable capital assets	\$ 8,652,411	
Depreciable capital assets, net of depreciation	<u>36,224,894</u>	
Total capital assets		44,877,305

Accounts payable related to Construction in Progress are not due and payable in the current period and, therefore, are not reported in the funds. (469,532)

Interest liabilities not due and payable in the current period and, therefore, are not reported in the funds (260,719)

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

General bonds and notes payable	17,767,300	
Property taxes debt	654,826	
Compensated absences	1,592,868	
US Department of Rural Development	69,954	
Post-closure care costs	3,563,314	
PR Department of Labor - payment plan	381,861	
Claims and judgments	<u>1,533,751</u>	
Total long-term liabilities		<u>(25,563,874)</u>

Total Net Position of Governmental Activities \$ 16,418,528

<b>Net Change in Fund Balances (Deficit) - Total Governmental Funds</b>	<b>\$ (4,705,435)</b>
Amounts reported for governmental activities in the Statement of Activities are different because:	
Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Position, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period.	1,083,963
Depreciation expense on capital assets is reported in the Government-Wide Statements of Activities and Change in Net Position, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds.	(20,418)
Interest expense on long-term debt was reported in the Government-Wide Statement of Activities and Change in Net Position, but it did not require the use of current financial resources. Therefore, interest expense was not reported as expenditures in Governmental Funds. The following amount represented the change in accrued interest from prior year.	(260,719)
Bonds and notes proceeds provide current financial resources to Governmental Funds, but issuing debt increase long-term liabilities in the Government-Wide Statement of Net Position. Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long-term liabilities in the Government-Wide Statement of Net Position. This is the amount by which debt proceeds exceed the debt service principal payments.	(394,000)
Repayment of long term property tax debt is an expenditure in Governmental Funds, but the repayment reduces long-term property tax debt in the Government-Wide Statement of Net Position. This is the amount paid in the current year.	12,764
Long-term compensated absences are reported in the Government-Wide Statement of Activities and Changes in Net Position, but they do not require the use of current financial resources. Therefore, long-term compensated absences were not reported as expenditures in Governmental Funds. The following amount represent the change in long-term compensated absences from prior year.	1,298,502
Repayment of long-term debt PR Department of Labor (DOL) - payment plan is an expenditure in Governmental Funds, but the repayment reduces long term DOL in the Governmental-Wide Statement of Net Position but it did not require the use of current financial resources. The following amount represent the the change in long term debt DOL - payment plan prior year	83,085
Repayment of long-term interest due for accounts sold-CRIM is an expenditure in Governmental Funds, but the repayment reduce long-term account sold - CRIM debt in the Government-Wide Statement of Net Position. The following amount represent the change in long-term interest due for accounts sold-CRIM from prior year.	8,540
Long-term claims and judgments are reported in the Governmental-Wide Statement of Activities and Changes in Net Position, but they do not require the use current financial resources. Therefore, claims and judgements are not reported as expenditures in Governmental Funds. The following amount represent the change in long-term claims and judgements from prior year.	(1,465,382)
Accounts payable change is reported in the Government-Wide Statement of Activities and Changes in Net Position but not reported as in the Governmental Funds because they do not require the use of current financial resources. This is the amount reported in the current period.	(469,532)
<b>Change in Net Position of Governmental Activities</b>	<b>\$ (4,828,632)</b>

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Yabucoa** (the Municipality) is a local municipal government constituted in the Commonwealth of Puerto Rico (the Commonwealth). The Municipality has full legislative, fiscal and all other governmental powers and responsibilities expressly assigned by Public Act. 81 of August 30, 1991, as amended know as Autonomous Municipalities Act of the Commonwealth of Puerto Rico (Act No. 81). The Municipality is one of seventy-eight municipalities legally separated from the Commonwealth's government.

The Commonwealth's Constitution provides for the separation of powers of the executive legislative and judicial branches of the Commonwealth and the municipalities. However the Municipality's governmental system consists of executive and legislative branches only. A Mayor elected every four years by the citizens, exercises the executive power of the Municipality. The Municipal Legislature whose members are also elected every four years exercises the legislative power of the Municipality. The General Justice Court Systems of the Commonwealth which has jurisdiction over the Municipality exercises the judiciary power.

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

The accounting policies and financial reporting practices of the Municipality conform to accounting principles generally accepted in the United States of America ("USGAAP") as applicable to governmental units.

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, "Basic Financial Statements and Management's and Discussion and Analysis for State and Local Governments." This Statement, known as the Reporting Model, provides for the most significant change in financial reporting for state and local governments in over 20 years and affects the way the Municipality prepares and presents financial information. In addition to this Statement, GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" have been adopted and are reflected in these financial statements.

As part of this Statement, there is a reporting requirement regarding the capitalization of local government infrastructure (roads, bridges, traffic signals, etc.). This requirement allows an optional four-year delay for implementation to fiscal year ended on June 30, 2007. The Municipality elected to implement the retroactive capitalization of infrastructure assets.

On March 2009, the Municipality adopted the provisions of GASB Statement No.55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* (GASB No. 55), and GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards* (GASB No. 56).

GASB No. 55 incorporated the hierarchy of USGAAP for state and local governments into the Governmental Accounting Standards Board's (GASB) authoritative literature. The requirements in this Statement codify all USGAAP for state and local governments so that they derive from a single source.

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

GASB No. 56 incorporated into the Governmental Accounting Standards Board's (GASB) authoritative literature certain accounting and financial reporting guidance presented in the American Institute of Certified Public Accountants' Statements on Auditing Standards. This Statement addressed three issues not included in the authoritative literature that establishes *accounting* principles-related party transactions, going concern considerations, and subsequent events.

On July 1, 2009, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which modified the interpretations of certain terms within the definition of the special revenue funds and the types of activities the Municipality may choose to report in those funds. GASB No. 54 also clarified the capital projects fund type definition for better alignment with the needs of preparers and users. Definitions of other governmental fund types were also modified for clarity and consistency.

The provisions of the GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*, an amendment of Statements No. 14 and 34, were considered in the evaluation of the potential component units. This statement modifies certain requirements for inclusion of components units in the financial reporting entity and amends the criteria for reporting component units as if they were part of the primary government under certain circumstances.

The GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* (GASB 62), incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance included in FASB pronouncements, which does not conflict with or contradict GASB pronouncements, and eliminates the criteria to apply post November 30, 1989 FASB pronouncements that do not conflict with or contradict GASB pronouncements.

In current year, the Municipality adopted the provisions of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and the Net Position* establishing a new statement of net position format that reports separately all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (which is the net residual amount of the other elements). The Statement requires deferred outflows of resources and deferred inflows of resources to be reported separately from assets and liabilities. The financial reporting impact resulting from the implementation of GASB 63 in the Municipality's financial statements was the renaming of "Net Assets" to "Net Position", including changing the name of the financial statement from "Statement of Net Assets" to "Statement of Net Position".

The following is a summary of the significant accounting policies of the Municipality:

### A. Component Units

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 GASB Statement No. 14, as amended. The basic, but not the only criterion for including a potential component unit within the reporting entity is if a primary government is financially accountable for the entity. Financial accountability exists if the primary governmental 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 are such

1. **ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. Based on the above criteria the Municipality does not have component units to include within its reporting entity.

**B. Government-wide and fund financial statements**

Financial information of the Municipality is presented in this report as follow:

1. Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.
2. The government-wide financial statements (i.e. the statement of net position and the statement of activities) report information on all the activities of the Municipality and its component units, if any. 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. Interfund activity has been removed from these statements to minimize the duplicating effect on assets and liabilities within the governmental activities.

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

3. Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. Pursuant to the provisions set forth by GASB No. 54, the Municipality reported the following governmental funds in the accompanying governmental funds financial statements:

**General Fund** – is the Municipality main operating fund used to account for and report all financial and reported resources and governmental activities, except for those required to be accounted for in another fund. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) USGAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund. Its revenues consist mainly of taxes, licenses and permits, intergovernmental, charges for services and other.

**Capital Projects Fund – State and local Grants**– is a major governmental fund used to account for and report financial resources that are restricted or committed to expenditure for capital outlays, including the acquisition or construction of major capital facilities, including those outlays financed by the general obligation bond proceeds (other than those financed by proprietary funds or in trust funds for individuals, private organizations, or other governments). The use of the capital projects funds has been limited to only for major

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

capital acquisitions, construction or improvement activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalizable assets (such as furniture, office equipment, vehicles and other minor capital assets or improvements) have been reported in the governmental fund from which financial resources were used for the payment.

**Debt Service Fund** –is a major governmental fund used to account for and report for the accumulation of financial resources that are restricted for, and the payment of, principal and interest for: (1) bonds payable for which debt service payments are legally mandated to be accounted for in a debt service fund and (2) certain special long-term obligations for which the Municipality is been accumulating financial resources in advance to pay principal and interest payments maturing in future years.

The other governmental funds of the Municipality account for grants and other resources whose use is restricted for a particular purpose.

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

4. The notes to the financial statements provide information that is essential to a user's understanding of the basic financial statements.
5. Required Supplementary Information such as the budgetary comparison schedule-general fund and other types of data required by GASB.
6. Notes to the budgetary comparison schedule-general fund.
7. Supplementary information such as the Schedule of Expenditures of Federal Awards.

### C. Financial reporting presentation

The accounts of the Municipality are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Fund types are as follows:

**General Fund** - General Fund is the general operating fund of the Municipality. It is used to account for all financial resources not accounted for and reported in another fund.

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

**Capital Projects Fund – State and Local Grants** - Capital Projects Funds are used to account for all financial resources restricted, committed or assigned to expenditure for the acquisition or construction or improvement of major capital facilities and other assets.

**Special Revenue Fund – State and Federal Grants** - Special Revenue Funds are used to account and report the proceeds of specific revenue sources derived from state and federal grants that are restricted or committed to expenditure for specific purposes other than debt service or capital projects. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

**Debt Service Fund** - Debt Service Funds are used to account for the accumulation of resources for and the payment of, general long-term debt principal, interest, and related costs.

The outstanding balance of certain general long-term obligations for which debt service payments do not involve the advance accumulation of resources (such as certain notes payable, obligations under capital leases, accrued compensated absences, landfill obligation, claims and judgments, net pension liability and other long-term obligations) are only accounted for in the accompanying statement of net position. The debt service payments of such obligations are generally accounted for in the governmental fund which accounted for the financial resources used for the payment of such debts.

### D. Measurement focus, basis of accounting and financial presentation

**Government-wide financial statements** – The accompanying GWFS are prepared using the economic resources measurement focus and the accrual basis of accounting. Subject to the additional rules and limitations detailed below, revenues (including interest on deposits and investments) are generally recorded when earned and expenses are generally recorded when a liability is incurred, regardless of the timing of related cash flows.

All revenues, expenses, gains, losses, assets and liabilities resulting from exchange-like transactions are generally recorded when exchange takes place. In exchange transactions, each party to the transaction receives and gives up essentially equal values. An exchange-like transaction is one when there is an identifiable exchange and the values exchanged, though related, may not be quite equal. The accompanying basic financial statements include exchange-like transactions such as license fees, fines, penalties, forfeitures, permits, charges for services, and most miscellaneous revenues, which are recorded as revenues when collected because they are generally not measurable until actually received.

