

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO**

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2011

Forres Rompart, Sanchez Ruiz LLP

Certified Public Accountants and Business Consultants

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SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

CORRECTIVE ACTION PLAN



Torres Llompart, Sánchez Ruiz LLP

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Honorable Secretary of the
Department of Housing of the
Commonwealth of Puerto Rico
San Juan, Puerto Rico

Members of:

Division of CPA Firms
American Institute Certified Public Accountants
New York State Society of Certified Public Accountants
Puerto Rico State Society of Certified Public Accountants
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INDEPENDENT AUDITORS' REPORT

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major funds and the aggregate remaining fund information of the Department of Housing of the Commonwealth of Puerto Rico (PRDH), as of and for the year ended June 30, 2011, which collectively comprise the PRDH's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the PRDH's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The PRDH does not maintain adequate records for the inventory of housing units and land lots held for sale of the business-type activities and we were unable to satisfy ourselves about such balances through alternate procedures. Therefore, we were not able to obtain sufficient evidence to satisfy ourselves on the amounts reported as housing units and land lots held for sale which have a balance of \$42,955,051 as of June 30, 2011, in the accompanying statement of net assets.

In our opinion, except for the effects of any adjustments and additional disclosures that might have resulted had management furnished us with reasonably accurate data regarding the inventory of housing units and land lots held for sale, the balances and the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities and the business-type activities of the PRDH as of June 30, 2011, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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Honorable Secretary of the
Department of Housing of the
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San Juan, Puerto Rico

INDEPENDENT AUDITORS' REPORT (CONTINUED)

In addition, in our opinion, the financial statements referred to previously present fairly in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the PRDH of the Commonwealth of Puerto Rico as of June 30, 2011, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, and schedule of budgetary comparison on pages 4 through 17 and 53 to 54, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government 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 supplemental information in accordance with auditing standards generally accepted in the United States of America, which consisted principally 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 of the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

As discussed in Note A, the financial statements of the PRDH are intended to present the financial position and changes in financial position of only that portion of the governmental activities of the Commonwealth of Puerto Rico attributable to the transactions of the PRDH. They do not purport to, and do not, present fairly the financial position and changes in financial position of the Commonwealth of Puerto Rico in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards* we have also issued our report dated January 13, 2012, on our consideration of the PRDH's internal control over financial reporting and on our test of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Torres Blomquist, Sánchez Ruiz LLP

Certified Public Accountants and Business Consultants

Honorable Secretary of the
Department of Housing of the
Commonwealth of Puerto Rico
San Juan, Puerto Rico

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Our audit was conducted for the purpose of forming an opinion on the PRDH's financial statements as a whole. The accompanying schedule of expenditures of federal awards on pages 55 and 56 is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements of the PRDH. Such information is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements itself, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements taken as a whole.

Torres Blompart, Sánchez Ruiz LLP

January 13, 2012
License No. 221
San Juan, Puerto Rico

The stamp number 2633445 was
affixed to the original of this report.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

This section presents a narrative overview and analysis of the financial performance of the Department of Housing of the Commonwealth of Puerto Rico (the PRDH) as of and for the year ended June 30, 2011. The information presented here should be read in conjunction with the basic financial statements, including the notes thereto.

1. Financial Highlights Government-wide:

- Total assets increased from \$359 million in fiscal year 2010 to \$368 million at June 30, 2011, representing an increase of approximately \$9 million or (3%) in comparison with prior year.
- Total liabilities decreased from \$92 million in fiscal year 2010 to \$61 million at June 30, 2011, representing a decrease of approximately \$31 million or (34%) in comparison with prior year.
- Net assets grew from \$267 million in fiscal year 2010 to \$307 million at June 30, 2011, representing an increase of \$40 million or 15% in comparison with prior year.
- Change in net assets increased from \$16 million to \$40 million, representing an increase of approximately \$24 million or (151%) when compared to prior year.

2. Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the PRDH's basic financial statements. The PRDH's basic financial statements include three components: (1) government -wide financial statements, (2) fund financial statements, and (3) notes to the basic financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

Basic financial statements

The basic financial statements include two kinds of financial statements that present different views of the PRDH: the government-wide financial statements and the fund financial statements. These financial statements also include the notes to the basic financial statements that explain some of the information in the financial statements and provide more details.

Government – wide financial statements

The government-wide financial statements provide a broad view of the PRDH's operations in a manner similar to a private sector business. The financial statements provide both short and long-term information about the PRDH's financial position, which assists the PRDH in assessing the PRDH's economic condition at the end of the fiscal year. These are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means they follow methods that are similar to those used by most business. They take into account all revenue and expenses connected with the fiscal year even if cash involved has not been received or paid. The government -wide financial statements include two statements:

- **Statement of net assets** - presents all the PRDH's assets and liabilities with the difference between the two reported as net assets. Through times, increases or decreases in the PRDH net assets may serve as a useful indicator of whether the financial position of the PRDH is improving or deteriorating.
- **Statement of activities** - presents information showing how the PRDH's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the time of related cash flows. Thus, revenue and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenue for each function of the PRDH.

Both of these financial statements present the governmental activities of the PRDH. The government -wide financial statements can be found immediately following this discussion and analysis.

**DEPARTMENT OF HOUSING OF THE
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MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

Fund financial statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The PRDH, like other local governments, uses fund accounting to ensure and demonstrate compliance with finance - related legal requirements. The fund financial statements focus on individual parts of the PRDH governmental funds, reporting the PRDH's operations in more detail in the government - wide financial statements. All of the funds of the PRDH can be divided into two categories. It is important to note that these fund categories use different accounting approaches and should be interpreted differently. The two categories of funds are the following:

- **Governmental fund financial statements** – Governmental fund are used to account for essentially the same activities reported in the government - wide financial statements. However, unlike the government - wide financial statements, the governmental fund financial statements focus on near - term inflows and outflows of expendable resources.

They also focus on the balances of expendable resources available at the end of the fiscal year. Such information may be useful in evaluating the governments near - term financing requirements. This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short - term view of the PRDH's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the PRDH. Because the focus of the governmental funds is narrower than that of the government - wide financial statements, it is useful to compare the information presented for governmental fund with similar information presented for governmental activities in the government - wide financial statements. By doing so, readers may better understand the long-term impact of the government's near - term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between governmental fund and the governmental activities. These reconciliations are presented on the page immediately following each governmental fund financial statement.

The PRDH has one major governmental fund. That is, a major fund is presented in a separate column in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balances. The PRDH's major governmental fund is the general fund. The basic governmental funds financial statements can be found immediately following the government - wide financial statements.

DEPARTMENT OF HOUSING OF THE
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MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011

Fund financial statements (continued)

- **Proprietary fund financial statements:** The only proprietary fund operated by the PRDH is the Office for the Administration of Assets of the Corporation for Urban Housing Renovation (the CRUV) operation. The accounting used for proprietary funds is the accrual basis of accounting. The PRDH's proprietary fund record interest income from mortgage receivables and gain or losses from the sale of assets.
- **Fiduciary fund financial statements:** Fiduciary funds are not reflected in the government - wide financial statements because the resources of these funds are not available to support the PRDH's own activities. The accounting used for fiduciary funds is much like that used for proprietary funds.

The fiduciary funds present the following funds:

Ponce en Marcha

By law No. 206 of August 28, 2003, the Department of Justice of the Commonwealth of Puerto Rico obtained a line of credit of \$90 million with the purpose of complying with a judicial settlement in the case of the Municipality of Ponce vs. the Puerto Rico Highway Authority and others. In relation with such settlement, the PRDH is the fiscal agent of the funds for planning and development of several Municipality of Ponce projects. The restricted cash balance is \$1,505,107 at June 30, 2011 and is presented in the statement of fiduciary net assets.

Special Communities

The PRDH is responsible for receiving and distributing funds assigned by the Perpetual Trust Fund for Special Communities for the Development Program (the Program). The Program was established by Act No. 271 of November 21, 2002, and is funded through legislative appropriations and other grants. Program funds are distributed to the services providers based on the contracts made with the Perpetual Trust Fund for Special Communities. The restricted cash balance is \$104,946 and due from \$747,539 at June 30, 2011, is presented in the statement of fiduciary net assets.

Remedy Fund

The Municipality of Juncos establish and funded a trust fund for the purpose of implementing the two remedies selected by the U.S. Environmental Protection Agency (EPA) for the old Juncos Landfill Superfund site as set forth in the EPA "Decision Summary" documents dated September 24, 1991, and October 5, 1993, as amended by EPA, to correct environmental damage left by the old Juncos Landfill. As part of these remedies the PRDH was appointed as the administrator agent of the Remedy Funds.

**DEPARTMENT OF HOUSING OF THE
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MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

Fund financial statements (continued)

Remedy Fund (continued)

As part of the settlement agreement the PRDH establish \$1.5 million as Remedy Fund for construction. The restricted cash balance is \$1,455,726 at June 30, 2011 and is presented in the statement of fiduciary net assets.

The statement of net assets in liquidation - proprietary fund, statement of changes in net assets in liquidation - proprietary fund, and the statement of fiduciary net assets can be found immediately following the governmental fund financial statements.

Notes to financial statements

The notes provide additional information that is essential to a full understanding of the data provided in the government - wide and the fund financial statements. The notes to the financial statements can be found immediately following funds financial statements.

1. Government-wide Financial Analysis Statement of Net Assets

- Total assets increased from \$359 million in June 30, 2010 to \$368 million at June 30, 2011, representing an increase of \$9 million or (3%) in comparison with prior year. Within assets, there is an increase of \$32 million in due from related entity due to an accrual of the current year developer fees owed to the PRDH pursuant to the Partnership Agreement (see detail in Note G) and a decrease of \$26 million in the balances pending to be collected from HUD mainly due since July 1, 2010; HUD approved the transfer of the administration of HOME Investment Partnership Program (CFDA 14.239) from PRDH to the Puerto Rico Housing Financing Authority (PRHFA).
- Total liabilities decreased from \$92 million in June 30, 2010 to \$61 million at June 30, 2011, representing a decrease of \$31 million or (34%) in comparison with prior year. Within liabilities, there is a decrease of \$26 million in deferred revenues which relates to the HOME program as explain above. In the other hand, there is a decrease in accounts payable of \$8 million which relates to the elimination during the current year of the last year significant overdraft in the cash account of \$3 million and the decrease in general invoices pending to be paid as of year-end, in comparison with prior year.
- Out of the \$307 million in net assets, \$27 million are invested in capital assets, \$40 million are restricted for specific program initiatives and \$240 million are unrestricted on the use.

**DEPARTMENT OF HOUSING OF THE
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MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

1. Government-Wide Financial Analysis Statement of Net Assets (Continued):

ASSETS	Governmental Activities		Change	Percent
	<u>2011</u>	<u>2010</u>		
Current Assets				
Cash and cash equivalents	\$ 70,316,056	\$ 63,264,864	\$ 7,051,192	11%
Cash with fiscal agent	2,047,874	1,560,082	487,792	31%
Due from:				
Agency Fund	747,539	-	747,539	100%
Federal government (HUD)	6,514	25,834,120	(25,827,606)	-100%
Related entity, current portion	41,070,209	9,067,961	32,002,248	353%
Mortgages and accounts receivable	204,752	212,043	(7,291)	-3%
Interest receivable on note	11,128,504	13,356,839	(2,228,335)	-17%
Other accounts receivable and other assets	<u>3,432,294</u>	<u>553,581</u>	<u>2,878,713</u>	520%
Total current assets	<u>128,953,742</u>	<u>113,849,490</u>	<u>15,104,252</u>	13%
Capital Assets				
Furniture, equipment and vehicles	5,860,723	7,146,152	(1,285,429)	-18%
Parking and building	5,137,029	5,137,029	-	0%
Building	30,000,000	30,000,000	-	0%
Building Improvements	21,013,268	16,288,636	4,724,632	29%
Less accumulated depreciation	<u>(11,489,979)</u>	<u>(7,806,021)</u>	<u>(3,683,958)</u>	47%
	50,521,041	50,765,796	(244,755)	0%
Land	<u>793,717</u>	<u>983,700</u>	<u>(189,983)</u>	-19%
Total capital assets	<u>51,314,758</u>	<u>51,749,496</u>	<u>(434,738)</u>	-1%
Other Noncurrent Assets				
Note receivable from related entity, noncurrent portion	102,889,957	102,889,957	-	0%
Due from related entity, noncurrent portion	16,636,341	16,700,181	(63,840)	0%
Restricted deposit	5,775,050	14,824,319	(9,049,269)	-61%
Land lots held for sale or lease	42,996,466	39,322,151	3,674,315	9%
Restricted land lot	<u>19,200,000</u>	<u>19,200,000</u>	<u>-</u>	0%
Total other noncurrent assets	<u>187,497,814</u>	<u>192,936,608</u>	<u>(5,438,794)</u>	-3%
TOTAL ASSETS	<u>\$367,766,314</u>	<u>\$358,535,594</u>	<u>\$ 9,230,720</u>	3%

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

1. Government-wide Financial Analysis Statement of Net Assets (Continued):

LIABILITIES	Governmental Activities		Change	Percent
	<u>2011</u>	<u>2010</u>		
Current Liabilities				
Notes payable, current portion	\$ 12,242,772	\$ 13,640,090	(\$1,397,318)	-10%
Accounts payable	3,337,039	12,035,409	(8,698,370)	-72%
Accrued liabilities	4,314,507	3,973,686	340,821	9%
Due to Public Building Authority, current portion	-	186,552	(186,552)	-100%
Accrued legal claims, current portion	455,753	380,753	75,000	20%
Accrued compensated absences, current portion	3,157,580	3,153,260	4,320	0%
Voluntary termination benefits	1,140,288	-	1,140,288	100%
Deferred revenues	-	<u>25,836,886</u>	<u>(25,836,886)</u>	-100%
Total current liabilities	<u>24,647,939</u>	<u>59,206,636</u>	<u>(34,558,697)</u>	-58%
Noncurrent Liabilities				
Notes payable, noncurrent portion	22,171,304	24,317,566	(2,146,262)	-9%
Accrued:				
Legal claims, noncurrent portion	4,859,628	4,764,981	94,647	2%
Compensated absences, noncurrent portion	3,489,439	3,508,855	(19,416)	-1%
Voluntary termination benefits	<u>5,853,124</u>	<u>-</u>	<u>5,853,124</u>	100%
Total noncurrent liabilities	<u>36,373,495</u>	<u>32,591,402</u>	<u>3,782,093</u>	12%
Total Liabilities	<u>61,021,434</u>	<u>91,798,038</u>	<u>(30,776,604)</u>	-34%
NET ASSET				
Invested in capital assets, net of related debt	26,979,860	25,307,863	1,671,997	7%
Restricted	39,702,135	55,377,991	(15,675,856)	-28%
Unrestricted	<u>240,062,885</u>	<u>186,051,702</u>	<u>54,011,183</u>	29%
TOTAL NET ASSETS	<u>\$306,744,880</u>	<u>\$266,737,556</u>	<u>\$ 40,007,324</u>	15%

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

2. Government-wide Financial Analysis Statement of Activities

- Total net revenues of governmental activities changed from a net revenue of \$1,243,051 in fiscal year 2010 to a net revenue of \$4,554,088 during fiscal year ended on June 30, 2011, representing an increase in net revenues of \$3,311,037. Within governmental activities, tenant, utilities services and maintenance revenues decreased by \$1.8 million during the current fiscal year mostly related to a decrease in revenues obtained to conduct these services.
- General revenues increased during the current year by \$14 million, from \$21 million in fiscal year 2010 to \$35 million in the current fiscal year. This increase is mostly driven by a decrease in interest and investment income of \$10 million and an increase of management and developer fees of \$23 million.

