



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS**

Independent Auditors' Report

**Basic Financial Statements and
Supplemental Schedules**

Year Ended June 30, 2017

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS**

**FINANCIAL STATEMENTS AND SUPPLEMENTAL SCHEDULES
YEAR ENDED JUNE 30, 2017**

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS**

**FINANCIAL STATEMENTS AND SUPPLEMENTAL SCHEDULES
YEAR ENDED JUNE 30, 2017**

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INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and
Municipal Legislative Body
Municipality of Aguas Buenas
Aguas Buenas, Puerto Rico

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining funds information of the **Municipality of Aguas Buenas** (“the **Municipality**”), as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the **Municipality’s** basic financial statements as listed in the table of contents. We did not audit the financial statement of the Espiritu Santo Project, which represents 100% of total assets, net position and revenue of the business type activities.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the business type activities and the blended component unit. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Espiritu Santo Project, is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Basis for Qualified Opinion on Governmental Activities

The net pension liability and deferred outflows/inflows of resources in governmental activities of the government-wide statement of net position, and pension expense for the current period change in that liability in governmental activities of the government-wide statement of activities were derived from the application of the proportional share included in the unaudited financial statements, notes and required supplementary information of the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico, cost-sharing multiple-employer pension plan. We were unable to obtain sufficient appropriate audit evidence about the proportional share used to determine the deferred outflows/inflows of resources, net pension liability, and pension expenses of the governmental activities and the information disclosed in the notes of the pension plan. Consequently, we were unable to determine whether any adjustments to these amounts and disclosures were necessary. The net pension liability and deferred outflows/inflows of resources represent 65 percent of the total liabilities, 100 percent and 4% of deferred outflows/inflows of resources, respectively, as of June 30, 2017, while pension expense represents 6 percent of total expenses for the fiscal year then ended.

Qualified opinion on Governmental Activities

In our opinion, except for the effects of the matter described in the "Basis for Qualified Opinion on Governmental Activities" paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Governmental activities of the Municipality, as of June 30, 2017, and the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Qualified Opinion on Governmental Fund Financial Statements

We did not audit the financial statements of the Espiritu Santo Project which have been included in the Municipality's Statement of Net Position as of June 30, 2017. Accordingly, we are not able to satisfy ourselves as to the fairness of presentation of these financial statements.

Qualified opinions governmental fund financial statements

In our opinion, based on our audit and the report of other auditor, and except for the effect of the matter described in the "Basis for Qualified Opinion on governmental funds financial statements" paragraph, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the Municipality as of June 30, 2017, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Unmodified Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2017, and the respective changes in financial position and, where applicable, cash flows thereof for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America

Emphasis-of-Matter

Uncertainty about Ability to Continue as a Going Concern – Commonwealth of Puerto Rico

The Municipality is an instrumentality of the Commonwealth of Puerto Rico (“the Commonwealth”). The accompanying financial statements of the Municipality have been prepared assuming that the Commonwealth will continue as a going concern. Also, the Municipality received substantial funds and loans from the Commonwealth. As discussed in Note 12 to the basic financial statements, the Commonwealth’s recurring deficits, negative financial position, further deterioration of its economic condition, and inability to access the credit markets raises substantial doubt about the ability to continue as a going concern. Management’s plans regarding these matters are also described in Note 12. The financial statements of the Municipality do not include any adjustments that might result from the outcome of this uncertainty. Our opinions are not modified with respect to this matter.

Other Matters

Required Supplementary Information

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

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality’s basic financial statements. The accompanying Financial Data Schedules – Section 8 Housing Choice Vouchers Program, as required by U.S. Department of Housing and Urban Development, and the Schedule of Expenditures of Federal Awards, as required by Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Costs Principles, and Audit Requirements for Federal Award, is presented for purposes of additional analysis and is not required part of the basic financial statements.

The Financial Data Schedules – Section 8 Housing Choice Vouchers Program and the Schedule of Expenditures of Federal Awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America.

In our opinion, the Financial Data Schedules – Section 8 Housing Choice Vouchers Program and the Schedule of Expenditures of Federal Awards are fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated August 30, 2018, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Municipality's internal control over financial reporting and compliance.

Guzman Castro & Co., CPAs PSC
CERTIFIED PUBLIC ACCOUNTANTS
San Juan, Puerto Rico
August 30, 2018

Stamp # E358442 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the original of this report

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Municipality of Aguas Buenas (the "Municipality") discussion and analysis has been designed with the followings goals:

- a) Assist the reader in focusing on significant financial issues,
- b) Provide an overview of the Municipality's financial activity,
- c) Identify changes in the Municipality's financial position (its ability to address the next and subsequent year challenges),
- d) Identify any material deviations from the financial plan (the approved budget), and;
- e) Identify individual fund issues or concerns.

Since the Management's Discussion and Analysis (MD&A) is designed to focus on the current year activities, resulting changes and currently known facts, please read it in conjunction with the Municipality's financial statements.

FINANCIAL HIGHLIGHTS

- The Municipality net position decreased by \$1,731,889.
- Net position amounts to \$5,380,922.
- Capital expenditures amounted to \$470,793.
- General fund deficit decreased by \$767,823.

USING THIS ANNUAL REPORT

This annual report consists of a series of new financial statements with a change in the focus from previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

Government-Wide Financial Statements

The Government-Wide Financial Statements are designed to provide users of the financial statements with a broad overview of the Municipality's finances in a manner similar to private-sector companies.

The Statement of Net Position presents information on all of the Municipality's assets and liabilities, with the difference between both reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

The Statement of Activities presents information showing how the Municipality's net assets changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the Statement of Activities that will only result in cash flows in future fiscal periods. The Statement of Activities is focused on both the gross and net cost of various activities, which are provided by the government's general tax and other revenues. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

Fund Financial Statements

The Fund Financial Statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only one kind of fund which is the governmental fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government Wide Financial Statements. However, unlike the Government Wide Financial Statements, Government Fund Financial Statements focus on near term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

Because the focus of governmental funds is narrower than that of the government wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government wide financial statements. By doing so, users of the basic financial statements may better understand the long-term impact of the Municipality's near term financial decisions. Both of the Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Infrastructure Assets

Historically, a government's largest group of assets (infrastructure – roads, bridges, traffic signals, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in government financial statements. GASB 34 requires that these assets be valued and reported within the governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the modified approach) which periodically (at least every third year), by category, measures and demonstrates its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statement users in evaluating a local government and its performance over time. The Municipality has elected to depreciate infrastructure assets instead of using the modified approach.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Position

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. The Municipality's net position totaled \$68.1 and \$69.6 million at the end of 2017 and 2015, respectively.

The largest portion of the Municipality's net assets consists of the investment made throughout the years in capital assets such as land, buildings, equipment and infrastructure. The Municipality uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although, the Municipality's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from the Debt Service Fund, since the capital assets themselves cannot be used to liquidate these liabilities. The amounts restricted for debt service represents another portion of the net assets, and these are resources subject to external restrictions for the purposes explained above.

**Condensed Statement of Net Position
June 30, 2017 and 2016**

	<u>2017</u>	<u>2016</u>
Current assets	\$ 3,211,596	\$ 7,234,046
Capital assets	28,932,773	29,576,233
Deferred outflow of resources	<u>816,694</u>	<u>816,694</u>
Total assets	<u>32,961,063</u>	<u>37,626,973</u>
Current liabilities	1,436,547	3,544,650
Deferred inflows of resources	653,101	663,430
Noncurrent liabilities	<u>28,088,444</u>	<u>26,306,082</u>
Total liabilities	<u>30,178,092</u>	<u>30,514,162</u>
Invested in capital assets, net of related debt	21,701,727	22,713,972
Restricted	3,828,056	4,638,457
Unrestricted	<u>(20,677,478)</u>	<u>(20,239,618)</u>
Total net position	<u>\$ 4,852,305</u>	<u>\$ 7,112,811</u>

Changes in Net Position

The Municipality's net position decreased by \$1,731,889. Approximately 71 percent of the Municipality's total revenue came from grants and contributions, including federal aid, while 19 percent resulted from taxes. The Municipality's expenses cover a range of services. The largest expenses were for general government, public works and public housing and welfare.

**Condensed Statement of Activities
June 30, 2017 and 2016**

	2017	2016
Program revenues		
Charges for services	\$ 464,246	\$ 427,862
Operating grants and contributions	1,910,324	2,609,161
Capital grants and contributions	-	1,658,677
General revenues		
Property taxes	2,138,136	2,686,827
Municipal license tax	656,401	633,871
Sales and use taxes	1,225,831	1,097,866
Grants and contributions not restricted to specific programs	8,802,448	6,329,876
Interest and investment earnings	19,010	79,841
Miscellaneous	210,996	258,625
Total revenues	15,427,392	15,782,606
Expenses		
General government	8,579,117	4,103,215
Public safety	338,344	717,891
Health and welfare	2,310,031	2,716,615
Public works	2,388,000	5,039,108
Culture and recreation	877,332	464,012
Community development	370,042	458,707
Economic Development	152,659	381,674
Education	1,103,806	2,251,339
Interest on long-term debt	1,039,950	353,539
Total expenses	17,159,281	16,486,100
Change in net position	(1,731,889)	(703,494)
Net position, beginning of year	7,112,811	7,816,305
Net position, end of year	\$ 5,380,922	\$ 7,112,811

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 a combined fund balance of \$3.4 million compared to a fund balance of \$3.7 million in the prior year.

The general fund is included within the governmental funds; it is the chief operating fund of the Municipality. As of June 30, 2017, the general fund has a deficit of \$.4 million. The fund deficit decreased by \$.8 million during fiscal year 2017.

GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the Municipality Council revised the Municipality's budget to reclassify certain expenditures among the different governmental functions. Such reclassifications were necessary to provide for the developments that affected the Municipality's finances.

Actual revenues and expenditures were mostly on line with budgeted amounts except for general government expenditures which were \$1.6 million lower than budgeted due to fiscal control measures established by the current major.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2017, amounts to \$51.2 million, net of accumulated depreciation of \$22.3 million, leaving a net book value of \$28.9 million. This investment in capital assets includes land, buildings, improvements, equipment, intangibles, infrastructure and construction in progress. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The total decrease in the Municipality's investment in capital assets for the current fiscal year was about 2.18% in terms of net book value. Actual expenditures to purchase or construct capital assets were \$.5 million for the year. Depreciation charges for the year totaled \$1.1 million.

The Municipality finances a significant portion of its construction activities through bond issuances. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2017, the Municipality has approximately \$1.8 million of unexpended proceeds from grants and bonds that are committed to future construction activities.

Debt Administration

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

The 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." Act No. 64 provides that a municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Redemption Fund and the annual amounts collected with respect to such municipality's Special Additional Tax (as defined below), as projected by GDB, will be sufficient to service

to maturity the municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of 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. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal grant revenues may vary if new grants are available but the revenue also is very predictable.

Those factors were considered when preparing the Municipality's budget for the 2017-2018 fiscal year.

FINANCIAL CONTACT

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
Statement of Net Position
June 30, 2017

ASSETS	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
Cash	\$ 3,118,536	\$ 93,060	\$ 3,211,596
Cash with fiscal agent	2,048,329	-	2,048,329
Intergovernmental receivable	435,411	-	435,411
Other assets	-	43,672	43,672
Restricted cash	-	204,967	204,967
Capital assets	28,611,427	321,346	28,932,773
Total assets	<u>\$ 34,213,703</u>	<u>\$ 663,045</u>	<u>\$ 34,876,748</u>
 DEFERRED OUTFLOWS OF RESOURCES			
Contribution to employee's plan	<u>\$ 816,694</u>	<u>\$ -</u>	<u>\$ 816,694</u>
 LIABILITIES			
Accounts payable and accrued liabilities	\$ 970,278	\$ 14,413	\$ 984,691
Due to other governmental agencies	341,269	-	341,269
Claims and assessments	125,000	-	125,000
Noncurrent liabilities:			
Due within one year	352,911	78,405	431,316
Due in more than one year	27,735,533	41,610	27,777,143
Total liabilities	<u>\$ 29,524,991</u>	<u>\$ 134,428</u>	<u>\$ 29,659,419</u>
 DEFERRED INFLOWS OF RESOURCES			
Deferred revenues:			
Municipal license tax	\$ 514,461	\$ -	\$ -
Unamortized investment employee's retirement plan	138,640	-	138,640
Total deferred inflows of resources	<u>\$ 653,101</u>	<u>\$ -</u>	<u>\$ 138,640</u>
 NET POSITION			
Invested in capital assets, net of related debt	\$ 21,701,727	\$ -	\$ 21,701,727
Restricted:			
Capital projects	1,779,727	-	1,779,727
Debt service	2,048,329	-	2,048,329
Net position (Deficit)	(20,677,478)	528,617	(20,148,861)
Total net position	<u>\$ 4,852,305</u>	<u>\$ 528,617</u>	<u>\$ 5,380,922</u>

See notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
Statement of Activities
For the year ended June 30, 2017

Functions/programs	Expenses	Program Revenues			Net (expenses) revenues and changes in net position		
		Charges for Services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Business-type activities	Total
Governmental Activities:							
General government	\$ 8,579,117	\$ 110,388	\$ -	\$ -	\$ (8,468,729)	\$ -	(8,468,729)
Public safety	338,344	-	-	-	(338,344)	-	(338,344)
Health and welfare	2,019,238	-	1,910,324	-	(108,914)	-	(108,914)
Public works	2,388,000	-	-	-	(2,388,000)	-	(2,388,000)
Culture and recreation	877,332	-	-	-	(877,332)	-	(877,332)
Community development	370,042	-	-	-	(370,042)	-	(370,042)
Economic Development	152,659	-	-	-	(152,659)	-	(152,659)
Education	1,103,806	-	-	-	(1,103,806)	-	(1,103,806)
Interest on long-term debt	1,033,555	-	-	-	(1,033,555)	-	(1,033,555)
Total governmental activities	\$ 16,862,093	\$ 110,388	\$ 1,910,324	\$ -	\$ (14,841,381)	\$ -	(14,841,381)
Business-type activities:							
Housing	290,793	353,858	-	-	-	63,065	63,065
Interest	6,395	-	-	-	-	(6,395)	(6,395)
Total business-type activities	297,188	353,858	-	-	-	56,670	56,670
Total functions/programs	\$ 17,159,281	\$ 464,246	\$ 1,910,324	\$ -			
General revenues:							
Property taxes					\$ 2,138,136	\$ -	\$ 2,138,136
Municipal license tax					656,401	-	656,401
Sales tax					1,225,831	-	1,225,831
Grants and contributions not restricted to specific programs					8,802,448	-	8,802,448
Interest, fines and penalties					14,729	4,281	19,010
Miscellaneous					210,996	-	210,996
Total general revenues					13,048,541	4,281	13,052,822
Change in net position					(1,792,840)	60,951	(1,731,889)
Net position at beginning of year					6,645,145	467,666	7,112,811
Net position at end of year					\$ 4,852,305	\$ 528,617	\$ 5,380,922

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
Balance Sheet
June 30, 2017

	General Fund	Debt Service	Capital Projects	Total
ASSETS				
Cash and cash equivalents	\$ 607,389	\$ -	\$ 2,511,147	\$ 3,118,536
Cash with fiscal agent	-	2,048,329	-	2,048,329
Intergovernmental receivable	141,759	68,719	224,933	435,411
Due from other funds	290,750	-	-	290,750
Total assets	\$ 1,039,898	\$ 2,117,048	\$ 2,736,080	\$ 5,893,026

LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCES

LIABILITIES

Accounts payable and accrued liabilities	\$ 538,639	\$ -	\$ 431,639	\$ 970,278
Due to other governmental units	107,305	-	233,964	341,269
Claims and assessments	125,000	-	-	125,000
Due to other funds	-	-	290,750	290,750
Total liabilities	770,944	-	956,353	1,727,297