The Municipality groups its non-exchange transactions into the following four (4) classes in the accompanying basic financial statements: (a) derived tax revenues, (b) imposed non-exchange revenues, (c) government mandated non-exchange transactions, and (d) voluntary non-exchange transactions. In the case of derived tax revenue transactions, which result from assessments that the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred (such as municipal license tax). In the case of imposed non-exchange revenue transactions (such as property taxes), which result from assessments made by the Municipality on non-governmental entities, including individuals, other than assessments on exchange transaction, receivables are generally recorded in the period when an enforceable legal claim has arisen. Property taxes and municipal license taxes are generally recorded as revenues (net of amounts considered not collectible) in the fiscal year when resources are required to be used for the first fiscal year that the use of the resources is permitted.

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

For government-mandated non-exchange transactions (such as intergovernmental grants and contributions), receivables and revenues are generally recorded when all eligibility requirements imposed by the provider have been met. For the majority of grants, the Municipality must expend resources on the specific purpose or project before the provider reimburses any amounts. Therefore, revenue is generally recognized as qualifying reimbursable expenditures are incurred.

For voluntary non-exchange transactions (such as donations and certain grants and entitlements) receivables and revenues are generally accounted for in the same manner as government-mandated non-exchange transactions discussed above.

Interests on deposits are recorded when earned since these revenues are considered both measurable and available at June 30, 2013. Receipts of any type of revenue sources collected in advance for use in the following fiscal year are recorded as unearned revenues.

According to GASB No. 34, all general capital assets and the unmatured long-term liabilities are recorded only in the accompanying statement of net position. The measurement focus and the basis of accounting used in the accompanying GWFS differ significantly from the measurement focus used in the preparation of the GFFS. Therefore, the accompanying GFFS include reconciliations, as detailed in the accompanying table of contents, to better identify the relationship between the GWFS and the GFFS.

**Government Fund Financial Statements** – The accompanying GFFS are reported using the current financial resources measurements focus and the modified accrual basis of accounting. Revenues are generally recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current fiscal year or soon enough thereafter to pay liabilities of the current fiscal year. For this purpose, the Municipality generally considers most revenues (municipal licenses taxes, construction excise taxes, sales and use taxes, interests on deposits, intergovernmental grants and contributions and certain charges for services) to be available if collected within sixty (60) days after June 30, 2013. At June 30, 2013, all revenues sources met this availability criterion.

Property taxes are all considered susceptible to accrual if commonly collected within sixty (60) days following the end of the fiscal period, unless unusual circumstances justify a greater period.

Other revenue sources considered susceptible to accrual include municipal license taxes, sales and use taxes, construction excise taxes, intergovernmental grants and contributions, interests on deposits and charges for services. These principal revenue sources meet both measurability and availability criteria in the accompanying GFFS.

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In a manner similar to the GWFS, but subject to and limited by the availability criteria discussed above, all revenues, expenses, gains, losses, assets and liabilities resulting from exchange, exchange-like transactions are also generally recorded when the exchange takes place while all revenues, expenses, gains, losses, and assets resulting from non-exchange transactions are recorded when an enforceable legal claim arises or when all eligibility requirements imposed by the provider have been met, applicable. Interests on deposits are recorded when earned since these revenues are considered both measurable and available at June 30, 2013.

Pursuant to the provisions of GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements* (GASBI No. 6), in the absence of an explicit requirement (i.e., the absence of an applicable modification, discussed below) the Municipality generally accrues a governmental fund liability and expenditure (including salaries, professional services, supplies, utilities, etc.) in the period in which the government incurs the liability, to the extent that these liabilities are normally expected to be liquidated in a timely manner and in full with current available financial resources. The accompanying Balance Sheet – Governmental Funds generally reflects only assets that will be converted into cash to satisfy current liabilities.

Long-term assets and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying Balance Sheet – Governmental Funds. At the same time, long-term liabilities (generally, those unmatured that will not require the use of current financial resources to pay them) are not accounted for in the accompanying Balance Sheet – Governmental Funds.

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

### E. Assets, liabilities and net position

1. **Cash, cash equivalents, and cash with fiscal agent-** The Municipality's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

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. Also, cash with fiscal agent consists of unused proceeds of bonds and notes issued for the acquisition of equipment and construction of major capital improvements.

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

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

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 represents the balance due from the Municipal Revenue Collection Center (CRIM) resulting from the final liquidations of advances made by CRIM to the Municipality corresponding to collections from property taxes and legislative appropriations from the Commonwealth of Puerto Rico plus final liquidation of contributions in lieu of taxes payable by the Puerto Rico Electric Power Authority (PREPA) to the Municipality. During the last years, the Puerto Rico Electric Power Authority has not been financially able to afford the cost of the Contribution in Lieu of Taxes as required by Section 22(b) of Act Number 83-1941, as amended. For those years, the Authority has recognized a partial credit for each year and has amortized the remaining amount owed during the three subsequent fiscal years. As of June 30, 2013, the Contribution in Lieu of Taxes corresponding to the Municipality of Yabucoa amounted to \$3,139,065. Management anticipates that due to the serious financial limitations being encountered by PREPA, the remaining non-credited balance of such amount will be amortized during the fiscal years 2014, 2015 and 2016. Intergovernmental Receivables in the debt service fund represent the amounts due from the CRIM resulting from the excess of current year property tax collections over current year advances. Intergovernmental receivable in the special revenue or capital project funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded or state funded programs.

During the beginning of fiscal year 2008-2009, the Municipality resolved the contract signed with the Secretary of the Treasury to collect and distribute the revenues produced by the sales and use tax. As part of the new organizational chart implemented for the Finance Directorate, a new unit was created under such directorate which has been responsible to manage this function at the Municipality's level. Such decision has been beneficial for the Municipality in its search for additional increases in current revenues derived from such tax.

3. **Inventories-** Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net position.
4. **Capital assets-** Capital assets, which include land and land improvements, buildings, structures and building improvements, machinery and equipment (including equipment held under capital leases), furniture and fixtures, licensed vehicles, construction in progress, and infrastructure. The Municipality defines capital asset as assets with an initial, individual cost of more than \$500 and an estimated useful life in excess of one year. Such assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Capital assets of the Municipality are depreciated using the straight-line method over the following estimated useful lives:

<u>Description</u>	<u>Useful Life</u>
Land Improvements	20 years
Buildings, structures and building improvements	30 to 50 years
Infrastructure	20 to 50 years
Motor Vehicles	5 years
Furniture and fixtures	5 to 20 years
Machinery and equipment	5 to 20 years
Equipment held under capital leases	3 to 5 years

- 5. Unearned revenues-** In the GFFS, unearned revenues arises when one of the following situations occur:
- a. Potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period (unavailable revenue). As previously discussed, available is defined as due (or past due) at June 30, 2013 and collected within 60 days thereafter to pay obligations due at June 30. In subsequent periods, when both criteria are met, the liability for unearned revenue is removed and revenue is recognized.
  - b. The Municipality receives resources before it has a legal claim to them (unearned revenue). In subsequent periods, when the revenue recognition criterion is met, the liability for unearned revenue is removed and revenue is recognized.

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

- 6. Long-term obligations-** The liabilities reported in the government-wide financial statements included general and special obligation bonds and notes, and other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities.

In the fund financial statements, governmental fund types recognize bond issuances cost, during the current period. The face amount of debt issued is reported as other financing sources, while bond issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures

- 7. 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. All vacation pay is accrued when incurred in the government-wide financial statements.

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 current rate, if the employee has at least 10 years of service with the Municipality. All sick leave pay and salary related benefits are accrued when incurred in the governmental-wide financial statements when the employee meets such criteria.

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

8. **Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund when the liability is incurred.
9. **Fund Balances** – On July 1, 2009, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which enhanced the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied. This statement establishes fund balance classifications that comprise a hierarchy upon the use of the resources reported in governmental funds.

Pursuant to the provisions of GASB No. 54, the accompanying GFFS report fund balance amounts that are considered restricted, committed, assigned and unassigned, based on the relative strength of the constraints that control how specific amounts can be spent, as described as follows:

- a. **Restricted** – Represent resources that can be spent only for the specific purposes stipulated by constitutional provisions, external resource providers (externally imposed by creditors or grantors), or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
- b. **Committed** – Represent resources used for specific purposes, imposed by formal action of the Municipal's highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by a similar law, ordinance or resolution, no later than the end of fiscal year.
- c. **Assigned** – Represent resources intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed (generally executive orders approved by the Mayor). Intent can be expressed by the Municipal Legislature, the Mayor or by an official or body to which the Municipal legislature delegates authority in conformity with the Autonomous Municipalities Act of Puerto Rico, as amended. In governmental funds other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed.
- d. **Unassigned** – Represent the residual classification for the Municipality's general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned. Negative fund balance amounts are assigned amounts reduced to the amount that will raise the fund balance to zero. Consequently, negative residual amounts in restricted, committed and assigned fund balance classifications have been reclassified to unassigned fund balances.

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely. However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balances amounts as of for the fiscal year ended June 30, 2013.

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In situations when expenditure is made for a purpose for which amounts are available in multiple fund balance classifications, the Municipality generally spends committed resources first, and then unrestricted resources. Within unrestricted resources, the Municipality generally spends committed resources first, followed by assigned resources, and then unassigned resources.

- 10. Net position** - Net position has been reported pursuant to the provisions of GASB Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position. Net Position represents the difference between all assets plus deferred outflows of resources and all liabilities plus deferred inflows of resources. The Net Position consists of net resources restricted by external parties (such as debt covenants, creditors, grantors, contributions, laws or regulations of other governments, ect.) or net position for which constraints are imposed by the constitutional provisions or enabling legislation.

Enabling legislation consists of legislation that authorizes the Municipality to assess, levy, charge or otherwise mandate payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

A legally enforceable enabling legislation restriction is one that a party external to the Municipality (such as citizens, public interest groups, or the judiciary) can compel the Municipality to honor. The Municipality periodically reevaluates the legal enforceability of an enabling legislation to determine if any of the resources raised by the enabling legislation are used for a purpose not specified by the enabling legislation or if the Municipality has other cause for consideration.

The classification of restricted net position identifies resources that have been received or earned by the Municipality with an explicit understanding between the Municipality and the resource providers that the resources would be used for specific purposes. Grants, contributions and donations are often given under those kinds of conditions. Bond indentures also often limit the use of bond proceeds to specific purposes.

Internally imposed designation of resources, including earmarking, are not reported as restricted net position. These designations consist of management's plans for the use of resources, which are subject to change at the discretion of the Municipal Legislature.

In the government-wide statements, net position is segregated into three categories:

- a. **Net investment in capital assets:** Represent the component of the net position that consist of capital asset balances net of accumulated depreciation and outstanding balances of any bonds, notes and other borrowings that are attributable to the acquisition, construction, or improvement of those assets. This category should not include cash that is restricted to capital asset acquisition or construction (unspent bond proceeds).
- b. **Restricted net position:** Represents the component of the net position that is subject to restrictions beyond the Municipal's control. These include restrictions that are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or restrictions imposed by the law through constitutional provisions or enabling legislation (including enabling legislation passed by the government itself).