For the year ended June 30, 2011 net assets changed as follows:

Function/Program	Net (Expenses) Revenues and Changes in Net Assets		Change	Percent
	<u>2011</u>	<u>2010</u>		
Governmental Activities				
General, administrative and others	\$ (985,345)	\$ (4,206,406)	\$3,221,061	-77%
Construction and rehabilitation	(1,833,249)	(3,025,573)	1,192,324	-39%
Child care and development	-	16,719	(16,719)	-100%
Tenants, utility services and maintenance	8,721,186	10,516,997	(1,795,811)	-17%
Interest expense	(904,976)	(869,038)	(35,938)	4%
Housing repairs and maintenance	<u>(443,528)</u>	<u>(1,189,648)</u>	<u>746,120</u>	-63%
Total Governmental Activities	<u>4,554,088</u>	<u>1,243,051</u>	<u>3,311,037</u>	266%
Business-type Activities				
General and administrative	(1,172,058)	(1,213,671)	41,613	-3%
Housing held for sale	<u>1,215,179</u>	<u>(5,419,338)</u>	<u>6,634,517</u>	-122%
Total Business-type Activities	<u>43,121</u>	<u>(6,633,009)</u>	<u>6,676,130</u>	-101%
	<u>4,597,209</u>	<u>(5,389,958)</u>	<u>9,987,167</u>	-185%

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
JUNE 30, 2011**

2. Government-wide Financial Analysis Statement of Activities (Continued)

	<u>Changes in Net Assets</u>		<u>Change</u>	<u>Percent</u>
	<u>2011</u>	<u>2010</u>		
General Revenues:				
Management and developer fees	32,038,026	9,131,801	22,906,225	251%
Interest and investment income	606,901	10,672,288	(10,065,387)	-94%
Other	<u>2,765,188</u>	<u>1,522,768</u>	<u>1,242,420</u>	82%
TOTAL GENERAL REVENUES	<u>35,410,115</u>	<u>21,326,857</u>	<u>14,083,258</u>	66%
CHANGES IN NET ASSETS	40,007,324	15,936,899	24,070,425	151%
NET ASSETS, BEGINNING	<u>266,737,556</u>	<u>250,800,657</u>	<u>15,936,899</u>	6%
NET ASSETS, ENDING	<u>\$306,744,880</u>	<u>\$266,737,556</u>	<u>\$40,007,324</u>	15%

3. Governmental Fund Results - Balance Sheet

- Total assets of the governmental fund increased by \$8 million. This increase is the net effect of an increase of \$35 million in other receivables due to an accrual of the current year developer fees owed to the PRDH amounting to \$32 million pursuant to the Partnership Agreement and a decrease of \$26 million in federal grant receivables which is caused mainly to HUD approval since July 1, 2010, the transfer of the administration of HOME Investment Partnership Program (CFDA 14.239) from PRDH to PRHFA.
- Total liabilities decreased by \$54 million in comparison with prior fiscal year as a result of the decrease in deferred revenues of \$45 million and the decrease in accounts payable by \$9 million.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
JUNE 30, 2011**

3. Governmental Fund Results - Balance Sheet (Continued)

	<u>2011</u> <u>Combined</u>	<u>2010</u> <u>Combined</u>	<u>Changes</u>	<u>Percent</u>
ASSETS				
Cash and cash equivalents	\$ 62,963,478	\$ 62,690,045	\$ 273,433	0%
Cash with fiscal agent	2,047,874	1,560,082	487,792	31%
Federal grant receivable	6,514	25,834,120	(25,827,606)	-100%
Note receivable – related	102,889,957	102,889,957	-	0%
Interest receivable on note	11,128,504	13,356,839	(2,228,335)	-17%
Due from Agency Fund	747,539	-	747,539	100%
Due from other funds	108,262	-	108,262	100%
Other receivables	61,138,844	26,229,259	34,909,585	133%
Other assets	-	92,464	(92,464)	-100%
Total Assets	<u>241,030,972</u>	<u>232,652,766</u>	<u>8,378,206</u>	4%
LIABILITIES				
Accounts payable and accrued Liabilities	3,016,011	11,603,306	(8,587,295)	-74%
Due to other funds	6,896,498	7,072,911	(176,413)	-2%
Deferred revenues	-	44,989,364	(44,989,364)	-100%
Total Liabilities	<u>9,912,509</u>	<u>63,665,581</u>	<u>(53,753,072)</u>	-84%
FUND BALANCE	<u>\$231,118,463</u>	<u>\$168,987,185</u>	<u>\$ 62,131,278</u>	37%

4. Governmental Fund Results Statement of Revenues, Expenditures and Changes in Fund Balances

- Total revenues increased by \$38 million which is mostly driven by the net effect of the recognition of management and developers fees income of \$41 million during the current year and a decrease of \$19 million in federal grants due to the elimination of HOME program.
- Total expenditures decreased by \$23 million when compared with prior fiscal year. The main driver of this fluctuation has to do with a decrease of \$20 million of housing, repairs and maintenance when compared with the prior fiscal year balance.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
JUNE 30, 2011**

4. Governmental Fund Results Statement of Revenues, Expenditures and Changes in Fund Balances (continued)

	<u>2011</u> <u>Combined</u>	<u>2010</u> <u>Combined</u>	<u>Changes</u>	<u>Percent</u>
REVENUES				
State appropriations	\$ 40,290,807	\$ 37,251,031	\$ 3,039,776	8%
Sale and lease of land lots	3,206,872	3,488,877	(282,005)	-8%
Rent revenues	4,443,000	5,258,055	(815,055)	-16%
Indirect costs	10,242,187	5,146,219	5,095,968	99%
Federal grants	57,347,117	76,197,948	(18,850,831)	-25%
Interest and investment income	8,347,580	377,689	7,969,891	2110%
Management and developers fees	41,105,987	-	41,105,987	100%
Other	<u>2,099,348</u>	<u>1,555,845</u>	<u>543,503</u>	35%
TOTAL REVENUES	<u>\$167,082,898</u>	<u>\$129,275,664</u>	<u>\$37,807,234</u>	29%
EXPENDITURES				
General and administrative	\$ 34,822,426	\$ 38,549,458	(\$ 3,727,032)	-10%
Construction and rehabilitation	12,110,632	12,554,151	(443,519)	-4%
Capital outlays	57,547	1,269,108	(1,211,561)	-95%
Tenants, utilities services and Maintenance	53,068,931	51,069,046	1,999,885	4%
Housing, repairs and maintenance	443,528	20,355,329	(19,911,801)	-98%
Debt service payments				
Principal	3,543,580	3,652,976	(109,396)	-3%
Interest	<u>904,976</u>	<u>869,038</u>	<u>35,938</u>	4%
TOTAL EXPENDITURES	<u>\$104,951,620</u>	<u>\$128,319,106</u>	<u>(\$23,367,486)</u>	-18%

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO.
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
JUNE 30, 2011**

5. Business Type Activities

The Proprietary Fund was presented in conjunction with the basic financial statements. Such financial statements purport to present the financial results of the Office for the Administration of Assets of the Corporation for Urban Housing Renovation (the CRUV). This financial statement can be found right after the governmental funds. Below please find a summarized version of the financial results on this fund.

Statement of Net Assets in Liquidation

	<u>2011</u>
ASSETS	
Current assets	\$14,345,566
Noncurrent assets	<u>68,028,782</u>
TOTAL ASSETS	<u>\$82,374,348</u>
LIABILITIES	
Current liabilities	\$ 4,820,630
Noncurrent liabilities	<u>207,134</u>
TOTAL LIABILITIES	5,027,764
NET ASSETS IN LIQUIDATION	<u>77,346,584</u>
TOTAL LIABILITIES AND NET ASSETS IN LIQUIDATION	<u>\$82,374,348</u>

Statement of Changes in Net Assets in Liquidation

Additions to net assets in liquidation	\$ 185,509
Cost and expenses	(682,160)
Reorganization items	4,023,431
Distributed net assets	<u>(2,702,316)</u>
Change in net assets in liquidation	824,464
NET ASSETS AT BEGINNING OF YEAR	<u>76,522,120</u>
NET ASSETS AT END OF YEAR	<u>\$77,346,584</u>

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
JUNE 30, 2011**

6. Budgetary information

No significant difference between the amended budget and actual amounts in the general fund was found. The information is presented as follows:

	<u>Original Budget</u>	<u>Amended Budget</u>	<u>Actual</u>	<u>Variance</u>
REVENUES				
Legislative appropriations	\$20,445,732	\$20,445,732	\$20,445,732	\$ -
EXPENDITURES				
General and administrative	<u>20,445,732</u>	<u>20,445,732</u>	<u>20,378,647</u>	<u>67,085</u>
EXCESS OF REVENUES OVER EXPENDITURES	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 67,085</u>	<u>\$67,085</u>

7. Capital assets

At June 30, 2011, the PRDH had \$51,314,758 net of depreciation, invested in Capital Assets, including building, equipment, furniture and fixtures, and vehicles. The net decrease of \$434,738 when compared with balance at June 30, 2010 is mostly related to the depreciation of the year. Please find below the summarized information regarding the capital assets as of June 30, 2011:

Capital Assets - Including PRDH and CRUV

Non depreciable capital assets

Land \$ 793,717

Depreciable capital assets:

Building 30,000,000
 Building improvements 21,013,268
 Furniture, equipment and vehicles 5,860,723
 Parking and building 5,137,029

Total Assets 62,011,020

Less accumulated depreciation (11,489,979)

Total capital assets being depreciated, net 50,521,041

Total capital assets, net \$51,314,758

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
JUNE 30, 2011**

8. Other Currently Known Facts

Partnership Agreement

On September 29, 2011 the PRDH received the amount of \$100 million from Vivienda Modernization 1, LLC for the repayment of note receivable principal and interest of \$87.8 million and \$12.2 million, respectively.

9. Contacting the PRDH Financial Management

The PRDH's financial statements are designed to present users with a general overview of its finances. If you have questions about the report or need additional information, please contact the Finance Director.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
GOVERNMENT - WIDE
STATEMENT OF NET ASSETS
JUNE 30, 2011**

	<u>PRIMARY GOVERNMENT</u>		<u>TOTAL</u>
	<u>GOVERNMENTAL ACTIVITIES</u>	<u>BUSINESS TYPE ACTIVITIES</u>	
ASSETS			
Current assets			
Cash and cash equivalents (Note B)	\$ 62,963,478	\$ 7,352,578	\$70,316,056
Cash with fiscal agent (Note D)	2,047,874	-	2,047,874
Due from:			
Agency Fund	747,539	-	747,539
Federal government (Note E)	6,514	-	6,514
Related entity, current portion (Note G)	41,070,209	-	41,070,209
Other funds (Note F)	(6,788,236)	6,788,236	-
Mortgages and accounts receivable (Note C)	-	204,752	204,752
Interest receivable on note (Note G)	11,128,504	-	11,128,504
Other accounts receivable and other assets	<u>3,432,294</u>	<u>-</u>	<u>3,432,294</u>
Total current assets	<u>114,608,176</u>	<u>14,345,566</u>	<u>128,953,742</u>
Noncurrent assets			
Note receivable from related entity, noncurrent portion (Note G)	102,889,957	-	102,889,957
Due from related entity, noncurrent portion (Note G)	16,636,341	-	16,636,341
Restricted deposit (Note B)	-	5,775,050	5,775,050
Land lots held for sale or lease (Note H)	41,415	42,955,051	42,996,466
Restricted land lot (Note H)	-	19,200,000	19,200,000
Capital assets, net (Note I)	<u>51,216,077</u>	<u>98,681</u>	<u>51,314,758</u>
Total noncurrent assets	<u>170,783,790</u>	<u>68,028,782</u>	<u>238,812,572</u>
TOTAL ASSETS	<u>\$285,391,966</u>	<u>\$82,374,348</u>	<u>\$367,766,314</u>

Continues

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
GOVERNMENT-WIDE
STATEMENT OF NET ASSETS (CONTINUED)
JUNE 30, 2011**

