



guzmán torres & co., psc

certified public accountants & business advisors

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

AUDITED FINANCIAL STATEMENTS AND
SINGLE AUDIT OF FEDERAL FINANCIAL
ASSISTANCE PROGRAM
YEARS ENDED JUNE 30, 2009 AND 2008

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PUERTO RICO METROPOLITAN BUS AUTHORITY

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INDEPENDENT AUDITORS' REPORT

Hon. Rubén A. Hernández Gregorat, MEM, P.E.
Secretary Department of Transportation and Public Works

We have audited the accompanying statements of net assets of Puerto Rico Metropolitan Bus Authority (the Authority), a component unit of the Commonwealth of Puerto Rico, as of June 30, 2009, and the related statements of revenues, expenses and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits. The financial statements of the Authority as of and for the year ended June 30, 2008, were audited by other auditors whose opinion dated April 15, 2009 expressed an unqualified opinion on those statements. As discussed in Note 12, the Authority has restated its 2008 financial statements during the current year to properly reflect the balance of transportation equipment and related accumulated depreciation. The other auditors reported on the 2008 financial statements before the restatement.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. 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 audits provide a reasonable basis for our opinion.

In our opinion, the 2009 financial statements referred to above present fairly, in all material respects, the financial position of Puerto Rico Metropolitan Bus Authority at June 30, 2009 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

We also audited the adjustments described in Note 2 that were applied to restate the 2008 financial statements. In our opinion, such adjustments are appropriate and have been properly applied.

In accordance with *Government Auditing Standards*, we have also issued our report, dated March 12, 2010 on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants 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 read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis information on pages 3 through 9 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards for the year ended June 30, 2009 is presented for purposes of additional analysis as required by the United States 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. This schedule is the responsibility of the Authority's management. Such schedule has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

As described in Note 11 to the financial statements, the Authority received operating assistance from the Commonwealth of Puerto Rico to assist in the financing of the Authority's operations. The amount of such assistance indicates that the Authority may require continued assistance in order to operate at its current level as a going concern.

Guzmán Torres & Co., P.S.C.

CERTIFIED PUBLIC ACCOUNTANTS
March 12, 2010

Stamp #2505874
was affixed to
the original of
this report.

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

MANAGEMENT DISCUSSION AND ANALYSIS
YEARS ENDED JUNE 30, 2009 AND 2008

The following discussion and analysis of the financial performance and activity of the Puerto Rico Metropolitan Bus Authority (“the Authority”) provides an introduction and understanding of the basic financial statements of the Authority for the fiscal years ended June 30, 2009 and 2008. This discussion was prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

Financial Highlights for 2009

- Net assets deficiency totaled \$19.6 million at June 30, 2009.
- Net assets deficiency increased by \$21.5 million in 2009, as compared to a decrease in of approximately \$.6 million in 2008.
- Net capital assets totaled \$51.5 million at June 30, 2009
- Net capital assets decreased by 12% at June 30, 2009, when compared with the balance at June 30, 2008 of \$58.7 million.

Financial Highlights for 2008 (as restated)

- Net assets efficiency totaled \$1.9 million at June 30, 2008.
- Net assets decreased by \$.6 million in 2008, as compared to a decrease of \$11.3 million in 2007.
- Net capital assets totaled \$58.7 million at June 30, 2008
- Net capital assets decreased by 9% at June 30, 2008, when compared with the balance at June 30, 2007 of \$53.6 million.

The Financial Statements

The basic financial statements provide information about the Authority’s business-type activities. The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the Governmental Accounting Standards Board (GASB).

During the year ended June 30, 2009 the Authority evaluated its accounting records and found that cost of transportation equipment and its related accumulated depreciation were not properly reflected in prior years issued financial statements. The effect of this adjustment was to increase the deficiency in net assets as of July 1, 2007 by approximately \$5,252,000 and to reduce the depreciation expense during the year ended June 30, 2008 by approximately \$466,000 and a related decrease in the net book value of transportation equipment at June 30, 2008 of \$4,786,000.

Financial analysis in this section is made considering the effect of the above adjustment.

Overview of the Financial Statements for Business-Type Activities

The financial statements consist of the (1) statement of net assets, (2) statement of revenues, expenses, and changes in net assets, (3) statement of cash flows, and (4) notes to the financial statements. The financial statements are prepared on the accrual basis of accounting, meaning that all expenses are recorded when incurred and all revenues are recognized when earned, in accordance with accounting principles generally accepted in the United States of America.

Statement of Net Assets

The statement of net assets reports all financial and capital resources of the Authority. The statement is presented in the format where assets equal liabilities plus net assets. Assets and liabilities are presented in order of liquidity and are classified as current (convertible into cash within one year) and non-current. The focus of the statement of net asset is to show a picture of the liquidity and health of the Authority's financial position as of the end of the year.

The Authority's net assets are reported in the following categories:

- *Net Assets Invested in Capital Assets, Net of Related Debt* —this component of net assets consists of all capital assets, reduced by the outstanding balances of any bonds, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Although the Authority's investment in its capital assets is reported net of related debt, it is noted that the resources required to repay this debt must be provided annually from operations and from the operating grant allocated annually by the Commonwealth of Puerto Rico, since the capital assets themselves can not be used to liquidate liabilities.
- *Unrestricted Net Assets* —this component includes all net assets that do not meet the definition of net assets invested in capital assets.

Statement of Revenues, Expenses, and Changes in Net Assets

The statement of revenues, expenses, and changes in net assets includes operating revenues, which consist of passenger and cargo revenues and equipment and property rentals and operating expenses, such as salaries and employees benefits, depreciation on capital assets, repairs and maintenance and other general administrative expenses; and non-operating revenue and expenses, such as the operating grants from the Commonwealth of Puerto Rico, interest and investment income, and interest expense. The focus of the statement of revenues, expenses, and changes in net assets is the change in net assets. This is similar to net income or loss and portrays the results of operations of the Authority for the entire operating period.

Statement of Cash Flows

The statement of cash flows discloses net cash provided by or used for operating activities, investing activities, noncapital financing activities, and from capital and related financing

activities. This statement also portrays the health of the Authority in that current cash flows are sufficient to pay current liabilities.

Notes to Financial Statements

The notes to financial statements are an integral part of the basic financial statements and describe the significant accounting policies, related-party transactions, deposits and investments, capital assets, long-term liabilities, defined-benefit pension plans, and the commitments and contingencies. The reader is encouraged to review the notes in conjunction with the management discussion and analysis and the financial statements.

Financial Analysis of the Authority's Business-Type Activities

Statements of Net Assets

The following table reflects a condensed summary of assets, liabilities, and net assets of the Authority as of June 30, 2009, 2008, and 2007:

	June 30,		
	<u>2009</u>	<u>2008</u>	<u>2007</u>
		<i>As Restated</i>	<i>As Restated</i>
ASSETS			
Current assets	\$ 10,712,321	\$ 21,785,936	\$ 16,371,956
Capital assets	51,519,173	58,688,677	53,624,553
Other assets	<u>267,071</u>	<u>267,886</u>	<u>267,071</u>
Total assets	<u>\$ 62,498,565</u>	<u>\$ 80,742,499</u>	<u>\$ 70,263,580</u>
LIABILITIES			
Current liabilities	\$ 44,656,321	\$ 39,719,492	\$ 21,220,272
Long-term liabilities	<u>37,409,974</u>	<u>39,129,982</u>	<u>46,490,205</u>
Total liabilities	<u>82,066,295</u>	<u>78,849,474</u>	<u>67,710,477</u>
NET ASSETS			
Invested in capital assets, net of related debt	51,519,173	58,688,677	53,624,553
Deficiency in unrestricted net assets	<u>(71,086,903)</u>	<u>(56,795,652)</u>	<u>(51,071,450)</u>
Total net assets	<u>(19,567,730)</u>	<u>1,893,025</u>	<u>2,553,103</u>
Total liabilities and net assets	<u>\$ 62,498,565</u>	<u>\$ 80,742,499</u>	<u>\$ 70,263,580</u>

June 30, 2009

Current assets decreased by 51% to \$10.7 million. The change in current assets is primarily due to a decrease in cash and cash equivalents and in capital contributions receivable.