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- c. **Unrestricted net position:** Represent the component of the net position that do not meet the definition of net position net invested in capital assets or restricted. Unrestricted assets are often designated to indicate that Management does not consider them to be available for general operations. These types of constraints are internal and Management can remove or modify them. Designations are not reported on the face of the statement of net position.

- 11. Accounting for Pension Costs-** On July 1, 2007, the Municipality adopted the provisions of GASBS No. 50, *Pension Disclosure*, which amended GASBS No. 27, *Accounting for Pensions by State and Local Government Employers*, by requiring disclosure of how the contractually required contribution rate is determined by governments participating in multi-employer cost-sharing pension plans.

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

For the purpose of applying the requirements of GASBS No. 27, the state Government of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multi-employer cost-sharing define benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate. The Municipality is considered a participant, and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Government of Puerto Rico and the basic financial statements of such retirement systems are part of the financial reporting entity of the Government of Puerto Rico.

- 12. Interfund and intra-entity transactions-** The Municipality has the following types of transactions among funds:

- a. **Operating Transfers-** Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
- b. **Intra-Entity Transactions-** Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.

- 13. Risk financing-** The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico. Under Act No. 63 of June 21, 2010, the Legislative Assembly of the Commonwealth of Puerto Rico, authorized the municipalities to procure and manage at their own discretion all insurance policies, including those related to health plans being provided to the municipal employees. The Municipality obtains medical insurance from a health insurance company for its employees. Different health coverage and premium options are negotiated each year by the Municipality. Premiums are paid on a monthly basis directly to the insurance company.

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, 2013 amounted to \$611,559.

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$528,810 for workers compensation insurance covering all municipal employees.

- 14. Use of Estimates-** The preparation of financial statements in conformity with USGAAP requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual amounts could differ from those estimates.

## 2. CASH AND CASH EQUIVALENTS

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

On July 1, 2005, the Municipality adopted the provisions of GASB Statement No. 40 (GASB No. 40), *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. This statement requires that state and local governments disclose essential risk information about deposits and investments. The disclosure requirements cover four main areas: (1) credit risk, (2) interest rate risk, (3) custodial credit risk, (4) foreign exchange exposure.

**Credit risk** – This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial and credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2013.

**Interest rate risk** – This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investment portfolio at June 30, 2013, (2) limiting the weighted average maturity of its investments to three months or less, and (3) keeping most of its bank deposits in interests bearing accounts generating interests at prevailing market rates. At June 30, 2013, the Municipality's investments in certificates of deposits are recorded at cost, which approximates their fair value. Therefore, the Municipality's management has concluded that at June 30, 2013, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

**Custodial credit risk** – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico* the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$250,000 per depositor.

## 2. CASH AND CASH EQUIVALENTS (CONTINUED)

In addition, public funds deposited in commercial banks are fully collateralized for the amounts deposit in excess of the federal depository insurance. All securities pledged as collateral are held, in the Municipality's name, by the Commonwealth's Secretary of Treasury Deposits with GDB are unassured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2013. Therefore, the Municipality's management has concluded that at June 30, 2013, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

**Foreign exchange risk** – The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, the Municipality is prevented from investing in foreign securities or any other types of investments in which foreign exchange risk exposure may be significant. Accordingly, Management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2013.

Under Commonwealth of 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).

Deposits - The Municipality's bank balances in commercial banks of approximately \$540,898 in the general fund were fully collateralized at June 30, 2013. In the other governmental funds there were deposits with commercial banks of approximately \$1,330,762 that were fully collateralized.

The deposits at GDB of approximately \$119,503 that is restricted for other purposes in the general fund, the \$1,474,178 that is restricted principally for capital projects in the capital project fund – state and local grants, the \$2,438,264 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

## 3. RECEIVABLES AND DUE FROM GOVERNMENTAL ENTITIES

**A. Property taxes** - Property taxes receivable recorded in the general fund amounted to \$1,207,753.

**B. Municipal License Tax**- the Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Act of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$3,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2013, the tax rates were as follows:

1. Financial business- 1.50% of gross revenues
2. Other organizations- 0.50% of gross revenues

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 April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2013, net of allowance for uncollectible accounts.

3. RECEIVABLES AND DUE FROM GOVERNMENTAL ENTITIES (CONTINUED)

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

- C. **Municipal sales and use tax** - The Municipality imposes a sales and use tax within the territorial limits of the Municipality pursuant to the Internal Revenue Code of the Government of Puerto Rico. This is a self-assed tax consisting of one and half percent (1.5%) on the sale price of a taxable item or on the purchase price of all usage or consumption of a taxable item. It is collected monthly in a tax return that is due twenty calendar days after the end of each month.

A portion of the sales tax amounting 0.2% is restricted for the payment of long-term debt and is recorded in the debt service fund. The remaining portion of the 1.5% is recorded in the general fund since is available for general operating purposes.

Sale tax receivable represents sales tax levied that were collected subsequent to June 30, 2013, but pertaining to current year period. At June 30, 2013, the sales and use taxes receivable amounted to \$61,304.

- D. **Due from Commonwealth Government** - In the General Fund, Due from Commonwealth Government represents expenditures incurred not yet reimbursed by other governmental entities. Following is a detail of the intergovernmental receivable:

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Treasury Department	\$ 250,000
Government Development Bank	308,911
<b>Total</b>	<b><u>\$ 558,911</u></b>

Due from Commonwealth Government of \$137,624 in the Debt Service Fund represents the amounts resulting from the current year sales and use tax collections and the additional property tax corresponding to June 2013 but not yet paid by the Municipal Revenue Collection Center, respectively.

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Treasury Department	\$ 50,599
Government Development Bank	87,025
<b>Total</b>	<b><u>\$ 137,624</u></b>

Due from Commonwealth Government of \$320,466 in Other Governmental Funds represents the amount owed to the Municipality from the 9-1-1 Service Government Board.

- E. **Due from Federal Government** - In the Other Governmental Funds, Due from Federal Government represents expenditures incurred not yet reimbursed by the Federal Government or the pass-through grantors. Following is a detail of amounts included in this item:

<u>Federal Program Description</u>	<u>Amount</u>
Community Development Block Grant – State’s Program	\$ 317,344
Child Care Development Block Grant	354,258
Disaster Grants – Public Assistance	143,770
<b>Total</b>	<b><u>\$ 815,372</u></b>

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2013, and interfund transfers during the fiscal year ended at June 30, 2013, are summarized as follows:

a. Due from/to other funds:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Other Governmental Funds	Reimbursable Expenditures	\$1,629,351
Other Governmental Funds	General Fund	Short-term borrowings	1,044,540
General Fund	Capital Projects Fund Local and State Grants	Reimbursable Expenditures	101,202
<b>Total</b>			<b><u>\$2,775,093</u></b>

b. Transfer in/out to other funds:

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Other Governmental Funds	Transfer of funds for operational activities	\$ 477,625
Other Governmental Funds	General Fund	Transfer of funds or operational activities	1,953,883
General Fund	Debt Service Fund	Debt Retirement	304,631
Capital Projects Fund – Local & State Grants	Other Governmental Funds	Transfer of funds or operational activities	745,540
<b>Total</b>			<b><u>\$ 3,481,679</u></b>

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**5. CAPITAL ASSETS**

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$500 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2013, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

<b>Governmental Activities:</b>	<b>Balance July 1, 2012</b>	<b>Additions</b>	<b>Retirements</b>	<b>Balance June 30, 2013</b>
Capital asset, not being depreciated:				
Land	\$ 8,021,703	\$ -	\$ -	\$ 8,021,703
Construction in progress	<u>-</u>	<u>630,708</u>	<u>-</u>	<u>630,708</u>
Total capital assets not being depreciated	<u>8,021,703</u>	<u>630,708</u>	<u>-</u>	<u>8,652,411</u>
Capital assets, being depreciated:				
Buildings structures and building improvements	22,648,306	90,124		22,738,430
Infrastructure	33,663,415	232,172		33,895,587
Vehicles machinery and equipment and furniture and fixtures	6,257,194	130,959		6,388,153
Office equipment under capital leases	<u>141,502</u>	<u>-</u>	<u>-</u>	<u>141,502</u>
Total capital assets being depreciated	<u>62,710,717</u>	<u>453,255</u>	<u>-</u>	<u>63,163,972</u>
Less accumulated depreciation for:				
Buildings structures and building improvements	(6,203,949)	(1,612)		(6,205,561)
Infrastructure	(12,158,394)	(4,594)		(12,162,988)
Vehicles, machinery and equipment and furniture and fixtures	(8,488,649)	(14,212)		(8,502,861)
Office equipment under capital leases	<u>(67,668)</u>	<u>-</u>	<u>-</u>	<u>(67,668)</u>
Total accumulated depreciation	<u>(26,918,660)</u>	<u>(20,418)</u>	<u>-</u>	<u>(26,939,078)</u>
Total capital assets being depreciated, net	<u>35,792,057</u>	<u>432,837</u>	<u>-</u>	<u>36,224,894</u>
Governmental activities capital assets, net	<u>\$ 43,813,760</u>	<u>\$ 1,063,545</u>	<u>\$ -</u>	<u>\$ 44,877,305</u>

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

<b>Governmental activities:</b>	<b>Amount</b>
General government	\$ 20,044
Public safety	302
Community development	<u>72</u>
<b>Total depreciation expense-governmental activities</b>	<b><u>\$ 20,418</u></b>

**6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

Accounts payable and accrued liabilities at June 30, 2013 are summarized as follows:

<u>Description</u>	<u>General Fund</u>	<u>Capital Projects Fund- State &amp; Local Grants</u>	<u>Debt Service Fund</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Accounts payable	\$ 4,023,138	\$ 7,700	\$ -	\$ 608,340	\$ 4,639,178
Accrued liabilities	242,430	-	-	-	242,430
<b>Total</b>	<b>\$ 4,265,568</b>	<b>\$ 7,700</b>	<b>\$ -</b>	<b>\$ 608,340</b>	<b>\$ 4,881,608</b>

**7. DUE TO OTHER GOVERNMENTAL ENTITIES**

The amounts due to other governmental entities in the General Fund include the following:

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Health Service Administration	\$ 1,608,659
Puerto Rico Aqueduct and Sewer Authority	854,880
Puerto Rico Department of Labor	26,257
General Services Administration	22,239
<b>Total</b>	<b>\$ 2,512,035</b>

**8. UNEARNED REVENUES**

**A. Municipal License Tax-** The unearned revenues of \$3,745,486 in the general fund relates to municipal license tax collected in fiscal year 2012-13 that will be earned in fiscal year 2013-14.

**B. Federal Government-** The unearned revenues presented in the other governmental funds represent the portion of federal grants received for which qualifying expenditures have not been incurred. Unearned revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Emergency Shelter Grant	\$ 9,723
Urban Development Action Grant	9,301
Homelessness Prevention and Rapid Re-housing Program	8,595
Justice Assistance Grant	5,892
Housing Opportunities for Persons with AIDS	3,574
Others	2,185
<b>Total</b>	<b>\$ 39,270</b>

## 9. 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 Legislation approved in August 1991. 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 liquidation statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end, subject to the verification by its Independent Auditors. 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. The CRIM issued the final liquidation noting that collections exceeded advances by \$437,062.