	<u>PRIMARY GOVERNMENT</u>		
	<u>GOVERNMENTAL</u>	<u>BUSINESS</u>	
	<u>ACTIVITIES</u>	<u>TYPE</u>	<u>TOTAL</u>
		<u>ACTIVITIES</u>	
LIABILITIES AND NET ASSETS			
LIABILITIES			
Current liabilities:			
Notes payable, current portion (Note J)	\$12,242,772	\$ -	\$12,242,772
Accrued legal claims, current portion (Note O)	455,753	-	455,753
Accounts payable	3,016,011	321,028	3,337,039
Other accrued liabilities	-	4,314,507	4,314,507
Accrued compensated absences, current portion (Notes K and M)	2,972,485	185,095	3,157,580
Accrued termination benefits (Note M)	<u>1,140,288</u>	<u>-</u>	<u>1,140,288</u>
Total current liabilities	<u>19,827,309</u>	<u>4,820,630</u>	<u>24,647,939</u>
Noncurrent liabilities:			
Notes payable, long-term portion (Note J)	22,171,304	-	22,171,304
Accrued legal claims, long-term portion (Note O)	4,652,494	207,134	4,859,628
Accrued compensated absences, long-term portion (Notes K and M)	3,489,439	-	3,489,439
Accrued termination benefits (Note M)	<u>5,853,124</u>	<u>-</u>	<u>5,853,124</u>
Total noncurrent liabilities	<u>36,166,361</u>	<u>207,134</u>	<u>36,373,495</u>
Total liabilities	<u>55,993,670</u>	<u>5,027,764</u>	<u>61,021,434</u>
Commitments and contingencies (Note O)			
NET ASSETS (NOTE P)			
Invested in capital assets, net of related debt	26,881,179	98,681	26,979,860
Restricted for:			
Supply of low and moderate income housing	-	24,975,050	24,975,050
Special revenue funds	14,727,085	-	14,727,085
Unrestricted	<u>187,790,032</u>	<u>52,272,853</u>	<u>240,062,885</u>
TOTAL NET ASSETS	<u>\$229,398,296</u>	<u>\$77,346,584</u>	<u>\$306,744,880</u>

See notes to financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
GOVERNMENT-WIDE
STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2011**

<u>Functions and programs</u>	<u>PROGRAM REVENUES</u>				<u>Governmental Activities</u>
	<u>Expenses</u>	<u>Charges for Services</u>	<u>Operating Grants and Contribution</u>	<u>Capital Grants and Contributions</u>	
Governmental activities:					
General and administrative	\$ (44,447,828)	\$10,242,187	\$33,220,296	\$ -	\$ (985,345)
Construction and rehabilitation	(12,110,632)	3,206,872	-	7,070,511	(1,833,249)
Tenant, utility services and maintenance	(53,068,931)	4,443,000	57,347,117	-	8,721,186
Housing repairs and maintenance	(443,528)	-	-	-	(443,528)
Interest expense	(904,976)	-	-	-	(904,976)
Total governmental activities	<u>(110,975,895)</u>	<u>17,892,059</u>	<u>90,567,413</u>	<u>7,070,511</u>	<u>4,554,088</u>
Business-type activities:					
General and administrative	(1,277,381)	-	105,323	-	(1,172,058)
Housing sales and adjustments	<u>1,134,993</u>	<u>13,862</u>	<u>66,324</u>	<u>-</u>	<u>1,215,179</u>
Total business —type activities	<u>(142,388)</u>	<u>13,862</u>	<u>171,647</u>	<u>-</u>	<u>43,121</u>
Total	<u>\$(111,118,283)</u>	<u>\$17,905,921</u>	<u>\$90,739,060</u>	<u>\$7,070,511</u>	<u>\$4,597,209</u>

Continues

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
GOVERNMENT-WIDE
STATEMENT OF ACTIVITIES (CONTINUED)
YEAR ENDED JUNE 30, 2011**

	<u>GOVERNMENTAL ACTIVITIES</u>	<u>BUSINESS - TYPE ACTIVITIES</u>	<u>TOTAL</u>
Net revenues	\$ 4,554,088	\$ 43,121	\$ 4,597,209
General revenues:			
Management and developer fees	32,038,026	-	32,038,026
Interest and investment income	491,398	115,503	606,901
Other	<u>2,099,348</u>	<u>665,840</u>	<u>2,765,188</u>
Total general revenues	<u>34,628,772</u>	<u>781,343</u>	<u>35,410,115</u>
CHANGE IN NET ASSETS	39,182,860	824,464	40,007,324
NET ASSETS AT BEGINNING OF YEAR	<u>190,215,436</u>	<u>76,522,120</u>	<u>266,737,556</u>
NET ASSETS AT END OF YEAR	<u>\$229,398,296</u>	<u>\$77,346,584</u>	<u>\$306,744,880</u>

See notes to financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMON WEALTH OF PUERTO RICO
FUND FINANCIAL STATEMENTS
BALANCE SHEET - GOVERNMENTAL FUNDS
JUNE 30, 2011**

	Section 8 Housing Choice Voucher	General Fund	Home Investment Partnership Program	Self Contribution Funds	Other Governmental Funds	Total Governmental Funds
ASSETS						
Cash and cash equivalents	\$14,656,966	\$83,585	\$ -	\$ 24,510,656	\$23,712,271	\$ 62,963,478
Cash with fiscal agent	-	-	-	-	2,047,874	2,047,874
Due from other funds	108,262	-	-	-	-	108,262
Due from Agency Fund	-	-	-	747,539	-	747,539
Federal grant receivables	-	-	-	5,269	1,245	6,514
Note receivable - related	-	-	-	102,889,957	-	102,889,957
Other receivables	451,840	-	-	71,768,917	46,591	72,267,348
Total Assets	<u>\$15,217,068</u>	<u>\$83,585</u>	<u>\$ -</u>	<u>\$199,922,338</u>	<u>\$25,807,981</u>	<u>\$241,030,972</u>
LIABILITIES						
Accounts payable and accrued liabilities	\$ 703,776	\$ 16,500	\$ -	\$ 1,015,943	\$ 1,279,792	\$ 3,016,011
Due to other funds	-	-	-	6,396,498	500,000	6,896,498
Total Liabilities	<u>703,776</u>	<u>16,500</u>	<u>-</u>	<u>7,412,441</u>	<u>1,779,792</u>	<u>9,912,509</u>
FUND BALANCE						
Nonspendable	-	-	-	172,506,413	-	172,506,413
Restricted	14,513,292	-	-	5,269	208,524	14,727,085
Committed	-	-	-	18,791,578	16,227,921	35,019,499
Assigned	-	67,085	-	1,206,637	7,591,744	8,865,466
TOTAL FUND BALANCE	<u>14,513,292</u>	<u>67,085</u>	<u>-</u>	<u>192,509,897</u>	<u>24,028,189</u>	<u>231,118,463</u>
TOTAL LIABILITIES AND FUND BALANCE	<u>\$15,217,068</u>	<u>\$83,585</u>	<u>\$ -</u>	<u>\$199,922,338</u>	<u>\$25,807,981</u>	<u>\$241,030,972</u>

See notes to financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET ASSETS
YEAR ENDED JUNE 30, 2011**

Fund balance — governmental funds	\$231,118,463
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets are not current financial resources and, therefore not reported in the funds	51,216,077
Land lots held for sale or lease are not current financial resources and therefore not reported in the funds	41,415
Notes payable regarding line of credit are not due and payable in the current period and therefore not included in the funds	(34,414,076)
Accrued legal claims are not due and payable in the current period and therefore are not included in the funds	(5,108,247)
Accrued compensated absences which are not payable in the current period are not included in the funds	(6,461,924)
Accrued termination benefits which are not payable in the current period are not included in the funds	<u>(6,993,412)</u>
Net assets of governmental activities	<u>\$229,398,296</u>

See notes to financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
YEAR ENDED JUNE 30, 2011**

	Section 8 Housing Choice Voucher	Home Investment Partnership Program	Self Contribution Funds	Other Governmental Funds	Total Governmental Funds
Revenues:					
State appropriations	\$ 23,220,296	\$ -	\$10,000,000	\$ 7,070,511	\$ 40,290,807
Sale and lease of land lots	-	-	1,264,846	1,942,026	3,206,872
Rent revenue	-	-	-	4,443,000	4,443,000
Indirect costs	-	-	10,242,187	-	10,242,187
Federal grants	57,347,117	-	-	-	57,347,117
Interest and investment income	179,340	-	7,856,182	312,058	8,347,580
Management and developers fees	-	-	41,105,987	-	41,105,987
Other	4,371	74,344	177,428	1,843,205	2,099,348
	<u>23,220,296</u>	<u>74,344</u>	<u>70,646,630</u>	<u>15,610,800</u>	<u>167,082,898</u>
Expenditures					
General and administrative	20,378,647	-	4,490,237	5,958,543	34,822,426
Construction and rehabilitation	-	-	11,292,082	818,550	12,110,632
Capital outlays	-	-	23,793	14,055	57,547
Tenants, utility services and maintenance	-	-	-	363,863	53,068,931
Housing repairs and maintenance	52,705,068	-	-	-	443,528
	443,528	-	-	-	-
	<u>20,378,647</u>	<u>-</u>	<u>15,806,112</u>	<u>7,155,011</u>	<u>100,503,064</u>
Debt service payments					
Principal	-	-	-	3,543,580	3,543,580
Interest	-	-	-	904,976	904,976
	<u>20,378,647</u>	<u>-</u>	<u>15,806,112</u>	<u>11,603,567</u>	<u>104,951,620</u>
Total expenditures	<u>20,378,647</u>	<u>-</u>	<u>15,806,112</u>	<u>11,603,567</u>	<u>104,951,620</u>
Excess of revenues over expenditures	<u>2,841,649</u>	<u>74,344</u>	<u>54,840,518</u>	<u>4,007,233</u>	<u>62,131,278</u>

Continues

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -
GOVERNMENTAL FUNDS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

	<u>General Fund</u>	<u>Section 8 Housing Choice Voucher</u>	<u>Home Investment Partnership Program</u>	<u>Self Contribution Funds</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Other financing sources (uses)						
(Out) to other funds	-	(7,282,258)	-	(65,755)	(666,923)	(8,014,936)
In from other funds	-	-	-	732,678	7,282,258	8,014,936
Total other financing sources(uses)	-	<u>(7,282,258)</u>	-	<u>666,923</u>	<u>6,615,335</u>	-
Excess of revenues over expenditures and other financing sources (uses)	2,841,649	(6,914,724)	74,344	55,507,441	10,622,568	62,131,278
Fund balances at beginning of year	<u>(2,774,564)</u>	<u>21,428,016</u>	<u>(74,344)</u>	<u>137,002,456</u>	<u>13,405,621</u>	<u>168,987,185</u>
Funds balances at end of year	<u>\$ 67,085</u>	<u>\$14,513,292</u>	<u>\$ -</u>	<u>\$192,509,897</u>	<u>\$24,028,189</u>	<u>\$231,118,463</u>

See notes to financial statements

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2011**

Excess of revenues over expenditures in the statement of revenues,
expenditures and changes in fund balances — governmental funds \$62,131,278

Amounts reported in the statement of activities are different because:

Governmental funds report capital outlays as expenditures. However,
in the statement of activities the cost of those assets is allocated over
their estimated useful lives as depreciation expense 57,547

Depreciation expense on capital assets is reported in the statement of
activities but does not require the use of current financial resources.
Therefore depreciation expense is not reported as expenditure in the
statement of governmental funds. (2,342,894)

Governmental funds report principal payments on note payable as
expenditures, whereas the principal payments reduce the long-term
obligations in the statement of activities 3,543,580

(Increase) decrease in accrued expenses which does not require the use
of current financial resources:

Accrued legal claims (169,647)
Due to Public Building Authority (186,552)
Accrued compensated absences 59,640
Accrued termination benefits (6,993,412)

Revenues in the governmental funds recognized in the statement of
activities in the prior year. (16,916,680)

Change in net assets of governmental activities \$39,182,860

See notes to financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
STATEMENT OF NET ASSETS IN LIQUIDATION - PROPRIETARY FUND
JUNE 30, 2011**

	<u>ENTERPRISE FUND</u> <u>Urban Renewal and</u> <u>Housing Fund</u>
ASSETS	
Current assets:	
Cash and cash equivalents (Note B)	\$ 7,352,578
Mortgages and accounts receivable, net (Note C)	204,752
Due from other funds (Note F)	<u>6,788,236</u>
Total current assets	<u>14,345,566</u>
Noncurrent assets:	
Housing units and land lots held for sale (Note H)	42,955,051
Restricted:	
Deposit (Note B)	5,775,050
Land lots (Note H)	19,200,000
Capital assets, net (Note I)	<u>98,681</u>
Total noncurrent assets	<u>68,028,782</u>
TOTAL ASSETS	<u>\$82,374,348</u>
 LIABILITIES AND NET ASSETS IN LIQUIDATION	
LIABILITIES	
Current liabilities:	
Accounts payable	\$ 321,028
Other accrued liabilities	4,314,507
Accrued compensated absences (Note K)	<u>185,095</u>
Total current liabilities	4,820,630
Noncurrent liability:	
Accrued legal claims, long-term portion (Note O)	<u>207,134</u>
Total liabilities	<u>5,027,764</u>
COMMITMENTS AND CONTINGENCIES (NOTE O)	
NET ASSETS IN LIQUIDATION (NOTE P)	
Invested in capital assets	98,681
Restricted for noncurrent assets and other purposes	24,975,050
Unrestricted	<u>52,272,853</u>
Total net assets in liquidation	<u>77,346,584</u>
TOTAL LIABILITIES AND NET ASSETS IN LIQUIDATION	<u>\$82,374,348</u>

See notes to financial statements.