DEFERRED INFLOWS OF RESOURCES

Unearned revenues:				
Municipal license tax	514,461	-	-	514,461
Property taxes	141,759	68,719	-	210,478
Total deferred inflows of resources	656,220	68,719	-	724,939

FUND BALANCES

Restricted	-	2,048,329	1,779,727	3,828,056
Unassigned	(387,266)	-	-	(387,266)
Total fund balances	(387,266)	2,048,329	1,779,727	3,440,790
Total liabilities, deferred inflows of resources and fund balances	\$ 1,039,898	\$ 2,117,048	\$ 2,736,080	\$ 5,893,026

Fund Balance Governmental Funds 3,440,790

Capital assets used in governmental activities are not financial resources and therefore not reported in the governmental funds. 28,611,427

Deferred contribution to employee's plan 816,694

Unamortized investment employee's retirement plan (138,640)

Deferred property tax 210,478

Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore not reported in the governmental funds. (28,088,444)

Net position **\$ 4,852,305**

See notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
Statement of Revenues, Expenditures and Changes in Fund Balances
For the year ended June 30, 2017

	General Fund	Debt Service	Other Governmental Funds	Total
REVENUES:				
Property taxes	\$ 1,722,358	\$ 1,140,846	\$ -	\$ 2,863,204
Municipal license tax	656,401	-	-	656,401
Sales tax	-	184,746	1,041,085	1,225,831
Licenses, permits and other local taxes	73,663	-	-	73,663
Charges for services	110,388	-	-	110,388
Interest, fines and penalties	14,729	-	-	14,729
Intergovernmental:				
Federal	-	-	1,874,587	1,874,587
Local	5,639,900	-	3,124,622	8,764,522
Other	221,329	-	(10,333)	210,996
Total revenues	8,438,768	1,325,592	6,029,961	15,794,321
EXPENDITURES:				
Current:				
General government	4,105,572	-	3,272,455	7,378,027
Public safety	338,344	-	-	338,344
Health and welfare	-	-	2,019,238	2,019,238
Public works	1,979,914	-	-	1,979,914
Culture and recreation	724,414	-	11,727	736,141
Community development	370,042	-	-	370,042
Urban development	152,659	-	-	152,659
Education	-	-	1,103,806	1,103,806
Capital outlays	-	-	470,793	470,793
Debt service:				
Principal	-	332,211	-	332,211
Interest	-	1,210,615	-	1,210,615
Total expenditures	7,670,945	1,542,826	6,878,019	16,091,790
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	767,823	(217,234)	(848,058)	(297,469)
OTHER FINANCING SOURCES (USES):				
Operating transfers from other funds	-	-	531,348	531,348
Operating transfers to other funds	-	(531,348)	-	(531,348)
Total other financing sources (uses)	-	(531,348)	531,348	-
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES AND OTHER FINANCING SOURCES (USES)	767,823	(748,582)	(316,710)	(297,469)
FUND BALANCES, at beginning of year	(1,155,089)	2,796,911	2,096,437	3,738,259
FUND BALANCES, at end of year	\$ (387,266)	\$ 2,048,329	\$ 1,779,727	\$ 3,440,790
Net change in fund balance governmental funds				\$ (297,469)
Amounts reported for governmental activities in the statement of activities are different because:				
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of these assets is depreciated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlays in the current period.				(602,924)
Revenues in the governmental funds previously recognized as revenues in the statement of activities				(935,546)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the governmental funds				210,478
Interest reconized in the governmental funds previously recognized in the statement of activities				177,060
The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. This amount is the net effect of these differences in the treatment of long-term debt and related items.				(344,439)
Change in net position				\$ (1,792,840)

See notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
STATEMENT OF FINANCIAL POSITION - PROPRIETARY FUNDS
JUNE 30, 2017**

ASSETS

Current Assets:

Cash	\$ 93,060
Other Current assets	43,672
Total current assets	<u>136,732</u>
Property and equipment	321,346
Restricted deposits	204,967
Other assets	<u>-</u>
Total	<u><u>\$ 663,045</u></u>

LIABILITIES AND NET POSITION

Liabilities:

Current liabilities:	
Current maturities of mortgage note	\$ 78,405
Accounts payable and accrued expenses	14,413
Total current liabilities	<u>92,818</u>
Long term debt, net of current maturities	<u>41,610</u>
Total liabilities	134,428
Net position:	<u>528,617</u>
Total	<u><u>\$ 663,045</u></u>

See notes to basic financial statements

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
STATEMENT OF ACTIVITIES - PROPRIETARY FUNDS
JUNE 30, 2017**

Revenues:	
Rent	\$ 353,858
Financial	4,281
	<hr/>
Total revenues	358,139
	<hr/>
Expenses:	
Administrative	113,520
Utilities	6,313
Operating Maintenance	79,355
Taxes and Insurance	29,655
Depreciation	61,950
Interest	6,395
	<hr/>
Total expenses	297,188
	<hr/>
Change in net position	60,951
Net position, beginning of year	403,244
	<hr/>
Net position, end of year	\$ 464,195
	<hr/> <hr/>

See notes to basic financial statements

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS
JUNE 30, 2017**

Cash flows from operating activities:	
Cash received	
Rentals	\$ 352,936
Other operating received	4,105
Interest received	176
Total cash received	<u>357,217</u>
Cash used	
Administrative	(46,249)
Utilities	(12,067)
Salaries and wages	(117,429)
Operating and maintenance	(24,575)
Property and liability insurance	(5,277)
Interest on mortgage	(7,324)
Management fees	(28,050)
Total cash used	<u>(240,971)</u>
Net cash provided by operating activities	<u>116,246</u>
Cash flows from investing activities:	
Purchase of property and equipment	(21,414)
Deductions from reserve for replacements and interest	(47,484)
Net cash used by investing activities	<u>(68,898)</u>
Cash flows from financing activities	
Mortgage principal payments	<u>(72,396)</u>
Net increase in cash	(25,048)
Cash at beginning of the year	<u>118,108</u>
Cash at end of the year	<u>\$ 93,060</u>

See notes to basic financial statements

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS
JUNE 30, 2017**

Reconciliation of change in net position to net cash provided by operating activities:

Cash flows from operating activities:

Change in net position	<u>\$ 64,422</u>
Adjustments to reconcile change in net position to net cash provided by operating activities:	
Depreciation	62,864
Decrease in accounts receivable	22,593
Increase (decrease) in:	
Accounts payable	(1,265)
Accrued vacations and bonus	<u>405</u>
Total adjustments	<u>84,597</u>
Net cash provided by operating activities	<u><u>\$ 149,019</u></u>

See notes to basic financial statements

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS**

**Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2017**

1. Reporting Entity

The **Municipality of Aguas Buenas** (the Municipality) of the Commonwealth of Puerto Rico is a local government constituted in 1838 with full legislative, fiscal and administrative powers to operate as a 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 legislative power of the Municipality is exercised by the Municipal Legislature, whose members are also elected every four years. The judiciary power is exercised by the General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality.

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

2. Basis of Presentation and Summary of Significant Accounting Policies

The accounting and reporting policies of the Municipality conform to accounting principles generally accepted in the United States of America (U.S. GAAP), as applicable to governmental entities. The Municipality follows Governmental Accounting Standards Board (GASB) pronouncements under the hierarchy established by GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, in the preparation of its financial statements.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses/expenditures during the reported period. Actual results could differ from those estimates.

Government-Wide and Fund Financial Statements

Government-Wide Financial Statements — The statement of Net position and the statement of activities report information on all activities of the Municipality. The effect of interfund balances has been removed from the government-wide statement of Net position (deficiency), except for the residual amounts due between governmental and business-type activities. Interfund charges for services among functions of the government-wide statement of activities have not been eliminated. The Municipality's activities are distinguished between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods

or services or interest earned on investment securities. Following is a description of the Municipality's government-wide financial statements.

The statement of net position presents the Municipality's assets and liabilities, with the difference reported as Net position. Net position is reported in three categories:

- Invested in capital assets, net of related debt, consist of capital assets, net of accumulated depreciation and amortization, and reduced by outstanding balances of bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets, if any.
- Restricted net position result when constraints placed on Net position use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- Unrestricted net position consists of Net position that does not meet the definition of the two preceding categories. Unrestricted Net position often is designated, in order to indicate that management does not consider them to be available for general operations. Unrestricted Net position often has constraints on use that are imposed by management, but such constraints may be removed or modified.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function. Program revenues include (1) interest income on loans and investments, changes in the fair value of investments, and fees and charges to customers for services rendered or for privileges provided and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Other items not meeting the definition of program revenues are reported as general revenues.

Fund Financial Statements — Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts. The financial activities of the Municipality that are reported in the accompanying basic financial statements have been classified into governmental and enterprise funds.

Separate financial statements are provided for governmental funds and enterprise funds. Major individual governmental and enterprise funds are reported as separate columns in the fund financial statements, with non-major funds being combined into a single column.

Fund balances for each governmental fund are displayed in the following classifications depicting the relative strength of the spending constraints placed on the purposes for which resources can be used:

- Nonexpendable — amounts that cannot be spent because they are not in a spendable form (such as inventories and prepaid amounts) or are legally or contractually required to be maintained intact.
- Restricted — amounts that can be spent only for specific purposes because of constraints imposed by external providers (such as grantors, bondholders, and higher levels of government), or imposed by constitutional provisions or enabling legislation.
- Committed — amounts that can be spent only for specific purposes determined by a formal action of the government's highest level of decision-making Municipality.
- Assigned — amounts the government intends to use for specific purposes that do not meet the criteria to be classified as restricted or committed.

- Unassigned — amounts that are available for any purpose.

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

Measurement Focus, Basis of Accounting, and Financial Statements Presentation

Government-Wide Financial Statements — The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met.

Governmental Funds Financial Statements — The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Municipality considers revenues to be available if they are collected within 120 days after the end of the fiscal year. Principal revenue sources considered susceptible to accrual include federal and Commonwealth funds to be received. Other revenues are considered to be measurable and available only when cash is received. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

Modifications to the accrual basis of accounting include:

- Interest on general long-term obligations is generally recognized when paid.
- Debt service principal expenditures and claims and judgments are recorded only when payment is due.

For financial reporting purposes, the Municipality classifies its governmental funds within the following categories:

General fund - The general fund is the Municipality's main operating fund and a major governmental fund, as defined below, used to account for all financial resources and governmental activities, except for financial resources 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) GAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund.

Debt service fund - The debt service fund is a major governmental fund, as defined below, used by the Municipality to account for the accumulation of resources 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/or (2) bonds payable or any general long-term debt for which the Municipality is being accumulating financial resources in advance to pay principal and interest payments maturing in future years. Consistently with the prior fiscal years' financial statement presentation, during the fiscal year ended June 30, 2017, the financial activity accounted for in the debt service fund was specifically related to bonds payable.

Special revenue funds - Special revenue funds are governmental funds, as defined below, used by the

Municipality to account for revenues derived from grants, contributions or other revenue sources that are either self-restricted by the Municipality or legally restricted by outside parties for use in specific purposes. The uses and limitations of each special revenue fund are specified by municipal ordinances or federal and state statutes. However, resources restricted to expenditures for purposes normally financed from the general fund are reported in the Municipality's general fund provided that all applicable legal requirements are appropriately satisfied. In this case, a special revenue fund to account for such kind of transactions will be used only if legally mandated.

Capital projects funds - Capital projects funds are governmental funds, used to account for the financial resources used for the acquisition, construction or improvement of major capital facilities and other assets. Significant capital outlays financed from proceeds of general obligation, public improvement or special obligation bonds accounted for in the capital projects funds.

The use of the capital projects funds has been reserved only for major 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 focus of the GFFS is on major governmental funds, which generally represent the Municipality's most important funds. Accordingly, the Municipality is required to segregate governmental funds between major and non-major categories within the GFFS. Major individual governmental funds are reported individually as separate columns in the GFFS, while data from all non-major governmental funds are aggregated into a single column, regardless of fund type.

By definition, the Municipality's general fund is considered a major governmental fund for financial reporting purposes. In addition, any other governmental fund would be classified as a major governmental fund in the GFFS if its total assets, liabilities, revenues or expenditures of that individual governmental fund are at least 10 percent of the corresponding element total (assets, liabilities, revenues or expenditures) for all governmental funds. For the purposes of applying the aforementioned major fund criteria, no eliminations of interfund balances have been made. Total revenues for these purposes means all revenues, including operating and non-operating revenues (net of allowances for uncollectible accounts), except for other financing sources. Total expenditures for these purposes mean all expenditures, including operating and non-operating expenditures, except for other financing uses.

Based on the aforementioned criteria, the Municipality's major governmental funds reported in the accompanying GFFS are: (1) the general fund, (2) the special revenue state and federal grants fund, and (3) the capital projects fund.

The Municipality periodically undertakes a comprehensive evaluation of its fund structure to ensure that 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 Municipality in the day-to-day accounting procedures have not been reported as individual governmental funds in the accompanying fund financial statements.

The accompanying GFFS are accompanied by the following schedules required by GAAP: (1) the reconciliation of the balance sheet - governmental funds to the statement of net position, and (2) the reconciliation of the statement of revenues, expenditures and changes in fund balances - governmental funds to the statement of activities.

Budgetary Control

The Mayor and its Administrative Cabinet prepare annual budgets each fiscal year for the Municipality's general fund and debt service fund. Such legally adopted budgets are based on expected expenditures by program and estimated resources by source. The annual budgets are developed using elements of performance-based program budgeting and zero-based budgeting, and include estimates of revenues and other resources for the ensuing fiscal year under laws and regulations existing at the time the budgets are prepared.

The Mayor must submit for the fiscal year commencing on the next July 1, an annual budgetary resolution project (the Project) to the Commissioner of Municipal Affairs of the Commonwealth (the Commissioner) and the Municipal Legislature no later than May 10 and May 15, respectively. The Commissioner preliminarily verifies that the Project complies with all the applicable laws and regulations and may provide comments and suggestions to the Mayor on or before June 30.

The Municipal Legislature has 10 business days, up to the immediately preceding June 30, to discuss and approve the Project with modifications. The Municipal Legislature may amend the budgets submitted by the Mayor but may not increase any items so far to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. After the Municipal Legislature modifies and preliminarily approves the Project, the modified Project is sent back to the Mayor for his approval or rejection within 6 days. The Mayor may decrease or eliminate any line item but may not increase or insert any new line item in the budgets. The Mayor may also veto the budgets in their entirety and return it to the Municipal Legislature with his objections. If the Mayor rejects the Project, the Municipal Legislature will have up to 8 days to adopt or reject the recommendations or objections of the Mayor. The approved Project is sent again to the Mayor, which then would have 3 days to sign and approve it.

If the budgets are not adopted prior to the end of the deadlines referred to above, the annual budgets for the preceding fiscal year, as approved by the Legislature and the Mayor, are automatically renewed for the ensuing fiscal year until the Municipal Legislature and the Mayor approve new budgets. This permits the Municipality to continue doing payments for its operations and other purposes until the new budgets are approved.

The annual budgets may be updated for any estimate revisions as well as fiscal year-end encumbrances, and may include any additional information requested by the Municipal Legislature. The Mayor may request subsequent amendments to the approved budgets, which are subject to the approval of the Municipal Legislature.

The Municipality's Department of Finance has the responsibility to ensure that budgetary spending control is maintained. For day-to-day management control purposes, expenditures plus encumbrances may not exceed budgeted amounts at the expenditure-type level of each cost center (activity within a program within a fund). The Mayor may transfer unencumbered appropriations within programs within funds. The Municipal Legislature may transfer amounts among programs within and among funds.