On January 26, 2000, Public Law No. 42 was enacted, which authorized the CRIM to obtain a loan up to \$200,000,000, and for a term not to exceeding 10 years, to allow for the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year ended June 30, 2000. The amounts that the Municipalities will collect from additional property taxes resulting from increases in the subsidy from the Commonwealth of Puerto Rico to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238, enacted on August 15, 1999. On October 11, 2001, Public Law No. 146 was enacted to amend Public Law No. 42, to extend the loan amortization period up to 30 years. The Statement of Net Position includes an outstanding debt balance of \$492,563 at June 30, 2013, related with Law No. 42.

Also, on October 11, 2002, Public Law No. 172 was enacted, to provide as an option for the Municipalities to include the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections for the fiscal year ended June 30, 2001 with the loan authorized through Public Law No. 42 enacted on January 26, 2000.

On June 26, 1997, Public Law No. 21 was enacted, authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable or equivalent in money. Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible.

## 9. PROPERTY TAXES (CONTINUED)

In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law No. 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities through a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law. During the first five years of the note, commenced in July 1, 2003, the Municipality shall pay only interest. At the end of the first five years of the note, the repayment terms and conditions of the note shall be renegotiated to allow the Municipality to pay the outstanding balance of the note in equal installments of principal plus interest, through maturity. The Statement of Net Position includes an outstanding debt balance of \$162,263 related to Law No. 146.

The annual tax rate is 10.83% for real property and 8.83% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, 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) 4.00% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

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.

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10. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2013, was as follows:

Description	Beginning Balance, as restated	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds payable	\$ 17,373,300	\$ 1,505,000	(\$ 1,111,000)	\$ 17,767,300	\$ 923,200
Public Act No. 42 January 20, 2001	505,327		(12,764)	492,563	13,566
Public Act No. 146 of October 11, 2001	170,803		(8,540)	162,263	8,540
U.S. Department of Rural Development	69,954			69,954	
Compensated absences	2,891,370		(1,298,502)	1,592,868	130,000
Post-closure care costs	3,563,314			3,563,314	
2011 Repayment Plan Department of Labor (467,597)	235,948		(128,699)	107,249	128,699
2012 Repayment Plan Department of Labor (\$170,321)		170,321	(41,435)	128,886	51,554
2012 Repayment Plan Department of Labor (\$302,566)	228,998		(83,272)	145,726	83,272
Claims and judgments	68,369	1,521,017	(55,635)	1,533,751	797,734
<b>Total</b>	<b>\$ 25,107,383</b>	<b>\$ 3,196,338</b>	<b>(\$ 2,739,847)</b>	<b>\$ 25,563,874</b>	<b>\$ 2,136,565</b>

- A. Legal debt margin-** The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment of property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds and notes payable, is paid with unrestricted funds.
- B. Bonds payable-** The Municipality issues general obligation, special obligation and public improvement bonds to finance the acquisition, construction and improvement of capital assets, as well as, to finance certain operating needs, including the payment to suppliers in certain circumstances.

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

As describe in **Note 9** the Municipality levies an annual additional special tax of 4.00 percent of the assessed value of personal and real property. The proceeds of this additional special tax are deposited in a sinking fund established at GDB whereby sufficient funds are set aside to redeem the bonds payable of the Municipality in minimum annual or semiannual principal and interest payments. The collections of this special tax are recorded in the Municipality's Debt sService Fund.

10. LONG-TERM LIABILITIES (CONTINUED)

For financial reporting purposes the outstanding balances of bonds represent the total principal to be repaid. Bonds payable is composed as follows at June 30, 2013:

Description	Balance at June 30, 2013
1990 General bond obligation for construction and improvement of infrastructure assets with an original amount \$225,000 due in installments of \$4,000 to \$18,000 through January 1, 2014, with interest of 6.0%	\$ 18,000
1993 General bond obligation for construction and improvement of infrastructure assets with an original amount \$135,000 due in installments of \$16,000 to \$47,000 through January 1, 2016, with interest of 5.0%	135,000
1994 General obligation bond for construction and improvements of infrastructure with an original amount of \$238,000 due in installments of \$6,000 to \$17,000 through January 1, 2016, with interest ranging of 5.0%	49,000
1995 General obligation bond for construction and improvements of infrastructure with an original amount of \$2,080,000 due in installments of \$45,000 to \$195,000 through July 7, 2014, with interest ranging from 4.70% to 7.25%	375,000
1995 General obligation bond for construction and improvements of infrastructure with an original amount of \$106,00 due in installments of \$2,000 to \$8,000 through January 1, 2019, with interest ranging of 4.50%	41,000
1995 General obligation bond for construction and improvements of infrastructure with an original amount of \$36,000 due in installments of \$1,000 to \$3,000 through January 1, 2019, with interest ranging of 4.50%.	13,000
1998 General obligation bond for operational debts payment with an original amount of \$3,310,000 due in installments of \$75,000 to \$305,000, through July 1, 2017, with interest ranging from 1.28% to 7.81%	1,320,000
2001 General obligation bond for operational debts payment with an original amount of \$600,000 due in installments of \$5,000 to \$50,000, through January 1, 2025, with interest ranging from 1.28% to 8.00%	465,000
2002 General obligation bond with an original amount \$1,910,000 due in installments of \$5,000 to \$295,000 through July 1, 2027, with interest ranging from 1.28% to 6.37%.	1,860,000
2003 General bond obligation with an original amount \$680,000 due in installments of \$10,000 to \$50,000 through July 1, 2027, with interest ranging from 4.17 %to 5.31%.	525,000
2003 General bond obligation with an original amount \$230,000 due in installments of \$5,000 to \$20,000 through July 1, 2027, with interest ranging from 4.17 %to 5.31%	180,000
2003 General bond obligation with an original amount \$300,000 due in installments of \$5,000 to \$30,000 through July 1, 2027, with interest ranging from 4.17% to 5.31%	235,000
2003 General bond with an original amount \$305,000 due in installments of \$5,000 to \$25,000 through July 1, 2028, with interest ranging from 4.17% to 5.31%	245,000
2003 General obligation bond for operational debts payment with an original amount of \$335,000 due in installments of \$5,000 to \$25,000, through July 1, 2027, with interest ranging from 1.53% to 6.50%	260,000

10. LONG-TERM LIABILITIES (CONTINUED)

Description	Balance at June 30, 2013
2003 General obligation bond for operational debts payment with an original amount of \$190,000 due in installments of \$5,000 to \$15,000, through July 1, 2028, with interest ranging from 1.53% to 6.50%	145,000
2005 General bond obligation with an original amount \$135,000 due in installments of \$5,000 to \$10,000 through July 1, 2030, with interest ranging from 4.23% to 5.31%	100,000
2005 General bond obligation with an original amount \$540,000 due in installments of \$10,000 to \$45,000 through July 1, 2030, with interest ranging from 4.23% to 5.33%	455,000
2005 General bond obligation with an original amount \$335,000 due in installments of \$5,000 to \$30,000 through July 1, 2030, with interest ranging from 4.23% to 5.33%	280,000
2006 General bond obligation with an original amount \$1,700,000 due in installments of \$70,000 to \$170,000 through July 1, 2020, with interest ranging from 1.53% to 6.62%	1,100,000
2006 General bond obligation with an original amount \$421,000 due in installments of \$12,000 to \$34,000 through July 1, 2031, with interest ranging of 4.25%	421,000
2008 General bond obligation with an original amount \$1,300,000 due in installments of \$20,000 to \$115,000 through July 1, 2032, with interest ranging from 1.53% to 7.50%	1,190,000
2008 Special obligation bond for operational debt payments with an original amount \$3,155,000 due in installments of \$40,000 to \$315,000 through July 1, 2032, with interest ranging from 1.53% to 6.50%	2,950,000
2008 Special obligation bond for operational debt payments with an original amount \$160,000 due in installments of \$2,300 to \$15,000 through July 1, 2032, with interest ranging from 1.53% to 7.25%	149,300
2009 General obligation bond for operational debts payment with an original amount of \$305,000 due in installments of \$5,000 to \$30,000, through July 1, 2034, with interest ranging from 4.75% to 7.50%	290,000
2011 Special obligation bond for operational debt payments with an original amount \$3,326,000 due in installments of \$300,000 to \$431,000 through July 1, 2035, with interest ranging from 6.00% to 6.50%	2,726,000
2012 General bond obligation with an original amount \$760,000 due in installments of \$25,000 to \$213,000 through July 1, 2021, with interest ranging from 6.00% to 7.00%	735,000
2013 General bond obligation with an original amount \$1,505,000 due in installments of \$20,000 to \$110,000 through July 1, 2037, with interest ranging of 6.00%	1,505,000
<b>Total general obligation bonds</b>	<b>\$ 17,767,300</b>

**10. LONG-TERM LIABILITIES (CONTINUED)**

These bonds and notes, except the 1998 Series \$ 3,310,000 bond, the 2003 Series \$680,000, the 2003 Series \$335,000 and \$190,000, and the 2009 Series \$305,000, are payable from the special ad valorem property tax of 4.00% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes. The before detailed bonds are payable with General Fund resources. The Series 2008 amounting \$3,155,000 and \$160,000, and 2011 Series \$3,326,000 are payable with the revenues generated from the collection of the .2% of the municipal sales and use tax imposed by the Municipality and collected by the Commonwealth of Puerto Rico Treasury Department.

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

Year Ending <u>June 30, 2013</u>	<u>Principal</u>	<u>Interest</u>
2014	\$ 1,024,200	\$ 466,176
2015	989,500	781,649
2016	884,000	723,912
2017	872,000	667,525
2018	914,000	610,500
2019-2023	3,949,600	2,502,631
2024-2028	4,328,000	1,531,029
2029-2033	2,970,000	594,371
2034-2038	1,836,000	82,313
<b>Total</b>	<b><u>\$ 17,767,300</u></b>	<b><u>\$ 7,960,106</u></b>

- C. Property Taxes Debts (Law No. 146 and Law No. 42)-** These amounts represents the balance owed to the Municipal Revenue Collection Center ("CRIM") at June 30, 2013 as described in Note 9.
- D. U.S. Department of Rural Development –** This amount represent the balance owed to the US Department of Rural Development related with federal funds appropriations made by the Municipality.
- E. Compensated absences-** The government-wide statement of net position includes approximately \$884,584 of accrued sick leave benefits, and approximately \$708,284 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.
- F. Post-closure care costs -** State and federal laws and regulations require the Municipality to place a final cover on its landfill site, when it stopped accepting waste, and perform certain maintenance and monitoring functions at the site for 30 years after closure. GASB statement No. 18 of "Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Costs," requires the Municipality to perform a study of the activities that need to be implemented at the Municipality's solid waste landfill facilities to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. The Municipality has not performed such a study but has recognized \$3,563,314 as an estimated current cost for landfill post-closure cares costs as of June 30, 2013. Actual costs may be different once a study has been made as per the required regulations and due to inflation, changes in technology, or changes in laws and regulations. The balance of post-closure costs is reported in the government-wide statement of net position.

## 10. LONG-TERM LIABILITIES (CONTINUED)

- G. Department of Labor repayment plans** – These amounts represent the balance owed to the Department of Labor related with unemployment compensation.
- H. Claims and judgments** – The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the General Fund when the liability is incurred.