Capital assets decreased by 12% to \$51.5 million due to retirement and disposition of transportation equipment that reached the end of their useful life. Capital assets are funded with the proceeds from operations and operating and capital grants from the Commonwealth of Puerto Rico. In addition, the Authority is a recipient of certain funds under Federal program 20.507 "Urban Mass Transportation Capital and Operating Assistance Formula Grant" granted by the Federal Transit Administration which is used to finance the capital improvement program. Total capital grants received from the Ports Authority during fiscal year 2009 amounted to approximately \$14.1 million.

Current liabilities increased by 11% to \$44.7 million. This increase consists principally of an increase in accrued expenses payable.

Long-Term Debt consists principally of amounts due to Scotia Bank of Puerto Rico related to a long-term financing obtained in prior years. The loan with Scotia Bank is payable in monthly principal installment of \$143,334 plus interests at fixed rate of 5.43% plus a spread as defined in the loan agreement (6.68% at June 30, 2009) due in February 12, 2012.

Net assets decreased to deficiency of by 1,134% to a net deficiency of \$19.6 million. This decrease was the result of an excess of expenses (operating and non-operating) over revenues (operating and non-operating) and capital grants of \$21.8 million. The largest portion of the Authority's net assets represents its investment in capital assets net of related debt outstanding used to acquire those capital assets.

June 30, 2008

Current assets increased by 33% to \$21.8 million. The change in current assets is primarily due to an increase in cash and cash equivalents and federal government appropriations.

Capital assets increased by 9.4% to \$58.7 due to capital assets acquired during the year net of related depreciation expense. Capital assets are funded with the proceeds from operations and operating and capital grants from the Commonwealth of Puerto Rico. In addition, the Authority is a recipient of certain funds under Federal program 20.507 "Urban Mass Transportation Capital and Operating Assistance Formula Grant" granted by the Federal Transit Administration which is used to finance the capital improvement program. Total capital grants received from the Ports Authority during fiscal year 2008 amounted to approximately \$22.3 million.

Current liabilities increased by 87% to \$39.7 million due principally to an increase in accounts payable and accrued expenses.

Long-Term Debt consists principally of amounts due to Scotia Bank of Puerto Rico related to a long-term financing obtained in prior years. The loan with Scotia Bank is payable in monthly principal installment of \$143,334 plus interests at fixed rate of 5.43% plus a spread as defined in the loan agreement (6.68% at June 30, 2008) due in February 12, 2012.

Net assets decreased by 25.8% to \$1.9 million. This decrease was the result of an excess of expenses (operating and non-operating) over revenues (operating and non-operating) and capital grants of \$.6 million. The largest portion of the Authority's net assets represents its investment in capital assets net of related debt outstanding used to acquire those capital assets.

The following table reflects a condensed summary of the revenues, expenses, and changes in net assets for the three years ended June 30, 2009:

	Years Ended June 30,		
	<u>2009</u>	<u>2008</u> <i>As Restated</i>	<u>2007</u> <i>As Restated</i>
Operating revenues	\$ 24,403,044	\$ 31,535,689	\$ 31,665,368
Operating expenses	<u>85,542,546</u>	<u>85,353,134</u>	<u>81,083,657</u>
Operating loss	<u>(61,139,502)</u>	<u>(53,817,445)</u>	<u>(49,418,289)</u>
Non-operating revenues:			
Operating grants	42,193,592	46,863,505	26,760,647
Interest income (expense), net	<u>(5,014,845)</u>	<u>(3,931,421)</u>	<u>(1,979,350)</u>
Total non-operating revenues	<u>37,178,747</u>	<u>42,932,084</u>	<u>24,781,297</u>
Loss before capital contributions	(23,960,755)	(10,885,361)	(24,636,992)
Capital contributions	<u>2,500,000</u>	<u>10,225,283</u>	<u>13,262,226</u>
Change in net assets	<u>(21,460,755)</u>	<u>(660,078)</u>	<u>(11,374,766)</u>
Net assets deficit at beginning of year			
As previously reported	6,679,201	7,805,086	19,179,852
Adjustment to prior year issued financial statements	<u>(4,786,176)</u>	<u>(5,251,983)</u>	<u>(5,251,983)</u>
As restated	<u>1,893,025</u>	<u>2,553,103</u>	<u>13,927,869</u>
Net assets deficit at end of year	<u>\$ (19,567,730)</u>	<u>\$ 1,893,025</u>	<u>\$ 2,553,103</u>

Year Ended June 30, 2009

Operating revenues which consisted principally of fares for transportation and other services, decreased by 23% to \$24.4 million. This decrease is due to a decrease in patronage during fiscal year 2009 as a result of general economic conditions. The Authority had a service contract with the Puerto Rico Highways and Transportation Authority (PRHTA) in which PRHTA paid the Authority a total of \$23,200,000 for certain transportation services during the year ended June 30, 2008. This contract was cancelled effective February 2009. The amount received by the Authority under this contract during the year ended June 30, 2009 amounted to \$13,654,545.

Operating expenses, which consisted principally of salaries and employees benefits, depreciation and amortization, repairs and maintenance, diesel, insurance, professional services and general and administrative increased by 0.22% to \$85.5 million.

Non-operating revenues consisted principally of operating grants from the Commonwealth of Puerto Rico and Federal Government. These operating grants from the Commonwealth of Puerto Rico are annual appropriations from the general fund. The amount appropriated annually depends on the approved budget of the Commonwealth of Puerto Rico.

In addition, the Authority receives operating and capital contributions from the U.S. Department of Transportation which are restricted to the acquisition and repairs of certain capital assets.

Year Ended June 30, 2008

Operating revenues consisted of fares for transportation and other services and service contract with the Puerto Rico Highways and Transportation Authority (PRHTA). These revenues decreased by .41% to \$31.5 million. This decrease is due to a decrease in patronage during fiscal year 2008 as a result of general economic conditions. The Authority had a service contract with PRHTA in which PRHTA paid the Authority a total of \$23,200,000 for certain transportation services.

Operating expenses, which consisted principally of salaries and employees benefits, depreciation and amortization, repairs and maintenance, diesel, insurance, professional services and general and administrative increased by 5.2% to \$85.4 million mainly due to an increase in salaries and employees benefits, oil and diesel and depreciation.

Non-operating revenues consisted principally of operating grants from the Commonwealth of Puerto Rico and Federal Government. These operating grants from the Commonwealth of Puerto Rico are annual appropriations from the general fund. The amount appropriated annually depends on the approved budget of the Commonwealth of Puerto Rico.

In addition the Authority receives operating and capital contributions from the U.S. Department of Transportation which are restricted to the acquisition and repairs of certain capital assets.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At June 30, 2009, the Authority had invested approximately \$51.5 million in capital assets (net of related depreciation) including transportation equipment, land and buildings and machinery and equipment used in the operations. At June 30, 2008, the Authority had invested approximately \$58.7 million in capital assets.

