# AUDITED FINANCIAL STATEMENTS AND OMB CIRCULAR A-133 REPORT

Government of the United States Virgin Islands Year Ended September 30, 2006 With Report of Independent Auditors

# ERNST & YOUNG

# Audited Financial Statements and OMB Circular A-133 Report

Year Ended September 30, 2006

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### Report of Independent Auditors

The Honorable Governor of the Government of the United States Virgin Islands:

We have audited the accompanying financial statements of the governmental activities, businesstype activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of the United States Virgin Islands (the Government), as of and for the year ended September 30, 2006, which collectively comprise the Government's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Government's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the following component units:

- The Virgin Islands Public Finance Authority (PFA), a blended component unit, which represents 100% of the assets, fund balance, and revenue of the PFA Debt Service Fund (a major fund); 100% of the assets, fund balance, and revenue of the PFA Capital Projects Fund (a major fund); 100% of the assets, net assets, and revenue of the West Indian Company (a major fund); 1.94%, 2.03% and 0.66% of the assets, net assets/fund, and revenue of the aggregate remaining fund information; 88.44% and 1.03% of the assets and revenues of the governmental activities; 54.63%, 41.97%, and 22.45% of the assets, net assets, and revenue of the \$89.8 million net deficit of the governmental activities.
- The Virgin Islands Lottery (VI Lottery), a nonmajor enterprise fund, which represents 0.22% and 4.85%, respectively, of the assets and revenues of the aggregate remaining fund information, and 4.22% and 33.54%, respectively, of the assets and revenue of the business-type activities. The VI Lottery net deficit represents \$1.6 million of the \$1,554.6 million net assets/fund balance and \$75.4 million of the aggregate remaining fund information and business-type activities, respectively.
- The Tobacco Settlement Financing Corporation, a blended component unit, which represents 0.59%, 0.72%, and 0.28%, respectively, of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information, and 0.78% and 0.11%, respectively, of the assets and revenue of the governmental activities. The Tobacco Settlement Financing Corporation net assets represent \$2.5 million of the \$89.8 million net deficit of the governmental activities.



- The Employees' Retirement System of the Government of the Virgin Islands (GERS), a fiduciary component unit (pension trust fund), which represents 93.14%, 95.03%, and 28.40%, respectively, of the assets, net assets/fund balance, and revenue of the aggregate remaining fund information.
- The Virgin Islands Housing Authority (VIHA), Virgin Islands Public Television System, Virgin Islands Economic Development Authority (VIEDA), Magens Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), the Virgin Islands Housing Finance Authority (VIHFA), and the Waste Management Authority, discretely presented component units, which collectively represent 26.25%, 28.39%, and 17.69%, respectively, of the assets, net assets, and revenue of the aggregate discretely presented component units.

These financial statements were audited by other auditors whose reports have been furnished to us, and our opinions, insofar as they relate to the amounts included for the activities, funds, and component units indicated above, are based on the reports of other auditors.

Except as discussed in the following five paragraphs, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and 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. The financial statements of the PFA, Juan Luis Hospital and Medical Center, Magens Bay Authority, Tobacco Settlement Financing Corporation, Waste Management Authority, and Employees' Retirement System of the Government of the Virgin Islands were not audited in accordance with Government Auditing Standards. We were not engaged to perform an audit of the Government's internal control over financial reporting. Our audit included 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 Government's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.



The report of other auditors on the 2006 financial statements of the VIHFA, a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence to determine whether land held for sale amounting to \$25 million was fairly stated.

The report of other auditors on the 2006 financial statements of VIEDA, a discretely presented component unit, was qualified because they were unable to obtain sufficient audit evidence to determine whether loans receivable of \$2.1 million were fairly stated.

The report of other auditors on the 2006 financial statements of the Employees' Retirement System of the Government of the Virgin Islands (GERS), a fiduciary component unit (pension trust fund), was qualified because GERS maintains investments in a limited partnership valued at \$51 million, whose fair value has been estimated in the absence of a readily determinable fair value. GERS' estimate is based on information provided by the general partner of the limited partnership. The effect on the financial statements as a result of GERS' inability to document its procedures for determining fair value of the investment is not determinable. In addition, GERS maintains its real estate investment in the GERS complex related to the St. Thomas building held for lease based on historical cost. As of September 30, 2006, this real estate investment amounted to approximately \$18.6 million. Such investment should be presented at fair value in accordance with U.S. generally accepted accounting principles. In addition, GERS' real estate investment in Havensight Mall is also based on historical cost, less accumulated depreciation. As of September 30, 2006, this real estate investment amounted to \$60.5 million. Such investment should be presented at fair value in accordance with U.S. generally accepted accounting principles. Finally, GERS did not maintain requisite documentation to support the cash overdraft balance with the Government stated at \$10.5 million as of September 30, 2006.

The report of other auditors on the 2006 financial statements of the VI Lottery, a nonmajor enterprise fund, was qualified because they were unable to obtain sufficient audit evidence to determine whether capital assets of \$305 thousand, accounts receivable of \$1 million, and due to the general fund of \$4.5 million were fairly stated.

The basic financial statements do not include a liability for workers' compensation claims and, accordingly, the Government has also not recorded an expense for the current period change in that liability. The Government's records do not permit, nor is it practical to extend our auditing procedures sufficiently to determine the extent by which the business-type activities and aggregate remaining fund information as of and for the year ended September 30, 2006 may have been affected by this condition.

Because of the matters discussed in the preceding two paragraphs of this report, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial position of the business-type activities and aggregate remaining fund information as of September 30, 2006 and the changes in financial position for the year then ended.

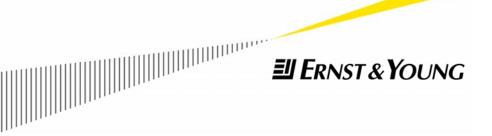
In our opinion, based on the report of other auditors, except for:

• The effect of the adjustments, if any, as might be determined to be necessary, had the other auditors been able to obtain sufficient audit evidence to determine whether 1) land held for sale amounting to \$25 million in the financial statements of VIHFA and 2) loan receivables \$2.1 million in the financial statements of VIEDA, were fairly stated as described in paragraphs four and five above, the financial statements referred to above present fairly, in all material respects, the financial position of the aggregate discretely presented component units of the Government of the United States Virgin Islands, as of September 30, 2006, and the respective changes in financial position thereof for the year then ended in conformity with U.S. generally accepted accounting principles.

Finally, in our opinion, based on our audit and the reports of other auditors, the financial statements referred to previously present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the Government of the United States Virgin Islands, as of September 30, 2006, and the respective changes in financial position and respective budgetary comparison for the general fund for the year then ended in conformity with U.S. generally accepted accounting principles.

As described more fully in Note 15 to the financial statements, as of October 1, 2005, the fund balance/net assets of the general fund, unemployment insurance fund, other nonmajor enterprise funds, governmental activities, and business-type activities were restated by \$62.9 million, \$2.2 million, \$8.4 million, \$13.8 million, and \$10.6 million, respectively.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 16, 2009, on our consideration of the Government's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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.



The management's discussion and analysis in pages 6 through 17 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We and the other auditors 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 opinions on the financial statements that collectively comprise the Government's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis, as required by U.S. Office of Management and Budget Circular A 133, *Audit of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. The schedule of expenditures of federal award has been subjected to auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Ernst + Young LLP

March 16, 2009

Management's Discussion and Analysis

Year Ended September 30, 2006

### Introduction

The following discussion and analysis presents an overview of the financial position and activities of the Government of the United States Virgin Islands (the Government) as of and for the fiscal years ended September 30, 2006 and 2005.

#### **Government-wide Financial Statements**

The government-wide financial statements are designed to present an overall picture of the financial position of the Government. These statements consist of the statement of net assets and the statement of activities, which are prepared using the economic resources measurement focus and the accrual basis of accounting. This means that current year's revenue and expenses are included regardless of when cash is received or paid, producing a view of financial position similar to that presented by most private-sector companies.

The statement of net assets combines and consolidates the Government's current financial resources with capital assets and long-term obligations.

Both of the above-mentioned financial statements have separate sections for three different types of the Government programs or activities. These three types of activities are as follows:

*Governmental Activities* – The activities in this section are mostly supported by taxes and intergovernmental revenue (federal grants). Most services normally associated with the primary government (PG) fall into this category, including general government, public safety, health, public housing and welfare, education, transportation and communication, and culture and recreation.

**Business-Type Activities** – These functions normally are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities of the Government include the operations of the (i) unemployment insurance program and (ii) the West Indian Company (WICO). Both of these programs operate with minimal assistance from the governmental activities of the Government.

*Discretely Presented Component Units* – These are operations for which the Government has financial accountability even though they have certain independent qualities as well. For the most part, these entities operate similar to private sector businesses and the business-type activities described above. The Government's discretely presented component units are presented in two categories, major and nonmajor. This separation is determined by the relative size of the entities' assets, liabilities, revenue, and expenses in relation to the total of all component units.

### Management's Discussion and Analysis (continued)

#### **Fund Financial Statements**

Fund financial statements focus on the most significant (or major) funds of the Government. A fund is a separate accounting entity with a self-balancing set of accounts. The Government uses funds to keep track of sources of funding and spending related to specific activities. The Government uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

A major fund is a fund whose revenue, expenditures or expenses, assets, or liabilities (excluding extraordinary items) are at least 10% of the corresponding totals for all governmental or enterprise funds and at least 5% of the aggregate amount for all governmental and enterprise funds for the same item. The general fund is always considered a major fund. In addition to funds that meet the major fund criteria, any other governmental or enterprise fund that the Government believes is particularly important to the financial statements may be reported as a major fund.

All of the funds of the Government are divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

#### Governmental Funds

Governmental funds are accounted for using the modified accrual basis of accounting, which measures cash and other assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the PG's general governmental operations and the basic services it provides. The reconciliation following the fund financial statements explains the differences between the governmental activities, reported in the government-wide financial statements, and the governmental funds' financial statements. The General Fund, the PFA Debt Service, and the PFA Capital Projects Fund are reported as major governmental funds.

The General Fund is the PG's primary operating fund. It accounts for all financial resources of the PG, except those required to be accounted for in another fund.

The PFA Debt Service accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by the Virgin Islands Public Finance Authority (PFA) on behalf of the Government.

The PFA Capital Projects Fund accounts for bond proceeds of debt issued by the PFA on behalf of the Government. The bond proceeds have been designated for certain necessary public safety and capital development projects which are accounted for in this fund.

Management's Discussion and Analysis (continued)

### **Proprietary Funds**

Services provided to outside (nongovernmental) customers are reported in enterprise funds. Enterprise funds are accounted for using the economic resources measurement focus and the accrual basis of accounting. These are the same business-type activities reported in the government-wide financial statements.

The unemployment insurance fund and the West Indian Company (WICO) fund are major proprietary funds.

The unemployment insurance fund is a federally mandated program to manage unemployment insurance.

The WICO fund accounts for the activities of WICO, which owns a port facility including a cruise ship pier, and manages a shopping mall and a rental complex.

### Fiduciary Funds

The Government is the trustee, or fiduciary, for several agency funds.

The fiduciary activities are reported in a separate statement of fiduciary net assets and a statement of changes in fiduciary net assets.

#### Financial Analysis of the Government as a Whole

The PG and its component units experienced an economic downturn following the slowdown of the U.S. economy in fiscal year 2002 and the events of September 11, 2001. As explained in note 14 to the basic financial statements, the Government initiated specific actions to improve its future cash flows through the issuance of long-term debt, the development of a series of detailed revenue enhancement and expenditure reduction initiatives, and the enactment of certain laws directed toward improving the Government's financial situation.

### Management's Discussion and Analysis (continued)

In fiscal year 2006, the Government issued the 2006 Series A Tobacco Settlement Asset-Backed Capital Appreciation Bonds amounting to \$48.1 million with an issue value of \$7.3 million net of accretion of \$40.8 million for the purpose of financing several capital, hospital and health development projects. Also issued in 2006 were the 2006 Series A Revenue Bonds and the 2006 Series Revenue Notes. The 2006 Series A Revenue Bonds amounting to \$219.49 million were issued for the purpose of advance refunding the 1999 Series A bonds and funding capital projects of the PG. The 2006 Series Note in the amount of \$4 million were issued to finance the purchase of fire equipment, train fire fighters and make renovations and repairs to the territories fire stations. In fiscal year 2005, the Government issued the 2004 Series A Bonds amounting to \$94 million to fund wastewater treatment and solid waste capital projects of the PG; and the Series 2005 Subordinate Lien Revenue Notes amounting to \$6.35 million to finance the acquisition of a fleet of vehicles for the police department.

#### **Financial Analysis of the Primary Government**

Total assets of the government as of September 30, 2006 and 2005 were \$1.833 billion and \$1.712 billion, respectively, an increase of approximately \$121 million. Total liabilities as of September 30, 2006 and 2005 were \$1.847 billion and \$1.852 billion, respectively, a decrease of approximately \$5 million.

For the year ended September 30, 2006, the PG net deficit of \$14 million consisted of \$136 million invested in capital assets, net of related debt; \$169 million restricted by statute or other legal requirements that were not available to finance day-to-day operations of the Government; and an unrestricted net deficit of \$319 million. For the year ended September 30, 2005, the PG net asset deficit of \$141 million consisted of \$158 million invested in capital assets, net of related debt; \$317 million restricted by statute or other legal requirements and were not available to finance day-to-day operations of the Government; and an unrestricted net deficit of \$141 million consisted of \$158 million invested in capital assets, net of related debt; \$317 million restricted by statute or other legal requirements and were not available to finance day-to-day operations of the Government; and an unrestricted net deficit of \$624 million.

For the fiscal year ended September 30, 2006, the PG earned program and general revenue amounting to \$1.181 billion, and reported expenses of \$1.055 billion, resulting in a decrease in the net deficit of \$126 million. For the fiscal year ended September 30, 2005, the PG earned program and general revenue amounting to \$1.116 billion, and reported expenses of \$981 million, resulting in a decrease in the net deficit of \$135 million.

### Management's Discussion and Analysis (continued)

Overall, revenue increased of approximately \$65 million in fiscal year 2006, when compared to fiscal year 2005. Expenses increased in fiscal year 2006 when compared to fiscal year 2005 by \$75.4 million. A summary of net assets (deficit) and changes in net assets (deficit) for the primary government follows:

#### **Net Assets (Deficit) – Primary Government**

September 30, 2006 and 2005 (In thousands)

	Governmen	tal activities	B	usiness-ty	pe a	ctivities	 T	otal	
	2006	2005		2006		2005	 2006		2005
		(As restated)			(As	restated)		(A	s restated)
Assets									
Current assets	\$ 1,065,638	\$ 1,012,438	\$	55,188	\$	50,422	\$ 1,120,826	\$	1,062,860
Capital assets	639,669	587,902		46,295		43,823	685,964		631,725
Other assets	25,337	16,545		377		407	 25,714		16,952
Total assets	1,730,644	1,616,885		101,860		94,652	 1,832,504		1,711,537
Liabilities									
Long-term debt outstanding	1,175,118	1,143,194		20,719		20,545	1,195,837		1,163,739
Other liabilities	645,412	679,791		5,687		8,682	 651,099		688,473
Total liabilities	1,820,530	1,822,985		26,406		29,227	 1,846,936		1,852,212
Net Assets									
Invested in capital assets, net of									
related debt	110,094	134,513		25,576		23,278	135,670		157,791
Restricted	130,141	282,898		38,920		33,998	169,061		316,896
Unrestricted (deficit)	(330,111)	(623,511)		10,958		8,149	 (319,153)		(615,362)
Total net assets									
(deficit)	\$ (89,876)	\$ (206,100)	\$	75,454	\$	65,425	\$ (14,422)	\$	(140,675)

# Management's Discussion and Analysis (continued)

#### Changes in Net Assets (Deficit) – Primary Government

#### September 30, 2006 and 2005

(In thousands)

	Gover	nmenta	l Activities	B	usiness-ty	pe A	ctivities	То	tal
	200	6	2005		2006		2005	2006	2005
Revenue:									
Program revenue:									
Charges for services	\$ 3	3,687	\$ 31,110	\$	53,067	\$	48,895	\$ 86,754	\$ 80,005
Operating grants and contributions		6,448	170,963	Ŧ		Ŧ	-	146,448	170,963
General revenue:		- , - ,	,					- / -	
Taxes	87	2,108	789,122		_		_	872,108	789,122
Interest and other		2,984	72,596		2,076		2,427	75,060	75,023
Other general revenue		973	1,094				,	973	1,094
Total revenue	1,12	6,200	1,064,885		55,143		51,322	1,181,343	1,116,207
Expenses:									
General government	41	4,306	371,052		_		-	414,306	371,052
Public safety	5	8,220	54,101		_		_	58,220	54,101
Health	10	9,271	99,681		_		-	109,271	99,681
Public housing and welfare	7	0,736	67,228		_		_	70,736	67,228
Education	19	6,395	205,419		_		_	196,395	205,419
Transportation and communication	6	0,700	63,109		_		-	60,700	63,109
Culture and recreation		6,852	9,879		_		-	6,852	9,879
Termination of swaption fee	2	6,910	-		-		-	26,910	-
Interest on long-term debt	6	1,648	61,996		-		-	61,648	61,996
Unemployment insurance		_	-		5,151		7,568	5,151	7,568
West Indian Company		_	-		9,638		9,763	9,638	9,763
Workmen's Compensation		_	-		9,121		9,112	9,121	9,112
VI Lottery		_	-		15,708		10,733	15,708	10,733
Other business-type activities		-	-		10,434		11,732	10,434	11,732
Total expenses	1,00	5,038	932,465		50,052		48,908	1,055,090	981,373
Increase (decrease) in net assets									
before transfers	12	1,162	132,420		5,091		2,414	126,253	134,834
Transfers	(	4,938)	3,528		4,938		(3,528)		_
	(	4,938)	3,528		4,938		(3,528)		_
Change in net assets	11	6,224	135,948		10,029		(1,114)	126,253	134,834
Net assets (deficit), beginning of year	(20	6,100)	(342,048)		65,425		66,539	(140,675)	(275,509)
Net assets (deficit), end of year,									
as restated in 2005	\$ (8	9,876)	\$ (206,100)	\$	75,454	\$	65,425	\$ (14,422)	\$ (140,675)

### Management's Discussion and Analysis (continued)

The Virgin Islands Office of Management and Budget of the PG prepares an annual executive budget subject to approval by the Governor and the Legislature of the Virgin Islands. The executive budget is prepared on a budgetary basis similar to the cash basis of accounting. The executive budget includes only those funds that are subject to appropriation by law. More information regarding budgetary procedures is provided in Note 3 of the basic financial statements. A summary of the budgetary report for the General Fund of the PG, included on page 25 of the financial statements, follows:

#### Revenue and Expenditures – Budget and Actual – Budgetary Basis – General Fund

#### Year Ended September 30, 2006

(In thousands)

	Original Budget	Amended Budget		Actual		<u> </u>	ariance
Total revenue Total expenditures	\$ 523,448 667,859	\$	523,448 741,677	\$	664,207 665,890	\$	140,759 75,787
Excess of expenditures over revenue	 (144,411)		(218,229)		(1,683)		216,546
Other financing sources	 73,633		73,433		98,296		24,863
Efficiency of revenue and other financing sources under expenditures	\$ (70,778)	\$	(144,796)	\$	96,613	\$	241,409

For fiscal year 2006, the PG realized a revenue variance \$141 million due to an increase in the collection of certain tax revenues. The PG realized a \$74 million variance in expenditures due to controlled spending. The PG realized a \$24 million variance in other financing sources due to the fact that transfers to the General Fund were higher than budgetary estimates.