The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriation) is at the functions/program level within the general and debt service funds, respectively.

Under the laws and regulations of the Commonwealth the appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided.

Budgetary Accounting

The Municipality's annual budgets are prepared using the budgetary (statutory) basis of accounting, which is not in accordance with GAAP.

According to the budgetary basis of accounting, revenue is generally recorded when cash is received. Short-term and long-term borrowings may be used to finance budgetary excess of expenditures over revenues.

The Municipality uses encumbrance accounting to record the full amount of purchase orders, contracts and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control. Accordingly, expenditures are generally recorded when the related expenditure is incurred or encumbered. Available appropriations and encumbrances are established to lapse one fiscal year after the end of the fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment. Unencumbered appropriations and encumbrances lapse at fiscal year-end. Other appropriations, mainly capital projects appropriations, are continuing accounts for which the Municipal Legislature has authorized that unspent balance from the prior year be carried forward and made available for current spending.

The accompanying statement of revenues and expenditures - budget and actual - budgetary basis - general fund, provides information about the general fund's original budget, its amendments, and the actual results of operations of such governmental fund under the budgetary basis of accounting for the fiscal year ended June 30, 2017.

Deposits and Investments

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

Accounts Receivable

Receivables consist of all revenues earned but not collected at June 30, 2017. These accounts receivables are stated net of estimated allowances for uncollectible accounts, which are determined based upon past collection experience, historical trends, current economic conditions and the periodic aging of accounts receivable.

Activities among governmental 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 inter-fund loans) or "advances to/from other funds" (i.e. the non-current portion of inter-fund loans), as applicable. All other outstanding balances between funds are reported as "due to/from other funds"

Use of Estimates

The preparation of the accompanying basic financial statements in conformity with GAAP requires

management to make significant estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the basic financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Inter-fund Activities

The Municipality has the following types of reciprocal and non-reciprocal inter-fund activities recorded among governmental funds in the accompanying GFFS:

Inter-fund loans — Represent amounts provided with a requirement for repayment, which are recorded as “due from” in the lender governmental fund and “due to” in the borrower governmental fund. Inter-fund receivables, which are not considered to be currently available financial resources, are reported as advances. For amounts not expected to be collected within a reasonable period of time, inter-fund receivables/payables are reduced to the estimated realizable value and the amount that is not expected to be repaid is reported as an operating transfer from the governmental fund that made the loan.

Inter-fund transfers — Represent flows of assets (permanent reallocation of financial resources among governmental funds) without equivalent flows of assets in return and without a requirement for repayment.

Operating transfers are reported as other financing sources in the governmental fund making transfers and as other financing sources in the governmental fund receiving transfers.

Inter-fund reimbursements — Represent repayments from the governmental fund responsible for particular expenditures or expenses to the governmental fund that initially paid for them.

Capital Assets

Capital assets used in governmental activities include land and land improvements, buildings, structures and building improvements, machinery and equipment, furniture and fixtures, vehicles, construction in progress, and infrastructure. These assets are capitalized and reported in the accompanying statement of net position. Infrastructure assets are generally stationary in nature and include roads, bridges, streets and sidewalks, drainage systems and other similar assets.

For financial reporting purposes, the Municipality defines capital assets as assets with an individual cost of \$5,000 or more at the date of acquisition, construction or improvement, and with useful lives extending beyond one year. All assets with individual costs under \$5,000 or with useful lives not exceeding one year, are charged directly to expense in the government-wide statement of activities. In the governmental funds, all capital assets are recorded as capital outlays (expenditures).

In the statement of net position, all capital assets are recorded at cost or estimated historical cost if actual cost was unavailable, except for donated capital assets, which are recorded at their estimated fair value at the date of donation. Estimated historical costs based on deflated current costs were used to value a significant portion of the infrastructure constructed or acquired prior to June 30, 2002 and certain lands, buildings, structures and building improvements.

Major outlays for capital assets and improvements are capitalized in the statement of net assets as projects are constructed. The costs of normal maintenance and repairs that do not add value to the asset

or materially extend capital asset lives are not capitalized.

Depreciation and amortization expense is recorded only in the government-wide statement of activities. However, there is no depreciation or amortization recorded for land and construction in progress. Depreciable capital assets are generally depreciated or amortized over their estimated useful lives under the straight-line method. The estimated useful lives of major capital asset categories are:

<u>Description</u>	<u>Years</u>
Buildings	50
Infrastructure	10
Building and site improvements	25
Vehicles	10
Machinery and equipment	7

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

Unearned Revenues

In the GFFS, unearned revenue arises when one of the following situations occur:

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.

Compensated Absences

Compensated absences are accounted for under the provisions of Statement No. I6, *Accounting for Compensated Absence*, issued by GASB (GASB No. 16). Compensated absences include paid time off made available to employees in connection with vacation, sick leave and compensatory time. The liability for compensated absences recorded in the accompanying statement of net position is limited to leave that: (1) is attributable to services already rendered on or before June 30, 2013 and (2) is not contingent on a specific event that is outside the control of the Municipality' and the employee (such as illness). Compensated absences that relate to future services or are contingent on a specific event outside the control of the employer or the employee are accounted for in the period when those services are rendered or those events take place.

The liability for compensated absences includes salary-related costs, which are directly and incrementally related to the amount of salary paid to the employee (such as employer's share of Social Security taxes and Medicare taxes).

The vacation policy of the Municipality provides for the accumulation of regular vacations at a rate of 2.5 days per month (30 days per year) per employee. Employees accumulate regular sick leave at a rate of 1.5 days per month (18 days per year). Employees accumulate compensatory time at a rate of 1.5 times the overtime worked. All vacation and sick leave days accumulated by employees in excess of 30 days and 90 days, respectively, are paid to employees each year, if not consumed, as required by law. In the case of compensatory time, the excess of 240 hours is paid to employees each year, if not consumed. .

Upon termination of employment, an employee receives compensation for all accumulated unpaid regular vacation leave at the current rate. In the case of regular sick leave, if the employee terminates his or her employment before reaching 10 years of services, such regular sick leave is not paid to the employee, if not consumed. In addition upon termination of employment, an employee does not receive compensation for compensatory time, if not consumed previously. After 10 years of services, any regular sick leave balance is paid to the employee. Accumulated vacation time is fully vested to the employee at any time.

The liability for compensated absences is reported in the statement of net position. A liability for compensated absences is reported in the GFFS only when matured (when payment is due), for example, as a result of employee resignations or retirements.

Long-term Debt

The long term liabilities reported in the accompanying statements of net position include the Municipality's bonds payable, notes payable, accrued compensated absences, and accrued legal claims and judgments if any.

All long-term debt to be repaid from governmental resources is reported as liabilities in the accompanying statement of net position. Principal and interest payments on bonds due on July 1, 2017 are recorded as governmental Fund liabilities in the GFFS (debt service fund) when resources are available in the debt service fund (June 30, 2017). In the GFFS, the face amount of debt issued (gross debt reported) is reported as other financing sources when issued.

Accounting for Pension Costs and Post-Employment Benefits

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

The government of the Commonwealth 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 defined benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate.

The Municipality is considered a participant, and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Commonwealth of Puerto Rico and the basic financial statements of such retirement systems are part of the financial reporting entity of the Commonwealth of Puerto Rico.

Risk Management

The Municipality carries commercial insurance covering casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Commonwealth's Department of Treasury (the Department of Treasury) on behalf of all municipalities of Puerto Rico. The Department of Treasury pays the insurance premiums on behalf of the Municipality and then is reimbursed each year through monthly equal payments deducted from the Municipality's gross property tax collections made by the Municipal Revenue Collection Center ("CRIM", by its Spanish acronyms), a governmental entity responsible for billing and collecting property taxes on behalf of all municipalities of Puerto Rico.

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

The Municipality obtains workers' compensation insurance coverage through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. Workers' compensation insurance premiums are also paid through monthly deductions made by CRIM from the Municipality's gross property tax collections.

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

The Municipality also obtains medical insurance coverage from several health insurance companies for its employees. Different health insurance coverage and premium options are negotiated each year by the Department of Treasury on behalf of the Municipality. The current insurance policies have not been canceled or terminated at June 30, 2017.

Future Adoption of Accounting Pronouncements — The GASB has issued the following statements:

- GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, which is effective for periods beginning after June 15, 2017—except those provisions that address employers and governmental nonemployer contributing entities for pensions that are not within the scope of Statement 68, which are effective for fiscal years beginning after June 15, 2017.
- GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which is effective for periods beginning after June 15, 2017.

- GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which is effective for periods beginning after June 15, 2017.
- GASB Statement No. 77, *Tax Abatement Disclosures*, which is effective for periods beginning after December 15, 2015.
- GASB Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*, which is effective for periods beginning after December 15, 2015.
- GASB Statement No. 80, *Blending Requirements for Certain Component Units—an amendment of GASB Statement No. 14*, which is effective for periods beginning after June 15, 2017.
- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, which is effective for periods beginning after December 15, 2017.
- GASB Statement No. 82, *Pension Issues—an amendment of GASB Statements No. 67, No. 68, and No. 73*, which is effective for periods beginning after June 15, 2017.
- GASB Statement No. 83, *Certain Asset Retirement Obligations*, which is effective for periods beginning after June 15, 2018.
- GASB Statement No. 84, *Fiduciary Activities*, which is effective for periods beginning after December 15, 2018.
- GASB Statement No. 85, *Omnibus 2017*, which is effective for periods beginning after June 15, 2017.

Management is evaluating the impact that these statements will have on the Municipality's basic financial statements.

2. Credit Risk

The following is essential information about credit risk, interest rate risk, custodial credit risk, and foreign exchange exposure of deposits and investments of the Municipality at June 30, 2017:

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 of Puerto Rico, the Municipality has adopted, as its custodial credit risk policy, the *Statement of Uniform Investment Guidelines for the Municipalities of the Commonwealth of Puerto Rico*, issued by the Government Development Bank for Puerto Rico. Accordingly, the Municipality is only allowed to invest in obligations of the Commonwealth of Puerto Rico, obligations of the United States of America, certificates of deposit, 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 is not allowed to invest in marketable securities or any other type of investments (debt securities) for which credit risk exposure may be significant. Consequently, at June 30, 2017 and for the fiscal year then ended, the Municipality invested only in certificates of deposit in commercial banks, which are insured by the Federal Deposit Insurance Corporation (FDIC), generally up to a maximum of \$250,000 per depositor. No investments in debt or equity securities were made during the fiscal year ended June 30, 2017. Therefore, the Municipality's management has

concluded that the credit risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2017.

Interest rate risk - This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt or equity investments in its investments portfolio at June 30, 2017, (2) limiting the weighted average maturity of its investments in certificates of deposit to periods of three months or less and (3) keeping most of its banks deposits and certificates of deposit in interest bearing accounts generating interest at prevailing market rates as required by the *Statement of Uniform Investment Guidelines for the Municipalities of the Commonwealth of Puerto Rico, issued by the Government Development Bank for Puerto Rico* (the adopted policy of the Municipality). At June 30, 2017, the interest rate risk associated with the Municipality's cash and cash equivalent is considered low since the investment portfolio of the Municipality consists of certificates of deposit and do not include debt securities or any type of investments that could be affected by changes in interest rates. .

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. In addition, public funds deposited in commercial banks by the Municipality are fully collateralized for the amounts deposited in excess of the federal depository insurance. All securities pledged as collateral are held in the Municipality's name by the agents of the Commonwealth's Secretary of Treasury. Deposits of GDB, are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2017. It is management's policy to only maintain deposits in banks affiliated to FDIC to minimize the custodial credit risk, except for GDB.

Therefore, the Municipality's management has concluded that at June 30, 2017, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

Foreign exchange risk — This is the risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, adopted by the Municipality, the Municipality is prevented from investing in foreign securities or any other types of investments for which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2017.

3. Property Taxes

The personal property tax is self-assessed by the taxpayer on a return which is to be filed by May 15 of each year with the CRIM, a governmental entity created by the government of Puerto Rico as part of the Municipal Governmental Autonomy Laws of 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 settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the 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, deferred revenue is recorded at June 30.

On January 26, 2000, Public Law No. 42 was enacted 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.

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 owed 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. 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.

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

The annual tax rate for fiscal year 2016-2017 is 10.53% for real property and 8.53% 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) 6.0% and 4.0%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 3.5% represents the ad valorem tax restricted for debt service. The Commonwealth also contributes an annual tax rate of 0.2% of the Property tax collected and such amount is accounted for similar to item (a) above.

Property tax revenues in the general and debt service funds amounted to \$1,722,358 and \$1,140,846, respectively, for the fiscal year ended June 30, 2017.

4. Municipal License Taxes

The Municipality is authorized to impose and collect municipal license taxes to any natural or legal person having trade or business activities within the territory of AGUAS BUENAS. This is a self-assessed tax generally based on the business volume of taxpayers, measured by gross revenues. The Municipality establishes the applicable tax rates. At June 30, 2017, the municipal license tax rates imposed by the Municipality were 1.50 percent for financial institutions and 0.50 percent for other types of taxpayers.

Each taxpayer must assess the corresponding municipal license tax by declaring the volume of business through a tax return to be filed every April 15, based on the actual volume of business (revenues) generated in the preceding calendar year. Taxpayers with a sales volume of \$3 million or more must include audited financial statements with their tax return filings. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration on April 15. The first installment of the tax covers the six-month period ended December 31, subsequent to the filing date of the declaration, while the second installment of the tax covers the six-month period ended June 30 of the subsequent calendar year. If a taxpayer elects to pay the tax in full on the filing date of the declaration (generally April 15), a 5 percent discount is granted automatically on the total tax amount due. Municipal license tax revenues for the fiscal year ended June 30, 2017 amounted to \$1,117,855 in the accompanying financial statements.

Any municipal license taxes collected in advance (that is, pertaining to a future fiscal year) are recorded as unearned revenues. Unearned municipal license tax revenues recorded in the accompanying GWFS and GFFS amounted to \$514,461 at June 30, 2017. This amount represents the municipal license taxes corresponding to fiscal year ending June 30, 2017 that were collected in advance during the last quarter of the current fiscal year, as required by law.

5. Sales and Use Taxes

The Municipality imposes a sales and use tax pursuant to the provisions of the Puerto Rico Internal Revenue Code, as amended. The tax consists of one percent (1.0%) on the sales price of taxable items or on the purchase prices of all usage, storage, or consumption of taxable items, excluding wholesales. The sales and use tax is a self-assessed tax collected by the Municipality through monthly tax returns due on the twentieth day of the immediate following month. The tax returns are filed by the respective businesses that are required by law to withhold the tax from consumers on each taxable product or

service. Sales and use tax revenues amounted to \$1,225,831 for the fiscal year ended June 30, 2017.

The commonwealth of Puerto Rico imposes a separate state sales and use tax of 0.5%, which is imposed and collected by the Puerto Rico Treasury Department through monthly tax return due on the twentieth day of the immediate following month. This 0.5% tax is administered by the Government Development Bank of Puerto Rico for the following purposes: (1) 0.2% is deposited in the new “Municipal Debt Service Fund”, strictly for granting loans to the municipalities of Puerto Rico; (2) 0.2% for the creation of the “Municipal Development Fund” percentage, which will be distributed among all municipalities pursuant to a statutory formula; and (3) 0.1%, for the creation of the “Permanent Improvements Fund”, to be distributed by the Legislature of the Commonwealth of Puerto Rico to carry out public works and permanent improvement projects in the municipalities of Puerto Rico.