## 11. PENSION PLAN

The Employee's Retirement System of the Commonwealth and its Instrumentalities (the Retirement System) is a cost-sharing multiple 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 Legislative Assembly of the Government of Puerto Rico. 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 completed ten years of creditable service are entitled to a deferred annuity benefit payable monthly for life.

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

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

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.

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). Employee's participation 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.

**11. PENSION PLAN (CONTINUED)**

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. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to 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 the 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 employer's contribution (9.275% of the employee's salary) will be used to fund the current plan. If at the time of retirement accumulated benefits amount to \$10,000 or less may elect to receive a lump sum distribution up to the accumulated benefits. Under the new program the retirement age is reduced from 65 to 60 for those employees who joined the current plan on or after April 1, 1990.

*Funding Policy*

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

Contribution requirements are established by law and are as follows:

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

*Annual Contribution*

The Municipality contributions during the year ended on June 30, 2013 are recognized as total pension expenditures/expenses in the category of administration as follows:

<u>Fiscal year</u>	<u>Law No. 447</u>	<u>System 2000</u>
2013	\$ 112,810	\$ 137,816

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

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2013, a copy of which can be obtained from the Retirement System, Minillas Station, PO Box 42003, San Juan, PR 00940-2003.

**12. RISK MANAGEMENT**

The Property Division, attached to the Municipality, is responsible of assuring that the Municipality's property is properly insured. Annually, the Property Division compiles the information of all property owned and its respective market value. After evaluating this information, the Property Division submits the data regarding the Municipality's properties to the Public Insurance Department at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities. Settled claims have not exceeded commercial coverage in any of the past three (3) fiscal years.

**13. COMMITMENTS AND CONTINGENCIES**

The Municipality has reported outstanding encumbrances amounting to \$68,025 in the General Fund at June 30, 2013. The Municipality intends to honor these encumbrances which will continue to be liquidate under the current year's budget during a lapse period that extends into the fiscal year.

**14. FUND BALANCE (DEFICIT)**

As of June 30, 2013, fund balance (deficit) is comprised of the following:

	General Fund	Capital Projects Fund –Local & State Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
<b>Restricted</b>					
General government	\$ -	\$ -	\$ -	\$ 1,041,902	\$ 1,041,902
Public safety					
Public works		1,365,276		38,790	1,404,066
Health and welfare				154,241	154,241
Culture and recreation				6,000	6,000
Economic development					
Community development					
Debt service			2,575,888		2,575,888
<b>Unassigned</b>	<u>(7,346,749)</u>				<u>(7,346,749)</u>
<b>Total fund balances (deficit)</b>	<u><u>\$(7,346,749)</u></u>	<u><u>\$ 1,365,276</u></u>	<u><u>\$ 2,575,888</u></u>	<u><u>\$ 1,240,933</u></u>	<u><u>\$ (2,164,652)</u></u>

## 15. FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

The GASB has issued the following statements that have effective dates after June 30, 2013:

- a. GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*). The requirements of this statement are effective for periods beginning after December 15, 2012.
- b. GASB Statement No. 66, *Technical corrections-2013 – an amendment of GASB Statements No. 10 and No.62*. The requirements of this statement are effective for periods beginning after December 15, 2012.
- c. GASB Statement No. 67, *Financial Reporting for Pension Plans-an amendment of GASB Statement No. 25*. The requirements of this statement are effective for periods beginning after June 15, 2013.
- d. GASB Statement No. 68 *Accounting and Financial Reporting for Pensions-an amendment of GASB Statement No. 27*. The requirements of this statement are effective for periods beginning after June 15, 2014.
- e. GASB Statement No. 69 *Government Combinations and Disposals of Government*. The requirements of this statement are effective for periods beginning after December 15, 2013. Early application is encouraged.
- f. GASB Statement No. 70 *Accounting and Financial Reporting for Non-exchange Financial Guarantees*. The provisions of this statement are effective for reporting beginning after June 15, 2013. Early application is encouraged.
- g. GASB Statement No. 71 *Pension transition for Contributions Made Subsequent to the Measurement Date-an amendment of GASB Statement No. 68*. The provision of this statement should be applied simultaneously with the provisions of Statement 68.

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

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16. PRIOR PERIOD ADJUSTMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

The following restatements have been made in the governmental fund financial statements, which are reported as an adjustment to the beginning fund balances:

Description	General Fund	Capital Projects Fund – Local & State Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Fund balance (deficit), beginning	\$ (4,074,908)	\$ 1,393,086	\$ 970,564	\$ 1,375,610	\$ (335,648)
<u>Correction of errors:</u>					
Overstatement of matured bonds and interest payable			1,303,780		1,303,780
Overstatement of due from other funds			(281,061)		(281,061)
Overstatement of accounts payable - P.R.E.P.A	1,927,000				1,927,000
Understatement of cash in General Fund	205,883				205,883
Understatement of cash bond unspent proceeds account	6,629				6,629
Overstatement of liabilities payable	2,421,147				2,421,147
Overstatement of accounts payable - DOL	100,426				100,426
Understatement of accounts receivable -GDB	46,719				46,719
Overstatement of accounts receivable - P.R.E.P.A	(1,903,043)				(1,903,043)
Understatement of accounts payable - P.R.A.S.A	(536,730)				(536,730)
Overstatement of cash in General Fund	(187,186)				(187,186)
Overstatement of cash in Special Revenue Fund	-	-	-	(227,133)	(227,133)
Fund balance (deficit), beginning, as restated	<u>\$ (1,994,063)</u>	<u>\$ 1,393,086</u>	<u>\$ 1,993,283</u>	<u>\$ 1,148,477</u>	<u>\$ 2,540,783</u>

B. GOVERNMENTAL WIDE FINANCIAL STATEMENTS

The following restatements have been made in the governmental wide financial statements, which are reported as an adjustment to the beginning net position:

Description	Governmental Activities
Net position - beginning	\$ 19,499,126
Correction of prior year payables and receivables	1,748,034
Net position - beginning, as restated	<u>\$ 21,247,160</u>

## 17. SUBSEQUENT EVENTS

### *Act. No 3 of April 4, 2013*

On April 4, 2013, the Governor of Puerto Rico signed into law Act No. 3 of 2013, which represents a comprehensive reform of the ERS. Act No. 3 became effective on July 1, 2013 and amends the provisions of the different benefits structures under the ERS, including, but not limited, to the following:

- For active participants of the contributory defined benefit programs under Act No. 447 of 1951 and Act No. 1 of 1990, all retirement benefits accrued through June 30, 2013 will be frozen, and thereafter, all future benefits will accrue under the defined contribution formula used for System 2000 participants, and will be paid at retirement through a lifetime annuity.
- Increases the minimum pension for current retirees from \$400 to \$500 per month.
- The retirement age for Act No. 447 participants will be gradually increased from age 58 to age 61.
- The retirement age for current System 2000 participants is increased gradually from age 60 to age 65.
- Eliminates the "merit annuity" available to participants who joined the ERS prior to April 1, 1990.
- The retirement age for new employees is increased to age 67, except for new state and municipal police officers, firefighters, and custody officers, which will be age 58.
- The employee contribution rate will increase from 8.275% to 10.275%.
- For System 2000 participants, the retirement benefits will no longer be paid as a lump sum distribution, instead, they will be paid through a lifetime annuity.
- Eliminates or reduces various retirement benefits previously granted by special laws, including Christmas and summer bonuses. The Christmas bonus payable to current retirees is reduced from \$600 to \$200 and is eliminated for future retirees. The summer bonus will be eliminated.
- Disability benefits will be eliminated and substituted for a mandatory disability insurance policy.
- Survivor benefits will be modified.

In addition, the Commonwealth has proposed incremental annual contributions from the General Fund of \$140 million per year, for the next 20 years, to increase the liquidity and solvency of the ERS. An appropriation for such annual contribution has been included in the Commonwealth's proposed budget for the fiscal year 2014.

Based on current census data, expectations of market conditions and other actuarial information provided by consulting actuaries, the changes instituted by Act No. 3, along with the additional annual contributions of \$140 million to be received from the Commonwealth during the next 20 years, will be sufficient to cover the System's current and future obligations.

## 17. SUBSEQUENT EVENT (CONTINUED)

The successful implementation of these measures cannot be assured, as it is dependent upon future events and circumstances whose outcome cannot be anticipated.

On June 30, 2013, the Commonwealth of Puerto Rico enacted Acts No. 40 through No. 48 (also known as the Comprehensive Tax Reform Acts), which amended the following Acts, Regulations and Codes: 1) the Puerto Rico Insurance Code under Act No. 77 of June 19, 1957, as amended, 2) the Property Tax Act under Act No. 83 of 1991, 3) the Savings and Loans Cooperatives Act under Act No. 255 of 2002, as amended, 4) the Puerto Rico Sales Tax Financing Corporation (COFINA) Act under Act No. 91 of 2006, 5) several articles of Act No. 1 of 2011 (also known as the Internal Revenue Code for a New Puerto Rico), 6) the Fiscal Reform Act of 2006 under Act No. 103 of 2006, 7) Act No. 164 of 2001, and 8) Act No. 221 of May 15, 1948. All these amendments are designed to achieve, among other things, an expansion of the revenue base of the general fund of the Commonwealth of Puerto Rico, and are expected to bring additional and consistent tax revenue. The aforementioned amendments involve, among other changes, the imposition of the sales and use taxes to certain business to business transactions, as defined, previously excluded, and other procedural changes (Acts No's. 40 and 42).

### **Act. No. 18 of 2014**

On January 24, 2014, was signed the Act No. 18 of 2014, to create the "Law of Municipal Administration Fund", to establish a special fund called the "Municipal Administration Fund", authorize municipalities to pledge the funds deposited in the Local Government Fund to which they are to secure the repayment of any loan, bond, note or other evidence of debt, whose repayment source are the funds deposited in the Special Fund and to meet any expenditure budget of the municipality and the municipality any activity or project, authorize the Government Development Bank for Puerto Rico to make disbursements for the purposes set out in this Act, amend paragraph (b) of Section 4020.01, amend paragraph (b) of Section 4020.02, and amend paragraph (a) and to repeal paragraph (e) of Section 6080.14 of the Act No. 1-2011, as amend, known as the "Internal Revenue Code for a New Puerto Rico", in order to restructure the sales and use tax so that the tax rate is six (6) percent state level and one (1) percent at the municipal level.

### **Act. No 19 of 2014**

On January, 24, 2014, the Commonwealth of Puerto Rico enacted Act No. 19 (also known as the Municipal Financing Corporation Act), to authorize the creation of a public corporation and instrumentality of the Commonwealth of Puerto Rico, attached to the Government Development Bank for Puerto Rico known as "Municipal Financing Corporation" (COFIM, by its acronyms in Spanish), with the power to issue and/or use other mechanisms to pay or refinance the debt incurred by the municipalities, whose payment of principal and interest is supported by municipal sales and use taxes; establish that the first collections of municipal sales and use tax of one percent (1%) will be collected by municipalities and deposited directly to the Redemption Fund of the Municipal Financing Corporation; establish that bonds and obligations issued by the "Municipal Financing Corporation" will be payable and secured by the pledge of the greater of (i) a fixed amount of the municipal sales and municipal tax or (ii) the amount of the municipal sales and use tax fixed at zero point three percent (0.3%) collected during the previous fiscal year; and amend the paragraph (c) of section 4050.06, amend paragraph (a) of section 4050.07, amend paragraph (a) and (b) of section 4050.08, amend paragraph (a) of section 4050.09, and amend paragraphs (b), (c) and (d), repeal paragraph (e) and renumber paragraph (f) as (e) of section 6080.14 of the Act 1-2011, as amended, known as the "Internal Revenue Code for a new Puerto Rico".