Torres Blompart, Sánchez Ruiz LLP

Certified Public Accountants and Business Consultants

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
STATEMENT OF CHANGES IN NET ASSETS IN LIQUIDATION –
PROPRIETARY FUND
YEAR ENDED JUNE 30, 2011**

	<u>ENTERPRISE FUND</u> <u>Urban Renewal and</u> <u>Housing Fund</u>
Additions to net assets in liquidation:	
Mortgage interest revenues (Note Q)	\$ 66,324
Rent	105,323
Administrative charges	<u>13,862</u>
Total additions to net assets in liquidation	185,509
Costs and expenses	
Operating and administrative expenses	<u>(682,160)</u>
Deduction to net assets in liquidation before reorganization items and distributions	<u>(496,651)</u>
Reorganization items:	
Adjustments to estimated value of housing units and land lots held for sale	3,837,309
Professional fees	(595,221)
Interest earned on:	
Unrestricted investments	66,372
Restricted investments	49,131
Other income	<u>665,840</u>
Total reorganization items	<u>4,023,431</u>
Increase to Net Assets in Liquidation Before Distributions	3,526,780
Distributed net assets, restricted for social interest projects	<u>(2,702,316)</u>
Net increase in net assets in liquidation	824,464
Net assets in liquidation, at beginning of year	<u>76,522,120</u>
Net assets in liquidation, at end of year	<u>\$77,346,584</u>

See notes to financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
STATEMENT OF FIDUCIARY NET ASSETS
JUNE 30, 2011**

	AGENCY FUND		
	<u>Ponce en Marcha</u>	<u>Special Community</u>	<u>Remedy Fund</u>
ASSETS			
Restricted cash (Note N)	\$1,505,107	\$104,946	\$1,455,726
Due from special community	-	747,539	-
	<u>\$1,505,107</u>	<u>\$852,485</u>	<u>\$1,455,726</u>
LIABILITIES			
Due to government units (Note N)	\$1,505,107	\$104,946	\$1,455,726
Due to governmental fund	-	747,539	-
	<u>\$1,505,107</u>	<u>\$852,485</u>	<u>\$1,455,726</u>

See notes to financial statements.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES**

Organization

The Commonwealth of Puerto Rico was constituted on July 25, 1952, under the provisions of its Constitution as approved by the people of Puerto Rico and the Congress of the United States of America. The Commonwealth's Constitution provides for the assignation of powers to the executive, legislative and judicial branches of the government. The Commonwealth assumes responsibility for public safety, public health, public housing, wealth, education and economic development.

The Department of Housing of the Commonwealth of Puerto Rico (PRDH) was created by Act No. 97 of June 10, 1972. Through a Secretary appointed by the Governor of the Commonwealth, the PRDH is engaged in the implementation of the governmental policy related to the public housing. This includes, among other things, the acquisition, sale, lease and operation of public housing projects and land development to provide housing to low and moderate-income families.

By Act No.58 of August 9, 1991, the Puerto Rico Public Housing Administration (PRPHA), created by Act No. 66 of August 17, 1989, was ascribed to the PRDH, and designated to assume certain assets, liabilities and operations of the Puerto Rico Urban Renewal and Housing Corporation (PRURHC), which is currently under liquidation by an Enterprise Fund within the PRDH.

The Enterprise Fund was created to implement the provisions of Law No. 106 (the Law) of June 30, 1998. This Law terminated the operations of the former Office of Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation (former CRUV). The Enterprise Fund will continue with the liquidation of the assets of the Corporation for Urban Housing Renovation. The accompanying statement of net assets in liquidation and the statement of changes in net assets in liquidation were prepared in the liquidations basis of accounting.

Financial reporting entity

The PRDH is for financial reporting purposes, part of the Commonwealth of Puerto Rico. Because PRDH is part, for financial reporting purposes, of the Commonwealth, its financial data is included as part of the Commonwealth of Puerto Rico financial statements.

The PRDH accompanying financial statements are issued solely to comply with the Single Audit Act of 1984, P.L. 98-502, and the Single Audit Act Amendments of 1996, P.L. 104-156 and for the information and use of the PRDH management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)**

Summary of significant accounting policies

The accompanying basic financial statements of the PRDH have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as prescribed by the Governmental Accounting Standard Board (GASB).

Basis of presentation and fund accounting

The accounts of the PRDH are organized on the basis of Governmental Funds. Each fund is accounted for by a separate set of self-balancing accounts that comprises its assets, liabilities, fund balance, revenues and expenditures. Fund financial statements report detailed information about the PRDH. The focus of governmental fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column.

The following are the governmental funds presented in the financial statements as of and for the year ended June 30, 2011:

General — This fund includes the current financial resources, which relate to the general operations of the PRDH. These operations consist of the general administration and other activities not accounted for in the U.S. Department of Housing and Urban Development (HUD) Programs major funds.

Section 8 Program — This major fund accounts for grants received from HUD. The Grant is restricted for accomplishing objectives of the Housing Voucher Program, which provides rental assistance to help very low-income families afford decent, safe and sanitary rental housing.

Self Contribution Fund - This fund is maintained by the PRDH to account for current financial resources received from proceeds of sale and rent of land lots, indirect costs, fees for elderly care and other revenues collected from sources other than intergovernmental or federal subsidies. Also, it includes the resources and expenditures received and used respectively for the improvement of the PRDH's main-building.

Urban Renewal and Housing Fund - This fund is maintained by the PRDH to account for current financial resources received to liquidate the assets of the former Puerto Rico Urban Renewal and Housing Corporation (PRURHC) and to meet its financial obligations with the proceeds of the liquidation.

In addition, the PRDH reports the following fiduciary fund:

Agency - This fiduciary fund is custodial in nature (assets equal liabilities) and does not involve measurement of the PRDH results of operations (see Note N).

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND) SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)**

Basis of presentation and fund accounting (continued)

Measurement focus and basis of accounting

Measurement focus refers to what is being measured in a fund's operating statement, while basis of accounting refers to the timing in which transactions are recognized in a fund's operating statement. The governmental funds use a current financial resources measurement focus and are accounted for using the modified accrual basis of accounting.

Under the modified accrual basis of accounting, revenues are recorded when susceptible to accrual, i.e., when they become both measurable and available. Measurable means that the amount of the transaction can be determined, while available means collectible within sixty (60) days of the end of the current fiscal period.

Federal grants revenues are financial resources approved by HUD and are recorded in the accounting period in which the resources are collectible and available for expenditure in the current accounting period. Legislative appropriations, which represent annual appropriations from the Commonwealth of Puerto Rico, are recorded when approved, collectible and available for expenditure in the current accounting period.

Statutory (budgetary) accounting

The PRDH's total available spending authorization, which is considered its budget, is adopted in accordance with a statutory basis of accounting, which is not in accordance with the modified accrual basis of accounting. Revenues are generally recognized when cash is received. Expenditures are generally recorded when the related expenditure is incurred or encumbered. Until June 30, 2001, available appropriations and encumbrances were established to lapse three (3) years after the end of the fiscal year. Effective July 1, 2001, available appropriations and encumbrances will lapse the year following the end of the fiscal year when the encumbrance was established, by means of Act No.123 from August 17, 2001, which amended the existing appropriations and encumbrances lapsing provision of Act No. 230 from July 23, 1974.

Amounts required settling claims and judgments against the PRDH, and certain other liabilities are not recognized until they are encumbered or otherwise processed for payment. Under the statutory basis of accounting, the PRDH 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 PRDH governmental funds, encumbrance is a significant aspect to budget control.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)**

Summary of significant accounting policies (continued)

Budgetary control

For budgetary purposes, encumbrance accounting is used. The encumbrances (that is purchase orders, contracts and other commitments of appropriated resources) are considered expenditures when a commitment is made. For GAAP reporting purposes, encumbrances, outstanding at fiscal year-end are reported as reservations of budgetary appropriations and GAAP fund balances and do not constitute expenditures or liabilities on a GAAP basis, because such commitments will be honored during the subsequent fiscal year.

The Department of the Treasury and the Office of Management and Budget of Puerto Rico has the responsibility to ensure that budgetary spending control is maintained in the PRDH. Budgetary control is exercised through the Puerto Rico Integrated Financial Accounting System ("PRIFAS").

PRIFAS ensures that encumbrances or expenditures are not processed if they exceed the PRDH's total available spending authorization. The legal level of budgetary control at the PRDH is for general fund expenditures.

Risk financing

The Commonwealth of Puerto Rico purchases commercial insurance covering casualty, theft, tort, claims, and other losses for the PRDH. The PRDH reimburses the Commonwealth for premium payments made on its behalf. The PRDH's current insurance policies have not been canceled or terminated.

For worker's compensation, the State Insurance Fund Corporation, a component unit of the Commonwealth of Puerto Rico, provides the workers compensation to the PRDH's employees.

PRDH is authorized to deposit only in financial institutions approved by the Department of the Treasury of the Commonwealth of Puerto Rico, and such deposits should be kept in separate accounts in the name of the PRDH. The restricted cash includes purchase option deposits to be credited to sales of housing properties. The deposits are transferred to the general account when the sale is consummated.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)**

Summary of significant accounting policies (continued)

Inter-fund balances

Inter-fund receivables and payables outstanding at year end are referred to as due to/from other funds. The general fund provides services, at cost, to the HUD Programs Funds, with the attempts of recovering such amounts in a period of one (1) year or less.

Eliminations are made in the government wide statements of the amounts reported as inter-fund receivables and payables.

Capital assets

Capital assets used in the governmental operations are accounted for in the Government - Wide financial statement of net assets, rather than in the Governmental Funds. When capital assets are purchased, such are recorded as capital outlays' expenditures in the governmental funds. They are stated at cost.

Major modernizations and betterments are capitalized, while replacements, maintenance and repairs, which do not improve or extent the life of an asset, are not. When assets are sold, retired or otherwise disposed of, the cost is removed.

Depreciation of capital assets is computed and recorded under the straight-line method. Estimated useful lives of the various classes of depreciable capital assets are: parking and building to forty (40) years and other capital assets three (3) to five (5) years.

Compensated absences

The vacation policy of the Commonwealth of Puerto Rico that applies to the PRDH employees provides for the accumulation of two and a half (2.5) days per month. Vacation time accumulated is fully vested to the employees from the first day of work up to a maximum of sixty (60) days. PRDH's employees accumulate sick leave at a rate of one and a half (1.5) days per month up to a maximum of ninety (90) days. Upon retirement, an employee receives all accumulated unpaid leave at the current rate, if the employee has at least ten (10) years of service with the Commonwealth of Puerto Rico.

Mortgage interest income

Interest income on mortgages is recorded when collected due to the high delinquency rate.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)**

Summary of significant accounting policies (continued)

Use of estimates

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

Cash and cash equivalents

The PRDH considers all highly liquid investments with maturity of three (3) months or less when purchased to be cash equivalents. The cash balances are available to meet current operating requirements in various interest-bearing accounts with the Governmental Development Bank, Commercial Banks and Puerto Rico Housing Bank and Finance Agency.

Federal grants

Contributions received from federal grants are credited to operating revenues under the HUD Programs in the accounting period in which they are earned and become measurable.

Housing units and lots held for sale

Housing units and lots held for sale are stated at their net realizable value determined by the PRDH's management based on previous sales of similar housing units and appraised values. PRDH does not record all changes in estimated realizable value of all the housing units and lots held for sale due to the high cost of appraisal services and the short time benefit of one year of such services, until there is an interested buyer. Housing units and lots held for sale consists of low cost housing units, non-low cost housing units and land lots.

Governmental — wide financial statements

The statement of net assets and the statement of activities display information of all of the non-fiduciary activities of the PRDH, the primary government, as a whole. The PRDH activities are considered governmental type.

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)

Summary of significant accounting policies (continued)

Governmental — wide financial statements (continued)

The government-wide statements are prepared using the economic resources measurement focus and the accrual basis of accounting. This approach differs from the manner in which governmental fund financial statements are prepared. Therefore, governmental fund financial statements include reconciliations with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

For the most part, the effect of inter-fund activity has been removed from these statements. The government—wide statement of activities presents a comparison between expenses, both direct and indirect, and program revenues for each of the programs of the governmental activities of the PRDH.

Direct expenses are those that are specifically associated with a service or program and therefore clearly identifiable to a particular function. Indirect expenses for centralized services and administrative overhead are allocated among the programs and functions using a full cost allocation approach and are presented separately to enhance comparability of direct expenses between governments that allocate direct expenses and those that do not.

Program revenues include charges paid by the recipients of the goods or services offered by the programs and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues which are not classified as program revenues are presented as general revenues.

The comparison of program revenues and expenses identifies the extent to which each program is self-financing or draws for the general revenues of the PRDH.

Net assets

Net assets are the difference between assets and liabilities in the governmental wide statements. Net assets are segregated in the following three (3) categories:

Invested in capital assets, net of related debt - These consist of capital assets, less accumulated depreciation and reduced by any outstanding debt related to the acquisition, construction or improvement of those assets.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)**

Summary of significant accounting policies (continued)

Net assets (continued)

Restricted net assets - Result when constraints placed on net assets use are either externally imposed by grantors, contributors, laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation.

Unrestricted - These consist of net assets which do not meet the definition of the two (2) preceding categories.

Fund Balance

Beginning with fiscal year 2011, the PRDH implemented GASB Statement No. 54, "Fund Balance Reporting and Governmental Fund Type Definitions." This Statement provides more clearly defined fund balance categories to make the nature and extent of the constraints placed on a government's fund balances more transparent. The following classifications describe the relative strength of the spending constraints:

- Nonspendable—amounts that cannot be spent either because they are not in a spendable form or because they are legally or contractually required to be maintained intact.
- Restricted—amounts constrained to specific purposes by their providers (such as grantors), through constitutional provisions, or by enabling legislation.
- Committed—amounts constrained to specific purposes by the PRDH itself, using its highest level of decision-making authority (such as legislation). To be reported as committed, amounts cannot be used for any other purpose unless the PRDH takes the same highest level action to remove or change the constraint.
- Assigned—amounts the PRDH intends to use for a specific purpose. Intent can be expressed by the PRDH or by an official or body to which the PRDH delegates the authority.
- Unassigned—all amounts not included in other spendable classifications.

The PRDH establishes (and modifies or rescinds) fund balance commitments by passage of an ordinance or resolution. This is typically done through adoption and amendment of the budget. A fund balance commitment is further indicated in the budget document as a designation or commitment of the fund (such as for special incentives). Assigned fund balance is established by the PRDH through adoption or amendment of the budget as intended for specific purpose (such as the purchase of fixed assets, construction, debt service, or for other purposes).