6. Inter-fund Transactions

Inter- fund – receivables and payables at June 30, 2017 are summarized as follows:

<u>Fund</u>	<u>Receivable Fund</u>	<u>Payable Fund</u>
General	\$ 290,750	
Other Governmental		\$ 290,750
	<u>\$ 290,750</u>	<u>\$ 290,750</u>

Inter-fund receivables and payables represent the pending settlements of the aforementioned transfers, which are considered by management to be fully realizable at June 30, 2017.

7. Unearned Revenues

Unearned revenues of \$514,461 in the general fund is related to municipal license tax collected in fiscal year 2016-2017 that will be earned in fiscal year 2017-2018.

8. Long-Term Obligations

a) The general long-term debt activity for the fiscal year ended June 30, 2017 is as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental activities:					
Bonds and notes payable	\$ 7,234,800		\$ (325,100)	\$ 6,909,700	\$ 345,800
CRIM - Law 42	71,862		(2,703)	69,159	2,703
CRIM - Law 146	70,531		(4,408)	66,123	4,408
Compensated absences	1,225,557	1,253,620	(576,970)	1,902,207	-
Net pension liability	19,141,255			19,141,255	-
Total	27,744,005	1,253,620	(909,181)	28,088,444	352,911
Business-type activities:					
Mortgage payable	192,411		(72,396)	120,015	78,405
Total	\$ 27,936,416	\$ 1,253,620	\$ (981,577)	\$ 28,208,459	\$ 431,316

Historically, the general fund has been used to liquidate certain notes payable, compensated absences, federal cost disallowances and any other long-term liabilities other than bonds.

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 of Puerto Rico provide that the Municipality's public debt will constitute a first claim on the available revenue of the Municipality. Public debt includes bonds and bond anticipation notes. The good faith, credit and taxing power of the Municipality are irrevocably pledged for the prompt payment of the principal and interest of bonds.

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, 2017:

\$920,000 Public Improvement Bonds, Serial 1995-96 payable in annual installments ranging from \$60,000 to \$85,000 through July 1, 2020. Interest ranging from 6.58% to 6.63% payable in semiannual installments.	\$ 295,000
\$2,285,000 General Obligation Bonds, Serial 2005-2006 payable in annual installments ranging from \$75,000 to \$175,000, through July 1, 2030. Interest at 1.25% over LIBOR rate payable in semiannual installments.	1,695,000
\$255,000 General Obligation Bonds, Serial 2007-2008 due in annual installments ranging from \$10,000 to \$20,000 through July 1, 2031. Interest at 1.25% over LIBOR rate payable in semiannual installments.	200,000
\$955,000 General Municipal Obligation, Serial 2012 payable in annual installments ranging from \$55,000 to \$105,000 through July 1, 2025. Interest at 1.25% over LIBOR rate payable in semiannual installments.	725,000
\$119,800 General Obligation Note, POGM 2012 payable in annual installments ranging from \$15,000 to \$19,200 plus interest at 3.125% through January 1, 2023.	104,700
\$4,145,000 Special Obligation Bond, Serial 2012-11 payable in annual installments ranging from \$90,000 to \$345,000 through July 1, 2035. Interest at 1.5% over LIBOR prime rate due in semiannually installments.	3,705,000
\$270,000 Special Obligation Bond serial 2015-12 payable in annual installments ranging from \$20,000 to \$30,000 through July 1, 2023. Interest at 1.5% over LIBOR prime rate due in semiannually installments.	185,000
	<u>\$ 6,909,700</u>

Variable interest rates on serial bonds are reviewed periodically by GDB and are based on the fluctuation of GDB's weighted average rate for its commercial paper program. Under this program, GDB issues commercial paper: (1) in the taxable and tax-exempt markets of the United States of America, (2) in the Eurodollar market, and (3) to corporations having tax exemptions under the Commonwealth's Industrial Incentives Acts.

Annual debt service requirements of maturity for bonds and notes payable are as follows:

Year Ending June 30,	Principal	Interest
2018	\$ 345,800	\$ 418,466
2019	371,400	455,819
2020	397,100	429,350
2021	422,700	401,099
2022	363,500	373,866
2023-2027	1,909,200	1,460,575
2028-2032	1,855,000	791,988
2033-2037	1,245,000	194,813
	<u>\$ 6,909,700</u>	<u>\$ 4,525,974</u>

c. Advances from- CRIM- This amount represents the balance owed to CRIM at June 30, 2017 which will be repaid through a financing obtained by the CRIM with GDB, as explained in Note 3.

d. Compensated absences – The government-wide statement of net position includes \$1,902,207 of accrued sick leave benefits and accrued vacation benefits and related employer payroll cost, representing the Municipality's commitment to fund such costs from future operations.

e. Claims and assessments – On October 3, 2016 the Municipality enter in a settlement agreement with a former employee that claimed political discrimination. The total amount of the settlement was \$300,000 of which \$125,000 was pending to be paid at June 30, 2017.

9. CAPITAL ASSETS

Capital assets; those with an estimated useful live of five years or more from the time of acquisition by the Municipality and a cost of \$5,000 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in current year, including those changes for infrastructure and construction in-progress pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

Governmental Activities:	Balance July 1, 2016	Additions	Retirements	Balance June 30, 2017
Capital asset, not being depreciated:				
Land	\$ 2,710,693	\$ -	\$ -	\$ 2,710,693
Construction in progress	<u>6,906,227</u>	<u>-</u>	<u>-</u>	<u>6,906,227</u>
Total capital assets not being depreciated	<u>9,616,919</u>	<u>-</u>	<u>-</u>	<u>9,616,919</u>
Capital assets, being depreciated:				
Buildings and building improvements	24,988,794	377,437	-	25,366,230
Infrastructure	7,882,302	93,357	-	7,975,658
Equipment	3,241,643	-	-	3,241,643
Vehicles	<u>2,611,812</u>	<u>-</u>	<u>-</u>	<u>2,611,812</u>
Total capital assets being depreciated	<u>38,724,551</u>	<u>470,793</u>	<u>-</u>	<u>39,195,344</u>
Less accumulated depreciation for:				
Buildings and building improvements	(12,484,134)	(715,810)	-	(13,199,944)
Infrastructure	(1,354,146)	(199,391)	-	(1,553,537)
Equipment	(2,881,895)	(113,265)	-	(2,995,160)
Vehicles	<u>(2,406,944)</u>	<u>(45,251)</u>	<u>-</u>	<u>(2,452,195)</u>
Total accumulated depreciation	<u>(19,127,119)</u>	<u>(1,073,717)</u>	<u>-</u>	<u>(20,200,836)</u>
Total capital assets being depreciated, net	<u>19,597,432</u>	<u>(602,924)</u>	<u>-</u>	<u>18,994,508</u>
Governmental activities capital assets, net	<u>29,214,351</u>	<u>(602,924)</u>	<u>-</u>	<u>28,611,427</u>

Business-type activities:

Capital asset, not being depreciated:

Land	\$	<u>50,700</u>			\$	<u>50,700</u>
Total capital assets not being depreciated		<u>50,700</u>				<u>50,700</u>

Capital assets, being depreciated:

Buildings and building improvements		2,057,859	10,072			2,067,931
Equipment		<u>263,920</u>	<u>11,342</u>		-	<u>275,262</u>
Total capital assets being depreciated		<u>2,321,779</u>	<u>21,414</u>		-	<u>2,343,193</u>
Less accumulated depreciation		<u>(2,010,597)</u>	<u>(61,950)</u>		-	<u>(2,072,547)</u>
Business-type capital assets, net		<u>361,882</u>	<u>(40,536)</u>		-	<u>321,346</u>
	\$	<u>29,576,233</u>	\$	<u>(643,460)</u>	\$	<u>-</u>
					\$	<u>28,932,773</u>

10. Employees' Retirement Systems

A. Plan Description – The ERS is a cost-sharing, multi-employer defined benefit pension plan administered by the Puerto Rico Government Employees and Judiciary Retirement Systems Administration (the ERS and JRS Administration). It is a trust created by Act no. 447 on May 15, 1951 (Act no. 447), as amended, to provide pension and other benefits to retired employees of the Commonwealth, its public corporations and municipalities of Puerto Rico. The ERS began operations on January 1, 1952, at which date, contributions by employers and participating employees commenced. The ERS is a pension trust fund of the Commonwealth.

The ERS consists of different benefit structures pursuant to ACT No. 447, as amended, including a cost-sharing, multi-employer, defined benefit program, a defined contribution program (System 2000 program) and a defined contribution hybrid program. The pension plan is sponsored by the Commonwealth, public corporations, and municipalities of Puerto Rico.

Substantially all full-time employees of the Commonwealth and its instrumentalities (73 Commonwealth agencies, 78 municipalities, and 55 public corporations, including the ERS) are covered by the ERS. Membership is mandatory for all regular, appointed, and temporary employees of the Commonwealth, Commonwealth secretaries, head of public agencies and instrumentalities, among others.

The benefits provided to members of the ERS are established by Commonwealth law and may be amended only by the Legislature with the Governor's approval. Benefit provisions vary depending on date of membership.

On April 4, 2013, the Legislature enacted Act No. 3 which amended Act No. 447, Act no. 1 of February 16, 1990 (“Act No. 1”) and Act. No. 305 of September 24, 1999 (“Act No. 305 or System 200”) to establish, among other things, a defined contribution program similar to the System 2000 Program (the Defined Contribution Hybrid Program) to be administered by the ERS. Act No.3 of 2013, in conjunction with other recent funding and design changes, provided for a comprehensive pension design of the ERS. All regular employees hired for the first time on or after July 1, 2013, and former employees who participated in the Defined Benefit Program and the system 2000 Program, and were rehired on or after July 1, 2013, became members of the Defined Contribution Hybrid Program as a condition to their employment. In addition, employees who at June 30, 2013, were participants of previous plans will become part of the Defined Contribution Hybrid Program. Act No. 3 froze all retirement benefits accrued through June 30, 2012 under the Defined Benefit Program, and thereafter, all future benefits will accrue under the defined contribution formula used for the 2000 System Program participants. Ceasing future defined benefit accruals under Act 447 and Act 1 And converting to a member-funded hybrid plan will result in lower benefit payments as these tiers wind down and will make all future employer contributions available to pay benefits and bonds payable debt service.

Certain provisions are different for the three groups of members who entered the ERS prior to July 1, 2013 as described below:

1. Members of Act No. 447 are generally those members hired on or after April 1, 1990 (Defined Benefit Program).
2. Members of Act No. 1 are generally those members hired on or after April 1, 1990 and on or before December 31, 1999 (Defined Program).
3. Members of Act. No. 305 are generally those members hired on or after January 1, 2000 and on or before June 30, 2013 (Defined Contribution Program). Each member has a no forfeitable right to the value of his/her account. Members have three options to invest their contributions. Investment income is credited to the member’s account semiannually. The Commonwealth does not guarantee benefits at retirement age.

All regular employees hired for the first time on or after July 1, 2013, and former employees who participated in the defined benefit program and the System 2000 program, and were rehired on or after July 1, 2013, become members of the defined contribution hybrid program as a condition to their employment. In addition, employees who at June 30, 2013, were participants of previous programs will become part of the Defined Contribution Hybrid Program. Each member has a no forfeitable right to the value of his/her contributions to the Defined Contribution Hybrid account.

The assets of the defined benefit program, the defined contribution program and the defined contribution hybrid program are pooled and invested by the ERS. Future benefit payments will be paid from the same pool of assets. In addition, employers’ contributions for members hired on or after January 1, 2000 will be used by the ERS to reduce the unfunded status of the Defined Benefit Program.

This summary of plan provisions is intended to describe the essential features of the plan. All eligibility requirements and benefit amounts shall be determined in strict accordance with the plan document itself.

B. On April 4, 2014, the Governor of Puerto Rico signed into law Act No. 3 of 2014, which represents a comprehensive reform of the ERS. Act No. 3 became effective on July 1, 2014 and amended the provisions of the different benefit structures under the ERS, including, but not limited to, the following:

1. 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, 2014 were 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.
2. Increased the minimum pension for current retirees from \$400 to \$500 per month.
3. Increase the retirement age in a range within 58 to 63 years of age depending the act under which the employee is eligible for retirement.
4. Transitioning active participants under Act No. 1 and Act No. 447 to a defined contribution plan similar to System 2000.
5. Eliminated the “merit annuity” available to participants who joined the ERS prior to April 1, 1990.
6. The employee contribution rate was increased from 8.275% to 10%.
7. 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.
8. Eliminated or reduced various retirement benefits previously granted by special laws, including Christmas and summer bonuses. The Christmas bonus payable to current retirees was reduced from \$600 to \$200 and was eliminated for future retirees. The summer bonus was eliminated. Resulting employer contribution savings will be contributed to the ERS.
9. Disability benefits were eliminated and substituted for a mandatory disability insurance policy.
10. Survivor benefits were modified.

C. Effective for fiscal year ended June 30, 2015, the Municipality implemented de provision of the GASB 68, which accounting and Financial Reporting for Pension as recommended which required that the Municipalities’ governmental-wide financial Statements present the proportional net pension liability of the ERS. In addition, the GASB 68 required among other the following disclosures:

1. Employer’s proportionate share amount of collective net pension liability.
2. Employer’s proportionate percentage of collective net pension liability (including the basis on which it was determined) and change on its proportion since prior measurement debts.
3. Significant assumption used to measure total pension liability, including inflation, salary changes, discounts rate and mortality.

4. Measurement date of collective net pension liability and date of actuarial valuation on which the total liability is base.
5. Information about plan fiduciary net position.

Other information about the net pension liabilities should be disclosed as require supplemental information.

The effect in the financial Statement as of June 30, 2015 of the implementations of GASB 68 is as follow:

	Current Accounting Standards (GASB 27)	New Accounting Standards
Assets	\$35,344,219	\$35,344,219
Deferred outflows of resources		809,164
Liabilities	10,776,512	28,101,228
Deferred inflows of resources	495,799	634,439
Revenues	4,336,307	4,336,307
Expenses	13,726,650	14,502,372
Net Position (deficit)	\$24,071,908	\$ 7,417,716

The net position as prior reported was restated by \$16,654,192 due to the of implementation of GASB 68.

Pension Liabilities, Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2016, the Municipality reported a liability of \$19,140,755 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Municipality proportion of the net pension liability was based on a projection of the Municipality long-term share of contributions to the pension plan relative to the total projected contributions of the State and all participating school districts, actuarially determined. At June 30, 2015, the Municipality proportion was .05757 percent.