### Management's Discussion and Analysis (continued)

#### **Capital Assets**

Capital assets additions during fiscal year 2006 amounted to \$70.9 million for governmental activities, and \$4.6 million for business-type activities.

The Government's capital assets include land, land improvements, buildings, building improvements, machinery, equipment, infrastructure, and construction in progress as follows:

#### **Capital Assets – Primary Government**

(In thousands)

	Government	tal Activities	Business-ty	pe Activities	То	otal
	2006	2005	2006	2005	2006	2005
		(As restated)		(As restated)		(As restated)
Land and improvements	\$ 175,513	\$ 175,446	\$ 5,317	\$ 5,317	\$ 180,830	\$ 180,763
Building and improvements	337,774	334,363	49,638	49,137	387,412	383,500
Machinery and equipment	67,710	59,133	4,619	4,376	72,329	63,509
Infrastructure	133,776	127,471	_	_	133,776	127,471
Construction in progress	99,688	47,431	5,600	1,757	105,288	49,188
Total assets	814,461	743,844	65,174	60,587	879,635	804,431
Less accumulated depreciation	(174,792)	(155,942)	(18,879)	(17,064)	(193,671)	(173,006)
Total capital assets	\$ 639,669	\$ 587,902	\$ 46,295	\$ 43,523	\$ 685,964	\$ 631,425

Note 9 provides detailed information regarding the capital assets of the primary government and the component units of the Government

### Management's Discussion and Analysis (continued)

#### **Debt Administration**

The Government issues both general obligation bonds and revenue bonds. The Revised Organic Act [48 U.S.C. Section 1574 (b)(ii)] restricts the principal amount of general obligation debt that the Government may issue to no greater than 10% of the aggregate assessed valuation of taxable real property in the U.S. Virgin Islands. Following is a summary of bonds outstanding as of September 30, 2006:

#### **Primary Government – Bonds Payable**

(In thousands)

Bonds Payable	Final Maturity	Interest Rates (%)	Balance
<ul> <li>1998 Series A, C, D, and E Revenue and Refunding Bonds</li> <li>1999 Series A General Obligation Bonds</li> <li>1999 Series A Revenue Bonds</li> <li>2001 Series A Tobacco Bonds</li> <li>2002 Series Garvee Bonds</li> <li>2003 Series A Revenue Bonds</li> <li>2004 Series A Revenue Bonds</li> <li>2006 Series A, B, C &amp; D Tobacco</li> </ul>	2025 2010 2033 2031 2009 2033 2024	5.50 to 7.11 6.50 4.20 to 6.50 5.00 2.50 to 5.00 4.00 to 5.25 4.00 to 5.25	\$ 445,025 3,820 110,695 21,665 9,940 265,145 91,705
Turbo and Capital Appreciation Bonds 2006 Series A Revenue Bonds	2035 2029	6.25 - 7.625 3.50 - 5.00	7,290 219,490
Subtotal Deferred amount on refundings Bond premium Bond discount Bond accretion			1,174,775 (18,605) 19,058 (7,508) (190)
Total			\$ 1,167,530

Note 10 provides detailed information regarding all bonds of the U.S. Virgin Islands.

### Management's Discussion and Analysis (continued)

During fiscal year 2006, the 2006 Series A Revenue Bonds amounting to \$219.5 million; the 2006 Series Note amounting to \$4 million and the 2006 Series A Tobacco Settlement Asset-Backed Bonds with an issue value of \$7.3 million amounting to \$48 million were issued.

During fiscal year 2005, the 2004 Series A Revenue Bonds amounting to \$94 million were issued.

The PG made bond principal payments on all outstanding general and special revenue bonds amounting to \$192 million during fiscal year 2006, and \$24.4 million during fiscal year 2005.

The Government's bonds carry insured ratings of "AAA" and "Aaa" from Fitch Ratings and Moody's Investors Services, respectively. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained from the respective rating agency.

Other liabilities of the PG include:

#### **Primary Government – Other Liabilities**

#### September 30, 2006 and 2005

(In millions)

	2	006	2	005
			(As r	estated)
Accrued compensated absences Retroactive union arbitration liability Accrued litigation	\$	44 284 16	\$	48 276 23
Landfill closure and post closure costs Total other liabilities	\$	<u>33</u> 377	\$	29 376

#### **Economic Condition and Outlook**

The PG ended fiscal year 2006 with a deficit amounting to \$28.9 million, of which \$334 million relates to an unrestricted deficit. The PG is working towards a recovery from the recession of 2002 through a combination of revenue initiatives and budgetary restraint on expenditures.

### Management's Discussion and Analysis (continued)

#### **Revenue Initiatives**

The PG collects income tax revenue under the "mirror" income tax system. The Government's tax laws mirror the U.S. Internal Revenue Service (IRS) Code, Rules, and Regulations. The 2003 and 2004 Tax Acts passed by U.S. Congress may have a negative impact on revenue due to changes in sourcing of revenue rules as defined for the U.S. Virgin Islands, restrictions on residency rules, a decrease in tax rates, expanded tax credits, and expanded tax deductions. In January 2006, the U.S. Treasury issued final tax regulations for the territories and possessions defining residency and source of income. The Government has responded to these changes through meetings with the U.S. Treasury and the final regulations on residency were subsequently revised in November 2006.

In connection with a real property tax case instituted against the PG in the U.S. District Court of the Virgin Islands, the Government was enjoined for a four-month period in fiscal year 2003 from appraising and assessing any real property taxes until it modified its system of appraisal to comply with certain court mandates. As a result, effective August 2003, it has been using the 1998 assessment value to issue tax bills and collect taxes, and expects to continue to do so until a new appraisal system is implemented, which is intended to satisfy the court's decision, or the decision is reversed on appeal. In fiscal year 2004, the Government retained a consultant to modify its system of appraisal and to comply with the court mandates. In fiscal year 2006, legislation was introduced to Congress to move the control of property tax assessments from the federal government to the Government of the Virgin Islands.

The Government is currently in litigation challenging the computation of its corporate franchise tax. Of the four cases brought against the Government, one is currently before the Virgin Islands Territorial Court, and the remaining three cases are currently on appeal.

#### **Budgetary Control of Expenditures**

The PG faces the challenge of carryforward expenditures from prior fiscal years and increasing expenditures in the current fiscal year. Carryforward expenditures consist mainly of retroactive salary increases, which accumulated following Hurricanes Hugo, Marilyn and Bertha in the years of 1990 through 1998. At September 30, 2006 and 2005, unpaid retroactive salary increases amounted to \$284 million and \$276 million, respectively, which are reported as a liability of the Government within other noncurrent liabilities.

Current increasing governmental expenditures include increased health insurance premiums, pharmaceutical premiums, and salary expense. Expenditures are closely monitored and controlled through the budgetary process.

### Management's Discussion and Analysis (continued)

#### **Deficit Reduction Measures**

The PG has implemented a number of deficit reducing measures including: (i) withholding of local taxes on Government invoice payments, (ii) increasing local taxes such as the highway users tax and stamp tax; (iii) implementation of new local taxes including an excise tax on importation of personal goods and a petroleum tax; and (iv) exerting greater control of expenditures through the budgetary process, and (v) implementation of tax amnesties for property and gross receipts taxes.

These initiatives have been successful in reducing the PG deficit from \$153 million for fiscal year 2002, to \$29 million for fiscal year 2006, a reduction of \$124 million.

#### **Contacting the Government's Financial Management**

This financial report is designed to provide the Government's citizens, taxpayers, customers, and investors and creditors with a general overview of the Government's finances. If you have questions about this report, or need additional financial information, contact the Government of the United States Virgin Islands, Department of Finance, No. 2314 Kronprindsens Gade, St. Thomas, VI 00802.

# Statement of Net Assets (Deficit)

### September 30, 2006 (In thousands)

	Primary G	Government		
		Business-type		Component
	Activities	Activities	Total	Units
Assets	-			
Cash and cash equivalents	\$ 160,719	\$ 23,452	\$ 184,171	\$ 59,101
Investments	602,793	1,010	603,803	40,175
Receivables, net	263,146	3,953	267,099	61,250
Internal balances	6,522	(6,522)	_	_
Loans and advances	-	-	-	79
Due from component units, net	2,879	-	2,879	_
Note receivable	-	_	-	8,384
Due from primary government	_	_	-	4,482
Due from federal government	27,994	_	27,994	7,844
Inventories	-	24	24	27,370
Other assets	1,584	902	2,486	40,414
Restricted:	,		,	,
Cash and cash equivalents	_	32,369	32,369	41,775
Investments	_	_	_	72,758
Other	_	_	_	3
Capital assets	639,669	46,295	685,964	795,765
Deferred and other expenses	25,338	377	25,715	17,226
Total assets	1,730,644	101,860	1,832,504	1,176,626
Liabilities	,,·	- ,		, ,
Current liabilities:				
Accounts payable and accrued liabilities	80,099	3,521	83,620	101,088
Tax refunds payable	77,523	_	77,523	_
Unemployment insurance benefits	_	2,032	2,032	_
Customer deposits	_	_	_	18,238
Due to primary government	_	_	_	33,759
Due to component units	4,482	_	4,482	
Due to federal government		_		7,382
Interest payable	30,286	_	30,286	4,954
Unearned revenue	88,430	134	88,564	4,467
Other current liabilities	1,277	-	1,277	15,773
Noncurrent liabilities:	-,-,,		-,-//	10,,,,0
Due within one year:				
Loans payable	3,414	654	4,068	1,767
Bonds payable	29,612		29,612	10,975
Other liabilities	27,187	_	27,187	
Due in more than one year:	27,107		27,107	
Loans payable	4,174	20,065	24,239	19,808
Bonds payable	1,137,918	20,005	1,137,918	265,842
Other liabilities	336,118	_	336,118	29,682
Total liabilities	1,820,520	26,406	1,846,926	513,735
	1,020,320	20,400	1,040,920	515,755

(Continued)

# Statement of Net Assets (Deficit) (continued)

### September 30, 2006 (In thousands)

	Primary G	overnment		
	Governmental Activities	Business-type Activities	Total	Component Units
Net assets				
Invested in capital assets, net of related debt	110,094	25,576	135,670	560,273
Restricted for:				
Unemployment insurance	_	30,022	30,022	_
Debt service	130,141	_	130,141	_
Other purposes	_	8,898	8,898	92,535
Unrestricted (deficit)	(330,111)	10,958	(319,153)	10,383
Total net assets (deficit)	\$ (89,876)	\$ 75,454	\$ (14,422)	\$ 663,191

#### Statement of Activities

#### Year Ended September 30, 2006 (In thousands)

					Prog	ram Revenu	es			evenue (Expense) anges in Net Asset		
			. <u> </u>		0	perating		Capital	Pri	mary Governmen	t	
			Ch	arges for	Gr	ants and	C	Frants and	Governmental	Business-type		Component
	I	Expenses	5	Services	Con	tributions	Co	ontributions	Activities	Activities	Total	Units
Functions:												
Primary government:												
Governmental activities:												
General government	\$	414,306	\$	28,598	\$	27,685	\$	_	\$ (358,023)	\$ –	\$ (358,023)	\$ –
Public safety		58,220		564		8,834		_	(48,822)	_	(48,822)	-
Health		109,271		452		23,400		-	(85,419)	-	(85,419)	-
Public housing and welfare		70,736		1,594		49,619		-	(19,523)	-	(19,523)	-
Education		196,395		_		26,047		_	(170,348)	_	(170,348)	_
Transportation and communication		60,700		2,441		10,615		_	(47,644)	_	(47,644)	_
Culture and recreation		6,852		38		248		-	(6,566)	_	(6,566)	_
Termination of swaption fee		26,910		_		_		-	(26,910)	_	(26,910)	_
Interest on long-term debt		61,648		_		_		_	(61,648)	_	(61,648)	_
Total governmental activities		1,005,038		33,687		146,448		-	(824,903)	_	(824,903)	
Business-type activities:				,		,						
Unemployment insurance		5,151		1,476		_		_	_	(3,675)	(3,675)	_
West Indian Company		9,638		11,576		_		_	_	1,938	1,938	_
Workers' compensation		9,121		9,111		_		_	_	(10)	(10)	_
VI Lottery		15,708		18,500		_		_	_	2,792	2,792	_
Other		10,434		12,404		_		_	_	1,970	1,970	_
Total business-type activities		50,052		53,067		_		_		3,015	3,015	
Total primary government	\$	1,055,090	\$	86,754	\$	146,448	\$	_	(824,903)	3,015	(821,888)	
Component units:	-	,,	-	)		- 7 -			(- , )	- )	(- ))	
Virgin Islands Housing Authority	\$	41,691	\$	5,634	\$	30,371	\$	_	_	_	_	(5,686)
Virgin Islands Port Authority	Ψ	51,306	Ψ	39,279	Ψ		Ψ	2,796	_	_	_	(9,231)
Virgin Islands Water and Power Authority:		51,500		59,219				2,790				(),251)
Electric system		203,262		205,041		_		_	_	_	_	1,779
Water system		35,884		33,723		_				_		(2,161)
Virgin Islands Government		55,004		55,125								(2,101)
Hospital and Health Facilities Corporation:												
Roy L. Schneider Hospital		80,649		47,070		25,125		4,496				(3,958)
Juan F. Luis Hospital		61,916		28,980		23,123		2,674	-	—	—	(6,391)
University of the Virgin Islands		67,363		28,980		43,847		2,674	-	-	_	(5,371)
Other component units		67,363 19,168		5,273		43,847		· · ·	-	-	-	(5,371) 4,046
Total component units	\$	561,239	\$	<u>5,273</u> 379,953	\$	134,713	\$	<u>6,442</u> 19,600				(26,973)
rotai component units	Φ	301,239	¢	519,935	Ф	134,/13	Ф	19,000		-		(Continued)

(Continued)

#### Statement of Activities (continued)

Year Ended September 30, 2006 (In thousands)

	Net Re	evenue (Expense) a	nd	
	Cha	anges in Net Assets	es in Net Assets ry Government	
	Pri	ary Government           Business-type           Activities         Total           3,015         (821,888)           -         872,108           2,076         75,060           -         973           4,938         -           7,014         948,141           10,029         126,253		
	Governmental	Business-type		Component
	Activities	Activities	Total	Units
Total primary government and				
component units	(824,903)	3,015	(821,888)	(26,973)
General revenues:				
Taxes	872,108	-	872,108	-
Interest and other	72,984	2,076	75,060	11,170
Tobacco settlement rights	973	-	973	-
Transfers – internal activities of primary				
government	(4,938)	4,938	_	-
Total general revenue				
and transfers	941,127	7,014	948,141	11,170
Changes in net assets (deficit)	116,224	10,029	126,253	(15,803)
Net assets (deficit), beginning of year				
(as restated)	(206,100)	65,425	(140,675)	678,994
Net assets (deficit), end of year	\$ (89,876)	\$ 75,454	\$ (14,422)	\$ 663,191

#### Balance Sheet – Governmental Funds

#### September 30, 2006 (In thousands)

	General	PFA Debt Service	PFA Capital Projects	Go	Other overnmental	Go	Total overnmental
Assets							
Cash and cash equivalents	\$ 103,790	\$ -	\$ 31,774	\$	25,155	\$	160,719
Investments	271,129	167,597	140,422		23,645		602,793
Receivables:							
Taxes, net	234,982	27,380	_		-		262,362
Accrued interest and other	1,358	_	-		194		1,552
Due from:							
Other funds	8,846	_	313		11,420		20,579
Component units, net	2,879	-	_		-		2,879
Federal government	-	_	-		27,994		27,994
Other assets	-	_	-		34		34
Total assets	\$ 622,984	\$ 194,977	\$ 172,509	\$	88,442	\$	1,078,912
Liabilities and Fund Balances							
Accounts payable and accrued liabilities	\$ 59,335	\$ 416	\$ 4,349	\$	15,999	\$	80,099
Tax refunds payable	77,523	_	_		-		77,523
Due to:							
Other funds	10,879	_	-		3,178		14,057
Component units	4,482	_	-		_		4,482
Deferred revenue	242,747	64,420	-		12,541		319,708
Other current liabilities	-	-	_		1,277		1,277
Total liabilities	 394,966	64,836	4,349		32,995		497,146
Fund balances reserved for:							
Encumbrances	120,249	_	-		_		120,249
Debt service	-	130,141	_		7,145		137,286
Unreserved fund balance, reported in:							
General fund	107,769	_	-		_		107,769
Special revenue funds	-	_	-		66,530		66,530
Capital projects funds	_	_	168,160		(18,228)		149,932
Total fund balances	 228,018	130,141	168,160		55,447		581,766
Total liabilities and fund balances	\$ 622,984	\$ 194,977	\$ 172,509	\$	88,442	•	-