Major capital assets events during the years ended June 30, 2009 and 2008 include the acquisition and repairs of transportation equipment which were funded principally by capital contributions received.

Debt Administration

The Authority has an unsecured line of credit with a commercial bank in which the Authority may borrow up to \$3,000,000. Outstanding balance bears interest at 1.25% over LIBOR.

In addition a long-term note payable with the same commercial bank payable in monthly principal installment of \$143,334 plus a fixed interest rate of 5.43% plus a spread as defined in the loan agreement. A balloon payment for the principal amount outstanding is due on February 2012.

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our customers, investors, creditors, and the general public with a general overview of the Puerto Rico Metropolitan Bus Authority's finances and to show the accountability for economic resources that it receives. If you have questions about this report or need additional financial information, contact the administration Office at Puerto Rico Metropolitan Bus Authority, 37 De Diego Avenue, San Juan, Puerto Rico.

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENTS OF NET ASSETS
 JUNE 30, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
		<i>As Restated</i>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 1,169,682	\$ 4,364,286
Accounts receivable	3,416,436	10,787,205
Inventory	3,671,850	3,913,594
Prepaid expenses	<u>2,454,353</u>	<u>2,720,851</u>
Total current assets	10,712,321	21,785,936
CAPITAL ASSETS	51,519,173	58,688,677
OTHER ASSETS	<u>267,071</u>	<u>267,886</u>
TOTAL	<u>\$ 62,498,565</u>	<u>\$ 80,742,499</u>
LIABILITIES AND NET ASSETS (DEFICIT)		
CURRENT LIABILITIES:		
Borrowings under line of credit	\$ 3,000,000	\$ 3,000,000
Accounts payable	13,509,957	16,376,747
Accrued expenses payable	24,207,141	18,430,394
Deferred revenue	2,219,215	192,343
Current portion of long-term debt	<u>1,720,008</u>	<u>1,720,008</u>
Total current liabilities	44,656,321	39,719,492
LONG-TERM DEBT		
Notes payable, net of current portion	<u>37,409,974</u>	<u>39,129,982</u>
NET ASSETS (DEFICIT):		
Invested in capital assets, net of related debt	51,519,173	58,688,677
Unrestricted deficit	<u>(71,086,903)</u>	<u>(56,795,652)</u>
Net assets (deficit)	<u>(19,567,730)</u>	<u>1,893,025</u>
TOTAL	<u>\$ 62,498,565</u>	<u>\$ 80,742,499</u>

The accompanying notes are integral part of the financial statements

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
 YEARS ENDED JUNE 30, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
		<i>As Restated</i>
OPERATING REVENUES		
Passenger fares	\$ 10,120,615	\$ 7,541,995
Service contract with Puerto Rico Highways and Transportation Authority	13,654,545	23,200,000
Advertising and other	<u>627,884</u>	<u>793,694</u>
Total operating revenues	<u>24,403,044</u>	<u>31,535,689</u>
OPERATING EXPENSES		
Salaries and employee benefits	57,428,968	56,246,760
Diesel, gasoline, oil and lubricants	6,266,897	6,723,021
Depreciation and amortization	9,675,690	8,118,120
Materials, spare parts and repairs and maintenance	5,912,733	4,140,570
Utilities	1,607,215	1,441,309
Professional services	2,208,325	1,918,506
General and administrative	<u>2,442,718</u>	<u>6,764,848</u>
Total operating expenses	<u>85,542,546</u>	<u>85,353,134</u>
OPERATING LOSS	<u>(61,139,502)</u>	<u>(53,817,445)</u>
NON-OPERATING REVENUES (EXPENSES)		
Gasoline, diesel, petroleum and tax oil revenues	8,777,138	26,703,638
Operating grants:		
Commonwealth of Puerto Rico operating grant	19,277,374	8,024,447
Federal Government	14,139,080	12,135,420
Interest and other financing expenses	(5,041,703)	(3,979,756)
Interest income	<u>26,858</u>	<u>48,335</u>
Total non-operating revenues	<u>37,178,747</u>	<u>42,932,084</u>
LOSS BEFORE CAPITAL CONTRIBUTIONS	<u>(23,960,755)</u>	<u>(10,885,361)</u>
CAPITAL CONTRIBUTIONS	<u>2,500,000</u>	<u>10,225,283</u>
CHANGE IN NET ASSETS	<u>(21,460,755)</u>	<u>(660,078)</u>
NET ASSETS AT BEGINNING OF YEAR:		
As previously reported	6,679,201	7,805,086
Adjustment to prior year issue financial statements	<u>(4,786,176)</u>	<u>(5,251,983)</u>
As restated	<u>1,893,025</u>	<u>2,553,103</u>
NET ASSETS (DEFICIENCY), AT END OF YEAR	<u>\$ (19,567,730)</u>	<u>\$ 1,893,025</u>

The accompanying notes are integral part of the financial statements

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
		<i>As Restated</i>
OPERATING ACTIVITIES:		
Cash received from customers and users	\$ 24,256,985	\$ 29,915,259
Cash payments to suppliers for goods and services	(18,287,009)	(17,246,219)
Cash payments to employees for services	<u>(53,692,947)</u>	<u>(46,927,672)</u>
Net cash used in operating activities	<u>(47,722,971)</u>	<u>(34,258,632)</u>
NON-CAPITAL FINANCING ACTIVITIES:		
Operating grants received from:		
Federal Transit Administration	19,203,315	12,135,420
Commonwealth of Puerto Rico	32,533,977	34,728,085
Interest paid	(4,148,737)	(4,581,351)
Payment of notes payable	<u>(1,720,008)</u>	<u>(1,720,008)</u>
Net cash provided by non-capital financing activities	<u>45,868,547</u>	<u>40,562,146</u>
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition of capital assets	(3,867,038)	(13,019,221)
Capital contributions	<u>2,500,000</u>	<u>10,225,283</u>
Net cash used by capital and related financing activities	<u>(1,367,038)</u>	<u>(2,793,938)</u>
INVESTING ACTIVITIES:		
Interest received	<u>26,858</u>	<u>48,335</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(3,194,604)	3,557,911
CASH AND CASH EQUIVALENTS, at beginning of year	<u>4,364,286</u>	<u>806,375</u>
CASH AND CASH EQUIVALENTS, at end of year	<u>\$ 1,169,682</u>	<u>\$ 4,364,286</u>

The accompanying notes are integral part of the financial statements

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
		<i>As Restated</i>
RECONCILIATION OF OPERATING LOSS TO		
NET CASH USED IN OPERATING ACTIVITIES:		
Operating loss	\$ (61,139,502)	\$ (53,817,445)
Adjustments to reconcile operating loss to net cash used		
in operating activities:		
Depreciation and amortization	9,675,690	8,118,120
Loss on disposition of capital assets	1,360,852	-
Changes in operating assets and liabilities:		
Accounts receivable	(146,059)	(676,488)
Inventory	241,744	234,686
Prepaid expenses	266,498	-
Other assets	815	(815)
Accounts payable	(2,866,790)	9,934,267
Accrued expenses payable	4,883,781	1,949,043
Net cash used in operating activities	<u>\$ (47,722,971)</u>	<u>\$ (34,258,632)</u>

The accompanying notes are integral part of the financial statements

**PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)**

**NOTES TO FINANCIAL STATEMENTS
YEARS ENDED JUNE 30, 2009 AND 2008**

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Puerto Rico Metropolitan Bus Authority (the "Authority") is a public corporation created by Act No. 5 of May 11, 1959, as amended, to provide, develop, manage and maintain a public low-cost land transportation system for citizens within the Metropolitan Area of San Juan, Bayamon, Carolina, Guaynabo, Cataño, Loiza, Toa Baja and Trujillo Alto of Puerto Rico. This service is principally financed by appropriations from the Commonwealth of Puerto Rico, grants from the Federal Government and by passenger fares. The Authority is a component unit of the Commonwealth of Puerto Rico, and accordingly is included in the general-purpose financial statements of the Commonwealth. The powers normally exercised by a Board of Directors are vested with the Secretary of the Department of Transportation and Public Works (DTPW). The Authority is exempt from the payment of any taxes on its revenues and properties.