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (CONTINUED)**

Fund Balance (continued)

In the general fund, the PRDH strives to maintain an unassigned fund balance to be used for unanticipated expenditures and other financing sources and uses.

Subsequent events

In May 2009, the Financial Accounting Standards Board (FASB) established standards related to accounting for, and disclosure of, events that occur after the statement of position date, but before financial statements are issued or are available to be issued. Management has evaluated subsequent events through January 13, 2012, the date the financial statements were available to be issued.

NOTE B - CASH AND CASH EQUIVALENTS, AND RESTRICTED DEPOSITS

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

During the year, the PRDH invests its funds in interest bearing bank accounts and certificates of deposit. The PRDH is authorized to deposit only in institutions approved by the Department of the Treasury of the Commonwealth of Puerto Rico. Such deposits should be kept in separate accounts in the name of the PRDH. Under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of the amounts insured by the Federal Deposit Insurance Corporation. During the year ended June 30, 2011, the PRDH invested its funds in bank accounts bearing interest.

At June 30, 2011, the PRDH had commercial bank balances as follow:

Insured by the Federal Deposit Insurance Corporation	<u>\$233,886</u>
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In addition, as of June 30, 2011, the PRDH's custodial credit risk was approximately \$7.2 million, which was the bank balance of cash deposited at the Government Development Bank for Puerto Rico (as fiscal agent). These deposits are exempt from the collateral requirement established by the Commonwealth.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE B - CASH AND CASH EQUIVALENTS, AND RESTRICTED DEPOSITS
(CONTINUED)**

Business type activities -Enterprise fund:

At June 30, 2011, the PRDH had commercial bank balances as follow:

<u>Description</u>	<u>Amount</u>
Insured by the Federal Deposit Insurance Corporation	\$250,000
Collateralized by securities held by the pledging financial institution's trust department in the Enterprise Fund's name	<u>205,135</u>
	<u>\$455,135</u>

Additionally, as of June 30, 2011, the Enterprise Fund's custodial credit risk was approximately \$6.2 million, which is the bank balance of cash deposited at the Government Development Bank for Puerto Rico. These deposits are exempt from the collateral requirements established by the Commonwealth of Puerto Rico.

Restricted cash

On June 27, 2001, the PRDH and U.S. Housing and Urban Development (HUD) signed an Amendment to Memorandum of Understanding which required, among other things, the deposit of all residual receipts in a special escrow account. This account is required to maintain collateral in the form of investments to prevent risk of loss to the principal balance. All accrued interest shall be deposited in this account. Also, any profit generated from the sale of multifamily properties, as defined, should be deposited in this account within ten (10) business days after the sale is consummated. The funds deposited in this account shall be used for necessary and eligible activities within the Housing Programs of the PRDH that directly relate to the expansion of the supply of low and moderate income housing and other initiatives covered in the Housing Program such as; development of lots (Turnkey Lots), construction of housing for sale and construction or rehabilitation of infrastructure which might be needed to facilitate housing for qualified low income families. Withdrawals from the special escrow account shall only be made upon written authorization of the HUD Director of the Caribbean Multifamily Program Center and by PRDH.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE C - MORTGAGES AND ACCOUNTS RECEIVABLE

Mortgages and accounts receivable as of June 30, 2011, consist of the following:

<u>Description</u>	<u>Amount</u>
Mortgage notes	\$1,008,820
Other accounts receivable	<u>390,028</u>
	1,398,848
Less valuation allowance	<u>(1,194,096)</u>
	<u>\$ 204,752</u>

Mortgage notes receivable consist of first mortgages arising from the sale of housing units with interest rates ranging from 3.125% to 9%, maturing within a period of two (2) to nineteen (19) years. Due to delinquency of the Enterprise Fund's portfolio as of June 30, 2011, management's opinion is that certain mortgages notes are not collectible and that in order to realize a portion of their value, the housing units will have to be repossessed and subsequently sold.

NOTE D - CASH WITH FISCAL AGENT

The funds of the PRDH are under the custody of the Secretary of the Treasury of Puerto Rico pursuant to Act. No. 230 from July 23, 1974, as amended, known as "Commonwealth of Puerto Rico Accounting Law". The Treasury Department follows the practice of pooling cash and cash equivalents under the custody and control of the Secretary of the Treasury. The funds of the PRDH in such pooled cash accounts are available to meet its current operating requirements. No collateral is required to be maintained for these pooled accounts.

NOTE E - DUE FROM FEDERAL GOVERNMENT

Due from Federal Government consists of \$6,514 due from the U.S. Department of Housing and Urban Development (HUD) related to other programs. Grants are restricted/reserved mainly to provide assistance payments for housing repairs and maintenance, tenant services, utilities and eligible administrative costs associated with such programs.

NOTE F - INTER-FUND LOANS

Inter-fund receivables and payables generally reflect temporary loans, billings for services provided and recovery of expenditures. As of June 30, 2011, there was a balance due to the Enterprise fund of \$6,788,236.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE G - PARTNERSHIP AGREEMENT

On August 1, 2008, the PRDH became a general partner of Vivienda Modernization Holdings 1, S.E. (the "Partnership"), a Puerto Rico civil partnership that was formed on August 1, 2008 to acquire a 100% member interest in Vivienda Modernization 1, LLC ("the Project Company"), a Puerto Rico limited liability company. The Project Company was formed to acquire, develop, rehabilitate, own, maintain and operate 33 residential rental properties located in Puerto Rico ("Projects"). The properties are rented to low-income tenants and are operated in a manner necessary to qualify for federal low-income housing tax credits as provided for in Section 42 of the Internal Revenue Code ("IRC").

The investment partnership is Hudson Housing Tax Credit Fund XL LP (the "Investor Limited Partner"). The special limited partner is Hudson SLP XL LLC (the "Special Limited Partner"); a Delaware limited liability company (collectively with the Investor Limited Partner, referred to as the "Limited Partners").

Profits, losses and tax credits are allocated in accordance with the Partnership Agreement. Profits and losses from operations and low-income housing tax credits in any one year shall be allocated 99.98% to the Investor Limited Partner, 0.01% to the Special Limited Partner and 0.01% to the General Partner. As defined in the Partnership Agreement, certain transactions and occurrences warrant special allocations of profits and losses. All other losses shall be allocated to the extent allowable under Section 704(b) of the IRC.

Pursuant to the Partnership Agreement, the Limited Partners are required to provide capital contributions totaling approximately \$235 million to the Partnership ("Initial Projected Equity"), subject to potential adjustment based on the amount of low-income housing credits ultimately allocated to the Projects in addition to other potential occurrences as more fully explained in the Partnership Agreement. As of June 30, 2011, the Limited Partners have provided capital contributions totaling \$20,862,203.

Pursuant to the Partnership Agreement, the General Partner is required to provide capital contributions totaling \$10 to the Partnership. Should the Partnership have no sufficient funds available to pay the outstanding balance of the developer's fee thereof, the General Partner shall be required to provide additional capital contributions to the Partnership in an amount sufficient for the Partnership to pay such balance in full. The General Partner shall have no right or obligation to make any other capital contributions. As of June 30, 2011, the General Partner had provided no capital contributions.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE G - PARTNERSHIP AGREEMENT (CONTINUED)

Pursuant to the Partnership Agreement, the Project Company is required to pay an annual management fee of \$61,980 to the General Partner for services rendered in connection with the administration of the Partnership's business affairs. The fee shall be adjusted annually by 3% and is payable from gross effective income, as further defined in the Partnership Agreement. To the extent funds are available in the Social Services Subaccount, the Partnership is also required to pay the Puerto Rico Public Housing Authority (PRPHA) an additional annual fee of \$50,000 (refer to Note O for details). The fees are payable on December of each year and shall accrue. As of June 30, 2011, the General Partner has earned and was owed \$33,863.

On July 14, 2010, the General Partner and the Limited Partners (collectively, the "Partners") entered into a Memorandum of Understanding (the "MOU"). The MOU detail certain mutually agreed-upon resolutions to issues that have arisen during the course of construction and rehabilitation of the Projects, with the expectation of amending and restating the Partnership Agreement. The contemplated resolution include change to certain commitments of the Partners affecting tax credits delivery and the resulting capital to be contributed, as well as, various revisions to the respective rights and obligations of the Partners. On December 30, 2010, the Partners entered into the First Amended and Restated Agreement of Partnership.

Assurance reserve fund

Pursuant to the Partnership Agreement, the PRDH as general partner shall establish the Assurance Reserve Fund at initial closing in the amount of the initial capital contribution less \$4,000,000 (plus any initial capital contribution with respect to the apartment complexes).

Amounts in the Assurance Reserve Fund shall be used, (i) upon the request of the General Partner, subject to the consent of the Special Limited Partner, or (ii) upon the direction of the Special Limited Partner, to meet financial obligations of the General Partner, other than for excess development costs, as provided in the Agreement. As of June 30, 2011 such reserve was maintained in the Partnership. The amount owed to PRDH for the assurance reserve fund as of June 30, 2011, amounted to \$16,636,341.

Deferred purchase price note

Also, on August 7, 2008, the PRDH entered in a loan agreement with Vivienda Modernization 1, LLC (the "Project Company") in the amount of \$102,889,957 for the acquisition of 33 residential rental properties (the "Deferred Purchase Price Note").

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE G - PARTNERSHIP AGREEMENT (CONTINUED)

Deferred purchase price note (continued)

The Project Company shall make payments equal to the amount of net available capital contributions for the preceding calendar quarter. Net available capital contributions are defined as: (i) the aggregate capital contributions received by the Project Company during the preceding calendar quarter, less (ii) any increase in the Assurance Reserve funded from such capital contributions during the preceding quarter as permitted under the Partnership Agreement, plus (iii) any amount the Project Company no longer needs to maintain the Assurance Reserve.

The terms of the deferred purchase price note are described as set forth below:

Commitment:	\$102,889,957
Interest rate:	3.55%
Maturity date:	Later of (i) funding of the last installment of the third capital contribution or (ii) August 7, 2013

The note shall be a full recourse liability of the Project Company; however, none of the Project Company's members have personal liability. As of June 30, 2011, the principal balance outstanding on the deferred purchase price note was \$102,889,957 and accrued interest was \$11,128,504. As further explained in Note S, this note was collected in full in September 2011.

Developer's fees

Additionally, on August 7, 2008, Vivienda Modernization 1, LLC (the Project Company) entered into a Master Developer Agreement with the PRDH to perform services in connection with the development, rehabilitation, and modernization of certain housing projects ("Developer Agreement"). Pursuant to the Master Developer Agreement, the PRDH will earn a developer's fee in the amount of \$75,082,335 for services performed and to be performed. Payment of the developer's fee shall be subject to the terms and conditions of Section 6(a) (i-iv) of the Developer Agreement. As of June 30, 2011, the Project Company owed PRDH the amount of \$41,070,209.

NOTE H - HOUSING UNITS AND LAND LOTS HELD FOR SALE OR LEASE

The PRDH has an inventory of land lots held for sale or lease. This inventory was valued at a nominal amount of \$1 per land lot since it will be granted to low income families at no cost. For the year ended on June 30, 2011, the value of the land lots held for sale or lease was \$41,415.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

**NOTE H - HOUSING UNITS AND LAND LOTS HELD FOR SALE OR LEASE
(CONTINUED)**

Enterprise fund - business type activities

The Enterprise Fund has an inventory of housing units. Land lots held for sale consist of real estate properties including parcels of land, houses and apartments. These properties are stated at their realizable value determined by appraised values determined by independent appraisers or by estimated values provided by management. On August 3, 2000, the Legislature of the Commonwealth of Puerto Rico enacted Act No. 383 establishing that "Finca San Patricio" was to be retained for the development of a public urban forest.

Also, it instructed the Enterprise Fund to transfer the lot to the Department of Natural Resources. As of June 30, 2011, the transfer has not been made. This property is stated at its realizable value determined by appraised values determined by an independent appraiser.

NOTE I - CAPITAL ASSETS

A summary of the activity of capital assets for the governmental activities group follows:

	<u>Balance at June 30, 2010</u>	<u>Adjustments</u>	<u>Adjusted Balance at June 30 2010</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance at June 30, 2011</u>
Capital assets not being depreciated:						
Land	\$ 983,700	\$ (189,983)	\$ 793,717	\$ -	\$ -	\$ 793,717
Capital assets being depreciated:						
Vehicles, fixtures and equipment	6,768,725	(1,330,241)	5,438,484	57,547	(12,735)	5,483,296
Parking and building	5,137,029	-	5,137,029	-	-	5,137,029
Building	30,000,000	-	30,000,000	-	-	30,000,000
Building Improvements	<u>16,288,636</u> 58,194,390	<u>4,724,632</u> 3,394,391	<u>21,013,268</u> 61,588,781	<u>-</u> 57,547	<u>-</u> (12,735)	<u>21,013,268</u> 61,633,593
Less accumulated depreciation	<u>(7,539,362)</u>	<u>(1,328,977)</u>	<u>(8,868,339)</u>	<u>(2,342,894)</u>	<u>-</u>	<u>(11,211,233)</u>
	<u>50,655,028</u>	<u>2,065,414</u>	<u>52,720,442</u>	<u>(2,285,347)</u>	<u>(12,735)</u>	<u>50,422,360</u>
	<u>\$51,638,728</u>	<u>\$ 1,875,431</u>	<u>\$53,514,159</u>	<u>\$(2,285,347)</u>	<u>\$(12,735)</u>	<u>\$51,216,077</u>

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE I - CAPITAL ASSETS (CONTINUED)

Capital assets of the Enterprise Fund — Business type activities as of June 30, 2011, are summarized as follows:

<u>Description</u>	<u>Amount</u>
Office furniture and equipment	\$ 64,761
Computer equipment	196,438
Motor vehicles	<u>116,228</u>
	377,427
Less valuation allowance on capital assets	<u>(278,746)</u>
	<u>\$ 98,681</u>

NOTE J - NOTES PAYABLE

Notes payables as of June 30, 2011, are composed of the following:

Note payable under a line of credit to the Puerto Rico Housing Finance Authority (PRHFA) for the Santurce Rehabilitation Plan, through the approval by corporate resolutions during fiscal year ended June 30, 2002. The loan is secured by properties owned by another governmental agency. The credit line carries interest based on quarterly variable labor rate plus 1.25%, with a minimum annual interest rate of six percent (6%). Principal and interest are payable annually. The note payable was due on March 15, 2009 Management is on the process of refinancing the balance due.	\$10,079,178
Note payable to the Government Development Bank for Puerto Rico (GDB) in monthly installments of \$250,000, including principal, escrow and interest on a quarterly variable rate of .75% over LIBOR. The note is pledged by an assignment of the rent agreements of two (2) tenants	<u>24,334,898</u>
Less current portion	<u>34,414,076</u> <u>(12,242,772)</u>
Notes payable, long-term portion	<u>\$22,171,304</u>

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE J - NOTES PAYABLE (CONTINUED)

At June 30, 2011, scheduled aggregate principal and interest maturities of notes payable were approximately as follow:

Year ending June 30,	<u>Principal</u>	<u>Interest</u>
2012	\$12,242,772	\$ 242,691
2013	2,168,690	220,264
2014	2,191,353	197,601
2015	2,214,252	174,702
2016	2,237,390	151,564
2017-2021	11,542,576	402,194
2022-2026	<u>1,817,043</u>	<u>7,998</u>
	<u>\$34,414,076</u>	<u>\$1,397,014</u>

NOTE K - COMPENSATED ABSENCES

Employees accrue vacation leave at a rate of two and a half (2.5) days per month up to a maximum of sixty (60) days. Unpaid vacation time accumulated is fully vested to the employees from the first (1) day of work.