**18. ACCOUNTING RECORDS**

The accounting record of the Municipality of Yabucoa does not comply with the requirements established by the Public Act No. 81 of August 30, 1981 as amended, known as the Autonomous Municipalities Act of the Commonwealth of Puerto Rico. The records maintain related to assets and liabilities, revenues expenditures are not complete and accurate. The Municipality did not provide important information requested to perform our examination.

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF YABUCOA**

**Budgetary Comparison Schedule-  
General Fund  
For the Fiscal Year June 30, 2013**

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
<b>REVENUES:</b>				
Municipal license tax	\$4,699,100	\$4,699,100	\$2,766,849	\$ (1,932,251)
Municipal sales and use tax	1,000,000	1,000,000	853,402	(146,598)
Property taxes	2,231,749	2,231,749	2,231,750	1
Licenses, permits and other local taxes	1,920,720	1,920,720	279,437	(1,641,283)
Intergovernmental	8,284,701	8,284,701	8,291,528	6,827
Interest	304,801	304,801	157,199	(147,602)
Rent of Property	-	-	7,489	7,489
Miscellaneous	1,427,167	1,427,167	528,312	(898,855)
Fines and Forfeitures	20,000	20,000	2,939	(17,061)
<b>Total revenues</b>	<b>19,888,238</b>	<b>19,888,238</b>	<b>15,118,905</b>	<b>(4,769,333)</b>
<b>EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:</b>				
General government	11,821,314	11,930,683	11,588,012	342,671
Culture and recreation	493,155	598,535	477,615	120,920
Education	297,453	360,080	184,817	175,263
Health and welfare	2,462,254	2,374,266	1,145,327	1,228,939
Public safety	1,371,840	1,342,934	1,305,600	37,334
Public works	2,806,072	2,734,386	598,315	2,136,071
Operating transfer out and other funds	636,150	547,354	566,823	(19,469)
<b>Total expenditures, encumbrances and other financing uses</b>	<b>19,888,238</b>	<b>19,888,238</b>	<b>15,866,509</b>	<b>4,021,729</b>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (747,604)</b>	<b>\$ (747,604)</b>
<b>Explanation of Differences:</b>				
<b>Sources/inflows of resources:</b>				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$15,118,905
Differences-budget to GAAP:				
Non-budgeted transfer in				1,953,883
Long-term debt issued				1,505,000
GAAP adjustments to revenues				(962,325)
<b>Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances</b>				<b>\$17,615,463</b>
<b>Uses/outflows of resources:</b>				
Actual amounts (budgetary basis)"total charges to appropriations" from the budgetary comparison schedule				\$15,866,509
Differences-budget to GAAP:				
Non-budgeted expenditures				5,941,277
Prior year encumbrances recorded as current year expenditures for GAAP basis				766,559
Current year encumbrances recorded as expenditures for budgetary purposes				(68,025)
Non budgeted transfer out				461,829
<b>Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances</b>				<b>\$22,968,149</b>

See notes to the Budgetary Comparison Schedule-General Fund.

## 1. 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 USGAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2013 representing the Municipality's original budget. There were no supplemental appropriations for the year ended June 30, 2013.

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
<b>U.S DEPARTMENT OF AGRICULTURE</b>			
Direct Program:			
Child and Adult Care Food Program	10.558	N/A	\$ 8,669
<b>Total U.S. Department of Agriculture</b>			<b>8,669</b>
<b>U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>			
Direct Program:			
Section 8 Housing Choice Vouchers	14.871	N/A	680,730
Homeless Prevention and Rapid Re-Housing Program (HPRP) (Recovery Act Fund)	14.257	N/A	16,822
Pass-through the Commonwealth of Puerto Rico Office of Commissioner of Municipal Affairs:			
Community Development Block Grants – State's Program	14.228	Not Available	1,077,174
Pass-through the Commonwealth Municipality of San Juan			
Housing Opportunities for Persons with AIDS(HOPWA)	14.241	Not Available	1,781
<b>Total U.S. Department of Housing and Urban Development</b>			<b>1,776,507</b>
<b>U.S DEPARTMENT OF JUSTICE</b>			
Direct Program:			
Edward Byrne Memorial Program	16.738	N/A	46,289
Pass-through the Commonwealth of Puerto Rico Department of Justice:			
Edward Byrne Justice Assistance Grant (EBJAG) (Recovery Act Funded)	16.803	Not Available	75,000
<b>Total U.S. Department of Justice</b>			<b>121,289</b>

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
<b>U.S DEPARTMENT OF HUMAN SERVICES</b>			
Direct Program:			
Child Care and Development Block Grant	93.575	N/A	<u>243,022</u>
<b>Total U.S. Department of Human Services</b>			<u><b>243,022</b></u>
<b>U.S DEPARTMENT OF HOMELAND SECURITY</b>			
Direct Program:			
Disaster Grants – Public Assistance	97.036	N/A	<u>168,367</u>
<b>Total U.S. Department of Homeland Security</b>			<u><b>168,367</b></u>
<b>TOTAL EXPENDITURES OF FEDERAL AWARDS</b>			<u><b>\$ 2,317,854</b></u>

The accompanying notes are an integral part of this schedule.

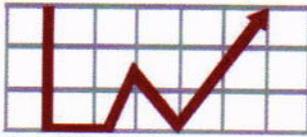
**1. BASIS OF PRESENTATION:**

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the **Municipality of Yabucoa** and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the fund financial statements. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

**2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:**

Expenditures of the federal awards as reported in the Statements of Revenues, Expenditures and Changes in Fund Balances – Governmental funds, are included within the Other Governmental Funds. The reconciliation between the expenditures in the basic financial statements and expenditures in the Schedule of Expenditures of Federal Awards is as follows:

Description	Other Governmental Funds	Total
Per Schedule of Expenditures of Federal Awards	\$ 2,317,854	\$ 2,317,854
Non-federal awards expenditures	2,889,116	2,889,116
<b>Total expenditures in the basic financial statements</b>	<b>\$ 5,206,970</b>	<b>\$ 5,206,970</b>



*López-Vega, CPA, PSC*

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

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

We were engaged to 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, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Yabucoa**, Puerto Rico, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated July 15, 2014.

**Internal Control over Financial Reporting**

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

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identify certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs as items **13-01** thru **13-05** to be material weaknesses.

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

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether **Municipality of Yabucoa's** financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items **13-06** thru **13-13**.

**Municipality of Yabucoa's Response to Findings**

**Municipality of Yabucoa's** response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. **Municipality of Yabucoa's** response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

**Purpose of this Report**

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

  
LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico  
July 15, 2014

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*López-Vega, CPA, PSC*

Certified Public Accountants / Management Advisors



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## INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

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

### Report on Compliance for Each Major Federal Program

We have audited **Municipality of Yabucoa's** compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of **Municipality of Yabucoa's** major federal programs for the year ended June 30, 2013. **Municipality of Yabucoa's** major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

### Management's Responsibility

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

### Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of **Municipality of Yabucoa's** major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about **Municipality of Yabucoa's** compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of **Municipality of Yabucoa's** compliance.

## INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133 (CONTINUED)

### **Basis for Qualified Opinion on Community Development Block Grants – State's Program and Section 8 Choice Voucher Program**

As described in 13-06 thru 13-12, in the accompanying schedule of findings and questioned costs, **Municipality of Yabucoa** did not comply with requirements regarding *cash management, davis bacon act, equipment and real property management, program income and reporting* that are applicable to Community Development Block Grants – State's Program (CFDA No. 14.228) in findings numbers 13-06 thru 13-10; with regarding *eligibility and reporting* that is applicable to Section 8 Housing Choice Voucher (CFDA No. 14.871) in finding numbers 13-11 and 13-12. Compliance with such requirements is necessary, in our opinion, for the **Municipality of Yabucoa** to comply with the requirements applicable to those programs.

### **Qualified Opinion on Community Development Block Grants – State's Program and Section 8 Choice Voucher Program**

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the **Municipality of Yabucoa** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on Community Development Block Grants – State's Program and Section 8 Housing Choice Voucher for the year ended June 30, 2013.

### **Other Matters**

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 13-06 and 13-13. Our opinion on each major federal program is not modified with respect to these matters.

**The Municipality of Yabucoa's** response to the noncompliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The **Municipality of Yabucoa's** response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

### **Report on Internal Control Over Compliance**

Management of **Municipality of Yabucoa** is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the **Municipality of Yabucoa's** internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of **Municipality of Yabucoa's** internal control over compliance.



*López-Vega, CPA, PSC*

Certified Public Accountants / Management Advisors

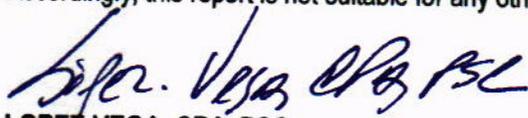
Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 13-07 and 13-08, 13-10 thru 13-12 to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned cost as items; 13-06, 13-09 and 13-13 to be significant deficiencies.

**Municipality of Yabucoa's** response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. **Municipality of Yabucoa's** response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

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

  
LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico  
July 15, 2014

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**Section I – Summary of Auditor’s Results**

**Financial Statements**

Type of auditor’s report issued:	<b>Disclaimer</b>	
Internal control over financial reporting:		
Material weakness identified?	Yes <input checked="" type="checkbox"/>	No
Significant deficiencies identified not considered to be material weaknesses?	Yes	None reported
Noncompliance material to financial statements noted?	Yes <input checked="" type="checkbox"/>	No

**Federal awards**

Internal Control over major programs:		
Material weakness identified?	Yes <input checked="" type="checkbox"/>	No
Significant deficiencies identified not considered to be material weaknesses?	Yes <input checked="" type="checkbox"/>	None reported

Type of auditor’s report issued on compliance for major programs: **Modified**

Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes <input checked="" type="checkbox"/>	No
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**Identification of major programs:**

CFDA Number	Name of Federal Program or Cluster
14.228	Community Development Block Grant – State’s Program
14.871	Section 8 Housing Choice Vouchers

Dollar threshold used to distinguish between Type A and Type B programs	<u>\$300,000</u>	
Auditee qualified as low-risk auditee?	Yes	No <input checked="" type="checkbox"/>

**Section II – Financial Statements Findings**

(All of the following findings are considered to be significant deficiencies. Those that are material weaknesses (MW) as labeled as such)

<b>Finding Reference</b>	<b>13-01</b>
<b>Requirement</b>	<b>Operating deficit of general fund (MW)</b>
<b>Statement of Condition</b>	The Municipality closed its fiscal year ended on June 30, 2013 with a fund balance deficiency in the general fund of \$7,346,749.
<b>Criteria</b>	Article 8.004(b) of the Municipalities Law established the Municipality cannot obligate or spend funds in excess of the ongoing fiscal year. No amount shall be expended or obligated in a given fiscal year in excess budgeted or authorized amounts by the Municipal Legislature.
<b>Cause of Condition</b>	The overstatement of estimated revenues accounts in prior years caused that the Municipality operated with a deficit.
<b>Effect of Condition</b>	The continued occurrence of this situation may result in possible significant fund limitations and eventual reduction or elimination of municipal services since future revenues will need to be used to pay for accumulated liabilities.
<b>Recommendation</b>	We recommended management to evaluate the adequacy of the provision for deficit reserve accounts in the next budget. Also, the Municipality's officers must evaluate the trend in the negative variance between budgeted revenues and actual revenues to reduce the budgeted expenditures by department (quarterly allocation process) and to avoid future operational deficits at year-end.
<b>Questioned Costs</b>	None
<b>Management Response and Corrective Action</b>	The Municipality have taken aggressive action to increase revenues and has implemented more efficient control over expenditures to reduce and, in a near future, eliminate the accumulated deficit and prevent future budget deficits.