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standards setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the significant accounting policies:

The Authority adopted the provisions of Governmental Accounting Standards Board Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting* (GASB No. 20). In adopting GASB No. 20, the Authority elected not to apply all Statements and Interpretations of the Financial Accounting Standards Board, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure issued after November 30, 1989.

Use of Estimates

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

Cash and Cash Equivalents

In the statement of cash flows, cash equivalents are defined as short-term, highly liquid investments that are readily convertible to known amounts of cash and are so near to their maturity that they present insignificant risk of changes in value because of changes in interest rates. In particular, they include cash on hand and on deposit and short-term investments with maturities of three months or less.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is an amount that management believes will be adequate to absorb possible losses on existing accounts receivable that may become uncollectible based on evaluations of collectability of accounts receivable and prior credit loss experience. Because of uncertainties inherent in the estimation process, management's estimate of credit losses inherent in the existing accounts receivable and related allowance may change in the future.

Inventories

Inventories, consisting of fuel, materials and supplies are valued at the lower of cost (first-in, first-out method) or market.

Capital Assets

Capital assets are recorded at historical cost or estimated historical cost, net of accumulated depreciation and amortization. Capital asset is defined by the Authority as assets with an initial cost of more than \$500 and an estimated useful life of more than one year. Depreciation and amortization is computed on a straight-line method over estimated useful lives of the related asset. Maintenance and repairs are charged to operations, while renewals and betterments are capitalized. When property and equipment are disposed of, the cost and applicable accumulated depreciation and amortization are removed from the respective accounts and the resulting gain or loss is recorded in operations.

The estimated useful lives of the capital assets follow:

Buildings and structures	40 years
Transportation equipment	12 years
Terminals	20 years
Machinery and equipment	5-10 years

The Authority periodically reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. During the year ended June 30, 2009 the Authority retired from operations transportation equipment which reached the end of its useful life. A loss of approximately \$1,360,000 was recorded as result of such retirement.

Vacation and Sick Leave

Compensated absences are accrued when earned by the employees. Employees may carryforward their compensated absences as permitted by statute and may settle them in a cash payment from the Authority, if employment has ceased.

Net assets

Net assets are classified in the following two components in the accompanying statements of net assets:

Invested in Capital Assets, Net of Related Debt

This component of net assets consists of capital assets net of accumulated depreciation and reduced by the outstanding balance of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction or improvement of those assets. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of this component of net assets. Rather that portion of the debt is included in the same net asset component as the unspent proceeds.

Unrestricted

Unrestricted net assets consist of net assets that do not meet the definition of invested in capital assets, net of related debt.

Operating Revenues and Expenses

The Authority distinguishes between operating and nonoperating revenues and expenses in its Statement of Revenues, Expenses, and Changes in Net Assets. The principal revenues of the Authority are charges received from patrons for the transportation services provided. The Authority also recognizes as operating revenue advertising charges to customers and other related transportation services. Operating expenses for the Authority include the costs of operating the transportation facilities, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Contributions

The Authority is a recipient of Federal funds received under grants with Federal Transit Administration (FTA) for the exclusive purpose of acquisition and repairs of certain capital assets with certain matching funds provided by the Commonwealth of Puerto Rico. Capital grants of the Authority are reported as non-operating revenues rather than contributed capital as required by GASB Statement No 33, *Accounting and Financial Reporting for Non-exchange Transactions*. Capital funding provided under these grants are considered earned as the related allowable expenditure are incurred.

In addition, the Authority receives operating grant from the Commonwealth of Puerto Rico. This grant, which is subject to annual appropriations, is used to finance the Authority's operations. Amount received under this grant is recorded as revenues in the period stated in the grant.

Reclassifications

Certain reclassifications have been made to the 2008 figures to conform to current year's presentation.

Risk Financing

The Authority carries commercial insurance to cover casualty, theft, claims and other losses. The current insurance policies have not been cancelled or terminated. The Authority has not settled any claims in excess of its insurance coverage during the three years. The Authority also pays premiums for workers compensation insurance to another component unit of the Commonwealth of Puerto Rico.

Accrual for legal claims

The estimated amount of the liability for legal claims is recorded on the accompanying Statements of Net Assets based on the Authority's evaluation of the probability of an unfavorable outcome in the litigation of such legal claims. The Authority consults with legal counsel upon determining whether an unfavorable outcome is expected. Because of uncertainties inherent in the estimation process, management's estimate of the liability for legal claims may change in the near term.

2. CASH AND CASH EQUIVALENTS

Cash and cash equivalents at June 30, 2009 and 2008 consist of cash on hand and on bank deposit accounts.

The Authority is restricted by law to deposit funds only in institutions approved by the Puerto Rico Treasury Department, and such deposits are required to be kept in separate accounts in the name of the Authority.

Pursuant to the Investment Guidelines for the Commonwealth adopted by Government Development Bank for Puerto Rico ("GDB"), the Authority may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, repurchase agreements, bankers acceptances, or in pools of obligations of the municipalities of Puerto Rico, among others. There are no investments at June 30, 2009 and 2008.

For deposits, custodial credit risk is the risk that in the event of bank failure, the Authority's deposits may not be returned to it. Under Puerto Rico statutes public funds deposited in commercial bank must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of the Commonwealth of Puerto Rico. The bank balance of the Authority's deposit at June 30, 2009 and 2008, excluding deposits in Government Development Bank for Puerto Rico described below, amounted to approximately \$1,393,000 and \$3,548,000, respectively, of which \$773,000 and \$300,000 are insured by Federal Deposit Insurance Corporation at June 30, 2009 and 2008 respectively.

In addition, at June 30, 2009 and 2008, the Authority maintained cash deposited at the Governmental Development Bank for Puerto Rico (GDB), in the amount approximately \$71,000 and \$810,000, respectively. These amounts are uncollateralized since by law, the governmental banks of the Commonwealth of Puerto Rico are exempt of the requirement of insuring the deposits of funds of the entities of the Commonwealth of Puerto Rico.

3. ACCOUNTS RECEIVABLE

Accounts receivable at June 30, 2009 and 2008 consist of:

	<u>2009</u>	<u>2008</u>
Operating and capital grants:		
Federal government	\$ 1,590,043	\$ 4,627,406
Commonwealth of Puerto Rico	197,105	4,676,570
Puerto Rico Highways and Transportation Authority	1,572,556	1,572,556
Other	439,754	1,223,402
Total	3,799,458	12,099,934
Less allowance for doubtful accounts	383,022	1,312,729
Total	<u>\$ 3,416,436</u>	<u>\$ 10,787,205</u>

4. INVENTORY

Inventory at June 30, 2009 and 2008 consists of:

	<u>2009</u>	<u>2008</u>
Spare parts	\$ 3,361,672	\$ 3,561,767
Diesel and gasoline	187,348	204,772
Supplies	122,830	147,055
Total	<u>\$ 3,671,850</u>	<u>\$ 3,913,594</u>

5. TRANSACTIONS WITH RELATED ENTITIES

The Authority had an agreement with the Puerto Rico Highways and Transportation Authority (PRHTA) in which PRHTA agreed to pay the Authority an annual amount of \$23,200,000 for certain transportation services to be provided by the Authority. During the year ended June 30, 2009 such agreement was terminated. Therefore the amount received by the Authority during the year ended June 30, 2009 amounted to \$13,654,545.