At June 30, 2015, the Municipality reported deferred outflows of resources and deferred inflows of resources from the following sources as a result of its requirement to contribute to ERS:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Pension contributions subsequent to measurement date	\$225,355	
Differences between actual and expected experience		
Changes in assumptions		
Change in employer's proportion and differences		
Between the employer's contributions and the		
employer's proportionate share of contributions		
Net differences between projected and actual earnings		
on plan investments	<u>591,339</u>	<u>139,210</u>
Total	<u>\$816,694</u>	<u>\$139,210</u>

The total pension liability in the June 30, 2015 actuarial valuations was determined using the following actuarial assumptions:

Measurement date	June 30, 2015
Amortization method	18 years closed (beginning July 1, 2014), level dollar
Actuarial cost method	Entry-age normal cost method
Remaining amortization period	17 years
Actuarial assumptions:	
Discount rate	3.80%
Inflation	N/A
Payroll growth	N/A
Projected salary increase	N/A
Investment rate of return	3.10%
Pre – retirement mortality	For general employees not covered under Act No. 127, RP-2014 Employee Mortality Rates for males and females adjusted to reflect Mortality Improvement scale MP-2015 from 2016 base year and projected forward using MP-2015 on a generational basis. For members covered under Act No. 127, RP-2014 Employee Mortality Rates with blue collar adjustments for males and females adjusted to reflect Mortality Improvement scale MP-2015 from 2016 base year and projected forward using MP-2015 on a generational basis. As generational tables, they reflect mortality improvements both before and after the measurement date. 100% of deaths while in active services are assumed to be occupational for members covered under Act No. 127.
Post-retirement health mortality	Rates which vary by gender are assumed for healthy retirees and beneficiaries based on a study of plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 92% of the rates from the UP-1994

Mortality Table for Males and 95% of the rates from the UP-1994 Mortality Table for Females, both projected from 1994 to 2010 using Scale AA. These base rates are projected using Mortality Improvement Scale MP-2015 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

Post-retirement disabled mortality

Rates which vary by gender are assumed for disabled retirees based on a study of plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 105% of the rates from the UP-1994 Mortality Table for Males and 115% of the rates from the UP-1994 Mortality Table for Females. These base rates are projected using Mortality Improvement Scale MP-2015 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

The net pension liability (information provided by Actuaries Valuation Report) as of June 30, 2015 is as follows:

<u>Net Pension liability</u>	<u>Total</u>	<u>Proportional Share</u> <u>(0.05757%)</u>
Total pension liability	\$32,669,162,000	\$18,807,136
Fiduciary net position (deficit)	<u>(578,633,000)</u>	<u>(333,199)</u>
Net pension liability	<u>33,247,795,000</u>	<u>19,140,255</u>
Fiduciary net position as a % of total pension liability	-1.77%	-1.77%
Covered payroll	3,319,280	1,622,226
Net pension liability as a % covered payroll	1,001.66%	1,179.07%

The following presents the Municipality proportionate share of the net pension liability using the discount rate of 3.80%, as well as what the Municipality a proportionate share of the net pension liabilities would be if it was calculate using a discount rate that is 1% lower (2.80%) or 1% higher (4.80%) than the current rate:

	1% Decrease <u>2.80%</u>	Current Discount Rate <u>3.80%</u>	1% Increase <u>4.80%</u>
Total pension liability	\$21,494,472	\$18,807,636	\$16,606,202
Fiduciary net position (deficit)	<u>(333,119)</u>	<u>(333,119)</u>	<u>(0)</u>
Net pension liability	<u>\$21,827,591</u>	<u>\$19,140,755</u>	<u>\$16,939,321</u>

The discount rates used to measure total pension liability were as follow:

	<u>June 30, 2014</u>	<u>June 30, 2015</u>
Discount rate	4.29%	3.80%
Long-term expected rate of return net of investment expense	6.75%	6.55%
Municipal bond rate*	4.29%	3.80%

*Bond Buyer General Obligation 20-Bond Municipal Bond Index

Change in Net Pension Liabilities (information provided by Actuaries Valuation Report) for the Year ended June 30, 2015 was a follow:

<u>Changes in Net Pension Liability</u>	<u>Total Pension Liability</u>	<u>Increase (Decrease)</u>		<u>Proportional Share .05757</u>
		<u>Plan Fiduciary Net Pension</u>	<u>Net Pension Liability</u>	
Balance as of 06/30/14	\$30,219,517,000		\$30,138,851,000	\$17,324,216
Changes for the year:		\$80,666.00		
Service Cost	425,564,000		425,564,000	244,997
Interest on total pension liability	1,279,556,000		1,279,556,000	736,640
Effect of plan changes				
Effect of economic / demography (gains) losses	(463,898,000)		(463,898,000)	(267,066)
Effect of assumptions changes or inputs	2,781,098,000		2,781,098,000	1,627,298
Benefit payments	(1,572,675,000)			
Administrative		(1,572,675,000)	25,744,000	14,821
		(25,744,000)		
Other expenses			13,242,000	7,623
		(13,242,000)		
Cost of bonds			194,400,000	111,916
		(194,400,000)		
Member contributions			(339,650,000)	(195,537)
Net investment income		339,650,000	(70,143,000)	(40,380)
Employer contributions	<u>0</u>	70,143,000	<u>(736,969,000)</u>	<u>(424,273)</u>
		<u>736,969,000</u>		
Balance as of 06/30/15	<u>\$32,669,162,000</u>	<u>\$(578,633,000)</u>	<u>\$33,247,795,000</u>	<u>\$19,140,255</u>

The employer contribution to the above-mentioned plans during the three-year ended June 30, 2016, 2015 and 2014 was as follow:

<u>YEAR</u>	<u>AMOUNT</u>
2016	\$225,354
2015	\$217,825
2014	\$176,000

These amounts represented the required contribution for the corresponding year.

The historical trend information regarding the accumulation of assets and pension benefit obligation in the ERS is not available. For the ten-year trend information, refer to the separately issued financial statements of the ERS as of and for the fiscal year ended June 30, 2015. The P.R. Retirement Plan Administration provides additional information of the ERS. They issue a public available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Commonwealth of Puerto Rico. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, P.R. 00940.

11. Commitments and Contingencies

The Municipality is defendant in various legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Public Act No. 104 of June 25, 1955, as amended, persons are authorized to sue the Municipality only for causes of actions set forth in said Act to a maximum amount of \$75,000 or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. It is management’s opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial condition of the Municipality.

The Municipality has reserved and committed funds for outstanding construction projects amounting to approximately \$1.8 million at June 30, 2017.

The Municipality receives financial assistance from the federal Governments of the United States of America and the Commonwealth in the form of grants and entitlements. Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal laws and regulations, including the expenditure of resources for eligible purposes. Accordingly, expenditures financed by these programs are subject to financial and compliance audits by the appropriate grantor. Disallowance as a result of these audits may become liabilities of the Municipality.

12. Deposits in Governmental Development Bank for Puerto Rico

The Governmental Development Bank for Puerto Rico (“Bank” or “GDB”) has traditionally served as interim lender to the Commonwealth and its public corporations (also referred to herein as instrumentalities) and municipalities in anticipation of the issuance of long term bonds and notes by such entities in the municipal bond market. The Bank has also provided financing to the Commonwealth and its instrumentalities to finance their respective budget deficits, collateral requirements under swap agreements and to meet mandatory payments of obligations.

As a result of this lending function, the Bank traditionally served as the principal source of short term liquidity for the Commonwealth, its public corporations and municipalities.

Loans to the Commonwealth and its instrumentalities constitute a significant portion of the Bank's assets. As a result, the Bank's liquidity and financial condition depends to a large extent on the repayment of loans made to the Commonwealth and its instrumentalities, which face significant fiscal and financial challenges. Conditions that adversely affect the ability of the Commonwealth and its instrumentalities to raise cash (including limited access to capital markets) and repay their interim and other loans to the Bank have an adverse effect on the Bank's liquidity and financial condition. Similarly, conditions that adversely affect the ability of the Bank to raise cash (including limited access to capital markets) or otherwise finance its loan portfolio also have an adverse effect on the Commonwealth and its instrumentalities, as the Bank's ability to continue providing interim financing to the Commonwealth and its instrumentalities is reduced.

The Bank faces significant risks and uncertainties and it currently does not have sufficient liquid financial resources to meet obligations when they come due, as further described below. As discussed below, pursuant to recently enacted legislation, the Governor has ordered the suspension of loan disbursements by the Bank, imposed restrictions on the withdrawal and transfer of deposits from the Bank, and imposed a moratorium on debt obligations of the Bank, among other measures.

During the fiscal year ended June 30, 2014, and subsequent to the end of such fiscal year, the Bank's liquidity position has been adversely affected by the Commonwealth and its instrumentalities' continued operational deficits and lack of capital markets access. These factors have resulted in delays in the repayment by the Commonwealth and its instrumentalities of outstanding loans with the Bank, which delays, in turn, have limited the Bank's ability to continue providing liquidity to the Commonwealth and its instrumentalities. The Commonwealth's General Fund budget for fiscal year 2014 included approximately \$291.3 million of appropriations to the Bank, including approximately \$270 million of appropriations to repay principal and interest on public sector loans. These appropriations were based on payment schedules proposed by the Bank, which are mostly based on a period of amortization of 30 years, at contractual interest rates. During fiscal year 2014, in order to address a significant revenue shortfall, Executive Order No. 2014-029 was issued, which modified the budgetary appropriation originally approved by the Legislative Assembly of the Commonwealth and thus modified the principal and/or interest payments actually received by the Bank. The amount of the appropriation was reduced from approximately \$291.3 million to \$30.1 million. This reduction was compensated with the funds obtained from the \$3.5 billion General Obligation Bonds issuance of March 2014. For fiscal year 2015, the Commonwealth and the Bank renegotiated the terms of such loans and the Commonwealth appropriated and paid the renegotiated debt service on the public sector loan portfolio of the Bank. During fiscal year 2015 the Bank received \$153.9 million of appropriations.

The budget proposed by the Executive Branch to the Legislative Assembly for fiscal year 2017 included an appropriation for the payment of debt owed by the Commonwealth and certain of its instrumentalities to the Bank of \$261 million, but was amended by the Legislative Assembly to reduce said appropriation to approximately \$18 million, all of which were received. Given the Commonwealth's deteriorating financial condition and ongoing fiscal crisis, there can be no assurance that the Commonwealth will be in a position to make any future appropriations for the payment of debt owed by the Commonwealth and its instrumentalities to the Bank.

COMMONWEALTH OF PUERTO RICO

The Commonwealth currently faces a severe fiscal, economic and liquidity crisis, the culmination of many years of significant governmental deficits, a prolonged economic recession (which commenced in 2006), high unemployment, population decline, and high levels of debt and pension obligations. Further stressing the Commonwealth's liquidity is the vulnerability of revenue streams during times of major economic downturns and large health care, pension and debt service costs. As the Commonwealth's tax base has shrunk and its revenues affected by prevailing economic conditions, health care, pension and debt service costs have become an increasing portion of the General Fund budget, which has resulted in reduced funding available for other essential services. The Commonwealth's very high level of debt and unfunded pension liabilities and the resulting required allocation of revenues to service debt and pension obligations have contributed to significant budget deficits during the past several years, which deficits the Commonwealth has financed, further increasing the amount of its debt. More recently, these matters and the Commonwealth's liquidity constraints, among other factors, have adversely affected its credit ratings and its ability to obtain financing at reasonable interest rates, if at all. As a result, the Commonwealth has relied more heavily on short-term financings and interim loans from GDB, and other instrumentalities of the Commonwealth, which reliance has constrained the liquidity of the Commonwealth in general and GDB in particular, and increased near-term refinancing risk. These factors have also resulted in delays in the repayment by the Commonwealth and its instrumentalities of outstanding GDB lines of credit, which delays have limited GDB's ability to continue providing liquidity to the Commonwealth and have caused GDB to fail to make a principal payment on its debt obligations. These factors are reflected in the deterioration of the Commonwealth's credit ratings. Since June 30, 2014, the principal rating agencies have continued to lower their rating on the general obligation bonds of the Commonwealth, which had already been placed within non-investment grade ratings in February 2014. They also lowered their ratings on the bonds of the PBA and COFINA, and on other bonds of various instrumentalities, including GDB, all of which were lowered multiple notches in the grading levels.

Complete financial statements of GDB and the Commonwealth can be obtained directly by contacting their respective administrative offices at:

Department of the Treasury of the Commonwealth of Puerto Rico
Área de Contabilidad Central
P.O. Box 9024140, San Juan, PR 00902

Government Development Bank for Puerto Rico
P.O. Box 42001, San Juan, PR 00940-2001

Deposits in GDB

As of June 30, 2017, the Municipality had cash in GDB amounting to \$1.4 million in the Debt Service Fund.

As previously explained, the Commonwealth and its public entities have not been able to repay their loans to GDB, which has significantly affected GDB's liquidity and ability to repay its obligations.

GDB faces significant risks and uncertainties and it currently does not have sufficient liquid financial resources to meet obligations when they come due, as further described below. Recently enacted legislation has ordered the suspension of loan disbursements by GDB, imposed restrictions on the

withdrawal and transfer of deposits from GDB, and imposed a moratorium on debt obligations of GDB, among other measures.

As a result of the reductions in liquidity experienced subsequent to June 30, 2014, GDB took a number of liquidity enhancing and conservation measures, and explored the sale of assets and other alternatives to address its liquidity needs. In light of GDB's significant debt service obligations during fiscal year 2017, these measures, however, are not expected to be sufficient to maintain GDB's operations in the ordinary course absent the completion of a capital market transaction, a restructuring of GDB's debt, and the payment by the Commonwealth of debt service on GDB's public sector loans payable from annual appropriations. As a result of the non-payment by the Commonwealth of the appropriation to GDB and GDB's inability to restructure its debt in light of the broader fiscal crisis faced by the Commonwealth, GDB was not in a position to pay principal on its debt obligations due on May 1, 2017 and continue operations in the ordinary course. In April 2017, the Governor imposed on GDB emergency operational restrictions and debt moratorium. The GDB has continued to pay interest on its debt obligations.

Due to the conditions and events described above, GDB's management believes substantial doubt exists in the GDB's ability to continue as a going concern.

Certificates of deposits in GDB are carried at cost based on the requirements of Statement No. 31 of the Governmental Accounting Standards Board (GASB 31) "Accounting and Financial Reporting for Certain Investments and for External Investment Pools". Management of the Municipality believes, even with the uncertainty surrounding the ability of the GDB to continue as a going concern, the cost basis remains the appropriate basis of accounting for such deposits based on the fact that the provisions of GASB 31 imply but do not mandate the recognition of the unrealized loss. Management of the Municipality has also evaluated if a contingency exist in the Deposits in GDB based on the requirements of Statement No. 62 of the Governmental Accounting Standards Board (GASB 62) "Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements" paragraphs 96 to 110.

Management believes that the existence of the contingency is reasonably possible but not probable at this time and that there is no sufficient information to reasonably estimate such contingency, if any. Accordingly, Management of the Municipality has concluded that no contingency needs to be recorded as of June 30, 2017.

13. Subsequent events

On July 14, 2017, the Financial Oversight and Management Board for Puerto Rico (Oversight Board) created by Congress authorized the Government Development Bank for Puerto Rico (GDB) to pursue the restructuring of its debts under Title VI of PROMESA and conditionally certified GDB's Restructuring Support Agreement (RSA) under the relevant provisions of Title VI.

The Oversight Board's decision was in response to a Fiscal Agency and Financial Advisory Authority (FAFAA) request, dated June 30, 2017, in which the agency noted that the proposed restructuring, along with certain related settlements contemplated by the RSA, will result in an efficient wind down of GDB's operations and a comprehensive financial restructuring of GDB's obligations. FAFAA noted further that by proceeding under Title VI of PROMESA with the requisite creditor support, GDB believes that it will realize its objective of maximizing value for its stakeholders, while avoiding the delay, expense and uncertainty associated with litigation.

The RSA provides for the organized and consensual restructuring of a substantial portion of GDB's liabilities, including GDB public bonds, deposit claims by municipalities and certain non-public entities and claims under certain GDB-issued letters of credit and guarantees (Participating Bond Claims). In exchange for releasing GDB from liability relating to these claims, the claim-holders will receive new bonds to be issued by a new entity (the Issuer).

Due to the effects of the hurricanes, loss of communication, impairment to municipal revenues and liquidity, and the impact to GDB real estate owned assets, FAFAA, GDB and the RSA Requisite Bondholders agreed on revising certain milestones. They agreed on certain amendments to the RSA structure (Amended RSA) resulting in:

- Simplified structure (one security offered to Participating Bond Claims instead of original three).
- All municipal deposits will be applied against corresponding municipal loans to provide cash flow relief to municipalities to mitigate near-term impact of hurricanes.