Employee's accumulated sick leave at a rate of one and a half (1.5) days per month up to a maximum of ninety (90) days. Upon retirement, and employee receives compensation for all accumulated unpaid sick leave at their then current rate of pay, if the employee has at least ten (10) years of services with the PRDH.

Total vested pay benefits accrued for compensated absences at June 30, 2011, amount to \$6,461,924 which activity for the year ended June 30, 2011, is summarized as follows:

<u>Balance at June 30, 2010</u>	<u>Additions</u>	<u>Decrease</u>	<u>Balance at June 30, 2011</u>	<u>Due within One (1) year</u>
<u>\$6,521,563</u>	<u>\$1,271,116</u>	<u>\$1,330,755</u>	<u>\$6,461,924</u>	<u>\$2,972,485</u>

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE K - COMPENSATED ABSENCES (CONTINUED)

Enterprise Fund – Business Type Activities:

<u>Balance at June 30, 2010</u>	<u>Additions</u>	<u>Decrease</u>	<u>Balance at June 30, 2011</u>	<u>Due within One (1) year</u>
<u>\$140,552</u>	<u>\$69,848</u>	<u>\$25,305</u>	<u>\$185,095</u>	<u>\$185,095</u>

NOTE L - EMPLOYEES' RETIREMENT PLAN

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

The System provides retirement, death and disability benefits pursuant to Act No. 447 from May 15, 1951, as amended. Disability retirement benefits are available to members for occupational and nonoccupational disability benefits. However, a member must have at least the (10) year of service to receive non-occupational disability benefits.

No benefit are payable if the participant receives a refund of higher accumulated contribution. Retirements benefits depend upon age at retirement and the number of years of creditable service. Benefit vest after ten (10) years of plan participation. Members who have attained and age of at least fifty-five (55) years and have completed at least twenty-five (25) years of creditable service or members who have attained age of at least fifty-eight (58) years and have completed at least ten (10) years of creditable services, are entitled to an annual benefit, payable monthly for life.

Additional information of the System is provided in its most recent actuarial valuation for the year ended June 30, 2001, a copy of which can be obtained from the System at 437 Ponce de León Avenue, Hato Rey, Puerto Rico 00918, telephone number (787) 759-4410.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE M – VOLUNTARY TERMINATION BENEFITS

On July 2, 2010, the Commonwealth enacted Act No. 70 to establish a program that provides benefits for early retirement or economic incentives for voluntary employment termination to eligible employees, as defined, including employees of the PRDH. Act No. 70 established that early retirement benefits will be provided to eligible employees that have completed between 15 to 29 years of credited service in the Retirement System and will consist of biweekly benefits ranging from 37.5% to 50 % of each employee' salary, as defined. In this early retirement benefit program, the PRDH will make the employee and the employer contributions to the Retirement System and pay the corresponding pension until the employee complies with the requirements of age and 30 years of credited service in the Retirement System. Economic incentives are available to eligible employees who have less than 15 years of credited service in the Retirement System or who have at least 30 years of credited service in the Retirement System and the age for retirement or who have the age for retirement. Economic incentives will consist of a lump-sum payment ranging from one-month to six-month salary based on employment years. For eligible employees that choose the economic incentives and have at least 30 years of credited service in the Retirement System and the age for retirement or have the age for retirement, the PRDH will make the employee and the employer contributions to the Retirement System for a five year period. Additionally, eligible employees that choose to participate in the early retirement benefit program or that choose the economic incentive and have less than 15 years of credited service in the Retirement System are eligible to receive health plan coverage for up to 12 months in a health plan selected by management of the PRDH.

The financial impact resulting for the benefits granted to participants on this program was the recognition within the PRDH's financial statements of a liability of \$6,993,412 in the statement of net assets as of June 30, 2011 and a charge of \$6,993,412 in the statement of activities for the year ended June 30, 2011. At June 30, 2011, unpaid long-term benefits granted on this program were discounted at 2.95%.

NOTE N - AGENCY FUND

Ponce en Marcha

By Law No. 206 of August 28, 2003, the Department of Justice of the Commonwealth of Puerto Rico obtained a line of credit of \$90 million with the purpose of complying with a judicial settlement in the case of the Municipality of Ponce vs. the Puerto Rico Highway Authority and others. In relation with such settlement, the PRDH is the fiscal agent of the funds for planning and development of several Municipality of Ponce projects. The restricted cash balance is \$1,505,107 at June 30, 2011 and is presented in the statement of fiduciary net assets.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE N - AGENCY FUND (CONTINUED)

Special Communities

The PRDH is responsible for receiving and distributing funds assigned by the Perpetual Trust Fund for Special Communities for the Development Program (the Program). The Program was established by Act No. 271 of November 21, 2002, and is funded through legislative appropriations and other grants. Program funds are distributed to the services providers based on the contracts made with the Perpetual Trust Fund for Special Communities. The restricted cash balance is \$104,946 and the due from special community \$747,539 at June 30, 2011 and is presented in the statement of fiduciary net assets.

Remedy Fund

The Municipality of Juncos establish and funded a trust fund for the purpose of implementing the two remedies selected by the U.S. Environmental Protection Agency (EPA) for the old Juncos Landfill Superfund site as set forth in the EPA "Decision Summary" documents dated September 24, 1991, and October 5, 1993, as amended by EPA, to correct environmental damage left by the old Juncos Landfill. As part of these remedies the PRDH was appointed as the administrator agent of the Remedy Funds.

As part of the settlement agreement the PRDH establish \$1.5 million as Remedy Fund for construction. The restricted cash balance is \$1,455,726 at June 30, 2011 and is presented in the statement of fiduciary net assets.

NOTE O - COMMITMENTS AND CONTINGENCIES

Interagency agreement

On August 7, 2008, the PRDH (also referred to as the "General Partner"), the Puerto Rico Public Housing Authority (PRPHA), the Puerto Rico Housing Finance Authority (the "Authority"), and the Government Development Bank for Puerto Rico (the "GDB") entered into an Interagency Agreement (the "Agreement").

Pursuant to the Agreement, the PRPHA and the PRDH determined it would be advantageous for the housing projects to undergo comprehensive modernization and/or construction, which will be undertaken and operated by the Vivienda Modernization 1, LLC (the "Project Company"), whose sole member is the partnership, of which the PRDH is the General Partner (see Note G). Pursuant to the Agreement, the PRDH determined that the PRPHA is better suited to satisfy certain obligations and authorized the PRPHA to perform certain duties on behalf of the PRDH, as further detailed in Section 1(a-1) of the Agreement.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE O - COMMITMENTS AND CONTINGENCIES (CONTINUED)

Interagency agreement (continued)

The PRDH, with agreement from the Authority and the GDB, created a fund to support the programs of the PRDH (the "Program Modernization Fund"). The Program Modernization Fund will be held jointly by the GDB and the PRDH. The PRDH will use the Program Modernization Fund from time to time to finance the costs of modernizing and/or constructing other affordable units and to provide grants to the Authority.

The Authority shall assign to the PRPHA all payments received from the Project Company in accordance with appropriate loan documents. The PRDH also assigned to the PRPHA a portion of the purchase price as reimbursement of certain costs incurred previously by the PRPHA for the rehabilitation or construction of a portion of the units.

Finally, the PRDH and the PRPHA acknowledged that some of the public housing rental developments included in the Projects were subdivided from larger projects owned by the PRPHA. The PRDH and PRPHA will permit the use of the facilities by all residents of the main and subdivided rental developments.

Ground lease

On August 1, 2008, the PRDH entered into a ground lease agreement with Vivienda Modernization Holdings 1, S.E., a related entity. The lease is for a period of 99 years and requires a payment of \$1 per project. The related entity is required to use the land and property to rehabilitate, construct, develop and maintain public housing apartment.

Operating leases

The PRDH has long-term operating lease agreements for substantially all of its office facilities for periods up to thirty (30) years.

Litigation - PRDH

The PRDH is defendant in a number of lawsuits. As stated by legal counsel, the PRDH has recorded a provision of \$5,108,247 in its governmental activities to cover its exposure to these lawsuits. The amount of the required reserve in other litigations that may result from the final settlement of these other lawsuits cannot be presently determined. In these case, the ultimate amount that the PRDH may be required to pay as a result of the financial settlement of these lawsuits, if any, shall be funded through an appropriation from the Legislature of the Commonwealth of Puerto Rico.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE O - COMMITMENTS AND CONTINGENCIES (CONTINUED)

Litigation - PRDH (continued)

The activity for the year related to the provision is as follows:

<u>Balance at June 30, 2010</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at June 30, 2011</u>	<u>Due within One year</u>
<u>\$4,938,600</u>	<u>\$2,287,611</u>	<u>\$2,117,964</u>	<u>\$5,108,247</u>	<u>\$455,753</u>

Litigation – enterprise fund

At June 30, 2011, the Enterprise Fund is defendant in several lawsuits generally incidental to its operations; some of these cases were originated by the predecessor entity. Law No. 106 of June 1998 prescribed that the Enterprise Fund will not be liable for any pending litigation in excess of the legal reserve of \$3,000,000. Any excess of legal claims over the reserve will be paid from the general fund of the Commonwealth of Puerto Rico. At June 30, 2011, the accrued legal claims of \$207,134 are included in the statement of net assets in liquidation.

Federal and state awards

The PRDH participates in a number of federal financial assistance programs funded by the federal government. Expenditures financed by these programs are subject to financial and compliance audits by the appropriate grantors or their representatives. If expenditures are disallowed due to noncompliance with grant program regulations, the PRDH may be required to reimburse the grantors for such expenditures.

The PRDH is from time to time audited by the Office of the Controller for Puerto Rico (the Controller) which audits could result in request for reimbursements or other resolutions. These amounts, if any, of expenditures, which may be disallowed, cannot be determined at this time. Management believes that such disallowances, if any, will not have a material effect in the financial statements of the PRDH.

NOTE P – DISTRIBUTED NET ASSETS

The Enterprise Fund is required to transfer all unrestricted cash available to the PRDH, after any payroll debt as of June 30, 1998 has been paid off to its employees, as well as any proceed from sale of assets and from mortgages, and after the deduction of operating and administrative expenses, among others, in order to comply with Law No. 106 of August 16, 2001, as amended.

Also, the Enterprise Fund is required to transfer restricted cash available to be used for necessary and eligible activities within the housing programs of the PRDH that directly relate to the expansion of the supply of low and moderate income housing and other initiatives covered in the housing programs.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

NOTE Q – MORTGAGE INTEREST REVENUES

During the fiscal year ended June 30, 2011, the Enterprise Fund recorded mortgage interest revenues of \$66,324 and principal payments of \$690,348 for a total of \$756,672 in mortgage revenues.

NOTE R - FUND BALANCE

As of these financial statements, the PRDH has adopted GASB Statement No. 54, which redefined how fund balances of the governmental funds are presented in the financial statements. For the details of the fund balances classified definition please refer to Note A.

General Fund

The General Fund has Assigned Fund Balance of \$67,085 at June 30, 2011.

Section 8 Housing Choice Voucher Fund

The Section 8 Housing Choice Voucher Fund has Restricted Fund Balance of \$14,513,292 related to the Federal Awards to fulfill the Agency's affordable housing programs.

Self Contribution Fund

The Self Contribution Fund has Nonexpendable Fund Balance of \$172,506,413 related principally to accounts and note receivable based on the Partnership Agreement, see detail in Note G. Federal grant of \$5,269 is considered Restricted Fund Balance. The Committed Fund Balance of \$18,791,578 relates to specific purposes constrained provided by the Act. 173 of August 31, 1996, as amended; and the Assigned Funds Balance of \$1,206,637 is related to professional services contracts.

Other Governmental Funds

The non-major fund has a Special Revenue Restricted Fund Balance designated for specific purposes of \$208,524 related to federal grants. Also the PRDH has a Committed Fund Balance of \$16,227,921 relate to legislation resolution. The remaining Assigned Fund Balance of \$7,591,744 is related to a debt service fund.

NOTE S – SUBSEQUENT EVENT

Partnership Agreement

On September 29, 2011 the PRDH received the amount of approximately \$100 million from Vivienda Modernization 1, LLC for the repayment of note receivable principal and interest of \$87.8 million and \$12.2 million, respectively. See Note G.