6. CAPITAL ASSETS

The following schedule summarizes the capital assets held by the Authority as of June 30, 2009 and 2008:

	<u>Balance at June 30, 2008</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at June 30, 2009</u>
	<i>Restated</i>			
Assets not being depreciated:				
Land and improvements	\$ 2,569,210	\$ -	\$ -	\$ 2,569,210
Assets being depreciated:				
Buildings and improvements	17,869,096			17,869,096
Terminals	4,100,692			4,100,692
Transportation equipment	96,404,604	-	(19,739,036)	76,665,568
Machinery and equipment	34,178,753	3,867,043	(197,848)	37,847,948
Total	152,553,145	3,867,043	(19,936,884)	136,483,304
Less accumulated depreciation	96,433,678	9,675,695	(18,576,032)	87,533,341
Capital assets being depreciated, net	56,119,467	(5,808,652)	(1,360,852)	48,949,963
Total capital assets, net	<u>\$ 58,688,677</u>	<u>\$ (5,808,652)</u>	<u>\$ (1,360,852)</u>	<u>\$ 51,519,173</u>

	<u>Balance at June 30, 2007</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at June 30, 2008</u>
	<i>Restated</i>			
Assets not being depreciated:				
Land and improvements	\$ 2,569,210	\$ -	\$ -	\$ 2,569,210
Assets being depreciated:				
Buildings and improvements	17,869,096			17,869,096
Terminals	4,100,692			4,100,692
Transportation equipment	86,349,866	12,781,604	(2,726,866)	96,404,604
Machinery and equipment	33,979,151	237,617	(38,015)	34,178,753
Total	142,298,805	13,019,221	(2,764,881)	152,553,145
Less accumulated depreciation	91,243,462	7,955,097	(2,764,881)	96,433,678
Capital assets being depreciated, net	51,055,343	5,064,124	-	56,119,467
Total capital assets, net	<u>\$ 53,624,553</u>	<u>\$ 5,064,124</u>	<u>\$ -</u>	<u>\$ 58,688,677</u>

7. BORROWINGS UNDER LINE OF CREDIT

The Authority has an unsecured line of credit with a commercial bank in which the Authority may borrow up to \$3,000,000. Borrowings under this of line of credit are by the assignment of diesel tax revenues and bear interest at LIBOR plus a spread as defined in the agreement (1.57% and 4% at June 30, 2009 and 2008, respectively).

A summary of the activity in the line of credit during the years ended June 30, 2009 and 2008 follows:

	<u>Balance at 2008</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at 2009</u>	<u>Current Portion</u>
Borrowings under line of credit	\$ 3,000,000	\$ -	\$ -	\$ 3,000,000	\$ 3,000,000
	<u>Balance at 2007</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at 2008</u>	<u>Current Portion</u>
Borrowings under line of credit	\$ 3,000,000	\$ -	\$ -	\$ 3,000,000	\$ 3,000,000

8. LONG-TERM DEBT

Long-term debt at June 30, 2009 and 2008 consist of:

	<u>Balance at 2008</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at 2009</u>	<u>Current Portion</u>
Secured note payable to bank	\$ 40,849,990	\$ -	\$ (1,720,008)	\$ 39,129,982	\$ 1,720,008
	<u>Balance at 2007</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at 2008</u>	<u>Current Portion</u>
Secured note payable to bank	\$ 22,303,832	\$ 43,000,000	\$ (24,453,842)	\$ 40,849,990	\$ 1,720,008

The note payable to bank is secured by the assignment of diesel tax revenues and is payable in monthly principal installments of approximately \$144,000 plus interest at fixed rate of 5.43% plus a spread as defined in the loan agreement.

Estimated maturities of this note payable during the next years are as follows:

Year ending	
June 30,	
2010	\$ 1,720,000
2011	1,720,000
2012	<u>35,689,982</u>
Total	<u>\$ 39,129,982</u>

9. RETIREMENT PLAN

Substantially all the Authority's employees participate in the Retirement System of the Commonwealth of Puerto Rico ("the System"), a cost sharing multi-employer defined benefit pension plan. The payroll for employees covered by the System for the years ended June 30, 2009 and 2008 was approximately \$30 million and \$36 million, respectively.

All Authority's employees, who at the time of employment are 55 years old or less, are eligible to participate in the System. Employees who retire at or after age 55 with 25 years of credited service or age 58 with 10 years of credited service are entitled to a retirement benefit, payable each month for life, computed based on a benefit rate set forth by Commonwealth statute.

The System also provides death and disability benefits established by Commonwealth statute. Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$550 of monthly gross salary. The Authority is required by the same statute to contribute 9.275% of the participant's gross salary.

On September 24, 1999, an amendment to Act No. 447 of May 1, 1951, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employees participating in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Employees joining the Authority on or after January 1, 2001, will only be allowed to become members of System 2000. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that takes into account each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) and investment income as defined in the Plan. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000.

Total employer contributions during the years ended June 30, 2009 and 2008 under this plan amounted to approximately \$2,772,000 and \$2,249,000 respectively.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2009 and 2008, a copy of which can be obtained from the Retirement System Administration, Minillas Station, P.O. Box 42003, San Juan, PR 00940.

10. COMMITMENTS AND CONTINGENT LIABILITIES

Litigation

The Authority is involved in litigation arising in the normal course of operations. Management believes that its ultimate liability, if any, in connection with these matters will not have a material effect on the Authority's financial condition and results of operations. Due to uncertainties in the settlement process, it is at least reasonably possible that management's view of the outcome of these claims will change in the near term. However, based on advice of legal counsel, management has recorded an estimated litigation and claim loss of approximately \$4,490,000 and \$2,235,000 as of June 30, 2009 and 2008, respectively.

Federal Assistance Programs

The Authority is a subrecipient of a federal financial assistance program. This program is subject to audits in accordance with the provisions of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, or to compliance audits by grantor agencies. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although the Authority expects such amounts, if any, not to be significant.

11. OPERATING FINANCIAL ASSISTANCE FROM THE COMMONWEALTH OF PUERTO RICO

As shown in the accompanying financial statements, the Authority has incurred in accumulated losses after operating and capital contributions in the amount of \$72 million and as of June 30, 2009 the Authority's liabilities exceeded its assets by approximately \$20 million. In addition, at June 30, 2009 the Authority has a working capital deficiency of approximately \$34 million making it difficult for the Authority to pay its liabilities in the normal course of business. These facts indicate that the Authority needs the continued support from the Commonwealth of Puerto Rico in the form of operating grants to continue to operate at its present level. Although the Commonwealth of Puerto Rico has experienced budget constrains during the current and prior years which have resulted in reductions in the operating grants provided to the Authority, management believes that with cost control programs, adherence to approved budget the Authority will be able to provide the transportation services with the assigned operating grant. Also management believes that since the transportation service provided by the Authority is an essential service to the people of Puerto Rico, the Commonwealth of Puerto Rico will continue to fund the operational deficits incurred by the Authority. Any significant reduction in these operating grants and financial support will affect the ability of the Authority to provide the transportation services and to continue as a going concern.