Implementation Date: Still in process

Responsible Person: Mr. Pedro A. Crespo Ortiz,  
Finance Department Director

**Section II – Financial Statements Findings**

<b>Finding Reference</b>	<b>13-02</b>
<b>Requirement</b>	<b>Financial Reporting – Accounting Records (MW)</b>
<b>Statement of Condition</b>	During our examination of the Municipality's accounting system, we detected that the Municipality does not have adequate and effective internal controls to ensure that all the required financial and budgetary information was recognized and reported in the proper accounting period. Also, the accounting system does not summarize the transactions in a formal General Ledger in order to properly record and account for the transactions of all of its Governmental Funds (Local, State and Federal funds).
<b>Criteria</b>	Sections (a) and (b) of the Law, indicates that the accounting management system established in the Municipality should provide adequate and effective financial information for management decisions and in accordance with Accounting Principles General Accepted in the United States of America and established by Governmental Accounting Standard Board.
<b>Cause of Condition</b>	The Municipality did not establish effective internal control over the transactions recorded on its accounting records. Also, the accounting data is not summarized in the form of a double-entry general ledger record.
<b>Effect of Condition</b>	The Municipality's accounting system did not provide updated and complete financial information that present the financial position, the result of operations and the change in fund balances. Such information is necessary to take management decisions.
<b>Recommendation</b>	We recommend that the Municipality should implement the necessary internal controls and procedures in order to maintain an accounting system that contains information pertaining to authorizations, obligations, unobligated balances, assets, liabilities, expenditures, interfund transactions, etc.
<b>Questioned Cost</b>	None
<b>Management Response and Corrective Action</b>	<p>The Municipality will reevaluate the internal controls over financial reporting in order to improve their design and effectiveness. We will strengthen our accounting personnel's training in the proper recording of financial and budgetary transactions so the Municipality's manual records include all the required accounting data. Monthly monitoring and follow-up procedures will be enforced by the Finance Department to ensure that the new internal controls are correctly implemented.</p> <p>Implementation Date: August 1, 2014</p> <p>Responsible Persons: Mr. Pedro A. Crespo Ortiz Finance Department Director</p>

**Section II – Financial Statements Findings**

<b>Finding Reference</b>	<b>13-03</b>
<b>Requirement</b>	<b>Capital Assets and Expenditures – Subsidiary Ledger (MW)</b>
<b>Statement of Condition</b>	The Municipality has not maintained complete and adequate records in order to obtain sufficient, competent evidential matter with respect to the Capital Assets reported in governmental activities and, accordingly, the amount by which this departure would affect the assets, net position, and expenses of the governmental activities is not determinable.
<b>Criteria</b>	Chapter IX, Article 9.002 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain updated property accounting records. Also, the GASB Statement No. 34 requires that all capital assets, including infrastructure, must be presented in the Statement of Net Position and that these assets must be depreciated during its useful life.
<b>Cause of Condition</b>	Competent and sufficient evidential matter related to the capital assets was not available to support the value, completeness and ownership of these assets.
<b>Effect of Condition</b>	The Municipality's Government-Wide Financial Statements does not present fairly, the financial position of the governmental activities, and the change in financial position of the Municipality.
<b>Recommendation</b>	We recommend that the Municipality should continue the compilation of documents to support the value, completeness and ownership of its capital assets, necessary to comply with the requirements of the GASB Statement No. 34.
<b>Questioned Cost</b>	None
<b>Management Response and Corrective Action</b>	The Municipality's Finance Department staff plans to continue in their effort to update the capital assets subsidiary ledger, principally the infrastructure assets.
	Implementation Date: August 1, 2014
	Responsible Persons: Mr. Pedro A. Crespo Ortiz Finance Department Director

Section II – Financial Statements Findings

<b>Finding Reference</b>	<b>13-04</b>
<b>Requirement</b>	<b>Accounting Records – Municipal Solid Waste Landfill Post-closure Care and Maintenance Cost Determination (MW)</b>
<b>Statement of Condition</b>	The Municipality did not comply with the requirements established by GASB Statement No. 18, Accounting for Municipal Solid Waste Landfill Closure and Post-closure costs. At June 30, 2013, the accompanying statement of net position presents a liability for post-closure care cost of the Municipality's solid waste landfill of \$3,563,314. However, this estimate has not been made based on a study in conformity with the regulatory requirements established by the EPA "Solid Waste Disposal Facility Criteria".
<b>Criteria</b>	Regulations set forth by the US Environmental Protection Agency (EPA) "Solid Waste Disposal Facility Criteria," the Municipality is required to place a final cover on its solid waste landfill site when it stops accepting waste, and to perform certain maintenance and monitoring functions at the site for 30 years after closure. GASB 18 requires the Municipality to perform a study of the activities that need to be implemented at the Municipality's solid waste landfill facilities to guarantee the maximum yield of available space and to comply with applicable state and federal regulations.
<b>Cause of Condition</b>	The Municipality did not maintain and adequate control of the accountability of the post- closure care cost of its solid waste landfill. In addition, the Municipality did not perform the study required by EPA and GASB 18.
<b>Effect of Condition</b>	The Municipality is not in compliance with GASB 18 and the "Solid Waste Disposal Facility Criteria" issued by the US Environmental Protection Agency.
<b>Recommendation</b>	We recommend management to perform the study of the activities that need to be implemented at the Municipality's solid waste landfill facilities and determine the amount of the liability that should be reported in the governmental activities.
<b>Questioned Costs</b>	None
<b>Management Response and Corrective Action</b>	The Municipality's Management will perform the required study in order to record a reasonable estimate of the post-closure costs of its landfill facilities in order to include that liability in the fiscal year 2013-2014 government-wide financial statements.  Implementation Date: August 1, 2014  Responsible Person: Mr. Pedro Crespo Ortiz Finance Department Director

**Section II – Financial Statements Findings**

<b>Finding Reference</b>	<b>13-05</b>
<b>Requirement</b>	<b>Cash Receipts – Revenue, Receivable – Collections (MW)</b>
<b>Statement of Condition</b>	We performed a cash receipt test and examined a sample of twenty five (25) collections. In twenty five (25) cases, the Treasurer did not include adequate evidential documentation (customer's remittance data as excise tax determination documents, and customer notification letters, etc.) to support the collections receipts CR01 and CR02.
<b>Criteria</b>	The Section Four (4) of the Chapter three (3) of the Revised Regulation on Basic Standards for Municipalities of Puerto Rico establishes that the Official Treasurer should realize a daily revision of amount collected and amounts credited in bank accounts to assure that the revenues has been duly accounted and processed in the period of collection and in the correct fund.
<b>Cause of Condition</b>	Internal control procedures failed to assure that daily collections are duly accounted for and duly recorded in the correct fund.
<b>Effect of Condition</b>	The Municipality did not comply with regulations stated in The Section Four (4) of the Chapter three (3) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico.
<b>Recommendation</b>	The Municipality should establish an adequate evaluation of office space and document control should be made to safeguard important documentation about daily transactions and taxpayer's files.
<b>Questioned Costs</b>	None
<b>Management Response And Corrective Action</b>	The Finance Department Director will strengthen the internal controls over the Municipality's Collection Office to ensure that all the supporting documentation related to the daily collections is safeguarded in an accessible location.
	Implementation Date: August 1, 2014
	Responsible Person: Mr. Pedro A. Crespo Ortiz Finance Department Director

Section III – Federal Award Findings and Questioned Costs

Finding Reference	13-06
Program	Community Development Block Grant/State Grants (CFDA 14.228); U.S. Department of Housing and Urban Development; Pass-through – State - Office of Commissioner of Municipal Affairs.
Requirement	Cash Management
Statement of Condition	During our audit procedures, we examined a sample of nine (9) fund requisitions and identified two (2) cases in which the program did not pay its obligations in the time required by Federal Regulations.
Criteria	<p>24 CFR Subpart C, Section 85.20 (b) (7), <i>Cash management</i>. Procedures for minimizing the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by grantees and sub grantees must be followed whenever advance payment procedures are used. Grantees must establish reasonable procedures to ensure the receipt of reports on sub grantees' cash balances and cash disbursements in sufficient time to enable them to prepare complete and accurate cash transactions reports to the awarding agency.</p> <p>24 CFR Subpart I, Section 570.489 (c), <i>Federal grant payments – (1) Payment</i>. The state shall be paid in advance in accordance with Treasury Circular 1075 (31 CFR part 205). The State shall use procedures to minimize the time elapsing between the transfer of grant funds and disbursement of funds by the State to units of general local government. Units of general local government shall also use procedures to minimize the time elapsing between the transfer of funds by the State and disbursement for CDBG activities.</p>
Cause of Condition	The Municipality's disbursements procedures failed to assure that funds requested and received from grantor be disbursed in compliance with the Code of Federal Regulations Requirements. The above conditions are the result of inadequate cash forecasting procedures because the Municipality has requested and received federal funds in excess of its immediate needs.
Effect of Condition	The Municipality did not comply with the OMB Common Rules, Subpart C, Section 85.20, (b) (7).
Recommendation	We recommend that management should strengthen its procedures to minimize the time elapsed between the transfer of funds from the federal agency and the disbursements made by the Municipality. Also, the Municipality should modify the cash forecasting process by establishing a system to adequately forecast the cash needs for the next five days, as established by CDBG regulations. Federal funds should only be requested when they are going to be disbursed immediately after receipt, or within five (5) business days.

**Section III – Federal Award Findings and Questioned Costs**

**Finding Reference**            **13-06 (Continued)**

**Questioned Costs**            None

**Management Response  
And Corrective Action**

The Municipality has implemented additional internal controls to ensure that the disbursement voucher package, with all of the required supporting documentation, is prepared when the request of funds is submitted to the agency. This will allow that, once the funds are received and deposited, the disbursement checks will be issued within the required 5-day period.