REQUIRED SUPPLEMENTARY INFORMATION

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
SCHEDULE OF BUDGETARY COMPARISON
YEAR ENDED JUNE 30, 2011**

	GENERAL FUND			
	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual Amounts in the Budgetary Basis</u>	<u>Variance Favorable (Unfavorable)</u>
Resources				
State appropriations	\$20,445,732	\$20,445,732	\$20,445,732	\$ -
Expenditures charged to Appropriations	<u>20,445,732</u>	<u>20,445,732</u>	<u>20,378,647</u>	<u>67,085</u>
Excess (deficiency) of resources under appropriations	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 67,085</u>	<u>\$67,085</u>

See note to schedule of budgetary comparison.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTE TO SCHEDULE OF BUDGETARY COMPARISON
YEAR ENDED JUNE 30, 2011**

NOTE A - BUDGETS AND BUDGETARY ACCOUNTING

The Department of Housing of the Commonwealth of Puerto Rico (PRDH) follows these procedures in establishing the budgetary data reflected in the financial statements:

- a. Formal budgetary integration is employed as a management control device during the year for the General Fund. The Department of the Treasury and the Office of Management and Budget of Puerto Rico has the responsibility to ensure that budgetary spending control is maintained in the PRDH. Budgetary control is exercised through the Puerto Rico Integrated Financial Accounting System ("PRIFAS").
- b. On or before November 15, the Secretary submits to the Office of Management and Budget of Puerto Rico a proposed operating budget for review and approval. OMB will submit the revised budget to the Legislature of the Commonwealth of Puerto Rico for final approval to be effective for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means for financing them.
- c. The budget is legally enacted through passage of a law.
- d. Unused appropriations for the annual budgeted funds lapse at the end of the year.
- e. The budget is prepared on the budgetary basis of accounting. The actual results of operations presented in the Schedule of Budgetary Comparison are in conformity with the budgetary accounting for a better comparison with the budget information. See Note A to the financial statements.

OTHER SUPPLEMENTARY INFORMATION

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2011**

Federal Grantor / Pass-Through Grantor / Program or Cluster Title	Federal CFDA Number	Federal Expenditures
U.S. Department of Housing and Urban Development/ Direct Programs:		
Shelter Plus Care	14.238	\$ 252,664
Section 8 Housing Choice Vouchers	14.871	57,163,294
Supporting Housing for Persons with Disabilities (Section 811)	14.181	<u>111,199</u>
		57,527,157
U.S. Department of Agriculture/Pass-through the Puerto Rico Department of Education		
Child and Adult Care Food Program	10.558	<u>24,745</u>
Total		<u><u>\$57,551,902</u></u>

See accompanying notes to Schedule of Expenditures of Federal Awards.

Forres Blompart, Sanchez Ruiz LLP

Certified Public Accountants and Business Consultants

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2011**

NOTE A - BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of the Puerto Rico Department of Housing (the PRDH) under programs of the federal government for the year ended June 30, 2011. The information in this Schedule is presented in accordance with the requirement of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of the PRDH, it is not intended to and does not purport to present the financial position, changes in net assets, or cash flows of the PRDH.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Expenditures reported on the Schedule are reported on the receipts and disbursements method of accounting. It is drawn primarily from the PRDH's internal accounting records, which are the basis for the PRDH's financial statements. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for States, Local, and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.
2. Pass-through entities identifying numbers were not available.
3. The titles of federal awards included in the Schedule are presented as described in the Catalog of Federal Domestic Assistance.

NOTE C - RELATIONSHIP TO THE STATEMENT

Expenditures included in the Schedule for the major programs agreed with the accompanying statement of revenues, expenditures and changes in fund balances - governmental funds.



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Honorable Secretary of the
Department of Housing of the
Commonwealth of Puerto Rico
San Juan, Puerto Rico

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

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Department of Housing of the Commonwealth of Puerto Rico (PRDH) as of and for the year ended June 30, 2011, which collectively comprise the PRDH's basic financial statements and have issued our report thereon dated January 13, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses.

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Honorable Secretary of the
Department of Housing of the
Commonwealth of Puerto Rico
San Juan, Puerto Rico

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

Internal Control over Financial Reporting (continued)

We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs as Findings No. 11-02 and 11-03 that we consider to be significant deficiencies in internal control over financial reporting. 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the PRDH's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as Findings No. 11-02 and 11-03.

We also noted certain other matters that we reported to management of the PRDH in a separate letter dated January 13, 2012.

The PRDH's response to the findings identified in our audit is described in the accompanying Corrective Action Plan. We did not audit the PRDH's response and, accordingly, we express no opinion on it.

Honorable Secretary of the
Department of Housing of the
Commonwealth of Puerto Rico
San Juan, Puerto Rico

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

Compliance and Other Matters (continued)

This report is intended solely for the information and use of the management and officials of the Puerto Rico Department of Housing, the Commonwealth of Puerto Rico, federal awarding agencies, pass-through entities, and other regulatory agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Toures Blompart, Sánchez Ruiz LLP

January 13, 2012
License No. 221
San Juan, Puerto Rico

The stamp number 2633446 was
affixed to the original of this report.



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San Juan, Puerto Rico

Members of:

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

Compliance

We have audited the compliance of the Puerto Rico Department of Housing of the Commonwealth of Puerto Rico (the PRDH) with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended June 30, 2011. The PRDH's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the PRDH's management. Our responsibility is to express an opinion on the PRDH's compliance based on our audit.

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

In our opinion, PRDH, complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2011. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as Findings No. 11-02 and 11-03.

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Honorable Secretary of the
Department of Housing of the
Commonwealth of Puerto Rico
San Juan, Puerto Rico

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONTINUED)**

Internal Control Over Compliance

Management of the PRDH is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered PRDH's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of PRDH's internal control over compliance.

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 the 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.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified certain deficiency in internal control over compliance that we consider to be a significant deficiency as described in the accompanying schedule of findings and questioned costs as Finding No. 11-03.

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

Honorable Secretary of the
Department of Housing of the
Commonwealth of Puerto Rico
San Juan, Puerto Rico

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONTINUED)**

Internal Control Over Compliance (continued)

The PRDH's response to the findings identified in our audit is described in the accompanying Corrective Action Plan. We did not audit the PRDH's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the management and officials of the Puerto Rico Department of Housing, the Commonwealth of Puerto Rico, federal awarding agencies, pass-through entities, and other regulatory agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Torres Blompart, Sanchez Ruiz LLP

January 13, 2012
License No. 221
San Juan, Puerto Rico

The stamp number 2633447 was
affixed to the original of this report.

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2011

SECTION 1-SUMMARY OF AUDITORS' RESULTS

1. The independent auditors' report on the financial statements expressed a qualified opinion on the governmental activities and the business-type activities of the PRDH because the effects of any adjustments and additional disclosures that might have resulted had management furnished us with reasonably accurate data regarding the inventory of housing units and land lots held for sale. In addition, the independent auditors' report on the financial statements, expressed an unqualified opinion on the respective financial position of each major fund, and the aggregate remaining fund information of the PRDH and the respective changes in financial position.
2. Deficiencies on internal control over financial reporting were identified, none of which were considered material weaknesses, and two of which were considered significant deficiencies.
3. A deficiency on internal control over compliance with requirements applicable to major federal award programs was identified, which was considered a significant deficiency.
4. The independent auditors' report on compliance with requirements applicable to major federal award programs expressed an unqualified opinion on the Section 8 Housing Choice Vouchers program (CFDA 14.871).
5. The PRDH did not qualify as a low-risk auditee as that term is defined in OMB Circular A-133.
6. The audit disclosed findings required to be reported under OMB Circular A-133.
7. A threshold of \$1,726,557 was used to distinguish between Type A and Type B programs, as those terms are defined in OMB Circular A-133.

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-01 ACCOUNTING RECORDS

Federal programs

All federal financial assistance programs

Category

Internal control

Compliance requirement

Special tests and provisions

Condition found

The accounting records of the PRDH are organized and maintained on the basis of governmental funds. Each fund is accounted for by a separate set of self-balancing accounts that comprises its assets, liabilities, fund balance, revenues and expenditures. Fund financial statements report detailed information about the PRDH. The focus of governmental fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column in the financial statements. During our financial and compliance audit procedures for the fiscal year ended June 30, 2011, we noted the following deficiencies related to the accounting procedures and financial reporting practices of the PRDH:

- The financial control systems did not prevent or detect material misstatements in operational results so that it was later necessary to make significant corrections to the results initially reported. Over ten journal entries with an effect in the change of net assets of \$54 million were posted in order to present the financial statements in accordance with GAAP.
- The Treasury Department of the Commonwealth of Puerto Rico provides accounting services to the PRDH through their accounting system (PRIFAS) for certain state funds during most of fiscal year ended June 30, 2011. PRIFAS has inappropriate as well as incomplete month-end and year-end reconciliation and closing procedures which prevent the timely processing of adjustments and financial statements. Accounting for federal programs is kept separately by the PRDH. The PRDH has not completed an internal control process for the conversion of the PRIFAS accounting data from budget/cash basis to the modified accrual basis of accounting which represents the basis used to prepare the financial statements. However, a project for this conversion is underway.

Forres Blompart, Sánchez Ruiz LLP

Certified Public Accountants and Business Consultants

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-01 ACCOUNTING RECORDS (CONTINUED)

Condition found (Continued)

- PRDH operates an Enterprise Fund (former Office of Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation or CRUV). During our audit we noted that CRUV maintains an inventory of housing units and land lots held for sale. However, such inventory is not complete and CRUV does not have reasonable knowledge of all the housing units and land lots that are pending to be included in the inventory. Also, the valuation of such properties is not in accordance with U.S. generally accepted accounting principles (GAAP).
- As further explained in Finding No. 11-02, we noted control deficiencies in the maintenance of the accounting records for property and equipment.

Criteria

Sections 20 (a) and (b) (1) to (3) and (6) on Subpart C of the OMB Common Rule establish that:

- a. A State must expand and account for grant funds in accordance with State laws and procedures for expending and accounting for its own funds. Fiscal control and accounting procedures of the State, as well as its subgrantees and cost-type contractors, must be sufficient to:
 - i. Permit preparation of reports required by this part and the statutes authorizing the grant, and
 - ii. Permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.
- b. The financial management systems of other grantees and subgrantees must meet the following standards:
 - i. Financial reporting - Accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or subgrant.

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-01 ACCOUNTING RECORDS (CONTINUED)

Criteria (continued)

- ii. Accounting records - Grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially-assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.
- iii. Internal control - Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.
- iv. Source documentation - Accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contracts and subgrant award documents, etc.

Also, Article No. 5 of Law No. 55 dated August 9, 1991, established the following disposition regarding the inventory of land and housing units held for sale: CRUV, through the Sales Division, will maintain a current inventory of real properties that from dispositions of the Law were transferred under the control of CRUV with the dissolution of the Special Trustee Office. The inventory of properties will be prepared and maintained in a way that will facilitate the search based on the Municipality location and will assign a number that will identify permanently such property in the inventory and will record all of the transactions made to such real property. Additionally, CRUV uses the liquidation basis of accounting for reporting purposes which is a basis in accordance with GAAP. This basis requires adjustment of the carrying amounts of assets to the amounts expected in liquidation. Therefore, under this basis, assets should be carried at estimated net realizable value.

Cause

Old practices within PRDH and other operational conditions have made difficult the implementation of corrective actions. However, the new accounting system is almost implemented.

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-01 ACCOUNTING RECORDS (CONTINUED)

Effect

These conditions prevent PRDH to prepare accurate and timely fiscal reports. PRDH contracted an outside consultant to assist management in the preparation of the PRDH's financial statements which they reviewed and approved. The consultants are also improving the maintenance of the accounting records.

Questioned costs

None

Recommendations

The PRDH shall revise its accounting practices and policies to provide for an accurate reporting financial system. PRDH should maintain its efforts to develop a unitary accounting system for all governmental funds in one general ledger. The PRDH shall emphasize the importance of maintaining an adequate filing system that allows the prompt retrieval of documents and related supporting documentation.

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-02 PROPERTY AND EQUIPMENT

Federal programs

All federal financial assistance programs

Category

Compliance / Internal control

Compliance requirement

Equipment and real estate property management

Condition found

To determine compliance with equipment and real estate property management requirements, we obtained an understanding of state's policies and procedures. Then, we performed tests of controls to determine if: a) state's policies and procedures have been complied with; b) established controls are effective; and c) to assess control risk.

After obtaining an understanding of the state's policies and procedures and performing our tests of controls, we noted the following:

1. When we started the audit on August 2011, we noted the following deficiencies in the records of property and equipment maintained by PRDH during the fiscal year ended June 30, 2011 (which are deficiencies noted in prior years):
 - a. The Property Division did not maintain an effective property and equipment system from which a current and complete subsidiary ledger can be prepared.
 - b. The accumulated depreciation subsidiary did not include the accumulated depreciation for most fixed assets. The accumulated depreciation is not supported by proper subsidiaries and it was not segregated by type of asset.
2. During the audit, PRDH contracted an external consultant to work with these deficiencies. By the end of the audit, management proposed certain journal entries to correct the records of property and equipment. As a result, beginning balances were adjusted as follow:

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-02 PROPERTY AND EQUIPMENT (CONTINUED)

Condition found (continued)

	<u>Balance at June 30, 2010</u>	<u>Adjustments</u>	<u>Adjusted Balance at June 30 2010</u>
Capital assets not being depreciated: Land	\$ 983,700	\$ (189,983)	\$ 793,717
Capital assets being depreciated:			
Vehicles, fixtures and equipment	6,768,725	(1,330,241)	5,438,484
Parking and building	5,137,029	-	5,137,029
Building	30,000,000	-	30,000,000
Building Improvements	<u>16,288,636</u>	<u>4,724,632</u>	<u>21,013,268</u>
	58,194,390	3,394,391	61,588,781
Less accumulated depreciation	<u>(7,539,362)</u>	<u>(1,328,977)</u>	<u>(8,868,339)</u>
	<u>50,655,028</u>	<u>2,065,414</u>	<u>52,720,442</u>
	<u>\$51,638,728</u>	<u>\$ 1,875,431</u>	<u>\$53,514,159</u>

PRDH was not able to identify the reasons for the adjustments in the beginning balances since this analysis has not been done before.