12. ADJUSTEMENT TO PRIOR YEARS ISSUED FINANCIAL STATEMENTS

During the year ended June 30, 2009, the Authority evaluated its accounting records and found that cost of transportation equipment and its related accumulated depreciation were not properly reflected in prior years issued financial statements. The effect of this adjustment was to increase the deficiency in net assets as of July 1, 2007 by approximately \$5,252,000 and to reduce the depreciation expense during the year ended June 30, 2008 by approximately \$466,000 and a related decrease in the net book value of transportation equipment at June 30, 2008 of \$4,786,000.

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2009

Federal Grantor/Pass-Trough Grantor/ Program Title	Federal CFDA Number	Federal Expenditures
Federal Transit Administration		
Direct		
Federal Transit Administration Capital and Operating Assistance Formula Grants	20.507	\$ <u>15,694,673</u>

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

NOTES SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2009

1. BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Puerto Rico Metropolitan Bus Authority (the "Authority") and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Government, and Non-Profit Organizations*. Therefore, some accounts in this schedule may differ from amounts presented in, or used in the preparation of the financial statements.



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

Hon. Rubén A. Hernández Gregorat, MEM, P.E.
Secretary Department of Transportation and Public Works

We have audited the financial statements of the Puerto Rico Metropolitan Bus Authority (the Authority) as of and for the year ended June 30, 2009 and have issued our report thereon dated March 12, 2010. 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. As described in Note 11 to the financial statements the Authority depends on the continued operating assistance from the Commonwealth of Puerto Rico to continue to operate at its current level.

Internal Control over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Authority's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Authority's financial statements that is more than inconsequential will not be prevented or detected by the Authority's internal control. We consider the deficiencies described in items 09-FS-01 through 09-FS-10 in the accompanying schedule of findings and questioned to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Authority's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. We believe that the significant deficiencies described in items 09-FS-01 through 09-FS-05 are also material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Authority'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 statement amounts.

However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items 09-FS-01 and FS-09-09.

This report is intended solely for the information and use of the Authority's management, the audit committee, and the U.S. Department of Transportation and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Guzmán Torres & Co., P.S.C.

CERTIFIED PUBLIC ACCOUNTANTS
March 12, 2010

Stamp # 2505875
was affixed to
the original of
this report.



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

Hon. Rubén A. Hernández Gregorat, MEM, P.E.
Secretary Department of Transportation and Public Works

Compliance

We have audited the compliance of the Puerto Rico Metropolitan Bus Authority (the "Authority") with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal program for the year ended June 30, 2009. The Authority's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Authority's management. Our responsibility is to express an opinion on the Authority'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, Audit 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 Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Authority's compliance with those requirements.

As described in items 09-SA-01 to 09-SA-05 in the accompanying schedule of findings and questioned costs, the Authority did not comply with requirements regarding activities allowed or unallowed, reporting, period of availability and cash management that are applicable to its Federal Transit Administration Capital and Operating Assistance Formula Grants. Compliance with such requirements is necessary, in our opinion, for the Authority to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Authority complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009.

Internal Control Over Compliance

The management of the Authority 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 Authority'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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over compliance.

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

A control deficiency in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item 09-SA-06 to be a significant deficiency.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We did not consider any of the deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses.

This report is intended solely for the information and use of the Authority's management, the audit committee, and the U.S. Department of Transportation and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Guzmán Torres & Co., P.S.C.

CERTIFIED PUBLIC ACCOUNTANTS
March 12, 2010

Stamp #2505876
affixed to original
of this report.

**PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2009**

SECTION 1 – SUMMARY OF AUDITORS’ REPORT

1. The type of opinion issued in the financial statements	Unqualified
2. The independent accountants’ report on internal control over financial reporting described:	
a. Significant deficiencies noted considered material weaknesses	Yes
b. Significant deficiency noted that is not considered to be a material weaknesses	Yes
3. Noncompliance considered material to the financial statements was disclosed by the audit	Yes
4. The independent accountants’ report on internal control over compliance with requirements applicable to major Federal awards described:	
a. Significant deficiency noted considered to be a material weaknesses	No
b. Significant deficiency noted that is not considered to be a material weaknesses	Yes
5. The opinion expressed in the independent accountants’ report on compliance with requirements applicable to major Federal awards	Qualified
6. The audit disclosed findings to be reported in accordance with Section .510(a) of OMB Circular A-133	Yes
7. The Authority’s major program was:	
<u>Name of Federal Program or Cluster</u>	<u>CFDA No</u>
Federal Transit Administration Capital and Operating Assistance Formula Grants	20.507
8. The threshold used to distinguish between Type A and Type B programs as those terms are defined in OMB Circular A-133	\$470,840
9. Auditee qualified as a low risk auditee under section .530 OMB Circular a-133	No

SECTION 2 - FINDINGS RELATING TO THE FINANCIAL STATEMENTS REREPORTED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Finding 09-FS-01 (Material Weakness)

See Finding 09-SA-01. This finding relates to non-compliance with grants, contract, laws and regulation that is required to be reported under Government Auditing Standards.

Finding 09-FS-02 (Material Weakness)

Condition:

During the year, numerous adjustments were made to correct the balances reflected by various accounts in the Authority's general ledger. In addition, since no monthly closings are performed, no interim financial statements are prepared making it difficult for management to make timely decisions.

Criteria:

Financial reporting and closing process should be documented in writing and should be communicated on a timely basis to all departments and individuals involved in the process.

Cause of condition:

The financial reporting closing process is informal and not well documented. In addition, roles and responsibilities in the financial closing and reporting are not communicated on a timely basis to appropriate departments and individuals.

Effect of condition:

The Authority was unable to comply with the reporting due date of September 30, 2009 required by the Department of Treasury of the Commonwealth of Puerto Rico. In addition the accounting department was unable to provide management with timely and reliable financial information that will assist management in making sound decisions

Recommendation:

In order to ensure that all accounting procedures are performed on a timely basis, management should establish policies to document the month and year end procedures that should be followed by the accounting department as well as any other department that provide financial information required for the preparation of financial statements. This could be accomplished by the develop of a comprehensive checklist that cover all procedures that the Authority determines necessary to be performed on a periodic basis including, but not limited to, month end procedures such as bank reconciliations, and general ledger account analysis, etc.

Finding 09-FS-03 (Material Weakness)

Condition:

Bank statements were accumulated for several months before they were reconciled to the appropriate general ledger controls.

Criteria:

Timely preparation of complete and accurate bank reconciliations is a key to maintaining adequate control over both cash receipts and disbursements.

Cause of Condition:

Lack of supervision of the individual preparing the reconciliations and policies that require monthly reconciliations

Effect of Condition:

Cash in bank is not properly safeguarded and subject to intentional or unintentional errors. In addition because the reconciliations are accumulated and not performed on a monthly basis, the process of performing the reconciliations is time consuming resulting in various adjustments made at year end and causing delays in the preparation of the financial statements.

Recommendation:

Bank reconciliations should be reconciled every month. The composition of unreconciled differences, if any, should be determined and followed up on, and any journal entries deemed necessary as a result be recorded. In addition, the bank reconciliations should be reviewed for accuracy and completeness on a timely basis by a designated officer. The review should include tests of mechanical accuracy and tracing of items on the reconciliation to the relevant source documents.