The RSA Summary are as follow:

- RSA is consistent with the previously certified GDB Fiscal Plan, as it contemplates the conclusion of the orderly wind-down of GDB and a Title VI Qualifying Modification for the restructuring of GDB's Participating Bond Claims.
- RSA contemplates dividing GDB's assets into (i) the Recovery Authority for the benefit of bondholders, municipal depositors, and non-government entity depositors, and (ii) the Public Entity Trust (PET) for the benefit of other Government Entity Depositors.
- GDB will continue to exist as a legal entity for the purpose of resolving (i) outstanding legal matters and claims that exist or may be asserted by or against GDB and (ii) certain public entity loans that will remain at GDB and for which GDB shall have a contractual duty to the Recovery Authority to use commercially reasonable best efforts to maximize proceeds and transfer such proceeds, if any, to the Recovery Authority.
- GDB and the PET will be pre-funded at the time of closing of the Restructuring (as defined in the RSA) and will not require further financial assistance from the Recovery Authority, the PET or the Government.
- Prior to the closing of the Restructuring, the Amended RSA will simplify the GDB restructuring transaction while simultaneously providing additional relief to municipalities as they recover from the severe damage and devastation caused to Puerto Rico and its municipalities in the wake of Hurricanes Irma and María. The amendment to the RSA provides that, upon consummation of the transaction, each municipality will be authorized to apply the full amount of deposits held at GDB against the balance of any loan owed by such municipality to GDB. Additionally, to provide municipalities with immediate liquidity, the amendment to the RSA gives each municipality the opportunity to receive immediate payment, before consummation of the transaction, of 55% of such municipality's undisbursed certified Excess CAE held at GDB in exchange for releases. The other 45% should be apply against the balance of any loan owed by such municipality to GDB.

- The amendment also results in a simplified structure whereby GDB’s financial creditors will exchange their claims for only one tranche of new bonds at an upfront exchange ratio of 55%. The RSA amendment is available on the Electronic Municipal Market Access website.

Management and Trust Structure Summary

- On or prior to the closing of the transaction, pursuant to the terms of the RSA and the GDB Restructuring Act, each as amended, available cash will be distributed as follows: Approximately (i) \$21 million for payment to certain municipalities of the Excess CAE Settlement; (ii) \$27.2 million for estimated operating cash and contingency requirements of GDB; (iii) transaction cost (including legal and professional fees and contemplated settlements); \$1.5 million for estimated operating cash requirements of the PET; and (v) distributable cash to the Recovery Authority (~\$324 million). All amount subject to change.
- Upon closing of the Restructuring, GDB will transfer the servicing of the Recovery Authority assets (or the New Bond Collateral) to a third-party servicer approved by GDB.

Also, the Oversight Board require a New Fiscal Plan that was approved on April 20, 2018.

- The Plan is based on the projected performance of GDB’s existing loan asset portfolio, based on recent historical results.
- Based on the assessment of GDB’s loan portfolio and the information available post-Hurricanes Irma and María, the Plan assumes currently performing municipal loans (after the corresponding application of municipal deposits against municipal loans), certain public-sector loans, and the sale of real estate owned assets are the only sources of revenue going forward.
- To the extent a loan asset is “non-performing”, the Plan assumes such loan remains “non-performing” and therefore would not be a source of future inflows, although GDB, or any successor entity, reserves the right to pursue collection efforts, subject to the limitations imposed by the GDB Restructuring Act.
- The Plan assumes the continued orderly sale or other legally available disposition of real estate owned assets, until such assets are transferred to the Recovery Authority per terms of the RSA.
- GDB has segregated approximately \$22 million in cash, corresponding to GDB’s obligations to former GDB employees that retired pursuant to various pre-retirement and voluntary separation programs. Promptly after the certification of the Plan, GDB shall transfer such funds to a new trust to be constituted by GDB for the benefit of said retired employees, releasing GDB from such obligations.

Employees' Retirement System

On June 25, 2017, the Puerto Rico Legislature Assembly approved the Joint Resolutions Numbers 186, 187, 188 and 189 to adopt the budget for fiscal year 2017-2018 in the amount of \$9.562 billion. This amount is compound of \$9.172 billion from General Fund revenues and \$390 million expected from the sale of Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (ERS), Judiciary Retirement System (JRS) and Teacher Retirement System (TRS)s' assets, except for the headquarters building of the TRS known as the Capital Center Building, North Tower, located in Hato Rey, Puerto Rico. To make retirement systems payments effective July 1, 2017, the budget separates \$2.038 billion under Office of Management and Budget supervision.

On August 23, 2017, was enacted the Act No. 106, known as the "Act to Guarantee Payment to Our Retirees and Establish a New Plan for Defined Contributions for Public Employees". This Act determined and declared that the ERS, JRS and TRS are in a financial emergency. As a result of this financial emergency, it is estimated that by August 2017 the ERS will not have liquid funds to meet its obligations. Likewise, it is estimated that the TRS will be without liquid funds in September 2017 and that the JRS will not have sufficient liquid funds by February 2018.

On May 21, 2017, the Oversight Board, on behalf of the Government of Puerto Rico, filed a petition for the ERS to avail itself of Title III protections of PROMESA. With the submission of the petition under Title III of PROMESA, a process of restructuring of the obligations of said system under the supervision of the United States District Court for the District of Puerto Rico was initiated. Faced with this situation, the Puerto Rico Legislature Assembly approved the Act No. 106 on August 23, 2017, to ensure that retirees continue to receive their pensions, protect the individual contributions of public employees and protect the future of them. In addition, as a corrective measure, the contributions of public employees must be segregated and protected, and a New Defined Contribution Plan (DCP) was established to ensure the future of public employees. Accordingly, a Defined Contribution Account (DCA), a trust account, separated from the general assets and accounts of the Government, was created as of July 1, 2017 in the name of each Participant, as established in Chapter 3 of this Act.

The New Defined Contribution Plan created, consists of the establishment of a trust fund, which will not be subject to the provisions of Act No. 219-2012, as amended, known as the "Trusts Act". Which will contain an individual account for each Participant of the Retirement Systems that becomes part of said program, as provided in Chapter 3. Individual contributions will be credited to the New Defined Contribution Plan of each Participant and the return on investment in accordance with Article 3.6 of this Act. The benefit related to these contributions will be provided to each Participant after their separation from Service, whether by withdrawal or otherwise, will depend on the totality of the contributions to the New Defined Contribution Plan accumulated in its account from the moment this Act comes into force, or the date on which the Participant entered the DCP and the profitability of these.

By this Act is hereby declared as public policy of the Government of Puerto Rico the protection of pensions of all public service retirees who were Participants in the three Retirement Systems mentioned above. Therefore, as of July 1, 2017, pursuant to the Joint Resolution of the House of Representative No. 188 of 2017, as certified by the Oversight Board on July 13, 2017, the Government of Puerto Rico became the direct payer of the pensions of the retirees. Given the weight that this implies on the General Fund, which is estimated at billions of dollars a year, the employer's contributions that had been made to the three Retirement Systems, as well as the Additional Uniform Contribution, as per provisions of Joint Resolutions Nos. 186, 187 and 188 of 2017, the Retirement Systems shall provide their available funds and the net proceeds of the liquidation of their assets to the General Fund to assist in the payment of Accumulated Pensions.

Also, by this Act is hereby created the Account for the Payment of Accumulated Pensions, a trust account, separated from the general assets and accounts of the Government, designated to pay the Accumulated Pensions by the ERS, JRS and TRS under the "pay as you go" scheme, as established in Chapter 2 of this Act. This trust account will be centralized and segregated from the general assets and accounts of the Government, in charge of the Department of the Treasury and will be devoted solely and exclusively to the purposes set forth in this Act, and subject to the terms and conditions established therein. Once Retirement Systems exhaust their assets, the Accumulated Pension Payment Account, which will be largely nourished by the General Fund, as provided in this Act, will assume and guarantee the payment of the Accumulated Pensions as established in this Act. However, the Municipalities, the Legislative Branch, the Public Corporations, the Government and the Administration of the Courts will be obliged to pay the "Pay-Go" Charge as appropriate to each one to nurture the Account for the Payment of the Accumulated Pensions.

As of July 1, 2017, as per Act No. 106 of 2017, the Participant shall not make individual contributions or payments to the Account for the Payment of Accumulated Pensions, nor additional contributions to their respective Retirement Systems. As of the effective date of this Act, any Participant in the Retirement Systems shall obligatorily contribute a minimum of eight-point five percent (8.5%) of his/her monthly remuneration to his DCA, up to the limit established by the Code. In addition, may voluntarily provide additional amounts, as permitted by the Code. Upon entry into force of this Act, Participants in the DCP shall have the right to adjust their current contribution to Retirement Systems to the minimum authorized by this article. Participants in the DCP may vary the percentage they wish to contribute to said Plan from time to time but may never be less than the minimum percent required by this Act.

As per Act No. 106 of 2017, effective July 1, 2017 the Additional Uniform Contribution imposed by Act No. 32 of 2011 and the employer contribution imposed by Act No. 3 of 2013, was eliminated and imposes the "Pay-Go" Charge that the Financial Advisory Authority and Fiscal Agency of Puerto Rico (FAAFA) created by Act No. 2-2017, determines and imposes on the Government, the Municipalities, the Legislative Branch, the Administration of Courts, the Public Corporations and other covered entities. This charge will be equivalent to the amount in effect paid to Pensioners and Beneficiaries from each covered entity. The Secretary of the Treasury or the person or entity designated by him shall be authorized to collect the "Pay-Go" Charge. In the case of the Municipalities, the administrative charges of the "pay as you go" scheme will not be included in the computation of the "Pay-Go" Charge. Regardless of the payment of the "Pay-Go" Charge by the employer, the disbursement of the benefits of all Pensioners and Beneficiaries are guaranteed by the General Fund through the "pay as you go" scheme, with the responsibility of the entities to remit the payment of said Charge in compliance with its obligations under this Act.

The FAAFA is authorized, after making a determination that the fiscal situation of the Government has stabilized and that the condition of the fiscal permits, to recommend to the Governor, in coordination with the Retirement Board, that a quantity be included in the budget to match the contributions of the Participants to the Defined Contribution Account. This determination must be made in accordance with the Certified Fiscal Plan and the provisions of PROMESA.

Hurricanes Irma and María

On September 6, 2017 and September 20, 2017, Hurricanes Irma and María devastated Puerto Rico. The Hurricanes caused unprecedented economic and infrastructure damages disrupting the daily lives of 3.4 million of residents, including housing, infrastructure, environment, safety, health and social services, and government and municipal operations. The response to the catastrophe by the U.S, and

Federal agencies has become one of the largest and most complex disaster recovery efforts in U.S. history. The eye of Hurricane Irma, a powerful Category 5 storm, skirts north of San Juan, Puerto Rico experiences a deluge and 100-mile-per-hour gusts but is avoids the worst of the storm's effects. Irma kills four people. It cuts off power to about two-thirds of the island's electricity customers, and about 34 percent of its population loses access to water.

María was the most devastating hurricane to hit Puerto Rico in nearly a century. Many lives were lost, homes and businesses suffered enormous damage, most crops and other agricultural assets were wiped out, and a significant part of the island's infrastructure was severely damaged: knocked out electric power across the entire island and triggered heavy flooding after estimated 30 inches of rain, severe destruction of the housing infrastructure, commercial and public buildings damaged and devastated agriculture and tourism. After María, only 5% of cell service, 44% of potable water since there are no electric power, and gas stations are destroyed in 60%. Puerto Rico authorities have estimated in \$94 billion to cover damages from insurances and assignments required from the Congress, part of which was approved by them.

Following the hurricanes, the initial job losses in Puerto Rico totaled about 4%, though employment is beginning to improve somewhat. This loss is considerably steeper than what has typically been experienced after most major natural disasters that have hit the United States. That being said, domestic air passenger data suggest that from September through November more than 150,000 people left Puerto Rico, net of arrivals. Looking ahead, recovery will be affected by a variety of factors, most notably the degree of out-migration, the level of external aid the economy receives, and the effectiveness of fiscal and other reforms in Puerto Rico.

Given the effects of this natural disaster on commercial activity in Aguas Buenas, both the Municipal Administration and the Central Government have implemented measures to support entrepreneurs, recognizing that a large percentage of them are not in a position to comply with the payment of taxes and other obligations to the government. These measures include the granting of waivers, payment plans, extensions and exemptions in some lines of taxes. Conversely, Central Government measures have also been implemented to support consumers. These include exempting small and medium merchants from the collection and payment of the sales and use tax, as well as the sale of prepared foods.

Measures taken by the Central Government, although may facilitate the process of recovery of employers and consumers of our City, represent a considerable reduction in municipal revenues.

PROMESA

The Oversight Board approved on April 19, 2018 the New Fiscal Plan as prepared by the Oversight Board and not the Commonwealth submitted plan. With the New Fiscal Plan, the municipalities will receive the subsidy that will be amortized until fiscal year 2024 instead of eliminating it in fiscal year 2019. The scope of the Fiscal Plan is described in that Note.

In preparing these financial statements, the Municipality has evaluated significant transactions for potential recognition or disclosure through August 30, 2018, the date the financial statements were issued. Based on such analysis, no additional transaction needs to be recorded or disclosed.

MUNICIPALITY OF AGUAS BUENAS
Budgetary Comparison Schedule - General Fund
For the year ended June 30, 2017

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts Budgetary Basis (See Note 1)	Final Budget- Positive (Negative)
REVENUES:				
Property taxes	\$ 1,722,357	\$ 1,722,357	\$ 1,722,358	\$ 1
Municipal license tax	692,000	692,000	656,401	(35,599)
Licenses, permits and other local taxes	238,216	238,216	73,663	(164,553)
Charges for services	252,292	252,292	110,388	(141,904)
Interest, fines and penalties	90,000	90,000	14,729	(75,271)
Intergovernmental	5,601,151	5,601,151	5,639,900	38,749
Other	868,709	868,709	221,329	(647,380)
Total revenues	<u>9,464,725</u>	<u>9,464,725</u>	<u>8,438,768</u>	<u>(1,025,957)</u>
EXPENDITURES:				
General government	5,674,306	5,674,306	4,105,572	1,568,734
Public safety	399,651	399,651	338,344	61,307
Public works	2,501,684	2,501,684	1,979,914	521,770
Culture and recreation	889,084	889,084	724,414	164,670
Economic development	-	-	370,042	(370,042)
Urban Development	-	-	152,659	(152,659)
Total expenditures	<u>9,464,725</u>	<u>9,464,725</u>	<u>7,670,945</u>	<u>1,793,780</u>
EXCES OF REVENUES OVER EXPENDITURES	<u>-</u>	<u>-</u>	<u>\$ 767,823</u>	<u>\$ 767,823</u>

Explanation of differences:

Sources/inflows of resources

Actual amounts (budgetary basis) "available for appropriation" from the
Total revenues as reported on the statement of revenues, expenditures, and
changes in fund balances.

\$ 8,438,768

Uses/outflows of resources

Actual amounts (budgetary basis) "total charges to appropriations" from the
budgetary comparison schedule.

\$ 7,670,945

See notes to budgetary comparison schedule

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS**

Notes to 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, 2017 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2017.