#### Amounts reported for governmental activities in the statement of net assets (deficit) are different because:

Capital assets used in governmental activities are not financial resources and,

therefore, are not reported in the funds.	639,669
Bond issue costs are not financial resources and, therefore, are not	
reported in the funds.	25,338
Because the focus of governmental funds is on short-term financing,	
some assets, primarily taxes receivable, will not be available to pay for current period	
expenditures. Those assets are offset by deferred revenue in the funds.	232,060
Interest on long-term debt is not accrued in the funds, but rather is	
recognized as an expenditure when due.	(30,286)
Long-term liabilities, including bonds payable, are not due and payable	
in the current period and therefore are not reported in the funds.	(1,538,423)
Deficit of governmental activities	\$ (89,876)

# Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds

Year Ended September 30, 2006 (In thousands)

			PFA Debt		PFA Capital		Other		Total
	General		Service	]	Projects	Go	overnmental	Go	vernmental
Revenues:									
Taxes	\$	642,744	\$ 187,043	\$	2,250	\$	29,549	\$	861,586
Federal grants and contributions		-	3,446		-		143,003		146,449
Charges for services		24,985	_		-		8,701		33,686
Tobacco settlement rights		-	-		-		1,016		1,016
Interest and other		31,394	6,353		12,715		22,522		72,984
Total revenues		699,123	196,842		14,965		204,791		1,115,721
Expenditures:									
Current:									
General government		307,942	-		6,322		91,300		405,564
Public safety		48,675	-		-		8,001		56,676
Health		86,258	-		4,603		15,095		105,956
Public housing and welfare		32,715	-		1,203		36,818		70,736
Education		172,301	-		-		18,447		190,748
Transportation and communication		37,189	-		2,395		16,657		56,241
Culture and recreation		5,098	_		-		1,489		6,587
Capital outlays		18,141	_		54,934		247		73,322
Debt service:									
Principal		-	190,810		2,262		1,220		194,292
Interest		-	61,172		188		981		62,341
Bond issuance costs		-	9,252		-		472		9,724
Total expenditures		708,319	261,234		71,907		190,727		1,232,187
Excess (deficiency) of revenue									
over (under) expenditures		(9,196)	(64,392)		(56,942)		14,064		(116,466)
Other financing sources (uses):									
Issuance of refunding bonds		-	178,580		40,910		7,290		226,780
Payment to refunding bond escrow agent		-	(17,372)		_		_		(17,372)
Fee on termination of swaption contract		-	_		(26,910)		_		(26,910)
Loans issued		-	_		4,000		_		4,000
Transfers from other funds		133,504	_		1,175		22,176		156,855
Transfers to other funds		(13,520)	(115,660)		(1,938)		(30,675)		(161,793)
Premium (discount) on bonds issued		-	11,572		-		(358)		11,214
Total other financing sources (uses), net		119,984	57,120		17,237		(1,567)		192,774
Net change in fund balances		110,788	(7,272)		(39,705)		12,497		76,308
Fund balance at beginning of year, as restated		117,230	137,413		207,865		42,950		505,458
Fund balance at end of year	\$	228,018	\$ 130,141	\$	168,160	\$	55,447	\$	581,766

### Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities – Governmental Funds

Year Ended September 30, 2006 (In thousands)

Net change in fund balances - total governmental funds	\$	76,308
Government funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.		51,767
Tax revenue in the statement of activities, which does not provide current financial resources, is not reported as revenue in the funds.		10,477
The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of the governmental funds. These transactions have no effect on net assets. This is the amount by which bond and loan proceeds of \$230,780 exceeded principal retirement of \$194,292 in the current period.		(36,488)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. This is the amount by which the increase in certain liabilities reported in the statement of net assets of the previous year increased expenses reported in the statement of activities that do not require the use of current financial resources.		112
Bond issue costs are expended in the governmental funds when paid, and are capitalized and amortized in the statement of activities. This is the amount by which current year bond issue costs exceeded amortization expense in the current period.		8,791
Bond premiums and discounts are reported as other financing sources and uses in the governmental funds when the bonds are issued, and are capitalized and amortized in the government-wide financial statements. This amount represents the capitalization of premiums on bonds issued during the current year of \$6,159 and the additional net interest expense of \$1,595 reported in the statement of activities related to the amortization of premiums, discounts deferred refunding loss, and accreted interest on capital appreciation bonds during the current year.		4,564
Certain interest reported in the statement of activities does not require the use of current financial resources and therefore is not reported as expenditures in the governmental funds. This amount represents the decrease in interest payable		
reported in the statement of net assets less accrued interest. Change in net assets of governmental activities	\$	693 116,224
Change in net assets of governmental activities	φ	110,224

### Statement of Revenues and Expenditures – Budget and Actual – Budgetary Basis – General Fund

Year Ended September 30, 2006 (In thousands)

	Original Budget		Amended Budget Actual			Positive/ (Negative) Variance		
Revenues:								
Taxes	\$	485,055	\$	485,055	\$	621,116	\$	136,061
Charges for services		10,206		10,206		16,076		5,870
Interest and other		28,187		28,187		27,015		(1,172)
Total revenues		523,448		523,448		664,207		140,759
Expenditures:								
Current:								
General government		178,173		223,574		306,542		(82,968)
Public safety		82,117		82,347		48,675		33,672
Health		84,224		92,910		86,258		6,652
Public housing and welfare		54,591		58,786		32,715		26,071
Education		213,389		217,465		171,460		46,005
Transportation and communication		32,830		40,647		16,183		24,464
Culture and recreation		22,535		25,948		4,057		21,891
Total expenditures		667,859		741,677		665,890		75,787
Excess of expenditures over revenue		(144,411)		(218,229)		(1,683)		216,546
Other financing sources (uses):								
Transfers from other funds		80,470		80,470		105,333		24,863
Transfer to other funds		(6,837)		(7,037)		(7,037)		_
Total other financing sources (uses), net		73,633		73,433		98,296		24,863
Excess of revenue and other								
financing sources over expenditures	\$	(70,778)	\$	(144,796)	\$	96,613	\$	241,409

# Statement of Net Assets - Proprietary Funds

#### September 30, 2006 (In thousands)

	Business-type Activities – Enterprise Funds							
				West				
	Uner	nployment		Indian				
	In	surance	(	Company		Other		Totals
Assets								
Current assets:								
Cash and cash equivalents	\$	164	\$	5,835	\$	17,453	\$	23,452
Investments at fair value		_		1,010		-		1,010
Receivables, net:								
Premiums receivable		1,358		-		-		1,358
Accrued interest and other		-		1,535		-		1,535
Other receivables		_		_		1,060		1,060
Due from other funds		_		_		300		300
Inventories and other current assets		_		_		24		24
Other assets		_		799		103		902
Total current assets		1,522		9,179		18,940		29,641
Noncurrent assets:								
Restricted cash and cash equivalents		30,549		1,820		_		32,369
Capital assets		_		35,492		10,803		46,295
Deferred expenses		_		377		-		377
Total noncurrent assets		30,549		37,689		10,803		79,041
Total assets		32,071		46,868		29,743		108,682
Liabilities								
Current liabilities:								
Accounts payable and accrued liabilities		_		1,478		2,043		3,521
Due to other funds		_		1,000		5,822		6,822
Unemployment insurance benefits		2,032		_		-		2,032
Unearned revenue		17		_		117		134
Loans payable related to capital assets		_		654		_		654
Total current liabilities		2,049		3,132		7,982		13,163
Noncurrent liabilities:								
Loans payable related to capital assets		_		20,065		_		20,065
Total liabilities		2,049		23,197		7,982		33,228
Net assets								
Invested in capital assets, net of								
related debt		_		14,773		10,803		25,576
Restricted		30,022		8,898		-		38,920
Unrestricted				_		10,958		10,958
Total net assets	\$	30,022	\$	23,671	\$	21,761	\$	75,454
				÷				· · · · ·

### Statement of Revenues, Expenses, and Changes in Fund Net Assets – Proprietary Funds

Year Ended September 30, 2006 (In thousands)

	Business-type Activities – Enterprise Funds								
	West								
	Unemp	oloyment	I	ıdian					
	Insu	rance	Co	mpany		Other		Total	
Operating revenues:									
Charges for services	\$	1,476	\$	11,576	\$	40,015	\$	53,067	
Total operating revenues		1,476		11,576		40,015		53,067	
Operating expenses:									
Cost of services		5,151		7,179		34,668		46,998	
Depreciation and amortization		_		1,521		594		2,115	
Total operating expenses		5,151		8,700		35,262		49,113	
Operating income (loss)		(3,675)		2,876		4,753		3,954	
Nonoperating revenue (expenses):									
Interest income		1,490		210		375		2,075	
Interest expense		_		(938)		_		(938)	
Total nonoperating revenue								i	
(expenses), net		1,490		(728)		375		1,137	
Income (loss) before operating transfers		(2,185)		2,148		5,128		5,091	
Transfers from other funds		-		_		5,938		5,938	
Transfers to other funds		_		(1,000)		_		(1,000)	
Change in net assets		(2,185)		1,148		11,066		10,029	
Net assets at beginning of year (as restated)		32,207		22,523		10,695		65,425	
Net assets at end of year	\$	30,022	\$	23,671	\$	21,761	\$	75,454	

### Statement of Cash Flows - Proprietary Funds

#### Year Ended September 30, 2006 (In thousands)

	Business-type Activities – Enterprise Funds West						
	Unon	Unemployment Indian					
		surance	Company		Other	г	Fotal
Cash flows from operating activities							
Receipts from customers and users	\$	940	\$ 10,497	\$	40,149	\$	51,586
Payments to beneficiaries		(5,231)	-	-	_		(5,231)
Payments to suppliers and employees		-	(7,537	')	(39,086)		(46,623)
Net cash provided by (used in)							
operating activities		(4,291)	2,960	)	1,063		(268)
Cash flows from noncapital financing activities							
Transfer from other funds		_	-	-	5,938		5,938
Transfers to other funds		_	(1,000	))	-		(1,000)
Net cash provided by (used in)				<i>.</i>			
noncapital financing activities		-	(1,000	))	5,938		4,938
Cash flows from capital and related financing activities							
Acquisition and construction of capital assets		_	(1,534	)	(3,055)		(4,589)
Principal paid on long-term debt		-	172	2	-		172
Proceeds from sale of asset		-	-	-	-		-
Interest paid on long-term debt		-	(908	3)	-		(908)
Net cash used in capital and related							
financing activities		-	(2,270	))	(3,055)		(5,325)
Cash flows from investing activities							
Interest and dividends on investments		1,490	210	)	375		2,075
Purchase of investments		-	(170	/	-		(170)
Net cash provided by investing activities		1,490	40		375		1,905
Net increase (decrease) in cash and cash equivalents		(2,801)	(270	))	4,321		1,250
Cash and cash equivalents at beginning of year (as restated)		33,514	7,925	;	13,132		54,571
Cash and cash equivalents at end of year	\$	30,713	\$ 7,655	5 \$	17,453	\$	55,821
Reconciliation of operating income (loss) to net cash							
provided by (used in) operating activities							
Operating income (loss)	\$	(3,675)	\$ 2,876	5 \$	4,753	\$	3,954
Adjustments to reconcile operating income (loss)							
to net cash provided by (used in) operating							
activities:							
Depreciation expense		-	1,521		594		2,115
Change in assets and liabilities:		(52.0)	(1.07)		1.50		(1.457)
Receivables, net		(536)	(1,079	")	158		(1,457)
Deferred revenue Other assets		(48)	-	-	(24) 382		(72) 382
Accounts payable and accrued expenses		(32)	(358	-	(4,800)		(5,190)
Net cash provided by (used in)		(32)	(330	<u>,</u>	(4,800)		(3,190)
operating activities	\$	(4,291)	\$ 2,960	) \$	1,063	\$	(268)
Reconciliation of cash and cash equivalents to the							
statement of net assets							
Cash and cash equivalents – current	\$	164	\$ 5,835	5 \$	17,453	\$	23,452
Cash and cash equivalents – restricted	Ψ	30,549	1,820			•	32,369
Cash and cash equivalents at end of year on		,	,-				<u> </u>
statement of cash flows	\$	30,713	\$ 7,655	5 \$	17,453	\$	55,821

# Statement of Fiduciary Net Assets - Fiduciary Funds

September 30, 2006 (In thousands)

		Pension Trust Funds	Agency Funds		
Assets					
Cash and cash equivalents:					
Unrestricted	\$	108,098	\$	8,431	
Restricted		51		_	
Investments		1,543,782		4,959	
Receivables, net:					
Loans and advances		112,557		-	
Accrued interest		5,605		_	
Other		4,605		_	
Other assets		11,260		_	
Total assets		1,785,958		13,390	
Liabilities					
Accounts payable and accrued liabilities		_		13,390	
Cash overdraft with the Department of Finance		10,454		-	
Cash overdraft with bank		3,533		-	
Unsettled securities purchased		7,376		_	
Securities lending collateral		271,162		_	
Notes payable		10,000		_	
Other liabilities		5,956		_	
Total liabilities	_	308,481		13,390	
Net assets held in trust for employees' pension benefits	\$	1,477,477	\$	_	

# Statement of Changes in Fiduciary Net Assets - Fiduciary Funds

Year Ended September 30, 2006 (In thousands)

	Pension Trust Funds
Additions:	
Contributions:	
Employer	\$ 65,061
Plan members	34,210
Total contributions	99,271
Investment income:	
Net appreciation of fair value of investments	62,705
Interest, dividends, and other, net	56,072
Real estate – rental income	3,645
	122,422
Less investment expense	18,118
Net investment income	104,304
Other income	263
Total additions	203,838
Deductions:	
Benefits paid	147,801
Refunds of contributions	2,935
Administrative and operational expenses	10,258
Total deductions	160,994
Change in net assets	42,844
Net assets, beginning of year	1,434,633
Net assets, end of year	\$ 1,477,477
Net assets, beginning of year	1,434,633

Notes to Basic Financial Statements

September 30, 2006

### **1. Summary of Significant Accounting Policies**

The Government of the United States Virgin Islands (the Government) is an unincorporated organized territory of the United States of America (United States). The powers of the Government are derived from and set forth in the Revised Organic Act of 1954, as amended. The Government assumes responsibility for public safety, health, public housing and welfare, education, transportation and communication, and culture and recreation.

The accompanying basic financial statements of the Government have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

The accompanying basic financial statements have been prepared primarily from accounts maintained by the Department of Finance of the Government. Additional data has been derived from reports prepared by other departments, agencies, and public corporations based on independent or subsidiary accounting systems maintained by them.

#### **Financial Reporting Entity**

The Government follows the provisions of GASB Statement No. 14, The Financial Reporting Entity, as amended by GASB Statement No. 39, Determining Whether Certain Organizations Are Component Units. These standards require that the Government's financial reporting entity be defined according to specific criteria. According to the standard for financial reporting purposes, the Government is a primary government (PG). The PG includes all Government departments, agencies, boards, and organizations that are not legally separate. In addition to the PG, the financial reporting entity includes blended and discretely presented component units. Component units include all legally separate organizations for which the Government's elected officials are financially accountable, and other organizations for which the nature and significance of their relationship with the Government are such that exclusion would cause the basic financial statements to be misleading or incomplete. The criteria used to define financial accountability include appointment of a voting majority of an organization's governing body and (i) the ability of the PG to impose its will on that organization or (ii) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the PG. The financial statements of the following component units are included in the financial reporting entity either as blended or as discretely presented component units in accordance with GAAP.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Financial Reporting Entity (continued)**

### (a) Blended Component Units

The following public benefit corporations, while legally separate from the Government, meet the criteria to be reported as part of the PG because they provide services entirely or almost entirely to the Government:

#### Virgin Islands Public Finance Authority

The Virgin Islands Public Finance Authority (PFA) was created as a public corporation and autonomous governmental instrumentality by Act No. 5365, the Government Capital Improvement Act of 1988, with the purpose of aiding the Government in the performance of its fiscal duties and in effectively carrying out its governmental responsibility of raising capital for essential public projects. Under the enabling legislation, PFA has the power, among other matters, to borrow money and issue bonds and to lend the proceeds of its bonds to the Government or any governmental instrumentality. The powers of PFA are exercised by a board of directors consisting of the Governor (Chairperson), the Commissioner of Finance, the Director of the Office of Management and Budget, and two representatives of the private sector appointed by the Governor with the advice and consent of the Legislature. PFA activities are blended within the PG because it is so intertwined with the Government that, in substance, they are the same. The PFA is reported as major funds.

PFA has a component unit, the West Indian Company (WICO), which is presented as an enterprise fund in the Government's basic financial statements as further described in Note 1(d).

#### **Tobacco Settlement Financing Corporation**

The Tobacco Settlement Financing Corporation (TSFC) was created in September 2001 under Act No. 6428 as a separate and independent corporation of the Government to purchase the rights, title, and interest in tobacco settlement litigation awards and to issue revenue bonds supported by the tobacco settlement rights. The responsibility for the operations of TSFC is vested in a board of directors composed of three Government officials appointed by the Governor and two private citizens. The activities of TSFC are limited to activities conducted on behalf of the Government. The TSFC is reported in the other aggregate fund information.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Financial Reporting Entity (continued)**

### (a) Blended Component Units (continued)

Complete audited financial statements of the PFA and TSFC blended component units can be obtained directly by contacting their respective administrative offices:

Administrative Offices of Blended Component Units

Virgin Islands Public Finance Authority 32-33 Kongens Gade St. Thomas, VI 00802

Tobacco Settlement Financing Corporation 32-33 Kongens Gade St. Thomas, VI 00802

#### (b) Discretely Presented Component Units

The following component units, consistent with GASB Statements No. 14 and 39, are discretely presented in the basic financial statements because of the nature of the services they provide and the Government's ability to impose its will. The component units are reported in a separate column to emphasize that they are legally separate from the PG and governed by separate boards.