Finding 09-FS-04 (Material Weakness)

Condition:

During the year ended June 30, 2009, subsidiary ledgers were not reconciled with general ledger. In particularly the accounts payable subsidiary was not reconciled with the general ledger during the year resulting in a significant unreconciled difference at end of the year.

Criteria:

Reconciliations of subsidiary ledgers with the general ledger quickly identify errors and needed corrections.

Cause of Condition:

No proper supervision of the accounting personnel and lack of policies that require monthly reconciliations of subsidiary ledgers with the general ledger.

Effect of Condition:

Since reconciliations were not performed during the year, errors and adjustments occurred, resulting in the need for significant corrections when the reconciliations were performed. In addition, it is time consuming to perform the reconciliations once a year and as a consequence it delays the release of the audited financial statements.

Recommendation:

The Authority should adopt a policy requiring monthly reconciliation of all balance sheet accounts to their subsidiary ledgers in order to ensure that accuracy of the monthly financial statements and underlying subsidiary ledgers. Any reconciling differences should be corrected before the books are closed for the month end.

Finding 09-FS-05 (Material Weakness)

Condition:

The Authority's year-end spare parts inventory listing initially was prepared from the perpetual records of quantities on hand at that date. It was subsequently determined that adjustment of the perpetual records to actual counts had not been made. Therefore, the perpetual records were not reliable and an adjustment to them was made. In addition the spare parts inventory perpetual records were not reconciled with the general ledger and with actual quantities on hand in the warehouse. Therefore differences are not identified and corrected on a timely basis.

Criteria:

Perpetual inventory records provide a method for proper safeguarding of inventory against loss intentional or unintentional errors.

Cause of Condition:

Perpetual inventory records are not updated on a timely basis for purchases and uses and are not reconciled with the general ledger.

Effect of Condition:

Perpetual inventory records do not reflect the actual value and quantities of the spare parts inventory. In addition, errors in spare parts inventory could go undetected resulting in improper safeguard of this asset.

Recommendation:

The Authority should implement procedures that require monthly reconciliations of the spare parts inventory as reflected in the general ledger and the perpetual inventory record. Differences should be investigated and adjusted.

In addition, to assure that perpetual records present an accurate reflection of quantities on hand, a formal program of cycle counting procedures should be instituted. These procedures should include the following:

- Formal scheduling of items to be counted and periodic management review to assure adherence to the schedule.
- Reconciliation of perpetual records and actual counts.
- Adjustment of perpetual records to actual quantities resulting from known differences and documentation of the reasons for such adjustments.
- Follow-up to determine the causes for differences so that procedural weaknesses may be remedied.
- Periodic reporting to appropriate Authority personnel of the results of the cycle counting procedures.

Finding 09-FS-06

Condition:

The Authority does not maintain a detail capital asset ledger.

Criteria:

Preparation of detailed capital asset records aids in the accounting of property disposals, substantiates insurance claims, provides information for the calculation of depreciation and provides control for the safeguarding of capital assets.

Cause of condition

The Authority does not have a policy in place that requires the preparation of detailed capital assets records and the related reconciliation with the general ledger

Effect of condition:

Capital assets are not properly safeguarded exposing such assets to loss or improper use. In addition, lack of detailed capital asset records could result in misstatements in depreciation and in the accounting of disposals during the year.

Recommendation:

The Authority should adopt a policy requiring the preparation and maintenance of a detailed capital assets ledger. This ledger should be reconciled with general ledger on a monthly basis and should provide as a minimum the following information:

- Description, asset or tag number and location
- Acquisition cost and date of acquisition
- Amount of the acquisition cost paid with Federal funds
- Assigned life and method of depreciation
- Depreciation taken on an annual basis and accumulation thereof

Finding 09-FS-07

Condition:

The Cubic System reported obtained from each bus at the end of the day, which details the number of passengers that used the service during the day and the related rates is not reconciled with the amount of cash delivered to Ranger American for deposit into the bank. Also, the equipment use to safeguard the money deposited in the bus sometimes gets stuck in the middle of the route and although the passenger deposits the money, it is not accounted in the Cubic System.

Criteria:

A control deficiency 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 misstatements on a timely basis.

Cause of Condition:

Bus drivers are not using the Cubic System to keep track of passengers using the service during the day and the applicable rates.

Effect of Condition:

Revenues from passengers are subject to errors and could be misstated.

Recommendation:

Bus drivers should be instructed and trained to use the Cubic System to keep track of the passenger activity during the days. This will assist management in making an independent verification of passenger revenues accounted for during a particular period.

Finding 09-FS-08

Condition:

During the audit, various adjustments were made to record suppliers' invoices and to adjust accrued liabilities that were not recorded in the proper accounting period.

Criteria:

Payables should be recorded in the period in which the goods or services are received in order to reflect proper cutoff and ensure that the financial statements are complete with respect to accounts payable and accrued liabilities.

Cause of condition:

The Authority records a payable only after the invoice and purchase order is processed and approved for payment and recording. Hence, goods or services can be received for which no payable is recorded.

Effect of condition:

Accounts payable and accrued liabilities are not properly recorded in the Authority's records or are recorded in the wrong accounting period.

Recommendation:

In year-end closing procedures, we recommended that the Authority identify all unmatched purchase orders, receiving reports, and invoices to determine receipts for which a payable or accrued liability should have been recorded.

Finding 09-FS-09

Condition:

During our audit, we noted the following with respect to the quarterly payroll tax returns:

1. Employee income tax withheld return for the quarter ended December 31, 2008 has not being prepared and therefore not filed with the Department of Treasury.
2. Tax returns for all quarters in the fiscal year ended June 30, 2009 reflect different gross salaries in the same quarters. For example the tax returns for the quarter ended September 30, 2008 reflect different gross salaries for social security, unemployment, etc.
3. Disability tax return for the quarter ended June 30, 2009 reflected a tax liability that was not calculated correctly.
4. Most of the tax returns for the fiscal year ended June 30, 2009 were filed late resulting in penalties for late filling.

5. Most of the payroll taxes are being paid late resulting in interest and penalties for late payment. Income tax withheld to employees has not been paid since March 2008 and at June 30, 2009, the total accumulated debt amounted to \$3,184,578 excluding interest and penalties of approximately \$900,000. In addition, at June 30, 2009 the Authority has an accumulated debt for workmen's compensation insurance in the amount of \$1,841,975. This could result in the Authority being declared a non-insured employer and being held responsible for all claim cost incurred under the workmen's compensation policy.

Criteria:

The law requires that quarterly tax returns be filed on a specific time during the year and that the payment be made as specified in the law. The law provides for interest and penalties for late filing and payment.

Cause of condition:

Lack of proper internal control procedures over the preparation, payment and filing of the payroll quarterly tax returns.

Effect of condition:

The Authority is not complying with related laws and regulations and is subject to the payment of penalties and interest for late filing and payment. In addition claims by employees could arise for not informing to the governmental agencies the correct amounts withheld to each employee.

Recommendation:

Proper controls and procedures should be established to assure that all payroll tax returns are prepared correctly and filed and paid on time as required by law in order to avoid penalties and interest for late filing and payment.

Finding 09-FS-10

Condition:

On November 2005, the Authority signed a contract with the Puerto Rico Highways and Transportation Authority (PRHTA) in which PRHTA will pay the Authority certain amounts per passenger served by the Authority as part of the Integrated Transportation System of the Commonwealth of Puerto Rico (ATI). The Authority billed PRHTA for services provided under this contract up to June 30, 2007. Although the Authority has continued to provide this service for no specific reason no more invoices were sent to PRHTA after June 30, 2007 and no collection efforts have been made to collect the balance outstanding at June 30, 2007. During fiscal year ended June 30, 2009, management made an analysis and determined that PRHTA owes the Authority a total of \$3,252,021 for services performed under this contract since inception to June 30, 2009. A schedule was prepared and sent to PRHTA for proper analysis, approval and collection.