**Housing
Choice
Voucher
(CFDA 14.871)**

<u>Line Item #</u>	<u>BALANCE SHEET</u>		
Assets	Current Assets Cash:		
111	Cash — Unrestricted	\$	123,580
113	Cash — Other restricted		9,866
100	Total Cash		<u>133,446</u>
150	Total Current Assets		<u>133,446</u>
Non-Current Assets	Fixed Assets:		
164	Furniture, Equipment & Machinery - Administration		16,256
166	Accumulated Depreciation		(15,585)
160	Total Capital Assets, Net of Accumulated Depreciation		<u>671</u>
180	Total Non-Current Assets		671
290	Total Assets and Deferred Outflow of Resources	\$	<u><u>134,117</u></u>
Liabilities and Equity	Liabilities		
	Current Liabilities:		
312	Accounts Payable <= 90 days		11,394
333	Accounts Payable — Other Government		26,625
310	Total Current Liabilities		<u>38,019</u>
300	Total Liabilities		38,019
Equity	Equity		
508.4	Net Investment in Capital Assets	\$	671
511.1	Restricted Net Position		6,032
512.1	Unrestricted Net Position		89,395
513	Total Equity — Net Position		<u><u>96,098</u></u>
600	Total Liab., Def. Inflow of Res., and Equity — Position	\$	<u><u>134,117</u></u>

See notes to the Financial Data Schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS

Financial Data Schedule
Income Statement
June 30, 2017

<u>Line Item #</u>	<u>INCOME STATEMENT</u>	<u>Housing Choice Voucher (CFDA 14.871)</u>
70600	HUD PHA Operating Grants	\$ 949,378
71100	Investment Income - Unrestricted	219
71500	Other Revenue	15,014
72000	Investment Income - restricted	51
70000	Total Revenue	<u>964,662</u>
	Expenses	
	Administrative:	
91100	Administrative Salaries	64,039
91200	Auditing Fees	2,930
91500	Employee Benefit Contributions — Administrative	10,152
91000	Total Operating - Administrative	<u>77,121</u>
96200	Other General Expenses	15,952
96000	Total Other General Expenses	<u>15,952</u>
96900	Total Operating Expenses	<u>93,073</u>
97000	Excess of Operating Revenue over Operating Expenses	<u>871,589</u>
97300	Housing Assistance Payments	845,396
97350	HAP Portability-In	10,083
97400	Depreciation Expense	1,986
		<u>857,465</u>
90000	Total Expenses	950,538
10000	Excess (Deficiency) of total revenues Over (Under) Total Expenses	<u>\$ 14,124</u>
	Memo Account Information:	
*11030	Beginning Equity	\$ 81,974
11040	Prior Period Adjustments, Equity Transfers and Correction of	-
*11170	Administrative Fee Equity	\$ 90,066
*11180	Housing Assistance Payments Equity	\$ 6,032
*11190	Unit Months Available	161
*11210	Number of Unit Months Available	142

See notes to the Financial Data Schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS

Notes to Financial Data Schedules
June 30, 2017

1. GENERAL

The accompanying Financial Data Schedules (FDS) includes the Section 8 Housing Choice Vouchers Program activities of the Autonomous Municipality of Aguas Buenas (Municipality). The information in the FDS is presented in accordance with the requirements of HUD's Uniform Financial Reporting Standards for HUD Housing Programs. Because the FDS presents only a selected portion of the operations of Municipality, it is not intended to and does not present the financial position or change in net position of the Municipality.

Therefore, some amounts presented in this Schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements. The Municipality reporting entity is defined in Note (1) (A) to the basic financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Assets, Liabilities, Net Assets, Revenues and Expenses reported on the FDS, are reported on the full accrual basis of accounting. They are recognized following the HUD's Uniform Financial Reporting Standards for HUD Housing Programs.

3. RELATIONSHIP TO BASIC FINANCIAL STATEMENTS

Assets, Liabilities and Net Assets/Position are presented in the Municipality's Statement of Net Position. Revenues and Expenses are reported in the Statement of Activities.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS
Schedule of Expenditures of Federal Awards
For the year ended June 30, 2017

FEDERAL GRANTOR/PASS THROUGH GRANTOR PROGRAM TITLE	FEDERAL CFDA NUMBER	Pass-Through Entity Identifying Number	2017 EXPENDITURES
US DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT			
Direct Programs:			
Housing Choice Voucher	14.871		935,854
Supportive Housing Program	14.235		52,623
Indirect Programs:			
Passed through P.R. Office of Municipal Affairs			
State Block Grant Program	14.228	N/A	<u>520,640</u>
Total US Department of Housing and Urban Development			<u>1,509,117</u>
US DEPARTMENT OF HEALTH AND HUMAN SERVICES			
Indirect Programs:			
Passed through P.R. Office of Municipal Affairs			
Child Care and Development Grant Program	93.575	N/A	<u>401,207</u>
Total US Department of Health and Human Services			<u>401,207</u>
US DEPARTMENT OF AGRICULTURE			
Indirect Program:			
Passed through PR Department of Education			
Child and Adult Food Program	10.558	N/A	<u>76,380</u>
TOTAL FEDERAL FINANCIAL ASSISTANCE			<u>\$ 1,986,704</u>

See notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS**

Notes to the Schedule of Expenditures of Federal Awards
June 30, 2017

NOTE 1 – BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Aguas Buenas and is presented on the modified accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. 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 Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance).

NOTE 2 – RELATIONSHIP TO BASIC FINANCIAL STATEMENTS

A reconciliation of total expenditures related to federal programs included in the statement of revenues, expenditures, and changes in fund balances – governmental funds to total expenditures included in the schedule of expenditures of federal awards is as follows:

Special Revenue and State and Federal Grants	\$ 6,878,019
Less:	
State Grants	<u>(4,891,315)</u>
Total expenditures in schedule of expenditures of federal awards	<u><u>\$ 1,986,704</u></u>

NOTE 3 - FEDERAL CFDA NUMBER

The CFDA number included in this schedule were determined based on the program name, review of grant contract information and the Office of Management and Budget's Catalog of Federal Domestic Assistance.

State or local government redistributions of federal awards to the Municipality, known as “pass-through awards”, should be treated by the Municipality as though they were received directly from the federal government. The Uniform Guidance requires the schedule to include the name of the pass-through entity and the identifying number assigned by the pass-through entity for the federal awards received as a sub recipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

NOTE 4 – INDIRECT COST RATE

The Municipality elected not to use the ten (10) percent of the minimum indirect cost rate allowed under the Uniform Guidance.



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 Honorable Mayor and
Municipality Legislative Body
Municipality of Aguas Buenas
Aguas Buenas, Puerto Rico

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Municipality of Aguas Buenas, Puerto Rico, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise Municipality of Aguas Buenas, Puerto Rico's basic financial statements, and have issued our report thereon dated August 30, 2018. Other auditors audited the financial statements of Espiritu Santo Project, as described in our report on Municipality of Aguas Buenas, Puerto Rico's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting of compliance and other matters that are reported on separately by those auditors.

Going Concern

The Municipality is an instrumentality of the Commonwealth of Puerto Rico (Commonwealth). Our report on the basic financial statements includes an emphasis-of-matter paragraph describing conditions, discussed in Note 12 to the basic financial statements, that raised substantial doubt about the Commonwealth of Puerto Rico's ability to continue as a going concern.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered Municipality of Aguas Buenas, Puerto Rico'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 Municipality of Aguas Buenas, Puerto Rico's internal control. Accordingly, we do not express an opinion on the effectiveness of Municipality of Aguas Buenas, Puerto Rico's internal control.

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. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Municipality of Aguas Buenas, Puerto Rico'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 is described in the accompanying schedule of findings and questioned cost as item 2017-001.

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.

Guzman Castro & Co., C.P.A.'s P.R.C.

CERTIFIED PUBLIC ACCOUNTANTS

San Juan, Puerto Rico

August 30, 2018

Stamp # E358443 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the original of this report

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

To Honorable Mayor and
Municipality Legislative Body
Municipality of Aguas Buenas
Aguas Buenas, Puerto Rico

Report on Compliance for Each Major Federal Program

We have audited Autonomous Municipality of **Aguas Buenas of the Commonwealth of Puerto Rico (Municipality)**'s **compliance** with the types of compliance requirements described in the *OMB Compliance Supplement* that could have direct and material effect on each of **Municipality's** major federal programs for the year ended June 30, 2017. **Municipality's** major federal programs are identified in the Summary of Auditor's Results Section of the accompanying Schedule of Findings and Questioned Costs.

Going Concern

The Municipality is an instrumentality of the Commonwealth of Puerto Rico (Commonwealth). Our report on the basic financial statements includes an emphasis-of-matter paragraph describing conditions, discussed in Note 12 to the basic financial statements, that raised substantial doubt about the Commonwealth of Puerto Rico's ability to continue as a going concern.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of **Municipality's** major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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'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 qualified and unmodified opinions on compliance for major federal programs. However, our audit does not provide a legal determination of **Municipality's** compliance.

Basis for Qualified Opinion

As described in the accompanying schedule of findings and questioned costs, **Municipality** did not comply with requirements regarding the following:

<u>Finding #</u>	<u>CFDA #</u>	<u>Program (or Cluster) Name</u>	<u>Compliance Requirement</u>
2017-002	14.871	Section 8 Housing Choice Vouchers Program	Eligibility
2017-003	14.871	Section 8 Housing Choice Vouchers Program	Reporting
2017-004	14.871	Section 8 Housing Choice Vouchers Program	Special Test and Provisions
2017-005	14.871	Section 8 Housing Choice Vouchers Program	Special Test and Provisions
2017-006	14.871	Section 8 Housing Choice Vouchers Program	Special Test and Provisions

Compliance with such requirements is necessary, in our opinion, for **Municipality** to comply with the requirements applicable to that program.

Qualified Opinion

In our opinion, except for the noncompliance described in the “Basis for Qualified Opinion” paragraph, **Municipality** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the major federal program for the year ended June 30, 2017.

Other Matters

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

Report on Internal Control over Compliance

Management of **Municipality** is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered **Municipality**’s internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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**’s internal control over compliance.

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

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 a 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 2017-002 through 2017-006 to be material weaknesses.

Municipality'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'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 the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Guzman Castro & Co., C.P.A.'s P.H.

CERTIFIED PUBLIC ACCOUNTANTS

San Juan, Puerto Rico

August 30, 2018

Stamp # E358444 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the original of this report

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF AGUAS BUENAS**

Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2017

SECTION 1 - SUMMARY OF AUDITORS' RESULTS

FINANCIAL STATEMENTS:

Type of auditors' report issued:

Governmental activities	<u>Qualified</u>
Governmental funds	<u>Qualified</u>

Internal control over financial reporting:

Material weakness(es) identified? x yes no

Significant deficiency(ies) identified that are not considered to be material weakness(es)? x yes none reported

Noncompliance material to financial statement noted? x yes no

FEDERAL AWARDS:

Internal control over major programs:

Material weakness(es) identified? x yes no

Significant deficiency(ies) identified that are not considered to be material weakness(es)? x yes none reported

Type of auditors' report issued on compliance for major programs:

Qualified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?

 x yes no

IDENTIFICATION OF MAJOR PROGRAM:

<u>Name of Federal Program</u>	<u>CFDA No.</u>
Section 8 Housing Choice Vouchers	14.871

Dollar threshold used to distinguish between type A and type B programs:

\$ 750,000

Auditee qualified as low-risk auditee?

 yes x no

SECTION 2 – FINANCIAL STATEMENT FINDINGS

Reference Number: 2017-001

Requirement: Operating deficit of general fund

Type: Significant deficiency in internal control, Noncompliance

This finding is similar to prior year finding (s) 2016-001

Condition:

The Municipality closed its fiscal year ended on June 30, 2017 with a deficit in the general fund of \$387,266.

Criteria:

In accordance with the Guide for the Administration of Municipalities Chapter IV, Section 19, the Finance Director has the responsibility of overseeing financial operations to prevent deficits in any municipal fund.

Article 8.004 (b) of Law 81 of Autonomous Municipalities establishes that the Municipality cannot obligate or spend funds more than the ensuing fiscal year. No amount shall be expended or obligated in a given fiscal year if exceeds its budgeted or authorized amounts by the Municipal Legislation.

Effect:

The Municipality did not comply with the Article 8.004 (b) of Law 81 of Autonomous Municipalities.

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.

Cause:

The overstatement of estimated revenues accounts in prior years caused that the Municipality operated with a deficit.

Recommendation:

The Municipality should continue its effort by revising and amending the budget as current information related to collections of budgeted revenues becomes available resources.

Questioned Costs

None

Reference Number: 2017-002

Agencies: U.S. Department of Housing and Urban Development

Programs: Section 8 Housing Choice Vouchers

CFDA Numbers: 14.871

Regulation Requirement: Eligibility for Individuals

Type: Internal Control and Compliance

Condition

We have performed an eligibility test for twenty-three (23) participant's files and noted the following exceptions:

1. In four files examined did not include Nutrition Assistance Program (NAP) certification.
2. In one file examined did not include evidence of Family Child Support (ASUME) Certification or Father Child Support Certification.
3. In three files examined did not include evidence Temporary Assistance Need Family (TANF) certification.
4. In six files examined did not include evidence of Enterprise Income Verification (EIV).
5. In one file examined did not include evidence of Family Photo.
6. In two files examined family photography not updated.
7. In two files examined did not include evidence tenant school enrollment certification.
8. In one file examined missing one tenant school enrollment certification.
9. In one file examined the married or divorce certification was missing in the file.
10. In one file examined missing non-debt certification Puerto Rico Aqueduct & Sewer Authority.
11. In one file examined missing non-debt certification Puerto Rico Electric Power Authority.
12. In three files examined missing birth certificate of some family members.
13. In one case Authorization to Release Information was missing in the file.
14. In one file examined Authorization to Release Information, not signed by tenant.
15. In one file examined Authorization to Release Information, not signed by tenant's spouse.
16. In one file examined we noted that the Authorization for Release of Information/Privacy Act Notice did not have the signature for all family members of 18 years old and up.
17. In six files examined missing date Authorization to Release Information.
18. In four cases the Form – 52675, Debts Owed to Public Housing Agencies and Termination was missing in the file.
19. In four files examined missing date on Form HUD – 52675, Debts Owed to Public Housing Agencies and Termination.
20. In seven files examined missing "Formulario Evaluación Record Criminal sobre Delitos Sexuales y/o Abuso de Menores".
21. In five files examined missing date in "Formulario Evaluación Record Criminal sobre Delitos Sexuales y/o Abuso de Menores".

Criteria

24 CFR Subpart K Section 982.516, *PHA responsibility for reexamination and verification* (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 of the following factors, or must document in the tenant file why third party verification was not available: (i) Reported family annual income; (ii) The Value of Assets, (iii) Expenses related to deduction from annual income; and (iv) Other factors that affect the determination of adjusted income.

24 CFR Subpart F, Section 5.611, established adjusted income and deduction federal regulation. 24 CFR Subpart E, Section 982.201, *Eligibility and Targeting*. When applicant is eligible: *General*, the PHA may only admit an eligible family to the program. To be eligible, the applicant must be a "family;" must be income-eligible in accordance with paragraph (b) of this section and 24 CFR part 5, subpart F; must be a citizen or a no citizen who has eligible immigration status as determined in accordance with 24 CFR part 5, subpart E. 24 CFR Subpart B, Section 5.230, *Consent by assistance applicants and participants*.

Housing Choice Voucher Program Guidebook, Chapter 12, Section (12.4), *Reexamination Procedures*. The Housing Authority Administrative Plan for the Fiscal Year 2007, Section 3.2, *Eligibility Criteria*, Section 6.4, *Term of the Housing Choice Voucher*, Section 9.0, *Determination of Family Income*, Section 10.0, *Verification*, Section 11.0, *Rent and Housing Payment*, Section 14.0, *Recertification*, Section 17.0, *Termination of the Lease and Contract*.

Effect

The Municipality may be qualifying participants that do not meet the eligibility requirements established by federal program and could have an effect in the performance on SEMAP report.

Cause

The Programs' officers did not maintain organized files and may not have obtained required documentation to validate the participant's eligibility. In addition, **The Municipality** has no effective monitoring review process for the program internal quality control.

Recommendation

The Municipality should establish strengthen internal procedures for proper supervision over the eligibility qualification process to ensure compliance with the requirements established in the federal regulations and to obtain all the documentation required to maintain in the files evidence of program participants eligibility.