#### Major Component Units

#### Virgin Islands Housing Authority

The Virgin Islands Housing Authority (VIHA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality by Act No. 903 on June 18, 1962 with the purpose of providing housing for low-income families. Up until August 2003, the powers of VIHA were exercised by a board of commissioners consisting of seven members as follows: the Commissioner of Housing and Community Renewal and six other members appointed by the Governor. In August 2003, the U.S. Department of Housing and Urban Development (HUD) determined that because of the severity of compliance violations, VIHA was declared to be in substantial default of its annual contributions contract (ACC) dated July 12, 1996 with HUD. The VIHA was placed in receivership and HUD assumed possession of all assets, projects, and programs.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Financial Reporting Entity (continued)**

#### Virgin Islands Housing Authority (continued)

Given the nature of VIHA's operations and the significance of its relationship with the Government, management believes that its exclusion from the financial reporting entity would cause the Government's basic financial statements to be incomplete and misleading. Accordingly, VIHA continues to be reported as a major component unit of the Government even though the Government no longer appoints its commissioners.

#### Virgin Islands Port Authority

The Virgin Islands Port Authority (VIPA) was created as a body corporate and politic constituting a public corporation and autonomous government instrumentality by Act No. 2375 of December 23, 1968, with the purposes of owning, operating, and managing all types of air and marine terminals. The powers of VIPA are exercised by a board of governors consisting of the Commissioner of Economic Development and Agriculture (Chairperson), the Attorney General, the Commissioner of Public Works, the Director of the Small Business Development Agency, and five other persons appointed by the Governor with the advice and consent of the Legislature.

#### Virgin Islands Water and Power Authority

The Virgin Islands Water and Power Authority (WAPA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality by Act No. 1248 of August 13, 1964, with the purpose of operating the water production and electric generation plants in the U.S. Virgin Islands. The powers of WAPA are exercised by a governing board consisting of nine members, all appointed by the Governor with the advice and consent of the Legislature, from which three are heads of cabinet-level executive departments or agencies and six other persons, who shall not be employees of the Government. WAPA is required by its bond resolutions to maintain separate audited financial statements for each system (the Electric and Water Systems).

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Financial Reporting Entity (continued)**

#### Virgin Islands Government Hospital and Health Facilities Corporation

The Virgin Islands Government Hospital and Health Facilities Corporation (VIGHHFC) was created by Act No. 6012 on August 23, 1994 and became active on May 1, 1999. Its purpose is to provide healthcare services and hospital facilities to the people of the U. S. Virgin Islands. The powers of VIGHHFC are exercised by a board of directors consisting of 15 members as follows: the Director of the Office of Management and Budget, the Commissioner of Finance, and 13 other members appointed by the Governor with the advice and consent of the Legislature. The VIGHHFC is composed of the Roy L. Schneider Hospital located in St. Thomas, and the Juan F. Luis Hospital and Medical Center located in St. Croix. Both entities issue separate audited financial statements. The Roy L. Schneider Hospital's financial statements include its component units: the Myra Keating Smith Community Health Center ("Health Center") of St. John, and the Charlotte Kimelman Cancer Institute ("Cancer Institute") on St. Thomas. The Health Center and Cancer Institute are legally separate organizations for which the Hospital is financially accountable. The Cancer Institute was under construction as of the end of the fiscal year.

#### University of the Virgin Islands

The University of the Virgin Islands (the University) was organized as an instrumentality of the Government under Act No. 852 of March 16, 1962, in accordance with Section 16(a) of the Revised Organic Act of 1954, as amended. The purpose of the University is the stimulation and utilization of the intellectual resources of the people of the U.S. Virgin Islands and the development of a center of higher education. The powers of the University are exercised by a board of trustees consisting of 17 members as follows: Chairman of the Board of Education, Commissioner of Education, and the President of the University, all serving as members ex-officio, 9 other members appointed by the Governor with the advice and consent of the Legislature, two other members elected by the board of trustees, one representative of the student body, one alumnus of the University, and another of the teaching faculty. The University was not organized as a self-sustaining entity and therefore receives substantial financial and other support from the Government.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Financial Reporting Entity (continued)**

### University of the Virgin Islands (continued)

The University's financial statements include its component units: The Foundation for the University of the Virgin Islands, The Reichhold Foundation, and the University of the Virgin Islands Research and Technology Park. The Foundation for the University of the Virgin Islands is a not-for-profit corporation whose purpose is to assist and support the University in accomplishing its charitable and educational mission. The Reichhold Foundation is a not-for-profit corporation that supports the arts and provides financial assistance in operating the Reichhold Center for the Arts on St. Thomas. The University of the Virgin Islands Research and Technology Park is a nontaxable public corporation developed to promote economic growth, development, and diversification in the Virgin Islands.

#### Nonmajor Component Units

### Virgin Islands Economic Development Authority

The Virgin Islands Economic Development Authority (EDA) was created by Act No. 6390 of December 21, 2000 as a body corporate and politic constituting a public corporation and semiautonomous instrumentality of the Government. EDA was created as an umbrella authority to assume, integrate, and unify the functions of the Economic Development Commission, the Small Business Development Administration, the Government Development Bank, and the Virgin Islands Industrial Development Park Corporation. The powers of EDA are exercised by a board of directors consisting of the members of the Virgin Islands Economic Development Commission, the Director of the Virgin Islands' Bureau of Internal Revenue, and five members not employed by the Government, but appointed by the Governor with the advice and consent of the Legislature.

#### Magens Bay Authority

Magens Bay Authority (MBA) was created as a corporate instrumentality by Act No. 2085 on December 20, 1967, with the purpose of acquiring, improving, and operating parks and beaches. The powers of MBA are exercised by a board of directors consisting of the Governor and six members initially appointed by the Governor. The board of directors is responsible for the appointment and reappointment of subsequent board members except that the Governor, with the advice and consent of the Legislature may, by appointment, fill any vacancy on the board of directors remaining unfilled for sixty days.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Financial Reporting Entity (continued)**

#### Virgin Islands Housing Finance Authority

The Virgin Islands Housing Finance Authority (VIHFA) was created as a body corporate and politic constituting a public corporation and autonomous governmental instrumentality of the Government by Act No. 4636 of October 20, 1981, with the purpose of stimulating low- and moderate-income housing construction and home ownership through the issuance of revenue bonds to obtain funds to be used for low-interest mortgage loans to qualified purchasers of low- and moderate-income housing. The powers of VIHFA are exercised by a board of directors consisting of the Commissioner of the Department of Housing, Parks, and Recreation (the Chairman), the Director of the Office of Management and Budget, and three persons not employed by the Government appointed by the Governor with advice and consent of the Legislature.

#### Virgin Islands Public Television System

The Virgin Islands Public Television System (PTS) was created as a body corporate and politic constituting a public corporation and autonomous instrumentality by Act No. 2364 on November 15, 1968, with the purpose of advancing the general welfare, education, cultural development, and awareness of public affairs of all the population of the U.S. Virgin Islands and to provide an effective supplement to the in-school education of children. The powers of PTS are exercised by a board of directors consisting of the Commissioner of Education, the Chairman of the Board of Education, three members appointed by the President of the Legislature, and four members, not more than two of whom should be employed by the Government and appointed by the Governor with the advice and consent of the Legislature. In addition, the Director of the Office of Management and Budget, the President of the University of the Virgin Islands, and the General Manager of PTS are ex-officio members of the board who are not entitled to vote.

Notes to Basic Financial Statements (continued)

#### **1.** Summary of Significant Accounting Policies (continued)

#### **Financial Reporting Entity (continued)**

#### Virgin Islands Waste Management Authority

The Virgin Islands Waste Management Authority (VIWMA) was established as a nonprofit, public, autonomous instrumentality of the Government of the Virgin Islands by Act No. 6638, approved by the Governor of the Virgin Islands on January 23, 2004. VIWMA provides environmentally sound management for the collection and disposal of solid waste in the territory, including operation and closure of landfills and wastewater collection, treatment and disposal. VIWMA is governed by a Board of Directors consisting of seven members.

Complete audited financial statements of the discretely presented component units can be obtained directly by contacting their administrative offices:

Administrative Offices

Virgin Islands Housing Authority 402 Estate Anna's Retreat P. O. Box 7668 St. Thomas, VI 00801

Virgin Islands Port Authority PO Box 301707 St. Thomas, VI 00803

Virgin Islands Water and Power Authority PO Box 1450 St. Thomas, VI 00804

Virgin Islands Government Hospital and Health Facilities Corporation 9048 Sugar Estate St. Thomas, VI 00802

University of the Virgin Islands 2 John Brewer's Bay St. Thomas, VI 00802

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Financial Reporting Entity (continued)**

Administrative Offices (continued)

Virgin Islands Economic Development Authority 1050 Norre Gade #5 St. Thomas, VI 00802

Magens Bay Authority PO Box 10583 St. Thomas, VI 00802

Virgin Islands Housing Finance Authority 3202 Demarara Frenchtown Plaza, Suite 200 St. Thomas, VI 00802

Virgin Islands Public Television System PO Box 7879 St. Thomas, VI 00801

Virgin Islands Waste Management Authority #1 La Grande Princesse, Suite BL1 Christiansted, VI 00820

All financial statements of the discretely presented component units have a fiscal year-end of September 30, 2006, except for WAPA and VIHA that have a year-ends of June 30, 2006 and December 31, 2005, respectively.

#### (c) Fiduciary Component Units

The following public benefit corporation is legally separate from the Government, meets the definition of a blended component unit, and is presented in the fund financial statements along with other fiduciary funds of the Government. Fiduciary funds are not reported in the government-wide financial statements.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Financial Reporting Entity (continued)**

#### Employees' Retirement System of the Government of the Virgin Islands

The Employees' Retirement System of the Government of the Virgin Islands (known as GERS) was created as an independent and separate agency of the Government with the purpose of administering the Government's defined-benefit pension plan established on October 1, 1959. Component units of the Government also participate in the cost-sharing, multiple employer defined benefit plan. The responsibility for the operation of GERS is vested in a board of trustees composed of seven members appointed by the Governor with the advice and consent of the Legislature.

Employee and employer contributions to GERS are recognized as additions to net assets held in trust for employees' pension benefits in the period in which employee services are performed, except for contributions pursuant to the Early Retirement Act of 1994, which are recorded as the cash is received. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan, except for benefits pursuant to Sections 8(a) and 8(b) of the Early Retirement Act of 1994, which are recorded when the subsidy provided by the Government is receivable and payable.

Complete audited financial statements of this component unit can be obtained directly by contacting their administrative office:

Employees' Retirement System of the Government of the Virgin Islands 3438 Kronprindsens Gade St. Thomas, VI 00802

#### **Government-wide and Fund Financial Statements**

The government-wide financial statements (that is, the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the PG and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the PG is reported separately from certain legally separate component units for which the PG is financially accountable. The statement of net assets (deficit) presents the reporting entities' nonfiduciary assets and liabilities, with the difference reported as net assets or net deficit.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Government-wide and Fund Financial Statements (continued)**

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

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

#### Measurement Focus, Basis of Accounting, and Financial Statement Presentation

#### (a) Government-wide Financial Statements

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

#### (b) Governmental Fund Financial Statements

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Government considers most revenue to be available if collected within 90 days of the end of the current fiscal year-end. Specifically, gross receipts taxes, property taxes, and income taxes are considered to be available if collected within 30, 60, and 90 days, respectively, after the end of the current

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

# Measurement Focus, Basis of Accounting, and Financial Statement Presentation (continued)

### (b) Governmental Fund Financial Statements (continued)

fiscal year-end. Grant revenue is considered to be available if collected within 12 months after the end of the current fiscal year-end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures are recorded only when payment is due.

Income taxes, gross receipts taxes, real property taxes, and grant funding are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period to the extent they are considered available. All other revenue items are considered to be measurable and available only when cash is received by the Government.

### (c) Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements

The financial statements of the proprietary funds, fiduciary funds, and discretely presented component units are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above.

Each proprietary fund has the option under GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting, to elect and apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless these conflict with a GASB pronouncement. The PG and most blended and discretely presented component units have elected not to apply FASB pronouncements issued after November 30, 1989 for its proprietary fund types. VIPA has elected to follow the FASB's pronouncements issued after November 30, 1989.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Fund Accounting**

The Government reports its financial position and results of operations in funds, which are considered separate accounting entities and discrete presentations of those component units, which are not required to be blended. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions. GASB No. 34, *Basic Financial Statements – and Management's Discussions and Analysis – for State and Local Governments*, establishes criteria (percentage of the assets, liabilities, revenue, or expenditures/expenses of either fund category or the governmental and enterprise funds combined) for the determination of major funds. Indirect costs are automatically allocated and reported in the program expense for each fund. Nonmajor funds are combined in a single column in the fund financial statements. The Government reports the following major funds:

#### (a) Governmental Funds

The Government reports the following major governmental funds:

- <u>General Fund</u> The General Fund is the Government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- <u>PFA Debt Service</u> The PFA Debt Service accounts for the resources accumulated, and payments made, for principal and interest on long-term general obligation debt issued by PFA on behalf of the Government.
- <u>PFA Capital Projects Fund</u> The PFA Capital Projects Fund accounts for bond proceeds of debt issued by the PFA on behalf of the Government. The bond proceeds have been designated for certain necessary public safety and capital development projects which are accounted for in this fund.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### Fund Accounting (continued)

### (b) Proprietary Funds

These funds account for those activities for which the intent of management is to recover, primarily through user charges, the cost of providing goods or services to the general public. The government reports the following major proprietary funds:

- <u>Unemployment Insurance Fund</u> The unemployment insurance fund accounts for the collection of unemployment premiums from employers in the U.S. Virgin Islands, and the payment of unemployment benefits to eligible unemployed recipients.
- <u>West Indian Company</u> WICO, a component unit of PFA, accounts for the activities of a cruise ship pier and shopping mall complex on the island of St. Thomas.

### (c) Fiduciary Funds

Fiduciary funds are used to account for assets held by the Government in a trustee capacity, or as an agent for individuals, private organizations, and other governmental units. The following are the Government's fiduciary funds:

- <u>Pension Trust Fund</u> The pension trust fund accounts for the activities of the Employees' Retirement System of the Government of the Virgin Islands, which accumulates resources for pension benefit payments to qualified employees.
- <u>Agency Fund</u> The agency fund is custodial in nature (assets equal liabilities) and does not involve measurement of the results of operations.

### **Cash and Cash Equivalents**

The Government follows the practice of pooling cash. The balance in the pooled cash accounts is available to meet current operating requirements, and any excess is invested in various interest-bearing accounts and time deposits with eligible depository institutions.

Cash equivalents of the proprietary funds and discretely presented component units consist of demand accounts, money market accounts, certificates of deposit with maturities of not more than 90 days from the date of acquisition, short-term U.S. government and its agencies' obligations and repurchase agreements with a U.S. commercial bank maturing within

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### Cash and Cash Equivalents (continued)

three months and collateralized by U.S. government obligations. Cash and cash equivalents of the discretely presented component units are maintained in separate bank accounts, from those of the PG, in their own names.

#### Investments

The primary Government and its component units follow the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures, an Amendment of GASB Statement No. 3.* GASB Statement No. 40 establishes and modifies disclosure requirements related to investment risks: credit risk (including custodial credit risk and concentrations of credit risk), interest rate risk, and foreign currency risk.

#### **Investment Policies**

Investment policies of the PG, its blended component units, major funds, and major component units are as follows:

- **Primary Government Investment Policies** Title 33, Chapter 117 of the Virgin Islands Code (V.I. Code) authorizes the Government to invest in U.S. Government and agencies obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, and corporate debt and equity obligations. As of September 30, 2006, the PG General Fund, a non-major governmental fund, and an agency Fund had invested in certificates of deposit with a local bank. Investments are reported at fair value.
- **Public Finance Authority Investment Policies** Under GASB Statement No. 31, Accounting and Financial Reporting for Certain Investments and for Most External Investment Pools, investments of the PFA are reported at fair value. Various bond resolutions of the PFA restrict investments to direct obligations of the U.S. Government, territories, possessions and states, specific bank obligations, investment agreements or similar funding agreements, shares or other interests in mutual funds, trusts or investment companies, corporate commercial paper, and money market portfolios consisting of any of the foregoing. The PFA has retained investment managers and investments for two major governmental funds of the Government, the PFA Debt Service Fund, and the PFA Capital Projects Fund.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Investment Policies (continued)**

- **Tobacco Settlement Financing Corporation Investment Policies** Various bond resolutions of this blended component unit restrict investments to direct obligations of the U.S. Government, territories, possessions and states, specific bank obligations, investment agreements or similar funding agreements, shares or other interests in mutual funds, trusts or investment companies, corporate commercial paper, and money market portfolios consisting of any of the foregoing. The Authority has retained investment managers and investments are held in trust by a commercial bank on behalf of the Authority. Investments are reported at fair value in the non-major governmental fund of the Government.
- West Indian Company Limited Investment Policies This blended business-type major fund of the Government maintains an investment policy that 1) limits investments in bonds to a maximum remaining maturity of 30 years (or estimated average life on mortgage-backed issues), 2) limits fixed income securities to a maximum of 40% and a minimum of 30% of the overall assets of the WICO portfolio, 3) limits corporate bond exposure to 45% of the fixed income portfolio, and 4) has no provision which limits or restricts investments in U.S. Government Treasury or Agency issues. WICO reports investments at fair value.
- Pension Trust Fund Investment Policies The board of trustees of the Government retirement system (GERS) have enacted policies that limit investments in certain investment categories and provide requisites for the institutions with which investment transactions may be entered into. Under those policies, GERS may invest in U.S. Government and agencies obligations, bonds or notes of any state, territory or possession of the United States, municipal bonds and obligations, foreign bonds, bonds of domestic railroad corporations, public utility bonds, industrial corporate bonds or trust certificates, common and preferred shares of foreign and domestic corporations, mutual funds, mortgage or personal loans to GERS members or retirees, and mortgage and asset-backed securities. Investments in bonds are subject to rating restrictions of BBB and may not exceed 2% of the portfolio. Investments in stock of a single corporation may not exceed 1% of the market value of the fund, or exceed 1% of the outstanding stock of the corporation. The aggregate amount of investments in stocks may not exceed 60% of the total investments of GERS. Anv investment of 20% or more of the aggregate value of the portfolio must be approved by twothirds of the membership of the board of trustees. The investments are administered by several professional investment managers and are held in trust by a commercial bank on behalf of the system.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Investment Policies (continued)**

Investments in equity securities in the GERS pension trust fund are reported at quoted market values. Shares of mutual funds are reported at the net asset value of shares held by GERS at year-end. Purchases and sales are recorded on a trade-date basis. Realized gains and losses on securities are determined by the average cost method.