Criteria:

Good internal control should include policies and procedures to assure that timely billings are prepared for all services performed and that timely collection efforts are performed to collect related amounts.

Cause of Condition:

Lack of proper internal control procedures over billings and collections and lack of proper supervision of accounting personnel in charge of billings and collection function.

Effect of Condition:

Since no timely billings and collection efforts are performed, the Authority's cash flows is affected by not collecting amounts due for services performed on time.

Recommendation:

The Authority should implement policies and procedures to require the timely billing and collection of all accounts receivable. This will improve the Authority's cash flows and will minimize the loss for uncollected receivable.

SECTION 3 – FINDINGS AND QUESTIONED COSTS RELATING TO FEDERAL AWARDS

Finding: 09-SA-01

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Compliance Requirement:

Activities allowed or unallowed

Reporting Requirement:

Material non-compliance in relation to a compliance requirement and material weakness in internal control over a major Federal program

Condition:

During the year ended June 30, 2009, the Authority received funds under Resolution 116, approved by the Legislature of the Commonwealth of Puerto Rico and which are restricted for the acquisition of certain capital assets as detailed in the Resolution. Of the amount received, \$2,249,680 was used to finance the acquisition of a communication system as permitted by the Resolution. Subsequent to the acquisition of the communication system, the Authority received \$1,799,744 from the Federal Transit Authority to finance the acquisition of the same communication system. The excess funds received were used for operational purposes.

Criteria:

Federal funds should not be requested to finance the acquisition of a capital asset already financed with restricted State funds.

Cause of Condition:

Authority's personnel misrepresented the related Federal Award regulation requesting reimbursement to finance a capital asset already acquired with restricted State funds.

Effect of Condition:

The U.S Department of Transportation may assess a claim against the Authority to recover Federal funds that might have been spent in unallowable activities.

Questioned Costs:

\$1,799,744

Recommendation:

The Authority should review information submitted in application to the Federal Transit Administration and monitoring procedures should be established to ensure that Federal Awards compliance requirements are always adhered to. Reimbursement should be requested only for allowable expenditures not previously reimbursed with other State or Federal funds.

Finding: 09-SA-02

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Compliance Requirement

Activities allowed or unallowed

Reporting Requirement:

Material non-compliance in relation to a compliance requirement and material weakness in internal control over a major Federal program

Condition:

During our audit of allowable activities, we noted Federal revenues of approximately \$452,114 in the current fiscal year for which the related expenditures were incurred and recorded in prior fiscal years as follows:

Year Ended June 30,	Amount
2002	\$ 14,368
2003	6,293
2004	8,705
2005	17,860
2006	42,971
2007	67,771
2008	<u>294,326</u>
Total	<u>\$ 452,294</u>

Although some of the expenditures are from previous fiscal year ended June 30, 2008, the lapse between the disbursement and the reimbursement from Federal Transit Administration is more than 4 months in certain cases.

Due to the age of the above expenditures, we were unable to determine if the above expenditures were not charged to the Federal program in previous fiscal year or that those expenditures represented allowable activities during current fiscal year.

Criteria:

Good internal control policy with respect to Federal awards should include procedures for the timely identification of expenditures charged to Federal programs when the activity occurs.

Cause of Condition:

The Authority personnel in charge of Federal awards failed to identify expenditures in the year the activity occurred.

Effect of Condition:

The Federal Transit Administration may assess a claim against the Authority to recover Federal funds that might have been claimed and used incorrectly.

Recommendation:

The Authority should develop procedures to ensure that expenditures chargeable to Federal awards are identified and claimed for reimbursement in the year the related activity occurs.

Finding: 09-SA-03

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Compliance Requirement

Reporting

Reporting Requirement:

Material non-compliance in relation to a compliance requirement

Condition:

During our procedure to test compliance with the federal program reporting requirement, we noted the following:

1. Information in annual Financial Status Report does not agree with related information in the Authority's general ledger.
2. In certain cases, the Quarterly Narrative Report for the quarter ended September 30, 2008, March 31, 2009 and June 30, 2009 were submitted late and the reports for the quarter ended December 31, 2008 were not prepared and submitted.

Criteria:

The Authority should submit reliable and timely financial information as required by the Federal award.

Cause of Condition:

The financial status reports are prepared by employees without adequate training in accounting and the lack of procedures coordinating the accounting information with the Authority's accounting division.

Effect of Condition:

The Authority is not complying with the reporting requirement of its Federal award.

Recommendation:

The Authority should review reports submitted to the U.S Department of Transportation and monitoring procedures should be established to ensure that Federal Awards compliance requirements are always adhered to.

Finding: 09-SA-04

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Compliance Requirement

Period of availability

Reporting Requirement:

Material non-compliance in relation to a compliance requirement

Condition:

Two disbursements out of a sample of 40 disbursements were made for expenditures incurred after the period of availability of the related Federal grant.

Criteria:

Expenditures allocated to a federal award should be within the period of the related grant including any extension granted by the Federal awarding agency

Cause of Condition:

The Authority personnel in charge of Federal awards failed to identify if the expenditures allocated were within the award period.

Effect of Condition:

The Federal Transit Administration may assess a claim against the Authority to recover Federal funds that might have been claimed and used incorrectly.

Questioned Costs:

\$207,963

Recommendation:

Procedures should be implemented to assure that expenditures submitted to the Federal Transit Administration for reimbursement are within the period of availability of the Federal award.

Finding 09-SA-05

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Compliance Requirement

Cash management

Reporting Requirement:

Material non-compliance in relation to a compliance requirement

Condition:

In 12 cases out of 43 disbursements selected to test compliance with cash management requirement, the disbursements were made after receipt of the federal funds.

Criteria:

Federal award requires the Authority to pay the disbursement before requiring the related disbursement from the Federal Transit Authority.

Cause of Condition:

Due to lack of funds, checks are printed and not delivered to the supplier until funds are available.

Effect of Condition:

Federal Transit Administration could claim reimbursement of federal funds not requested in accordance with program laws and regulations.

Recommendation:

Policies and procedures should be established to ensure that federal awards cash management compliance requirement is always adhered to.

Finding 09-SA-06

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Compliance Requirement

N/A

Reporting Requirement:

Significant deficiency in internal control over a major Federal program

Condition:

See Finding 09-FS-06. This finding relates to significant internal control over a major federal program that is required to be reported under OMB Circular A-133.

PUERTO RICO METROPOLITAN BUS AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)

SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2009

Reference No: 2008-4

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Recommendation:

We recommend that at least at the end of each fiscal year the general ledger capital assets accounts be reviewed to the detailed property subsidiary records. It will be desirable to perform this reconciliation on a quarterly basis.

Status of Corrective Action:

Not implemented. Reported as current year finding number 09-SA-06

Reference No: 2008-5

Federal Program:

20.507 Federal Transit Administration Capital and Operating Assistance Formula Grants

Federal Grantor:

Federal Transit Administration

Recommendation:

We recommend that the federal reports and information requiring accurate accounting data will be prepared by personnel with knowledge in accounting and supervised by Administration department's officers.

Status of Corrective Action:

Not implemented. Reported as current year finding number 09-SA-03