Questioned Cost

Could not be determined

Management Response

Refer to Grantee's Corrective Action Plan

Reference Number: 2017-003

Agencies: U.S. Department of Housing and Urban Development

Programs: Section 8 Housing Choice Vouchers

CFDA Numbers: 14.871

Regulation Requirement: Special Reporting

Type: Internal Control and Compliance

Condition

We have performed compliance test to twenty-three (23) participants' files, family report (HUD form 50058) and we noted the following exceptions:

1. In seven files examined, we noted that the Payment Standard reported in HUD's Form 50058 is incorrect. Therefore, the utilities reimbursement to tenant is incorrect.
2. Five files examined have incorrect the item 5i "Date of Last Annual HQS Inspection" and item 5h "Date of Unit Last Passed HQS Inspection" in HUD's Form 50058.

Criteria

24 CFR Subpart D Section 982.158 (a) establish that the PHA must maintain complete and accurate accounts and other records for the program in accordance with HUD requirements, in a manner that permits a speedy and effective audit. The records must be in the form required by HUD, including requirements governing computerized or electronic forms of record-keeping. The PHA must comply with the financial reporting requirements in CFR part 5, Subpart H. 24 CFR Subpart D Section 982.158 (b), establish that the PHA must furnish to HUD accounts and other record, reports, documents, and information, as required by HUD. For provisions on electronic transmission of required family data, see 24 CFR parts 908. 24 CFR Subpart D Section 982.158 (d), establish that the PHA must prepare a unit inspection report.

Effect

The Municipality could be exposed to noncompliance with the federal regulation as the result of the data processed in HUD Form-50058, Family Report and could have an effect in the performance on SEMAP report. In addition, errors in HUD Form-50058 income may result in incorrect adjusted annual income, total payment, tenant rent, and as a result, will also create incorrect HAP Payment.

Cause

The condition is the result of ineffective review procedures necessary to assure completeness of special report.

Recommendation

The Municipality should strengthen review procedures of the information recorded in HUD's Form-50058, Family Report.

Questioned Cost

Could not be determined.

Management Response

Refer to Grantee's Corrective Action Plan

Reference Number: 2017- 004

Agencies: U.S. Department of Housing and Urban Development

Programs: Section 8 Housing Choice Vouchers

CFDA Numbers: 14.871

Regulation Requirement: Special Test and Provisions – Reasonable Rent

Type: Internal Control and Compliance

Condition

We performed compliance test to twenty-three (23) participants' files and we noted the following exceptions:

1. In seven participant files examined, we noted that the Payment Standard that indicates the HUD's Form 50058 was incorrect according to the number of bedrooms on voucher and the Fair Market Value Table for the fiscal year 2016-2017.

Criteria

24 CFR Subpart B Section 982.54 (d) (15), establish that the PHA Administrative Plan must cover PHA policies on these subjects; the method of determining that the rent to owner is a reasonable rent (initially and during the term of a HPA contract). 24 CFR Subpart D Section 982.158 (f) (7), establish that the PHA must keep the following records to document the basis for PHA determination that rent to owner is a reasonable rent.

24 CFR, Subpart K, Section 982.503 (a), *Payment standard schedule*, (1) HUD publishes the fair market rents for each market area in the United States (see part 888 of this title). The PHA must adopt a payment standard schedule that establishes voucher payment standard amounts for each FMR area in the PHA jurisdiction. For each FMR area, the PHA must establish payment standard amounts for each "unit size." Unit size is measured by number of bedrooms (zero-bedroom, one-bedroom, and so on). (2) The payment standard amounts on the PHA schedule are used to calculate the monthly housing assistance payment for a family (§ 982.505). (3) The PHA voucher payment standard schedule shall establish a single payment standard amount for each unit size. For each unit size, the PHA may establish a single payment standard amount for the whole FMR area and or may establish a separate payment standard amount for each designated part of the FMR area.

24 CFR Subpart K Section 982.507 (4), establish that PHA determinate at all times during the assisted tenancy, the rent to owner may not exceed the reasonable rent as most recently determined or predetermined by the PHA.

Effect

The miscalculation can have an effect in the following: (1) total family share, (2) HAP to owner, (3) tenant rent to owner and, (4) utilities reimbursement to family (if apply) and could have an effect in the performance on SEMAP report.

Cause

The Municipality has no effective monitoring review process for the Payment Standard Payment applicable for the fiscal year and the Administrative Plan requirement for the payment standard and calculation to adequately determine the Reasonable Rent procedures during the reexamination process. In addition, the Program does not have an effective review over the documents required in the tenant file and in the evaluation of the Family Report (HUD – Form 50058)

Recommendation

The Municipality establishes review procedures to ascertain that the Payment Standard Payment applicable in the reexamination is computed correctly in accordance with federal regulation.

Questioned Cost

Could not be determined.

Management Response

Refer to Grantee's Corrective Action Plan

Reference Number: 2017- 005

Agencies: U.S. Department of Housing and Urban Development

Programs: Section 8 Housing Choice Vouchers

CFDA Numbers: 14.871

Regulation Requirement: Special Test and Provisions – Utility Allowance Schedule

Type: Internal Control and Compliance

Condition

We have performed utilities allowance test to twenty-three (23) participants' files and we noted the following exception:

1. In seven files examined the utility allowance calculated incorrectly in the Family Report (HUD Form – 50058).

Criteria

24 CFR, Subpart K, Section 982.517 (a), *Maintaining schedule*, (1) The PHA must maintain a utility allowance schedule for all tenant-paid utilities (except telephone), for cost of tenant-supplied refrigerators and ranges, and for other tenant-paid housing services (e.g., trash collection (disposal of waste and refuse)) (2) The PHA must give HUD a copy of the utility allowance schedule. At HUD's request, the PHA also must provide any information or procedures used in preparation of the schedule.

24 CFR, Subpart K, Section 982.517 (b), *How allowances are determined*, (1) The utility allowance schedule must be determined based on the typical cost of utilities and services paid by energy-conservative households that occupy housing of similar size and type in the same locality. In developing the schedule, the PHA must use normal patterns of consumption for the community as a whole and current utility rate. (2)(i) a PHA's utility allowance schedule, and the utility allowance for an individual family, must include the utilities and services that are necessary in the locality to provide housing that complies with the housing quality standards. However, the PHA may not provide any allowance for non-essential utility costs, such as costs of cable or satellite television. (ii) In the utility allowance schedule, the PHA must classify utilities and other housing services according to the following general categories: space heating; air conditioning; cooking; water heating; water; sewer; trash collection (disposal of waste and refuse); other electric; refrigerator (cost of tenant-supplied refrigerator); range (cost of tenant-supplied range); and other specified housing services.

The PHA must provide a utility allowance for tenant-paid air-conditioning costs if the majority of housing units in the market provide centrally air-conditioned units or there is appropriate wiring for tenant-installed air conditioners. (3) The cost of each utility and housing service category must be stated separately. For each of these categories, the utility allowance schedule must take into consideration unit size (by number of bedrooms), and unit types (e.g., apartment, row-house, town house, single-family detached, and manufactured housing) that are typical in the community. (4) The utility allowance schedule must be prepared and submitted in accordance with HUD requirements on the form prescribed by HUD.

Effect

The Municipality could be paying a utilities allowance to the participants incorrectly that could have an effect in the performance on SEMAP report.

Cause

The Program has no effective monitoring review process for the utility calculation to adequately determine the allowance that will be paid to the tenants. In addition, lack of effective supervision over the participant file to maintain all documents that support the utilities allowance.

Recommendation

The Municipality should establish review procedures to ascertain that tenant's utilities allowance are computed correctly in accordance with federal regulations.

Questioned Cost

Could not be determined.

Management Response

Refer to Grantee's Corrective Action Plan

Reference Number: 2017- 006

Agencies: U.S. Department of Housing and Urban Development

Programs: Section 8 Housing Choice Vouchers

CFDA Numbers: 14.871

Regulation Requirement: Special Test and Provision – HQS Enforcement

Type: Internal Control and Compliance

Condition

In testing the Housing Quality Standards Enforcement procedures, we examined five (5) inspection from HUD-52580 and we noted the following exceptions:

1. The inspection control list prepared by program and submitted to us was incomplete
2. In one file examined the inspection report was considered by the Inspector Office pass, however the unit had deficiencies/inconclusive that had to be repaired within 24 hours from the date of inspection report.
3. In one file examined did not have evidence that the unit was re-inspected.
4. In one case time elapsed between re-inspection and corrected deficiencies was more 30 days.
5. In two cases the inspection unit was considered by the Inspector Officer without deficiencies (pass), in the report prepared by program but the two inspections were failed.

Criteria

24 CFR, Subpart D, Section 982.158 (d), The PHA must prepare a unit inspection report.

24 CFR Subpart I, Section 982.404 (a), *Owner Obligation*. (1) The owner must maintain the unit in accordance with HQS. (2) If the owner fails to maintain the dwelling unit in accordance with HQS, the PHA must take prompt and vigorous action to enforce the owner obligations. PHA remedies for such breach of the HQS include termination, suspension or reduction of housing assistance payments and termination of the HAP contract. (3) The PHA must not make any housing assistance payments for a dwelling unit that fails to meet the HQS, unless the owner corrects the defect within the period specified by the PHA and the PHA verifies the correction. If a defect is life threatening, the owner must correct the defect within no more than 24 hours. For other defects, the owner must correct the defect within no more than 30 calendar days (or any PHA approved extension). (4) The owner is not responsible for a breach of the HQS that is not caused by the owner, and for which the family is responsible (as provided in Sec. 982.404 (b) and

Sec. 982.551 (c)). (However, the PHA may terminate assistance to a family because of HQS breach caused by the family.)

24 CFR Subpart I, Section 982.404 (b), *Family Obligation*. (1) The family is responsible for a breach of

the HQS that is caused by any of the following: (2) If an HQS breach caused by the family is life threatening, the family must correct the defect within no more than 24 hours. For other family-caused defects, the family must correct the defect within no more than 30 calendar days (or any PHA-approved extension). (3) If the family has caused a Breach of the HQS, the PHA must take prompt and vigorous action to enforce the family obligations. The PHA may terminate assistance for the family in accordance with Section 982.552.

24 CFR Subpart I Section 982.405, (a) The PHA must inspect the unit leased to a family prior to the initial term of the lease, at least annually during assisted occupancy, and at other times as needed, to determine if the unit meets the HQS. (See Sec. 982.305(b)(2) concerning timing of initial inspection by the PHA.). (b) The PHA must conduct supervisory quality control HQS inspections. (c) In scheduling inspections, the PHA must consider complaints and any other information brought to the attention of the PHA. (d) The PHA must notify the owner of defects shown by the inspection. (e) The PHA may not charge the family or owner for initial inspection or re-inspection of the unit.

Effect

The Municipality made housing assistance payment for units that did not meet housing quality standards that could have an effect in the performance on SEMAP report. Inadequate control over HQS Enforcement and HUD requirement could reduce or recapture Section 8 Voucher funds.

Cause

The Municipality did not implement and maintain adequate internal controls to ensure that housing quality inspection enforcement met HUD requirements.

Recommendation

The Municipality require the authority to inspect the units that did not meet minimum housing quality standard to verify that the owner and the tenant took appropriate corrective actions to make the unit repairs, if appropriate actions were not taken, **The Municipality** should abate the rents or terminate the housing assistance payment contract. **The Municipality** needs to implement internal controls and perform quality controls which ensure that units are inspected in a timely manner and inspections are accordance with its administrative plan and HUD requirement and should strengthen its monitoring procedures and internal control to take immediate action over the use of federal funds as required by federal regulations.

Questioned Cost

Could not be determined.

Management Response

Refer to Grantee's Corrective Action Plan



**GOBIERNO DE PUERTO RICO
MUNICIPIO AUTÓNOMO DE AGUAS BUENAS**

Honorable Javier García Pérez
Alcalde

SCHEDULE OF STATUS OF PRIOR YEAR AUDIT FINDINGS AND QUESTIONED COSTS

Audit Report: Reports on Compliance and Internal Control in Accordance with Governmental Auditing Standards and OMB Super Circular Uniform Guidance

Audit Period: June 30, 2017 – Fiscal Year 2016-2017

Principal Executive: Hon. Javier Garcia Perez

Contact Person: Sr. Juan Ortiz Rivera (Finance Director)

Phone: (787) 732-8621

Finding Number	Finding	Condition	Actions for Finding not Corrected or Partially Corrected	Questioned Costs	Status
2016-01	Deficit of General Fund	The Municipality closed it's fiscal year ended June 30, 2016 with a fund deficit, before providing reserves in the general fund of \$742,113.	The Municipality's Management concurs with the auditor's recommendation.	None	Not resolved yet. See current finding 2017-001.

I CERTIFY THAT THE INFORMATION ABOVE IS CORRECT

Hon. Javier Garcia Perez

Date



Honorable Javier García Pérez
Alcalde

CORRECTIVE ACTION PLAN

Audit Report: Reports on Compliance and Internal Control in Accordance with Governmental Auditing Standards and OMB Super Circular Uniform Guidance

Audit Period: June 30, 2017 – Fiscal Year 2016-2017

Principal Executive: Hon. Javier Garcia Perez

Contact Person: Sr. Juan Ortiz Rivera (Finance Director)

Phone: (787) 732-8621

Finding Number	Finding	Statement of Concurrence or Non-Concurrence	Corrective Action
2017-001	Operating deficit of General Fund	We concur with the finding	The Municipal Financial Team continues evaluating additional alternatives to decrease expenditures and increase revenues to avoid deficits in the current and future budgets and to reduce the accumulated deficit. Implementation Date: Effective Fiscal Year 2017-2018 Responsible Person: Mr. Juan Ortiz Rivera, Finance Director
2017-002	Eligibility for Individuals	We concur with the finding	The Municipality reviewed the Quality Control Sheets for each file where the documents will be verified before recertification process and after signing the contract.

Honorable Javier García Pérez
Alcalde

Finding Number	Finding	Statement of Concurrence or Non-Concurrence	Corrective Action
			Implementation Date: Effective Fiscal Year 2017-2018 Responsible Person: Elsa M Velazquez, Officer Worker Rafael E Mejias, Administrative Assistance Yaitza E Mendes Ortiz, Housing Director
2017-003	Special Reporting	We concur with the finding	The Revision of the document will be done in the first part of the Quality Control. Implementation Date: Effective Fiscal Year 2017-2018 Responsible Person: Elsa M Velazquez, Officer Worker Rafael E Mejias, Administrative Assistance Yaitza E Mendes Ortiz, Housing Director
2017-004	Special Tests and Provisions: Reasonable Rent	Non-Concurrence	HUD's regulations indicate that the payment standards and utilities allowances are based on the rooms per voucher not by rooms on the unit.
2017-005	Special Tests and Provisions: Utility Allowances Schedule	Non-Concurrence	HUD's regulations indicate that the payment standards and utilities allowances are based on the rooms per voucher not by rooms on the unit.
2017-006	Special Tests and Provisions: HQS Enforcement	We concur with the finding	The inspection control table was revised, where the different types of indicators are detailed.



**GOBIERNO DE PUERTO RICO
MUNICIPIO AUTÓNOMO DE AGUAS BUENAS**

Honorable Javier García Pérez
Alcalde

Finding Number	Finding	Statement of Concurrence or Non-Concurrence	Corrective Action
			Implementation Date: Effective Fiscal Year 2017-2018 Responsible Person: Nydis I Diaz Reyes Yaitza E Mendes Ortiz, Housing Director

I CERTIFY THAT THE INFORMATION ABOVE IS CORRECT

Hon. Javier Garcia Perez

Date