Investment by GERS in the Havensight Mall is carried at original purchase price plus appreciated value. Investment by GERS in GERS facilities in St. Thomas and St. Croix are carried at historical cost net of accumulated depreciation and amortization on the portion of the facilities occupied by GERS.

- Virgin Islands Water and Power Authority Investment Policies This major component unit is authorized under bond resolutions and the V.I. Code to invest in open accounts, time deposits, certificates of deposit, repurchase agreements, obligations of the United Stated government, and obligations of any state within the United States, mutual funds, and corporate commercial paper. Investments are reported at fair value.
- *Virgin Islands Port Authority Investment Policies* This major component unit is authorized under bond resolutions and the V.I. Code to invest in open accounts, time deposits, certificates of deposit, repurchase agreements, obligations of the United Stated government, and obligations of any state within the United States, mutual funds, and corporate commercial paper. Investments are reported at fair value.
- University of the Virgin Islands Investment Policies The board of trustees of this major component unit is responsible for the management of the University's investments which consist of U.S. Government securities and securities backed by the U.S. Government or its agencies and instrumentalities, common and preferred stocks, and mutual funds. Currently, the University's policies do not address risks associated with investments.
- Virgin Islands Government Hospital and Health Facilities Corporation Investment Policies – The board of trustees of this major component unit have not developed a formal investment policy. At September 30, 2006, investments were comprised of certificates of deposit which were reported at fair value.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Investment Policies (continued)**

• Virgin Islands Housing Authority Investment Policies – This major component unit is required by the U.S. Department of Housing and Urban Development ("HUD") to invest excess funds in obligations of the United States, certificates of deposit, or any other federally insured investment. HUD requires that deposits be fully collateralized at all times, and may be held by an unaffiliated bank or trust company for the account of the VIHA.

### Receivables

Taxes receivable represent amounts owed by taxpayers for individual and corporate income taxes, gross receipts taxes and real property taxes. Tax revenue is recognized in the governmental fund financial statements when they become both measurable and available based on actual collections during the months subsequent to the fiscal year end.

Federal government receivables represent amounts owed to the Government for reimbursement of expenditures incurred pursuant to federally funded programs.

Accounts receivable are reported net of estimated allowances for uncollectible amounts, which are determined based upon past collection experience and current economic conditions.

Subject to the provisions of the retirement law and subject to rules and regulations prescribed by the board of trustees of GERS, participants of the Pension Trust Fund have the right of obtaining loans from the Pension Trust Fund to finance a home, automobile, or other personal needs. The maximum mortgage loan that could be granted to members who have been contributing to the Pension Trust Fund for at least five years is \$250,000. The interest rate on new first mortgages was 8% and on second mortgages, 9% throughout the year. Members may also borrow up to \$50,000 to buy land.

Members who have contributed to the Pension Trust Fund for at least five years can borrow up to \$18,000 for the purchase of an automobile. The loans bear interest at 11% with a maximum term of four years. A member may also borrow up to 75% of their contributions to the Pension Trust Fund to a maximum borrowing of \$20,000 as a personal loan. The interest rate offered on personal loans was 9% throughout the year.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Receivables (continued)**

Member loans in the pension trust fund are valued at the outstanding loan principal balance less an allowance for estimated loan losses.

The accounts receivable from nongovernmental customers of the discretely presented component units are net of estimated uncollectible amounts. These receivables arise primarily from service charges to users. Accounts receivable from the PG and other component units that arise from service charges do not have significant allowances for uncollectible accounts.

### Inventories

In governmental fund types, the costs of inventories are recorded as expenditures when purchased. The proprietary fund types and component units recognize an asset when the inventory is purchased and an expense when it is consumed. Inventories in proprietary fund types are primarily valued at the lower of cost or market using the first-in, first-out method.

#### **Restricted Assets**

Restricted assets in the PG and discretely presented component units are set aside primarily for the payment of bonds, notes, construction funds, and other specific purposes.

### **Capital Assets**

Capital assets, which include land, land improvements, buildings, building improvements, machinery and equipment, construction in progress, and infrastructure assets are reported in the applicable governmental, business-type activities, and component unit columns in the government-wide financial statements as well as in the applicable proprietary funds reported in the fund financial statements.

The PG defines capital assets as assets that have an initial, individual cost and useful lives of: (i) \$5,000 for personal property with a useful life of five years; (ii) \$50,000 for buildings and building improvements with estimated useful lives of 40 and 20 years, respectively; (iii) \$100,000 for land improvements; and (iv) \$200,000 for infrastructure with an estimated useful life of 30 years. The value of all land acquired is capitalized.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Capital Assets (continued)**

Capital assets purchased or acquired are carried at historical cost or normal cost. The normal costing method to estimate cost based on replacement cost indexed by a reciprocal factor of the price increase from the appraisal date to the actual or estimated acquisition date was used to estimate the historical cost of certain land, buildings, and building improvements because invoices and similar documentation was no longer available in certain instances. Donated capital assets are recorded at fair value at the time of donation. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest costs are capitalized during the construction period only for business-type activities and various component units. The costs of routine maintenance and repairs that do not add value to the assets or materially extend asset lives are expensed as incurred.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements, as well as the proprietary funds and component units' financial statements.

Capital assets of the PG, excluding land and construction in progress, are depreciated on the straight-line method over the assets' estimated useful lives.

The capital assets of the component units are recorded in accordance with the applicable GASB and FASB statements and under their own individual capitalization thresholds. The estimated useful lives of capital assets reported by the component units are (i) 7 to 50 years for buildings and building improvements; (ii) 20 to 40 years for airports and marine terminals; and (iii) 3 to 20 years for vehicles and equipment.

### **Tax Refunds Payable**

During the calendar year, the Government collects individual income taxes through withholdings and payments from taxpayers. At September 30, the Government estimates the amount owed to taxpayers for overpayments during the first nine months of the calendar year. These estimated amounts and the actual tax refunds claimed for prior years but not paid at year-end are recorded as tax refunds payable and as a reduction of tax revenue.

Notes to Basic Financial Statements (continued)

### **1.** Summary of Significant Accounting Policies (continued)

#### **Deferred and Unearned Revenue**

Deferred revenue at the governmental fund level arises when potential revenue neither meets measurable nor available criteria for revenue recognition in the current period. Deferred revenue also arises when resources are received before the Government has a legal claim to them, as when grant moneys are received prior to incurring the qualifying expenditures. In subsequent periods, when the revenue recognition criteria is met, or when the Government has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet and the revenue is recognized. Unearned revenue at the government-wide and proprietary fund levels arises only when the Government receives resources before it has a legal claim to them.

#### Long-term Debt

The liabilities reported in the government-wide financial statements include the Government's bonds, long-term notes, and other long-term liabilities including vacation, retroactive union arbitration salaries, and legal claims. Bond premiums and discounts, losses incurred on bond refundings, and debt issuance costs are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premiums or discounts and deferred refunding losses.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Losses incurred on bond refundings are not recognized in the fund financial statements as the corresponding liability for the bonds is only recorded in the government-wide financial statements. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Fund Equity**

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

### Net Assets

Net assets are reported in three categories:

- *Invested in Capital Assets, Net of Related Debt* These consist of capital assets, net of accumulated depreciation and amortization, and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets. Debt pertaining to significant unspent debt proceeds is not included in the calculation of invested in capital assets, net of related debt. The unspent portion of the debt is presented, net of the related debt, as restricted net assets for capital projects.
- *Restricted Net Assets* These result when constraints placed on net assets, use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- Unrestricted Net Assets These consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

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

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Postemployment Benefits**

In addition to the pension benefits described in Note 13, the Government provides postretirement healthcare benefits, in accordance with the V.I. Code to all employees who retire from the Government on or after attaining age 55 with at least 30 years of service; except for policemen and firemen who can retire with at least 20 years of service. Currently, approximately 4,100 retirees meet those eligibility requirements. Healthcare benefits are provided through insurance companies whose premiums are paid by the retiree and the Government. The Government contributes three-fourths of the healthcare benefits' premiums. The Government does not accrue a liability for postemployment benefit costs, which are recognized on a pay-as-you-go basis. During the year ended September 30, 2006, the cost of providing postretirement healthcare benefits amounted to approximately \$13.4 million.

#### **Compensated Absences**

The vacation policy of the Government provides for the accumulation of four, six, or eight hours for each full biweekly pay period depending on the time of entry into government service. At the beginning of each calendar year, vacation leave is limited to 480 hours (60 days). However, the excess of 480 hours is considered by GERS for service credit towards the employees' retirement. This vacation policy does not apply to professional educational personnel of the Virgin Islands Department of Education, who receive compensation during the school breaks. Upon retirement, an employee receives compensation for unused vacation leave at the employee's base pay rate. Accrued compensated absences, including related benefits, are included in other liabilities in the government-wide financial statements.

Employees accumulate sick leave at a rate of four hours for each full biweekly pay period up to a maximum of 180 days. Separated employees do not receive payment for unused sick leave, therefore, a provision for accumulated sick leave is not required.

Compensated absences accumulation policies for the blended component units and discretely presented component units vary from entity to entity, depending upon negotiated bargaining agreements and other factors agreed upon between the management of these entities and their employees.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

### **Interfund and Intra-entity Transactions**

The Government has the following types of transactions among funds:

- *Interfund Transfers* Legally required transfers are reported as interfund transfers in (out) when incurred.
- *Intra-entity Transactions* These are transactions between the PG and its component units, and among the component units. Transfers between the PG and its blended component units are reported as interfund transfers, except for transfers within the same fund type. Similarly, receivables and payables between the PG and its blended component units are reported as amounts due to, and due from other funds. Transfers between the PG and discretely presented component units (and among those component units) are reported separately as revenue and expenses or expenditures. Amounts owed to and from discretely presented component units by the PG are reported separately from interfund payables and receivables.

#### **Risk Management**

With some exceptions, the Government does not carry general casualty or liability insurance coverage on its properties or the acts of its employees, relying instead on self-insurance and/or statutory liability limitations. However, as a result of an agreement with the Federal Emergency Management Agency (FEMA), with respect to properties and structures damaged by Hurricane Hugo and repaired with federal disaster assistance funds, the Government has obtained insurance for certain hospitals, schools, and other insurable public buildings that were repaired with such federal assistance. The Government purchases commercial insurance covering physical losses or damages against its property. The limit of liability for all risks, excluding earthquake, windstorm, and flood, is \$1 million for each and every occurrence except for windstorm and flood losses, which has a \$45 million limit. For physical losses arising from earthquake, the insurance policy has a limit of \$100 million for each and every occurrence and in the annual aggregate. Also, the Government has an enterprise fund that provides workers' compensation to both public and private employees.

The Government does not maintain accounting records in support of individual claim liabilities or for claims incurred but not reported (IBNR). Accordingly, workers' compensation claims are accounted for on a cash basis. Therefore, the basic financial statements do not include a liability for workers' compensation claims outstanding, including related IBNR, as of September 30, 2006.

Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Risk Management (continued)**

Certain component units are exposed to various risks of loss related to their specialized operations, which are mitigated by purchasing commercial insurance.

### **Future Adoption of Accounting Requirements**

GASB has issued the following statements that the Government or its component units have not yet adopted:

GASB Statement Number	_	Adoption Required in Fiscal Year
43	Financial Reporting for Postemployment Benefit Plans Other than Pension Plans	2007
45	Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions	2008
48	Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues	2008
49	Accounting and Financial Reporting for Pollution Remediation Obligations	2009
50	Pension Disclosures - an amendment of GASB	
	Statements No. 25 and No. 27	2008
51	Accounting and Financial Reporting for Intangible Assets	2010
52	Land and Other Real Estate Held as Investments by Endowments	2009

The impact of these statements has not yet been determined.

### Notes to Basic Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### **Use of Estimates**

Management of the Government has made a number of estimates and assumptions relating to the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

#### 2. Component Units

The basic financial statements include the financial statements of the following discretely presented component units:

- Virgin Islands Housing Authority
- Virgin Islands Port Authority
- Virgin Islands Water and Power Authority
- Virgin Islands Government Hospital and Health Facilities Corporation
- University of the Virgin Islands
- Economic Development Authority
- Magens' Bay Authority
- Virgin Islands Housing Finance Authority
- Virgin Islands Public Television System
- Waste Management Authority

### Notes to Basic Financial Statements (continued)

### **2.** Component Units (continued)

Condensed financial information of all discretely presented component units follows (expressed in thousands):

	Virgin	Virgin	Virgin Isla and Power		Hospital	nds Governme and Health Corporation	nt		
Inform ation on net assets	Islands Housing Authority	Islands Port Authority	Electric System	W ater System	Roy L. Schneider Hospital	Juan F. Luis Hospital	University of the Virgin Island	Other Component s Units	Total Component Units
Assets: Current assets Due from primary	\$ 9,322	\$ 19,114	\$ 80,420	\$ 17,802	\$ 21,287	\$ 10,739	\$ 57,682	\$ 20,707	\$ 237,073
government Due from federal government Restricted assets Capital assets, net Deferred expenses	798 88 63,849	3,016 2,037 8,808 270,776 1,562	51,696 202,289 13,271	- 8,956 48,570 926	 79,492 	1,000 29,599	754 4,009 29,229 44,517 1,467	712 15,759 56,673	4,482 7,844 114,536 795,765 17,226
Totalassets	74,057	305,313	347,676	76,254	100,779	41,338	137,658	93,851	1,176,926
Liabilities: Current liabilities Due to primary government Due to federal government Bonds payable	3,465 2,082	9,097  41,778	63,838 5,300 155,534	4,404 31,622	22,610 8,933 	23,538 20,520 	14,303 - 43,238	3,265 4,306 4,645	1 44,52 0 33,75 9 7,38 2 2 76,81 7
Loans payable Other noncurrent liabilities	3,683	1,460	16,600		875		1,681 45	1,834 25,079	21,575 29,682
To tal liabilities	9,230	52,335	241,272	36,026	32,418	44,058	59,267	39,129	513,735
Net assets: Invested in capital assets – net of related debt Restricted Unrestricted (deficit)	63,848  979	228,998 8,808 15,172	73,613 18,479 14,312	17,621 8,198 14,409	78,114 1,168 (10,921)	29,575 (32,295)	21,941 48,155 8,295	46,563 7,727 432	560,273 92,535 10,383
Total net assets	\$ 64,827	\$ 252,978	\$ 106,404	\$ 40,228	\$ 68,361	\$ (2,720)	\$ 78,391	\$ 54,722	\$ 663,191

### Notes to Basic Financial Statements (continued)

#### 2. Component Units (continued)

		Program revenue								
Information on statements of activities		Expenses		Charges for Services		Operating Grants and Contributions		Capital ants and atributions	Total Component Units	
Virgin Islands Housing Authority Virgin Islands Port Authority Virgin Islands Water and	\$	41,691 51,306	\$	5,634 39,279	\$	30,371	\$	2,796	\$	(5,686) (9,231)
Power Authority: Electric System Water System		203,262 35,884		205,041 33,723		-		-		1,779 (2,161)
Virgin Island's Government Hospital and Health Facilities Corporation:										
Roy L. Schneider Hospital		80,649		47,070		25,125		4,496		(3,958)
Juan F. Luis Hospital		61,916		28,980		23,871		2,674		(6,391)
University of the Virgin Islands Other component units	_	67,363 19,168		14,953 5,273	_	43,847 11,499		3,192 6,442		(5,371) 4,046
Total activities	\$	561,239	\$	379,953	\$	134,713	\$	19,600		(26,973)
General revenue: Interest and other										11,170
Changes in net assets										(15,803)
Net assets at beginning of year										678,994
Net assets at end of year									\$	663,191

#### 3. Stewardship, Compliance, and Accountability

#### **Budgetary Process and Control**

The V.I. Code requires the Governor to submit an annual balanced executive budget to be adopted by the Legislature for the ensuing fiscal year. The Governor is required by law to submit to the Legislature the annual executive budget no later than May 30. The annual executive budget is prepared essentially on a GAAP basis, except for encumbrances, which are reported as expenditures for budget reporting purposes, by the Virgin Islands Office of Management and Budget (OMB) working in conjunction with other Government offices and agencies. If the annual executive budget has not been approved before the commencement of any fiscal year, then the appropriations for the preceding fiscal year, insofar as they may be applicable, are automatically deemed reappropriated item by item. The annual executive budget, which includes those funds of the Government subject to appropriation pursuant to law, is composed of all

Notes to Basic Financial Statements (continued)

### 3. Stewardship, Compliance, and Accountability (continued)

#### **Budgetary Process and Control (continued)**

proposed expenditures and estimated revenue for the Government. The Legislature enacts the annual executive budget through passage of lump-sum appropriations for each department. The Legislature may add, change, or delete any items in the annual executive budget proposed by the Governor. Upon passage by the Legislature, the annual executive budget is submitted to the Governor, who may veto the budget partially or in its entirety and return it to the Legislature with his objections. A veto by the Governor can be overridden only by a two-third majority of all members of the Legislature. The Legislature is obligated by law to pass a final annual executive budget no later than September 30, the last day of the fiscal year. Supplemental budgetary appropriations' bills that are signed into law may be created during the year without the identification of a specific revenue source to finance them. In August 1999, the Legislature enacted the Financial Accountability Act (Act No. 6289). The purpose of the Financial Accountability Act is to require by law that the budget of the Government be balanced each year, and the appropriations in each fiscal year not exceed a verifiable revenue source.