**Implementation Date:**        August 1, 2014

**Responsible Person:**        Mr. Antonio Aponte Delgado  
Federal Program Director

**Section III – Federal Award Findings and Questioned Costs**

<b>Finding Reference</b>	<b>13-07</b>
<b>Program</b>	<b>Community Development Block Grant – State’s Program (CFDA No. 14.228) U.S. Department of Housing and Urban Development; Pass-through – State - Office of Commissioner of Municipal Affairs.</b>
<b>Requirement</b>	<b>Davis-Bacon Act (MW)</b>
<b>Statement of Condition</b>	<p>During our Davis-Bacon Act test, we evaluated the only construction contract active during fiscal year 2012-2013. The following will summarize the exceptions noted:</p> <ul style="list-style-type: none"><li>a) The contract did not contain the Davis Bacon Act clause.</li><li>b) The Municipality did not require the contractor to submit weekly payrolls.</li><li>c) We did not obtain evidence that the Municipality’s monitors certified the weekly payroll supplied by the contractors.</li><li>d) The Municipality did not apply adequate monitoring procedures to required on-site visits to monitor the classifications of workers and wage rates paid.</li><li>e) The contract did not contain provisions for payment of prevailing wage rate.</li></ul>
<b>Criteria</b>	Davis-Bacon Act, as amended DOL (40 USC 276a to 276a-7).
<b>Cause of Condition</b>	The Municipality’s controls and procedures failed to apply all monitoring system procedures developed to test applicable contractors with respect to payment of prevailing wages.
<b>Effect of Condition</b>	The Municipality is not in compliance with Davis-Bacon Act, as amended DOL (40 USC 276a to 276a-7).
<b>Recommendation</b>	<p>We recommend that the Municipality should establish defined procedures to monitor the enforcement of the Davis-Bacon Act’s regulation. Those procedures would include the following:</p> <ul style="list-style-type: none"><li>a) Include in the contract the Davis Bacon Act clause.</li><li>b) Require to the contractor to submit weekly payrolls and comply with prevailing wage rate.</li><li>c) On site visits;</li></ul>

**Section III – Federal Award Findings and Questioned Costs**

**Finding Reference**            **13-07 (Continued)**

- d) Obtain contractor's and subcontractor's weekly payrolls to be reviewed on a weekly basis to establish the degree of compliance and the nature and extend of violations, if any, and then, communicate contractors promptly about any failure in the payroll process.

**Questioned Costs**            None

**Management Response  
and Corrective Action**

The Office of the Commissioner of Municipal Affairs (OCAM) will provide the construction contract to the Municipal Secretary Office. The template will include the Davis Bacon Act clause that will be incorporated to all federal construction contracts. In addition, it was established that the Federal Programs Director, together with the Municipality's labor laws technician, will make the required on-site visits and reviews of the weekly payrolls.

Implementation Date:        August 28, 2014

Responsible Person:        Mr. Antonio Aponte Delgado  
Federal Program Director

**Section III – Major Federal Award Program Findings and Questioned Costs**

<b>Finding Reference</b>	<b>13-08</b>
<b>Program</b>	<b>Community Development Block Grant – State’s Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass-through State – Office of Commissioner of Municipal Affairs</b>
<b>Requirement</b>	<b>Equipment and Real Property Management (MW)</b>
<b>Statement of Condition</b>	<b>Section II – Financial Statements Findings – Finding Reference 13-03</b>

**Section III – Major Federal Award Program Findings and Questioned Costs**

<b>Finding Reference</b>	<b>13-09</b>
<b>Program</b>	<b>Community Development Block Grant – State’s Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass-through State – Office of Commissioner of Municipal Affairs</b>
<b>Requirement</b>	<b>Program Income</b>
<b>Statement of Condition</b>	During our audit of the program income requirements we noted that the Municipality submitted one of the reports after its due date.
<b>Criteria</b>	<p>Code of Federal Regulations 24, Subpart C, Part 85.20 (b) (2) states that the 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 grant or sub grant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.</p> <p>Code of Federal Regulations 24, Part 570.489 (e) (3) HUD requires vigorous state oversight of recovered funds retained at the local level. Community Development has the ultimate responsibility for the proper use of these funds and must ensure that Program Income is used in a manner consistent with requirements. For this reason, annual Program Income/Miscellaneous Revenue Reports are required. A grantee with the potential of generating recapture funds must submit a report for the fiscal year ending June 30.</p>
<b>Cause of Condition</b>	The Municipality did not maintain adequate internal controls in order to assure the proper determination, accounting and use of program income.
<b>Effect of Condition</b>	The Municipality is not in compliance with Code of Federal Regulations 24, Subpart C, Part 85.20 (b) (2), and Code of Federal Regulations 24, Part 570.489 (e) (3).
<b>Recommendation</b>	We recommend management to develop internal controls and procedures in order to assure that the handling of Program Income complies with federal and state requirements.
<b>Questioned Costs</b>	None
<b>Management Response and Corrective Action</b>	<p>The Municipality has established that the submission of these reports will be first done through email and subsequently delivered on hand by messenger in order to comply with the required deadlines.</p> <p>Implementation Date: August 1, 2014</p> <p>Responsible Person: Mr. Antonio Aponte Delgado Federal Program Director</p>

**Section III – Major Federal Award Program Findings and Questioned Costs**

<b>Finding Reference</b>	<b>13-10</b>
<b>Program</b>	<b>Community Development Block Grant – State’s Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass-through State – Office of Commissioner of Municipal Affairs</b>
<b>Requirement</b>	<b>Financial Reporting – Accounting Records (MW)</b>
<b>Statement of Condition</b>	<b>Section II – Financial Statements Findings – Finding Reference 13-02</b>

**Section III - Major Federal Award Program Findings and Questioned Costs**

<b>Finding Reference</b>	<b>13-11</b>
<b>Program</b>	<b>Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development</b>
<b>Requirement</b>	<b>Eligibility Test (MW)</b>
<b>Statement of Condition</b>	<p>During our Eligibility Test, we examined fifteen (15) participant's files and we found the following deficiencies:</p> <ul style="list-style-type: none"><li>a. EIV Income Report was not obtained for twelve (12) new admissions at the time of conducting the examination of the family income and compositions.</li><li>b. One (1) participant file the PHA did not documented the reasonable rent determination worksheet.</li></ul>
<b>Criteria</b>	<p>Code of Federal Regulations 24, Sections 5.609 established that as a condition of admission or continued occupancy, the tenant must provide all necessary information and documentation required and tenant's authorization to verify income eligibility. 24 CFR Subpart K Section 982.516 (a), established that PHA responsibility for reexamination of family income and composition at least annually, (2) the PHA must obtain and document in the tenant file third-party verification.</p> <p>Notice PIH 2010 - 19 (HA) established that for each new admission (form HUD-50058 action type 1), the PHA is required to do the following: i. Review the EIV Income Report to confirm/validate family-reported income within 120 days of the PIC submission date; and ii. Print and maintain a copy of the EIV Income Report in the tenant file; and iii. Resolve any income discrepancy with the family within 60 days of the EIV Income Report date.</p>
<b>Cause of Condition</b>	<p>The Program's officers did not obtain and complete the required documentation to validate the participant's eligibility. In addition, the Municipality has no effective monitoring review process for the program internal quality control.</p>
<b>Effect of Condition</b>	<p>The Program does not meet compliance with Code of Federal Regulations 24.</p>
<b>Recommendation</b>	<p>The Program should strengthen internal control procedures to monitor performance, ensure compliance with these requirements and train staff on documentation and verification process.</p>

**Section III - Major Federal Award Program Findings and Questioned Costs**

**Finding Reference**            **13-11 (Continued)**

**Questioned Costs**            None

**Management Response  
and Corrective Action**

The Municipality will strengthen its internal control over the management of the participant files in order to ensure that all the required documentation is included within the file. We will perform an internal audit of our participant files to verify that they include all the necessary information to evidence the participant's eligibility.

Implementation Date:    August 1, 2014

Responsible Person:    Mr. Antonio Aponte Delgado  
Federal Program Director

**Section III - Major Federal Award Program Findings and Questioned Costs**

<b>Finding Reference</b>	<b>13-12</b>
<b>Program</b>	<b>Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development</b>
<b>Requirement</b>	<b>Financial Reporting – Accounting Records (MW)</b>
<b>Statement of Condition</b>	<b>Section II – Financial Statements Findings – Finding Reference 13-02</b>

**Section III – Federal Award Findings and Questioned Costs**

<b>Finding Reference</b>	<b>13-13</b>
<b>Requirement</b>	<b>Single Audit Act</b>
<b>Statement of Condition</b>	The Single Audit Report for the fiscal year ended June 30, 2013, was not issued within nine (9) months after the end of the audit period.
<b>Criteria</b>	The Single Audit Act of 1984, as amended, require that the audit report must be submitted to the Federal Audit Clearinghouse no later than nine (9) months after the end of the audit period.
<b>Cause of Condition</b>	The Municipality did not comply with the established regulation as prescribed in OMB Circular A-133.
<b>Effect of Condition</b>	The Municipality could lose federal grants since the noncompliance with Act requirements.
<b>Recommendation</b>	Procedures should be implemented to ascertain that the Municipality complies with the established Federal Regulation, as prescribed by OMB Circular A-133.
<b>Questioned Costs</b>	None
<b>Management Response And Corrective Action</b>	We concur with this finding. The Municipality will establish a Financial Reporting Task Force composed of the management team of the Department of Finance and external consultants. We expect that the Single Audit reporting package for the fiscal year ended on June 30, 2014 will be completed on or before March 31, 2015.

Implementation Date: August 1, 2014

Responsible Person: Mr. Pedro A. Crespo Ortiz  
Finance Department Director

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)						
N/A	N/A	During the year ended June 30, 2012, no deficiencies, significant deficiencies, material weaknesses, or instance of noncompliance were detected related to the general purpose financial statements that were required to be reported in accordance with OMB Circular A-133.						
11-01	14.228	<p>The Municipality did not comply with the requirement of preparing and filling its federal financial reports on a timely basis. During our examination of the Federal Financial Reports. We noted that the Municipality did not send on time the quarterly report for the following period ended.</p> <table border="1" data-bbox="483 762 1279 840"> <thead> <tr> <th data-bbox="483 762 776 798"><u>Quarterly</u></th> <th data-bbox="776 762 1068 798"><u>Due/Date</u></th> <th data-bbox="1068 762 1279 798"><u>Date Submitted</u></th> </tr> </thead> <tbody> <tr> <td data-bbox="483 798 776 833">October-December</td> <td data-bbox="776 798 1068 833">January 30, 2011</td> <td data-bbox="1068 798 1279 833">February 11, 2011</td> </tr> </tbody> </table> <p>The corrective action was taken. Finding was cleared as of June 30, 2011.</p>	<u>Quarterly</u>	<u>Due/Date</u>	<u>Date Submitted</u>	October-December	January 30, 2011	February 11, 2011
<u>Quarterly</u>	<u>Due/Date</u>	<u>Date Submitted</u>						
October-December	January 30, 2011	February 11, 2011						
11-02	83.544	<p>The Municipality has not established effective cash management procedures. The following programs were reported with the same cash balances during the entire year: FEMA (Georges), FEMA (Rains), FEMA (Jeanne), FEMA (Dean) FEMA (October Rains)</p> <p>The corrective action was taken. Finding was cleared as of June 30, 2011.</p>						
11-03	83.544	<p>The Municipality transfer from the grant, mentioned, above the amount of \$332,118 to the Operating Account.</p> <p>The corrective action was taken. Finding was cleared as of June 30, 2011.</p>						