Criteria

Section 32 (b) Subpart C of the OMB Common Rule establishes that a State will use, manage, and dispose of equipment acquired under a grant by the State in accordance with State laws and procedures. In addition, section 32 (d) establishes that procedures for managing equipment (including replacement equipment), whether acquired in whole or in part with grant funds, until disposition takes place will, as a minimum, meet the following requirements:

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

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-02 PROPERTY AND EQUIPMENT (CONTINUED)

Criteria (continued)

- c. A control system must be developed to ensure adequate safeguards to prevent loss, damage, or theft of the property. Any loss, damage, or theft shall be investigated.
- d. Adequate maintenance procedures must be developed to keep the property in good condition.
- e. If the grantee or subgrantee is authorized or required to sell the property, proper sales procedures must be established to ensure the highest possible return.

Article XIV of the State's Property Rules and Regulations ("Reglamento #11: Control y Contabilidad de la Propiedad") sections (A) and (B) establish that the property registers of the Agencies should be supported by a physical inventory. The Property Division of the Puerto Rico Treasury Department (PRTD) will establish the date in which the agencies will perform their annual inventory.

Also, Section (D) of Article XIV establishes that the agencies will prepare the inventory in an electronic form using the SC795 Form, Fixed Assets Physical Inventory. The form SC795 and SC795.1 (Physical Inventory Certification) forms will be sent to the PRTD. The inventory should include the following: (1) description of the property; (2) the acquisition date; (3) cost of the property; (4) property class; (5) property number, and (6) source of funds for the purchase of property.

Effect

The PRDH is exposed to the risk of possible unauthorized use and disposition of equipment due to the lack of adequate internal controls and adequate property and equipment records.

Questioned costs

Could not be determined

Recommendations

The PRDH shall design and establish adequate controls and procedures to be followed by the Property Division. Property records shall include the required information to improve accountability, control and to detect possible loss or theft of property.

Torres Rompart, Sánchez Ruiz LLP

Certified Public Accountants and Business Consultants

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

FINDING NO. 11-02 PROPERTY AND EQUIPMENT (CONTINUED)

Recommendations (continued)

All property records shall be thoroughly reviewed to make sure that all information included in them is accurate and pertinent.

Additionally, a physical inventory of all equipment and property shall be performed at least annually and reconciled with the property records. Verification should be made to ascertain that property and equipment is being properly safeguarded and used solely for the authorized purposes.

DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

**FINDING NO. 11-03 SPECIAL TESTS AND PROVISIONS – HOUSING
QUALITY STANDARDS ENFORCEMENT – SECTION 8
HOUSING CHOICE VOUCHERS**

Federal program

CFDA 14.871 Section 8 Housing Choice Vouchers

Category

Compliance / Internal control

Compliance requirement

Special tests and provisions - housing quality standards enforcement

Condition found

To test compliance with the Housing Quality Standards (HQS) for the Section 8 Housing Choice Vouchers program, we selected forty (40) projects inspections for review from four (4) Regional Areas. During our test, we noted that in twelve (12) cases (30%) the PRDH failed to visit the properties on time (within 30 days granted) to ensure the owner corrected the deficiencies noted during the first inspection of the property.

Criteria

24 CFR section 982.404 (a) (3) establishes that 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).

Effect

Noncompliance with the above mentioned requirements could lead to significant administrative actions by the grantor, including cost disallowances. It could also be interpreted as a failure to achieve program objectives.

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2011

**FINDING NO. 11-03 SPECIAL TESTS AND PROVISIONS – HOUSING
QUALITY STANDARDS ENFORCEMENT – SECTION 8
HOUSING CHOICE VOUCHERS (CONTINUED)**

Questioned costs

Could not be determined

Recommendation

PRDH should improve the control system on compliance to ensure that timely action is taken whenever an owner of a dwelling property under the Section 8 Housing Choice Voucher program does not correct the cited HQS deficiencies within the specified correction period.

SCHEDULE OF PRIOR YEAR AUDIT FINDING

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2011**

The audit report for the year ended June 30, 2010, of the Puerto Rico Department of Housing, issued by Torres Llompart, Sanchez Ruiz, LLP, present audit findings corresponding to federal and states programs, some of them related to the Home Investment Partnership Program (HOME), CFDA #14.239. This program was transferred to the Administration for Housing Finance effective on July 1, 2010; therefore, the PRDH is not the entity responsible to prepare the Corrective Action Plan (CAP) for those findings going forward. Please find below a summary of the audit findings related to the HOME Program:

Finding No.

- 10-01 Accounting Records
- 10-02 Disbursement Tests
- 10-03 Davis Bacon Act
- 10-04 Eligibility- Home Investment Partnership Program
- 10-05 Property and Equipment
- 10-06 Performance Reporting- Home Investment Partnership Program
- 10-07 Sub recipient Monitoring- Home Investment Partnership Program
- 10-08 Special Tests and Provisions-Housing Quality Standards- Home Investment Partnership Program

Please find below the descriptions of the remaining audit findings and their status:

Finding No. 10-01- Accounting Records

Federal Program

14.871 Section 8 Housing Choice Vouchers Program

Category

Compliance/Internal Control

Compliance Requirement

Special tests and provisions

Condition Found

Deficiencies related to the accounting procedures and financial reporting practices of the Puerto Rico Department of Housing (PRDH).

Current Status

In process of implementation. During March 2012 we initiated the upgrade of the accounting system (Emphasys) to allow the reconciliation of the accounting records and the preparation of year-end financial statements in accordance with U.S. GAAP. This included training to the Accounting Department personnel. To accomplish this endeavor, we engaged a respected local Consulting Firm to support the PRDH personnel with the development of trainings and evaluating the adequacy of internal controls and monitoring systems.

Torres Llompart, Sanchez Ruiz LLP

Certified Public Accountants and Business Consultants

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2011**

For the FY 2010-2011 the Management provided the external auditors with a complete set of Financial Statements in accordance with GAAP.

Person Responsible: CPA Edwin Reyes Gonzalez, Auxiliary Secretary of Administration

Completion Date: Compliance with GAAP Financial Reporting June 30, 2011
Preparation of Manuals and Procedures, including training
to the Finance Department's staff September 30, 2012

Finding No. 10-02- Disbursement Test

Federal Program
14.871 Section 8 Housing Choice Vouchers Program

Category
Compliance/Internal Control

Compliance Requirement
Procurement and suspension and debarment

Condition Found
The audit found various instances in which the procurement files were incomplete when testing compliance and internal controls over allowability and procurement and suspension and debarment requirements.

Current Status
The recommendation was adopted in January 2011. The Secretariat for the Home Subsidy has designated Mr. José Quevedo Motta as the official responsible to verify the compliance with the suspension and debarment requirement before a contract is granted. Also, Management had developed a certification form (specifically prepared to verify compliance with Procurement & Debarment) that will be used by the Director of Procurement and the Legal Department who will certify that the vendor is not part of the suspended or debarred list.

Person Responsible: José Quevedo Motta, Administrative Official III
Lcda. Alessandra Rosa Tirado, Legal Department Director
Federal Program Directors

Completion Date: January 2011

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2011**

Finding No. 10-05- Property and Equipment

Federal Program

14.871 Section 8 Housing Choice Vouchers Program

Category

Compliance/Internal Control

Compliance Requirement

Equipment and real estate property management

Condition Found

PRDH's Property Division does not have an effective property and equipment system from which a current and complete subsidiary ledger can be prepared and did not perform reconciliation procedures between the property general ledger control accounts and the related subsidiaries. Most property and equipment subsidiaries were not available for review. Also, the auditor noted that the accumulated depreciation subsidiary did not include the accumulated depreciation for most fixed assets.

Current Status

Management acquired the module for the fixed asset inventory control which interface with the accounting system (Emphasys) in compliance with GASB 34. This improvement helps management detect possible loss or theft of property. We are also performing the implementation of a suitable internal control and monitoring system to reduce these risks.

A physical inventory of property, plant and equipment (PP&E) was performed during the FY 2010-2011 and reconciled with the accounting records. Also, an examination in detail of the sub-ledger of depreciation expense was performed to ascertain their accuracy and completeness.

Person Responsible: CPA Edwin Reyes Gonzalez, Auxiliary Secretary of Administration

Completion Date: Review of PP&E files and reconciliations	June 30, 2011
Preparation of Manuals and Procedures, including training to the Finance Department's staff	September 30, 2012

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2011**

**Finding No. 10-09- Special Tests and Provisions- Housing Quality Standards Enforcement-
Section 8 Housing Choice Vouchers**

Federal Program

14.871 Section 8 Housing Choice Vouchers Program

Category

Compliance/Internal Control

Compliance Requirement

Special tests and provisions- housing quality standards enforcement

Condition Found

PRDH failed to visit the properties on time (within 30 days granted) to ensure the owner corrected the deficiencies noted during the first inspection of the property.

Current Status

Written instructions were given to Section 8 Inspectors to assure that re-inspections to units that have failed are made accordingly in the specific time frame establish in federal regulation.

A software system "Emphasys Elite" provides an automatic abatement of HAP payments to owners who don't comply with the corrections of deficiencies within the specific time frame period. For monitoring purposes this software generates an Abatement and Payment Hold Listing Report whenever require. A Control Log of Deficiencies is received at Quality Control Assurance Area in a monthly basis to monitor compliance.

Person Responsible: Hilda I. Camacho, Section 8 Director

Carmina M. Osorio, HQS Quality Control Unit Admin Director
(Monitoring Process)

Completion Date: June 30, 2012

CORRECTIVE ACTION PLAN

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
CORRECTIVE ACTION PLAN AND MANAGEMENT RESPONSE
YEAR ENDED JUNE 30, 2011**

Finding No.

2011-01 Accounting Closing Procedures

2011-02 Property and Equipment

2011-03 Special Tests and Provisions-Housing Quality Standards Enforcement- Section 8
Housing Choice Vouchers

Please find below the corrective action plan and management response for the audit findings stated above:

Finding No. 2011-01- Accounting Closing Procedures

Federal Program

14.871 Section 8 Housing Choice Vouchers Program

Category

Internal Control

Compliance Requirement

Special tests and provisions

Corrective Action Plan:

In process of implementation. During March 2012 we initiated the upgrade of the accounting system (Emphasys) to allow the reconciliation of the accounting records and the preparation of year-end financial statements in accordance with U.S. GAAP. This included training to the Accounting Department personnel. To accomplish this endeavor, we engaged a respected local Consulting Firm to support the PRDH personnel with the development of trainings and evaluating the adequacy of internal controls and monitoring systems.

For the FY 2010-2011 the Management provided the external auditors with a complete set of Financial Statements in accordance with GAAP.

CRUV:

The administration contracted the services of an expert firm (Nextep) to update the inventory of properties available for sale and the related estimated values. The contract includes a development of a web page to facilitate access to the listing of properties with a detailed description and amenities of each one of them.

CRUV considers that the properties not included in the sub-ledger are not considered significant for the financial statements taken as a whole. In addition, we consider as a conservative approach

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
CORRECTIVE ACTION PLAN AND MANAGEMENT RESPONSE
YEAR ENDED JUNE 30, 2011**

not to include an estimate of the value of those properties in the financial statements. We also plan to make an evaluation during the up-coming fiscal year of the net realizable value of the properties by means of benchmarking with matching the values of properties recently sold and having similar characteristics. We considered that this approach should result in having a reasonable estimate of the net realizable value. Nevertheless, we will keep evaluating this option as we perform the analysis.

Person Responsible: CPA Edwin Reyes-González, Auxiliary Secretary of Administration

Completion Date: Compliance with GAAP Financial Reporting June 30, 2011

Preparation of Manuals and Procedures, including training
to the Finance Department's staff. September 30, 2012

Finding No. 2011-02- Property and Equipment

Federal Program

14.871 Section 8 Housing Choice Vouchers Program

Category

Compliance/Internal Control

Compliance Requirement

Equipment and real estate property management

Corrective Action Plan:

Management acquired the module for the fixed asset inventory control which interface with the accounting system (Emphasys) in compliance with GASB 34. This improvement helps management detect possible loss or theft of property. We are also performing the implementation of a suitable internal control and monitoring system to reduce these risks.

A physical inventory of property, plant and equipment (PP&E) was performed during the FY 2010-2011 and reconciled with the accounting records. Also, an examination in detail of the sub-ledger of depreciation expense was performed to ascertain their accuracy and completeness.

Person Responsible: CPA Edwin Reyes Gonzalez, Auxiliary Secretary of Administration

Completion Date: Review of PP&E files and reconciliations June 30, 2011

**DEPARTMENT OF HOUSING OF THE
COMMONWEALTH OF PUERTO RICO
CORRECTIVE ACTION PLAN AND MANAGEMENT RESPONSE
YEAR ENDED JUNE 30, 2011**

Preparation of Manuals and Procedures, including training
to the Finance Department's staff

September 30, 2012

**Finding No. 2011-03- Special Tests and Provisions- Housing Quality Standards
Enforcement- Section 8 Housing Choice Vouchers**

Federal Program

14.871 Section 8 Housing Choice Vouchers Program

Category

Compliance/Internal Control

Compliance Requirement

Special tests and provisions- housing quality standards enforcement

Corrective Action Plan

Written instructions were given to Section 8 Inspectors to assure that re-inspections to units that have failed are made accordingly in the specific time frame establish in federal regulation.

A software system " Emphasys Elite" provides an automatic abatement of HAP payments to owners who don't comply with the corrections of deficiencies within the specific time frame period. For monitoring purposes this software generates an Abatement and Payment Hold Listing Report whenever require. A Control Log of Deficiencies is received at Quality Control Assurance Area in a monthly basis to monitor compliance.

Person Responsible: Hilda I. Camacho, Section 8 Director

Carmina M. Osorio, HQS Quality Control Unit Admin Director
(Monitoring Process)

Completion Date: June 30, 2012