Once the budget has been enacted, fiscal control over expenditures made pursuant thereto is exercised by the Governor through the Director of OMB. During any fiscal year in which the resources available to the Government are not sufficient to cover the appropriations approved for such year, the Governor, through the Director of OMB, may take administrative measures to reduce expenditures. The Governor may also make recommendations to the Legislature for new taxes or any other necessary action to meet the estimated deficiency.

Budgetary control is exercised at the department level through an allotment process. Encumbrances and expenditures cannot exceed total allotment amounts. The Government's department heads may make transfers of appropriations within the department. Appropriation transfers between departments and supplemental appropriations require executive and legislative branch approval. Unencumbered and unexpended appropriations, not designated, lapse at fiscal year-end. Also, encumbrances are established at fiscal year-end to pay certain expenditures for travel and utility costs payable against current year appropriation authority, but to be expended in the subsequent year.

Notes to Basic Financial Statements (continued)

### 3. Stewardship, Compliance, and Accountability (continued)

### **Budget/GAAP Reconciliation**

The following schedule presents a comparison of the General Fund legally adopted budget with actual data on a budgetary basis. Because accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of timing and entity difference in the excess of revenue and other financing sources over expenditures and other financing uses for the year ended September 30, 2006 is presented below (expressed in thousands):

Excess of revenue and other financing sources (uses)		
over expenditures – budget basis	\$	96,613
Timing difference – change in encumbrances		(6,461)
Entity difference – excess of revenue and other financing sources over expenditures and other financing uses – activities with budgets not		
legally adopted		20,636
Excess of revenue and other financing sources	*	
over expenditures – GAAP basis	\$	110,788

Controls over spending in special revenue funds and nonappropriated funds are maintained at the Department of Finance by use of budgets and available resources (revenue). The Government makes appropriations to authorize expenditures for various capital projects. Budgets for capital projects normally remain available until completion of the project unless modified or rescinded.

### 4. Cash and Cash Equivalents

#### **Primary Government**

The PG and its blended component units consider all highly liquid investments purchased with an initial maturity of three months or less to be cash and cash equivalents. By law, banks, or trust companies designated as depository of public funds of the Government are to maintain corporate surety bond or pledge collateral satisfactory to the Commissioner of Finance to secure all governmental funds deposited.

### Notes to Basic Financial Statements (continued)

### 4. Cash and Cash Equivalents (continued)

#### **Primary Government (continued)**

At September 30, 2006, the PG held \$184.2 million in unrestricted cash and cash equivalents, and \$32.4 million in restricted cash and cash equivalents. Banco Popular de Puerto Rico held \$121 million, or 56% of the PG's cash and cash equivalents, and First Bank held \$89 million, or 41% of the PG's cash and cash equivalents. All of the PG's bank balances were fully collateralized.

#### **Pension Trust Fund**

The Government's retirement system (GERS) considers all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents. At September 30, 2006, GERS held \$80.0 million in money market accounts, and \$3.4 million in operational accounts.

#### **Component Units**

All component units of the Government consider all highly liquid investments purchased with an initial maturity of three months or less to be cash and cash equivalents. By law, banks or trust companies designated as a depository of public funds of the Government are to maintain corporate surety bond or pledge collateral satisfactory to secure all governmental funds deposited.

At September 30, 2006, component units held \$59.1 million in unrestricted cash and cash equivalents and \$41.8 million in restricted cash and cash equivalents, of which \$3 million was not insured, bonded or collateralized as required for public funds of the Government.

#### 5. Investments

#### **Primary Government Investments**

The PG and its component units have adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures, an Amendment of GASB Statement No. 3.* Following is a summary of the investments of the PG, categorized by investment type and maturity as of September 30, 2006:

Notes to Basic Financial Statements (continued)

#### **5.** Investments (continued)

#### **Primary Government Investments (continued)**

#### **Primary Government Investments**

(in thousands)

(	,	Ma	turity	(in ye	ears)		
	Fair	Less Than			0	ver 5	
	Value	1 Year			Y	ears	
Investments with contractual maturities							
Certificates of Deposit	\$ 240,498	\$ 240,498	\$	-	\$	_	
Portfolio Investments							
Commercial Paper	208,570	208,227		-		343	
Corporate Bonds	203	-		203		_	
U.S. Government Agencies and Notes	2,580	1,908		611		61	
Total investments with maturities	451,851	\$ 450,633	\$	814	\$	404	
Investments without contractual maturities							
Money Market and Mutual Funds	151,952						
Total Primary Government Investments	\$ 603,803						

*Interest Rate Risk.* Interest rate risk represents the exposure to fair market value losses arising from increasing interest rates. The PG does not have a formal investment policy that limits investment maturities as a means of managing such exposure. As a means of keeping the interest rate risk low, all investments held by the PG are short term in nature.

*Credit Risk.* The authorizing legislation of the PG does not limit investments by credit rating categories. Authorizing legislation does limit the investment choices of the PG to: direct obligations or obligations guaranteed by the United States, obligations of states, territories, possessions and commonwealths of the United States, obligations of international banking institutions, repurchase agreements, investment contracts, certificates of deposit, guaranteed investment contracts, shares in mutual funds, investment companies, corporate commercial paper, money market portfolio investments and investment pools.

Notes to Basic Financial Statements (continued)

### **5.** Investments (continued)

### **Primary Government Investments (continued)**

At September 30, 2006, the PG's investments in money market funds were rated AAAm by Standard & Poor's, and Aaa by Moody's Investor Service; PG's investment in commercial paper were rated A-1 or A-1+ by Standard & Poor's, and P-1 by Moody's Investor Services; and the PG's investment in U.S. government agencies were rated AAA by Standard & Poor's and Aaa by Moody's Investor Services.

*Concentration of Credit Risk.* The PG places no limit on the amount that may be invested in one issuer. At September 30, 2006, more than 5% of the PG's investments were invested in: Banco Popular de Puerto Rico Certificates of Deposit (26.03%), First Bank Certificates of Deposit (13.80%), General Electric Capital Corporation Commercial Paper (12.64%), Fidelity Treasury Money Market #696, Class 3 (12.34%), Morgan Stanley Dean Witter Commercial Paper (6.85%) and Goldman Financial Securities Money Market #474 (5.76%).

*Custodial Credit Risk.* The PG does not have a custodial risk policy. This is the risk that the PG will not be able to recover the value of its investments that are in the possession of an outside party. At September 30, 2006, \$362.3 million of investments were held in the name of The Bank of New York Trust Company, N.A, as trustee for the Government, and \$1 million were held in the name of Merrill Lynch, as trustee for the Government.

Notes to Basic Financial Statements (continued)

### **5.** Investments (continued)

#### **Pension Trust Fund Investments**

The pension trust fund (GERS) has implemented GASB Statement No. 40 by establishing separate investment guidelines and restrictions for each investment manager. Following is a summary of pension trust fund investments as of September 30, 2006:

#### **Pension Trust Fund Investments**

(in thousands)

		(in mousund	Maturity (in years)							
	Fair		Le	ess Than		1 to 5	(	6 to 10	Μ	ore Than
		Value	1	1 Year		Years		Years	1	0 Years
Investments with contractual maturities										
US government and agency obligations	\$	27,430	\$	_	\$	26,169	\$	1,261	\$	_
US Treasury notes	Ψ	61,474	Ψ	_	Ψ	52,717	Ψ	8,757	Ψ	_
US Treasury bonds		50,957		_				7,348		43,609
Corporate obligations		39,880		3,420		18,780		14,018		3,662
Foreign bonds		12,068		2,262				9,806		
Government obligations - foreign		57,820		11,653		30,214		15,953		_
Mortgage and asset backed securities		121,985		, 		2,749		1,774		117,462
Total Investments with maturities		371,614	\$	17,335	\$	130,629	\$	58,917	\$	164,733
<b>Investments without contractual maturities</b> Equity Securities Common stocks - U.S.	1	641,597								
Common stocks - foreign		123,337								
Preferred stocks - foreign		1,405								
Real Estate Investments										
Real estate investment trusts		1,348								
Havensight Mall - US Virgin Islands		60,513								
GERS Complex - US Virgin Islands		18,561								
Limited partnership		51,000								
Foreign currency exchange contract		184								
Securities lending short-term collateral										
investment pool		271,162								
Mutual funds		3,061								
Total pension fund investments	\$	1,543,782								

Notes to Basic Financial Statements (continued)

#### 5. Investments (continued)

#### Pension Trust Fund Investments (continued)

*Interest Rate Risk.* Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. GERS does not have a specific policy to manage interest rate risk, but requires investment managers to diversify by issue, maturity, sector, coupon, and geography. Investment managers retained by GERS follow specific investment guidelines and are evaluated against specific marker benchmarks that represent their investment style. Any exception from general guidelines requires approval from the GERS's board of trustees.

*Credit Risk.* GERS investment policy is designed to minimize credit risk by restricting authorized investments to only those investments permitted by statute, subject to certain additional limitations. These additional limitations consist of prohibitions against investments in derivative securities, options, futures or short positions. GERS investment policy allows investments in mortgage pass-through securities. The credit ratings of GERS debt and equity securities include:

Pension Trust Fund Investment Credit Ratings

(in thousands)				
			Credit	Ratings
		-	Standard &	
	Fair	Value	Poor	Moody's
US government and agency obligations	\$	27,430	AAA	ААА
US Treasury notes		61,474	AAA	AAA
US Treasury bonds	:	50,957	AAA	AAA
Corporate obligations		39,880	BBB- to AAA	BAA1 to AAA
Foreign bonds		2,262	AA	AA2
Foreign bonds		9,806	AAA	AAA
Government obligations - foreign		10,577	AA-	AA2
Government obligations - foreign		33,074	AAA	AAA
Government obligations - foreign		13,092	AAA	Not Rated
Government obligations - foreign		1,077	Not Rated	Not Rated
Mortgage and asset backed securities		671	A-	A3
Mortgage and asset backed securities	1	10,773	AAA	AAA
Mortgage and asset backed securities		10,541	Not Rated	Not Rated
Common stocks- US	6	41,597	Not Rated	Not Rated
Common stocks - foreign	1	23,337	Not Rated	Not Rated
Preferred stocks - foreign		1,405	Not Rated	Not Rated
Real estate investment trust		1,348	Not Rated	Not Rated
Real estate holdings - US Virgin Islands		79,074	Not Rated	Not Rated
Limited partnership	:	51,000	Not Rated	Not Rated
Foreign currency exchange contract		184	Not Rated	Not Rated
Securities lending short-term collateral				
investment pool	2	71,162	Not Rated	Not Rated
Mutual funds		3,061	Not Rated	Not Rated
Total investments	\$ 1,5	43,782		

Notes to Basic Financial Statements (continued)

### **5. Investments (continued)**

#### **Pension Trust Fund Investments (continued)**

*Concentration of Credit Risk.* Concentration of credit risk is the risk of loss attributed to the magnitude of the GERS investment in a single issuer of securities. GERS investment policies place limitations on portfolio composition by investment type to limit its exposure to concentration of credit risk. The investment policy provides that a minimum of 60% of GERS investment portfolio be invested in equity stocks and a minimum of 40% be invested in fixed income investments. At September 30, 2006, there were no investments in any one issuer that represent 5% or more of total investments.

*Custodial Credit Risk.* The custodial credit risk for investments is the risk that, in the event of the failure of a counterparty to a transaction, GERS will not be able to recover the value of an investment or collateral securities that are in the possession of an outside party. With the exception of underlying securities on loan secured by non-cash collateral, the entire investment portfolio of GERS was held with a single third-party custodian on behalf of GERS as of September 30, 2006. The fair value of underlying securities on loan secured by non-cash collateral amounted to \$7.0 million at September 30, 2006.

*Foreign Currency Risk.* Foreign currency risk is the risk of holding investments in foreign currencies and the risk that those foreign currencies may devalue. As of September 30, 2006, \$195.0 million of GERS portfolio was held in foreign currencies, with \$57.0 million held in Euro currency, \$51.2 million held in Japanese yen, \$29.4 million held in pound sterling, \$13.1 million held in Australian dollars, \$12.4 million held in Swiss francs and \$3.0 million held in Canadian dollars. GERS entered into various forward currency exchange contracts to manage exposure to changes in foreign currency exchange rates, and to facilitate the settlement of foreign security transactions. Risks associated with foreign exchange contracts include the movement in the value of foreign currency relative to the U.S. dollar and the ability of the counterparty to perform in accordance with the terms of the contract. Changes in the market value of open and closed forward contracts are reported with interest, dividends, and other income or losses reported at fair value. During the fiscal year ended September 30, 2006, GERS reported \$17.3 million in forward currency purchases, \$17.1 million in forward currency sales, and a foreign exchange loss of \$27 thousand.

#### Notes to Basic Financial Statements (continued)

#### **5.** Investments (continued)

#### **Pension Trust Fund Investments (continued)**

Securities Lending Transactions. The Government's statutes permit GERS to participate in securities lending transactions, and GERS has, via a securities lending authorization agreement (the Agreement), authorized State Street Bank and Trust Company (the Custodian) to lend its securities to broker-dealers and banks pursuant to a form of loan agreement. Lent securities are collateralized with cash, securities issued or guaranteed by the U.S. government, or irrevocable bank letters of credit. GERS does not have the ability to pledge or sell collateral securities delivered absent a borrower default. No restrictions were imposed during 2006 as to the amount of loans the Custodian can make on behalf of the GERS. Under the terms of the Agreement the Custodian must indemnify the Government for losses attributable to violations by the Custodian under the "standard of care" clause described in the Agreement. There were neither such violations during the fiscal year 2006 nor losses resulting from the default of the borrowers or the Custodian.

Loans are generally terminable on demand. The collateral received shall, in the case of loaned securities denominated in U.S. dollars or whose primary trading market is located in the U.S. or sovereign debt issued by foreign governments, have a market value of 102% of the market value of the security for domestic borrowers and 105% for foreign borrowers at the inception of the securities lending transaction. Such collateral should be kept at a minimum of 100% of the market value of the security for all borrowers throughout the outstanding period of the transaction. At September 30, 2006, approximately \$270.5 million of U.S. government and agency securities, fixed income, and equity corporate securities were on loan. The cash collateral received with a corresponding liability of an equal amount, is recorded in the statement of fiduciary net assets. The cash collateral received on each loan was invested, together with the cash collateral of other lenders, in a collective investment pool. As of September 30, 2006, such investment pool had a weighted average maturity of 49 days and an average expected maturity of 428 days. Because the loans were terminable at will, their duration did not generally match the duration of the investments made with cash collateral.

Notes to Basic Financial Statements (continued)

#### **5.** Investments (continued)

#### **Component Unit Investments**

Following is a summary of component unit investments, and maturities, as of September 30, 2006:

			Maturity (in years)							
	Fair		Less Than		1 to 5		6 to 10		Over 10	
		Value	_1	Year		Years	Y	ears		Years
Investments with contractual maturities										
Certificates of Deposit	\$	3,096	\$	3,096	\$	_	\$	_	\$	_
Mortgage backed securites		4,251		_		_		_		4,251
Corporate Bonds		5,467		_		_		_		5,467
U.S. Government Agencies & Notes		37,397		226		35,509		761		901
Investments with contractual maturities:		50,211	\$	3,322	\$	35,509	\$	761	\$	10,619
Investments without contractual maturities:										
Common stock		9,604								
Foreign investments		87								
Mutual funds		33,422								
Investment contracts		18,693								
Other investments		916								
Total component unit investments	\$	112,933								

## **Component Unit Investments**

(in thousands)

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The component units of the Government have not established formal policies which limit investment maturities as a means of managing such exposure and have some exposure to interest rate risk.

*Credit Risk.* The authorizing legislation of the component units does not limit investments by credit rating categories. Authorizing legislation limits the investment choices of the component units, as described in Note 1(g). The WAPA Electric System investments include an \$18.7 million guaranteed investment contract with the Royal Bank of Canada. The investment contract is rated Aa3 by Moody's and AA- by Standard & Poor's. The University of the Virgin Islands investments include corporate bonds amounting to \$2.5 million with a rating of A-AAA by Standard & Poor's.

Notes to Basic Financial Statements (continued)

### **5. Investments (continued)**

#### **Component Unit Investments (continued)**

*Concentration of Credit Risk.* The component units have no limits on the amount that may be invested in one issuer of securities. As of the fiscal year-end, the component units reported \$37.4 million in U.S. Government and agency securities issued or explicitly guaranteed by the U.S. government, and \$33.4 million in mutual funds which are excluded from concentration of credit risk. As of June 30, 2006, WAPA Electric held a guaranteed investment contract with the Royal Bank of Canada in the amount of \$18.7 million which represented 16.6% of component unit investments.

*Custodial Credit Risk.* The component units of the Government do not have custodial credit risk policies. This is the risk that the component unit will not be able to recover the value of its investments that are held in the possession of an outside party. At September 30, 2006, \$2.3 million of investments held by VIPA were held in the name of HSBC Bank USA as trustee and \$13.4 million of mutual funds held by the University of the Virgin Islands were held on behalf of the university.

#### 6. Receivables

#### **Primary Government Receivables**

Receivables for governmental funds at September 30, 2006 consist of the following (expressed in thousands):

	 General Fund	 FA Debt vice Fund	Total		
Income taxes Real property taxes Gross receipts taxes Tax receivables	\$ 230,980 57,823 	\$ 	\$	230,980 57,823 74,210 363,013	
Less allowance for doubtful accounts	 (53,821)	 (46,830)		(100,651)	
Net tax receivables Other long-term receivables – tobacco settlement rights	\$ 234,982	\$ 27,380		262,362 784	
Total receivables reported in the statement of net assets			\$	263,146	

### Notes to Basic Financial Statements (continued)

#### 6. Receivables (continued)

#### **Primary Government Receivables (continued)**

The Naval Appropriations Act created a separate tax structure for the U.S. Virgin Islands that mirrors the Internal Revenue Code of 1986, as amended. Income taxes are due from every corporation, partnership, individual, association, estate, or trust that meets the filing requirements of the U.S. Internal Revenue Code. A U.S. taxpayer who is a permanent resident of the U.S. Virgin Islands satisfies his Virgin Islands income tax obligations by filing his return with and paying income taxes to the Government. Virgin Islands residents are taxed by the Virgin Islands on their world-wide income. A nonresident of the U.S. Virgin Islands pays income taxes on his U.S. Virgin Islands source income to the Government. The revenue is recognized in the General Fund in the fiscal period for which the income tax return was filed. The revenue from income tax withholding and estimated payments are recognized in the General Fund as collected, net of estimated tax refunds.

Corporate income taxes are due by the 15th day of the third month following the close of the fiscal year and become delinquent if not paid on or before the due date.

Partnership and trust income taxes are due by April 15 of the following year for which the income tax was levied. Trust income taxes must be paid by the tax filing date.

Property taxes are levied each calendar year on all taxable real property located in the U.S. Virgin Islands. The revenue is recognized in the General Fund and in the fiscal period for which the property tax was levied, provided the tax is collected within 60 days subsequent to fiscal year-end, unless the facts justify a period greater than 60 days.

The Office of the Tax Assessor is responsible for the assessment of all taxable real property. Noncommercial real property subject to taxation is reassessed once every five years and commercial real property subject to taxation is reassessed biannually. The Tax Assessor prepares an annual assessment roll and schedule of collections for each parcel of real property that is used by the Department of Finance, as the basis for issuing tax bills to all taxpayers in the U.S. Virgin Islands.

Property taxes are levied by May 15 of each year in the name of the record owner on January 15 of the same year. The taxes are due on September 30 and become delinquent if not paid by October 30.

Notes to Basic Financial Statements (continued)

### 6. Receivables (continued)

### **Primary Government Receivables (continued)**

For businesses with gross receipts of \$120,000 per annum or less, gross receipts taxes are levied on an annual basis, based on 4% of gross receipts in excess of \$5,000. Businesses with annual gross receipts greater than \$120,000 and up to \$150,000 are levied on a monthly basis, based on 4% of gross receipts in excess of \$5,000 per month. Businesses with annual gross receipts of more than \$150,000, lose the \$5,000 monthly exemption and are levied on a monthly basis of 4% of gross receipts. The gross receipts tax is due within 30 calendar days following the last day of the calendar month collected.

### **Due from Component Units**

Due from component units consist of the following (expressed in thousands):

Due from component units	\$ 33,759
Less allowance for doubtful accounts	 (30,880)
Due from component units, net	\$ 2,879

### **Component Unit Receivables**

Component unit receivables at September 30, 2006, consist of the following (expressed in thousands):

Utility service charges	\$ 31,840
Port fees	3,783
Students	3,187
Patients	20,568
Other	 1,872
Total	\$ 61,250

Notes to Basic Financial Statements (continued)

### **6.** Receivables (continued)

### **Component Unit Receivables (continued)**

Loans and advances receivable at September 30, 2006, consist of the following (expressed in thousands):

	Fi Pen	Component Units		
Mortgage loans	\$	16,473	\$	_
Personal loans		98,759		-
Other loans and advances		325		129
Subtotal		115,557		129
Less allowance for uncollectible accounts		(3,000)		(50)
Loans and advances, net	\$	112,557	\$	79

### 7. Interfund Transactions

### **Interfund Transfers**

Interfund transfers constitute the transfer of resources from the fund that receives the resources to the fund that utilizes them. The most significant transfers to the General Fund from other governmental funds include a \$103 million transfer from the PFA Debt Service representing gross receipt tax revenue in excess of bond service requirements, and a \$26 million transfer from a non-major debt service fund representing property tax revenue no longer reserved for debt service requirements.

Significant transfers made from the General Fund include a transfer of \$6.9 million to the Emergency Molasses Fund (a non-major governmental fund), a transfer of \$3 million to the Government Insurance Fund (a non-major business-type fund), a transfer of \$1 million to the Crisis Intervention Fund (a non-major governmental fund), a transfer of \$1 million to the Rainy Day Fund (a non-major governmental fund), and a transfer of \$620 thousand to the Claims Fund (a non-major governmental fund). Significant transfers from the PFA Debt Service Fund include transfers of \$12.7 million to the PFA Operating Surplus Account, representing interest earned from unexpended bond proceeds.

Notes to Basic Financial Statements (continued)

### 7. Interfund Transactions (continued)

#### **Interfund Transfers (continued)**

Contributions from the Virgin Islands Lottery (a non-major business-type fund) amounted to \$4.4 million, with contributions to the Educational Initiative Fund (a non-major governmental fund) of \$2.3 million, a contribution to the Pharmaceutical Program Fund (a non-major governmental fund) of \$1.4 million, and a contribution to the General Fund of \$698 thousand.

Interfund transfers for the year ended September 30, 2006 consisted of the following (expressed in thousands):

T ran sfer to	G eneral Fund	PFA Debt Service Fund	C Pr	PFA apital ojects Tund	Gov	onmajor ernmental Funds	Fun I	terprise d – West ndian ompany_	Ent	n m ajor terprise `un ds	Total
General fund	\$ -	\$ 103,004	\$	-	\$	29,500	\$	1,000	\$	-	\$ 133,504
PFA debt service fund	-	-		-		-		-		-	-
PFA capital projects fund	_	-		_		1,175		_		-	1,175
Nonmajor governmental funds	9,520	12,656		-		_		_		-	22,176
Nonmajor enterprise funds	4,000	-		1,938		_		_		_	5,938
Total	\$ 13,520	\$ 115,660	\$	1,938	\$	30,675	\$	1,000	\$	-	\$ 162,793
Transfer from											
General fund	\$ –	\$ –	\$	-	\$	9,520	\$	_	\$	4,000	\$ 13,520
PFA debt service fund	103,004	-		-		12,656		-		_	115,660
PFA capital projects fund	-	-		-		_		_		1,938	1,938
Nonmajor governmental funds	29,500	-		1,175		_		-		_	30,675
Major enterprise fund – WICO	1,000	-		-		_		_		-	1,000
Nonmajor enterprise funds	-	-		_		-		_		-	-
Total	\$ 133,504	\$ -	\$	1,175	\$	22,176	\$	-	\$	5,938	\$ 162,793
									_		

### Notes to Basic Financial Statements (continued)

### 7. Interfund Transactions (continued)

#### **Due From/To Other Funds**

The following table summarizes interfund receivables and payables at September 30, 2006 (expressed in thousands):

Due to	Gen Fu		Ca Pro	FA pital ojects und	Gove	nmajor ernmental Funds	Fun I	terprise d – West ndian mpany	Ent	nmajor terprise Yunds	Total
General fund	\$	_	\$	-	\$	3,178	\$	1,000	\$	4,668	\$ 8,846
PFA capital projects fund Nonmajor governmental funds	10	,579		_		_		_		313 841	313 11,420
Total Governmental Funds	10	,579		_		3,178		1,000		5,822	20,579
Propriety fund – nonmajor Enterprise fund		300		_						_	300
Total	\$ 10	,879	\$	_	\$	3,178	\$	1,000	\$	5,822	\$ 20,879
Due from	_										
General fund	\$	_	\$	_	\$	10,579	\$	_	\$	300	\$ 10,879
Nonmajor governmental funds	3	,178		_		_		_		_	3,178
Total Governmental Funds	3	,178		_		10,579		_		300	14,057
Enterprise fund – West Indian											
Company	1	,000,		_		_		_		_	1,000
Nonmajor enterprise funds	4	,668		313		841		_		_	5,822
Total Enterprise Funds	5	,668		313		841		_		_	6,822
Total	\$8	,846	\$	313	\$	11,420	\$	_	\$	300	\$ 20,879

The due from/to other funds includes the following amounts due from the General Fund: \$3.6 million due to the PFA Operating Fund (a non-major governmental fund), \$3.5 million due to the Emergency Molasses Fund (a non-major governmental fund) for unpaid appropriations, and \$1.3 million due to the Elected Governor Retirement Fund.

### Notes to Basic Financial Statements (continued)

### 7. Interfund Transactions (continued)

### **Due From/To Other Funds (continued)**

Other balances composing the due from/to other funds include \$2.7 million owed from the bond proceeds fund (a non-major governmental fund) to the General Fund.

The due to the General Fund from the nonmajor enterprise funds amounting to \$4.7 million is mainly composed of the amount owed by the Virgin Islands Lottery to the General Fund amounting to \$4.5 million, consisting primarily of 8% of the total lottery revenue that is required to be transferred to the General Fund.

The due to non-major governmental funds from the non-major enterprise fund includes \$186 thousand due from the Virgin Islands Lottery to the Pharmaceutical Assistance to the Aged Fund, and \$233 thousand due from the Virgin Islands Lottery to the VI Educational Initiative Fund, consisting primarily of 15% and 25% of total lottery revenue that is required to be transferred to these funds.

#### 8. Restricted Assets

#### **Primary Government**

Restricted assets of proprietary funds and business-type activities include cash and cash equivalents as follows (expressed in thousands):

Restricted Assets – Proprietary Funds and Business-type Activities						
Unemployment insurance funds WICO debt service funds	\$	30,549 1,820				
Total restricted assets of proprietary funds and business-type activities	\$	32,369				

# Notes to Basic Financial Statements (continued)

### 8. Restricted Assets (continued)

### **Component Units**

Restricted assets of component units include cash and cash equivalents, investments, and receivables as follows (expressed in thousands):

#### **Restricted Assets – Component Units**

Cash and cash equivalents:	
Debt service and sinking fund requirements	\$ 15,306
Endowment funds	15,788
HUD project funds	88
Revolving loan funds	10,445
Other	 148
Total cash and cash equivalents	 41,775
Investments:	
Debt service and sinking fund requirements	24,721
Construction funds	21,749
Endowment funds	13,442
Renewal and replacement funds	7,680
Revolving loan funds	 5,166
Total investments	 72,758
Other:	
Accrued interest receivable	 3
Total restricted assets of component units	\$ 114,536

Notes to Basic Financial Statements (continued)

### 9. Capital Assets

### **Primary Government**

The capital assets activity for the governmental activities for the year ended September 30, 2006, is summarized as follows (expressed in thousands):

	]	eginning Balance s restated)	lance Additions		lditions Reductions		Ending Balance
	(A.	s residieu)					
Capital assets, not being depreciated							
Land	\$	172,113	\$	67	\$	_	\$ 172,180
Construction in progress		47,431		52,257		-	 99,688
Total capital assets,							
not being depreciated		219,544		52,324		_	 271,868
Capital assets, being							
depreciated:							
Land improvements		3,333		-		_	3,333
Infrastructure		127,471		6,305		-	133,776
Buildings and improvements		334,363		3,411		-	337,774
Machinery and equipment		59,133		8,927		350	 67,710
Total capital assets,							
being depreciated		524,300		18,643		350	 542,593
Less accumulated depreciation for:							
Land improvements		1,783		150		-	1,933
Infrastructure		21,864		4,378		-	26,242
Buildings and improvements		98,656		5,879		-	104,535
Machinery and equipment		33,639		8,727		284	42,082
Total accumulated							
depreciation		155,942		19,134		284	 174,792
Total capital assets, being							
depreciated, net		368,358		(491)		66	367,801
Governmental activities				·			
capital assets, net	\$	587,902	\$	51,833	\$	66	\$ 639,669

# Notes to Basic Financial Statements (continued)

### 9. Capital Assets (continued)

### **Primary Government (continued)**

Capital assets activity for the business-type activities for the year ended as of September 30, 2006, is summarized as follows (expressed in thousands):

	ginning Salance	Additions		Additions		Additions Reductions		alance
Capital assets, not being depreciated								
Land and land								
improvements	\$ 5,317	\$	-	\$	_	\$ 5,317		
Construction in progress	 1,757		3,843		_	 5,600		
Total capital assets,								
not being depreciated	 7,074		3,843		_	 10,917		
Capital assets, being depreciated:								
Buildings and improvements	49,137		501		_	49,638		
Machinery and equipment	 4,376		246		3	 4,619		
Total capital assets,								
being depreciated	 53,513		747		3	 54,257		
Less accumulated depreciation for:								
Buildings and improvements	15,179		1,428		_	16,607		
Machinery and equipment	1,885		388		1	 2,272		
Total accumulated depreciation	17,064		1,816		1	18,879		
Total capital assets,								
being depreciated, net	 36,449		(1,069)		2	 35,378		
Business-type activities								
capital assets, net	\$ 43,523	\$	2,774	\$	2	\$ 46,295		

Notes to Basic Financial Statements (continued)

#### 9. Capital Assets (continued)

### **Primary Government (continued)**

Depreciation and amortization expense was charged to functions/programs of the PG for the year ended September 30, 2006 as follows (expressed in thousands):

Governmental activities:	
General government	\$ 3,682
Public safety	2,234
Health	1,509
Education	6,041
Culture and recreation	308
Transportation and communication	 5,360
Total depreciation expense – governmental activities	\$ 19,134
Business-type activities:	
WICO (major enterprise fund) - depreciation and amortization	\$ 1,521
Nonmajor enterprise fund – depreciation	 295
Total depreciation and amortization – business-type activities	\$ 1,816

### **Component Units**

The capital assets activity for the discretely presented component units for the year ended September 30, 2006 is summarized as follows (expressed in thousands):

	Beginning Balance (As restated)	Additions	Reductions	En ding Balan ce
Capital assets, not being				
depreciated:	\$ 112.763	¢ 5.025	\$ 213	¢ 110.205
Land	+,	\$ 5,835	++	\$ 118,385
Construction in progress	55,712	40,223	39,622	56,313
Total capital assets,	1 60 47 5	16.050	20.025	17.4 (0.0)
not depreciated	168,475	46,058	39,835	174,698
Capital assets being depreciated:				
Buildings and improvements	1,204,747	34,813	240	1,239,320
Airport and marine terminal facilities	107,653	998	_	108,651
Personal property and equipment	86,136	13,895	3,232	96,799
Total capital assets				·
being depreciated	1,398,536	49,706	3,472	1,444,770
Less accumulated depreciation:				
Buildings and improvements	647,734	46,172	2,749	691,157
Airport and marine terminal				
facilities	69,365	4,711	-	74,076
Personal property and equipment	54,850	6,495	2,875	58,470
Total accumulated depreciation	771,949	57,378	5,624	823,703
Total capital assets being				
depreciated, net	626,587	(7,672)	(2,152)	621,067
Component unit capital				
assets, net	\$ 795,062	\$ 38,386	\$ 37,683	\$ 795,765

Notes to Basic Financial Statements (continued)

### 9. Capital Assets (continued)

### **Component Units (continued)**

Beginning balances of component unit capital assets were restated by \$15.5 million.

Depreciation expense charged to each component unit for the year ended September 30, 2006 was as follows (expressed in thousands):

Virgin Islands Housing Authority	\$ 8,858
Virgin Islands Port Authority	18,587
Virgin Islands Water and Power Authority:	
Electric system	16,328
Water system	2,811
Virgin Islands Government Hospital and	
Health Facilities Corporation:	
Roy L. Schneider Hospital	4,597
Juan F. Luis Hospital	2,265
University of the Virgin Islands	1,742
Other component units	 2,190
Total depreciation – component units	\$ 57,378

Notes to Basic Financial Statements (continued)

### **10. Long-Term Liabilities**

Long-term liabilities activity for the year ended September 30, 2006 were as follows (expressed in thousands):

	Beginning Balance (As restated)	Additions	Reductions	Ending Balance	Amounts Due Within One Year	Amounts Due Thereafter
Governmental activities:						
Bonds payable:						
1998 Series Revenue and	¢ 450 500	¢	<b>(1455)</b>	<b></b>	¢ 15.000	A 100 105
Refunding Bonds 1999 General Obligation Bonds,	\$ 459,790	\$ -	\$ (14,765)	\$ 445,025	\$ 15,620	\$ 429,405
Series A	4,765	-	(945)	3,820	1,005	2,815
1999 Series A Revenue Bonds	278,570	-	(167,875)	110,695	5,285	105,410
2001 Series A Tobacco Bonds	21,940	-	(275)	21,665	_	21,665
2002 Series Garvee Bonds	12,940	-	(3,000)	9,940	3,155	6,785
2003 Series A Revenue Bonds	268,020	—	(2,875)	265,145	2,990	262,155
2004 Series A Revenue Bonds	94,000	-	(2,295)	91,705	2,980	88,725
2006 Series A Tobacco Bonds	-	7,290	-	7,290	-	7,290
2006 Series A Revenue Bonds		219,490		219,490		219,490
Subtotal bonds payable	1,140,025	226,780	(192,030)	1,174,775	31,035	1,143,740
Less:	(1.0.10)	(1= 0=0)			(1.070)	(1= 222)
Deferred amount on refundings	(1,848)	(17,373)	616	(18,605)	(1,372)	(17,233)
Bonds premium	8,035	11,572	(549)	19,058	1,052	18,006
Bonds discount	(8,104)	(358)	954	(7,508)	(960)	(6,548)
Bonds accretion	(764)		574	(190)	(143)	(47)
Total bonds payable, net	1,137,344	220,621	(190,435)	1,167,530	29,612	1,137,918
Loans payable:						
Series 2006 Note	_	4,000	_	4,000	1,269	2,731
Series 2005 Note	5,850	-	(2,262)	3,588	2,145	1,443
				,		
Total loans payable	5,850	4,000	(2,262)	7,588	3,414	4,174
Other liabilities:				11.000		1.5.100
Accrued compensated absences	47,787	_	(3,707)	44,080	26,448	17,632
Retroactive union arbitration	263,297	8,876	_	272,173	_	272,173
Litigation	23,043	-	(9,022)	14,021	450	13,571
Landfill closure and postclosure	20.200	0.450		22.542		22 5 12
costs	29,290	3,452	-	32,742	-	32,742
Arbitrage		289		289	289	
Total other liabilities	363,417	12,617	(12,729)	363,305	27,187	336,118
Total governmental						
activities	\$ 1,506,611	\$ 237,238	\$ (205,426)	\$ 1,538,423	\$ 60,213	\$ 1,478,210
Business-type activities:	. , , .	,		. , ,		, , .
Notes payable: WICO	\$ 20,546	\$ 1,025	\$ (852)	\$ 20,719	\$ 654	\$ 20,065
	φ 20,340	φ 1,023	\$ (852)	φ 20,719	φ 034	φ 20,005
Fiduciary activities:						
Note payable	10.000	A 10.000	¢ (10.000)	<b></b>	to occ	<u>^</u>
Pension trust fund	\$ 10,000	\$ 10,000	\$ (10,000)	\$ 10,000	\$ 10,000	\$

Notes to Basic Financial Statements (continued)

### 10. Long-Term Liabilities (continued)

Accrued compensated absences, retroactive union arbitration liabilities, accrued litigation, and the landfill closure and post-closure costs are generally expected to be liquidated with resources derived from the General Fund.

### **Debt Margin**

Pursuant to 48 U.S.C. Section 1574(b)(i) of the Revised Organic Act, the Government may issue revenue bonds for public improvements or undertakings authorized by an act of the Legislature, without limitation as to principal amount. Such revenue bonds are payable solely from the revenue directly derived from and attributable to such public improvements or undertakings. Pursuant to 48 U.S.C. Section 1574(b)(ii), the Government is authorized to issue general obligation bonds for any public purpose provided that no such indebtedness is in excess of 10% of the aggregate assessed valuation of the taxable real property in the U.S. Virgin Islands. In addition, pursuant to 48 U.S.C. Section 1574(a) (Public Law 94-932), the U.S. Virgin Islands is authorized to issue bonds or other obligations in anticipation of the matching funds to be received from the federal government pursuant to 26 U.S.C. Section 7652(b)(3). There is no legal limit on the value of bonds that the Government may issue pursuant to 48 U.S.C. Section 1574(a). The Legislature of the U.S. Virgin Islands must authorize all bond issuances. PFA is authorized to issue bonds for the purpose of financing any project or for the purpose authorized by the Legislature. Given that PFA's powers to issue bonds are derived from 48 U.S.C. Section 1574(b), the bonds issued by PFA are subject to the limitations of said 48 U.S.C. Section 1574(b). On August 23, 1999, the Legislature amended the V.I. Code to add a Mandatory Balanced Budget Provision. Such provisions, specifically Title 2 of the V.I. Code Section 256, provide that the amount of debt of the Government existing on October 1, 2000 shall be the debt limit of the Government, exclusive of bond principal and interest that may become due. The debt limit specified under Title 2 of the V.I. Code Section 256 does not include bonds authorized by law for which a specific source of revenue is identified and committed to retiring those bonds. As used in Title 2 of the V.I. Code Section 256, the term "debt" means the total accumulated unpaid obligations that are due and payable, including unpaid income tax refunds, amounts owed to vendors, and current year unpaid debt service obligations, if any. As used in the statute, the term "debt" does not include that portion of principal or interest on bonds that is not yet due and payable.

Notes to Basic Financial Statements (continued)

### 10. Long-Term Liabilities (continued)

#### **Bonds Payable**

Bonds payable outstanding at September 30, 2006 are comprised of the following (expressed in thousands):

	Final	Interest	
Bonds Payable	Maturity	Rates (%)	Balance
1998 Series A, C, D, and E Revenue			
and Refunding Bonds	2025	5.50 - 7.11	\$ 445,025
1999 Series A General Obligation Bonds	2010	6.50	3,820
1999 Series A Revenue Bonds	2033	4.20 - 6.50	110,695
2001 Series A Tobacco Bonds	2031	5.00	21,665
2002 Series Garvee Bonds	2009	2.50 - 5.00	9,940
2003 Series A Revenue Bonds	2033	4.00 - 5.25	265,145
2004 Series A Revenue Bonds	2024	4.00 - 5.25	91,705
2006 Series A, B, C & D Tobacco			
Turbo and Capital Appreciation Bonds	2035	6.25 - 7.625	7,290
2006 Series A Revenue Bonds	2029	3.50 - 5.00	219,490
Subtotal			1,174,775
Less:			
Deferred amount on refundings			(18,605)
Bonds premium			19,058
Bonds discount			(7,508)
Bonds accretion			(190)
Total			\$1,167,530

### **Primary Government - Bonds Payable**

On May 1, 1998, PFA issued the revenue and refunding bonds series 1998 A, B, C, D, and E amounting to \$541.8 million, secured by general obligation notes issued by the Government. These bonds were issued for the purpose of, among other things, advance refunding of previously issued bonds in order to obtain lower interest rates.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Bonds Payable (continued)**

The proceeds of the 1998 Series A and B Bonds were placed in an irrevocable trust account to provide for all future debt service payments on the Highway Revenue Bonds Series 1989, Series 1991, Series 1992, Series 1993, and Series 1994 Bonds. At September 30, 2006, \$171.4 million of the above-mentioned defeased bonds were outstanding.

The proceeds of the Series 1992 Revenue Bonds were placed in an irrevocable trust to provide for all future debt service payments on the Series 1989 Revenue Bonds. At September 30, 2006, \$153.4 million of defeased bonds were outstanding. Assets held by irrevocable trusts for refunding of prior outstanding debt and the corresponding liabilities are not included in the Government's basic financial statements.

The 1998 Series C Bonds and the 1998 Series D Bonds were issued to pay, on behalf of the Government, the full principal balance and interest due and payable on the Revenue Anticipation Note, issued in February 1998. The remaining balance of the 1998 Series D Bonds amounting to approximately \$11.6 million was primarily provided to the Government for additional working capital. The net proceeds of the 1998 Series E Bonds amounting to \$104 million were primarily designated to fund the construction of certain capital projects amounting to \$94 million. The remaining \$10 million was deposited in a debt service reserve account.

The U.S. Department of the Treasury makes certain transfers to the Government of substantially all excise taxes imposed and collected under the Internal Revenue laws of the United States in any fiscal year on certain products produced in the U.S. Virgin Islands (primarily rum) and exported to the United States from the Virgin Islands. The amount required to be remitted to the Government by the U.S. Department of the Treasury is an amount no greater than the total amount of local revenue (primarily taxes) collected by the Government in each fiscal year. As a result, the term "matching fund revenue" is used to denote these payments. The Government has pledged the matching fund revenue, as described above, to the timely payment of principal and interest on the 1998 Series A, B, C, D, and E Bonds and the 2004 Series A Bonds. Thus, amounts to be received by the Government from federal excise taxes, mostly in rum, are deposited directly into trust accounts until the 1998 and 2004 Bonds are paid in accordance with the Indenture of Trust.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

#### **Bonds Payable (continued)**

Estimated prepayments of matching fund revenue are made to the Government prior to the beginning of each fiscal year, subject to adjustment for the amount of local revenue actually collected by the U.S. Department of the Treasury during such year. Prepayments of matching fund revenue are recorded as deferred revenue in the accompanying statement of net assets and the balance sheet of the governmental funds and recognized in the following year when earned. The adjustments for actual collections made to the estimated prepayments are recorded in the year determined.

In November 1999, the U.S. Congress approved an increase in the rate of federal excise taxes on rum transferred to the Government from \$10.50 to \$13.25 per proof gallon. The increase was retroactive to July 1999. The increase in rate has subsequently been extended two times and in December 2005, Congress again extended the \$13.25 per proof gallon rate to December 31, 2006.

Interest on the Revenue and Refunding Bonds Series 1998 A, C, D, and E and 1999 Bonds is payable semiannually on April 1 and October 1, and principal is payable annually on October 1. The Government is responsible for all principal and interest payments on the 1998 Series bonds. The principal due on October 1 and interest payments due on October 1 and April 1, are funded by the matching fund revenue and deposited into the debt service reserve accounts.

On April 13, 1999, a loan agreement was made between and among the Government, the PFA, International Business Machine Corporation (IBM), Banco Popular de Puerto Rico, and U.S. Trust Company of New York (Y2K Loan). The purpose of this loan was to finance certain costs of compliance by the Government with Year 2000 computer system issues. The loan was evidenced by the Government's issuance of General Obligation Bonds Series 1999 A amounting to \$18 million. Principal and interest are payable semiannually on January 1 and July 1. On July 9, 2001, the Government paid the outstanding IBM portion of the bonds amounting to \$7.4 million.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Bonds Payable (continued)**

The General Obligation Bonds Series 1999A are secured by the full faith and credit and taxing power of the Government, including a pledge on annual real property tax revenue from its taxation of the Hovensa Oil Refinery (the Refinery), which revenue is deposited in the Hovensa Property Tax Fund, and a contingent pledge of all franchise taxes on foreign sales corporations collected by the Government (Franchise Tax Revenue). Pursuant to the Hovensa Oil Contract, the Refinery agreed to pay \$14 million annually of real property taxes on the Refinery properties. Foreign sales corporations qualified to do business in the Virgin Islands must pay a franchise tax of \$1.50 for each thousand dollars of capital stock issued (Franchise Tax).

The Government did not comply with the requirement of the General Obligation Bonds 1999 Series to issue its audited financial statements within 180 days after year-end. The Government has not classified these bonds as current since the bonds were not called or paid within one year after September 30, 2006.

On November 16, 1999, PFA issued the 1999 Series A Revenue Bonds amounting to \$299.9 million. These bonds were issued to (i) pay certain working capital obligations of the Government, (ii) repay the Government outstanding tax and revenue anticipation notes, (iii) fund the Series debt service accounts, and (iv) pay certain costs of issuing the bonds.

On September 28, 2006, PFA advance refunded a portion of the 1999 Bonds with maturity dates of October 1, 2020 to October 1, 2029 totaling \$162.9 million. The proceeds of the refunding were placed in a trust account to provide for all future debt service payments on the 2020 through 2029 maturities of the bonds. Approximately \$180 million was deposited with the refunding bond escrow agent to fund the Escrow Fund accounts. At September 30, 2006, \$162.9 million of the defeased 1999 Series A Revenue Bonds remain outstanding.

The Government has pledged gross receipts taxes for the timely payment of the principal and interest on the 1999 Series A Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1. Gross receipts revenue amounted to \$142 million for the year ended September 30, 2006.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Bonds Payable (continued)**

On November 20, 2001, TSFC issued the 2001 Tobacco Settlement Asset-Backed Series A Bonds amounting to \$23.6 million of aggregate principal. The proceeds were used for the purpose of (i) purchasing all rights, title, and interest in certain litigation awards under the master settlement agreement (MSA) entered into by participating cigarette manufacturers, (ii) issuance of Tobacco Settlement Asset-Backed Bonds to pay the purchase price for the rights, and (iii) to provide funds for hospital and healthcare projects in the U.S. Virgin Islands.

Interest on the 2001 bonds is payable semiannually on each May and November 15, beginning with May 2002 for the term bonds amounting to \$15.5 million and convertible capital appreciation bonds amounting to \$8.2 million, with a nominal value of \$6.2 million.

The convertible capital appreciation bonds accrete interest prior to November 15, 2007 and accrue interest subsequent to that date. Interest on the capital appreciation bonds will compound on May 15th and November 15th.

2001 Series A Tobacco Bonds payable at September 30, 2006 amounted to \$21.7 million with unamortized accretion of \$414 thousand. Under early redemption provisions, any MSA payments exceeding annual debt service requirements of the 2001 Series A Tobacco Bonds must be applied to early redemption of principal. MSA payments and interest earnings on the trust funds during the year ended September 30, 2006, resulted in early redemption of \$275 thousand during fiscal year 2006.

On October 1, 2002, PFA issued the Series 2002 Revenue Bonds (Garvee Bonds), the proceeds of which amounted to \$20.8 million. The Garvee Bonds are special, limited obligations, secured solely by the pledge and assignment of the Government's security interest in Federal Highway Reimbursement Revenues. The bonds were issued to (i) fund construction costs related to renovation and construction of two sea docks, (ii) fund the Debt Service Reserve Accounts, and (iii) pay certain costs of issuing the bonds. The Series 2002 Bonds are not subject to redemption prior to maturity.

Interest and principal on the Series 2002 Revenue Bonds are payable semiannually on March 1 and September 1. As of September 30, 2006, the outstanding 2002 Revenue Bonds amounted to \$9.9 million.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Bonds Payable (continued)**

On February 28, 2003, PFA entered into a swaption contract that provided PFA with an up-front payment of \$8.3 million. The swaption contract gave the counterparty the option to make PFA enter into a pay-fixed, receive-variable interest rate swap. If the option was exercised, PFA would then expect to issue variable-rate refunding bonds. PFA had outstanding \$244 million in outstanding 1999 Series A Bonds with maturities from 2011 to 2029 at the time the contract was entered into. The 1999 Series A Bonds were callable by the PFA on October 1, 2010 at 101%. Having been advised by its underwriters and financial advisor that there were no net present value savings available to it by issuing conventional advance refunding bonds, PFA sold a LIBOR-based swaption to Lehman Brothers Special Financing, Inc. on the 2020 through 2029 maturities, totaling \$162.9 million. Lehman purchased the swaption for \$8.3 million and it was exercisable on July 1, 2010 only. As part of the 2006 Series Bonds issuance of September 28, 2006, the swaption contract was terminated and PFA made a termination payment to Lehman Brothers of \$26.9 million.

On December 17, 2003, PFA issued the Series 2003A Revenue Bonds, the proceeds of which amounted to approximately \$268 million. The bonds were issued to: (i) repay the Government outstanding Revenue Bond Anticipation Notes, Series 2003, (ii) fund certain necessary public safety and other public sector capital development projects, (iii) fund debt service accounts for the bond issuance, and (iv) pay certain costs of issuing the bonds.

The Government has pledged gross receipts taxes for the timely payment of the principal and interest on the Series 2003A Revenue Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1, beginning October 1, 2005. The Series 2003A Revenue Bonds are not subject to optional redemption prior to October 1, 2014.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Bonds Payable (continued)**

On December 1, 2004, PFA issued the 2004 Series A Bonds, the proceeds of which amounted to \$94 million. The Government has pledged the Matching Fund Revenues to the timely payment of principal and interest on the 2004 Series A Bonds. The bonds bear interest at 4.00% to 5.25% and mature from 2005 to 2024. The proceeds of the bonds were issued to: (i) finance the planning, development, constructing, renovating and equipping of wastewater treatment facilities and collection systems on St. Thomas and St. Croix, (ii) finance the repairs, renovations and construction of solid waste facilities in the Territory, (iii) finance the repair and construction of public roads in the Territory, (iv) provide start-up capital for the Virgin Islands Waste Management Authority, (v) fund the Series 2004A Senior Lien Debt Service Reserve Subaccount, and (vi) pay certain costs of issuing the Series 2004A Bonds. The Series 2004A Bonds are not subject to optional redemption prior to October 1, 2014.

On March 15, 2006, TSFC issued the 2006 Tobacco Settlement Asset-Backed Bonds, Subordinated Series 2006 A, B, C & D Turbo and Capital Appreciation Bonds amounting to \$48.1 million, with an issue value of \$7.3 (net of accretion of \$40.8). The bonds are secured and payable from collections including all Tobacco Settlement Revenues to be received by TSFC, reserves, amounts held in other accounts established by the indenture and TSFC's rights under the purchase agreement. The proceeds have been used for the purpose of (i) financing several capital, hospital and health development projects for the benefit of the Virgin Islands and its residents, (ii) pay certain costs of issuance relating to the Series 2006 Bonds, and (iii) fund operating costs.

Interest on the Series 2006 Tobacco Settlement Asset-Backed Bonds is not paid currently, but accretes from the date of delivery, compounded every May 15 and November 15, commencing May 15, 2006 through the final maturity date of May 15, 2035. Interest yields on the Bonds range from 6.25% to 7.63%. The series are subject to early redemption at accreted value beginning May 15, 2023, provided that the 2001 Tobacco Settlement Asset-Backed Series A Bonds have been paid in full.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Bonds Payable (continued)**

On September 28, 2006, PFA issued the 2006 Series Gross Receipts Revenue Bonds ("2006 Series Bonds"), the proceeds of which amounted to \$219.5 million. The Government has pledged gross receipts tax revenues for the timely payment of the principal and interest on the 2006 Series Bonds. Interest is payable semiannually on April 1 and October 1, and principal is payable annually on October 1, beginning October 1, 2007.

The 2006 Series Bonds bear interest at 3.50% to 5.00% and mature from 2007 to 2029. The proceeds of the bonds were issued to: (i) advance refund a portion of the Series 1999A Revenue Bonds, (ii) pay the cost of a termination fee in connection with an outstanding swap option agreement, (iii) fund certain capital projects, (iv) fund debt service reserve accounts, (v) pay certain costs of issuing the Series 2006 Bonds and (vi) fund a net payment reserve account for a new swap agreement in connection with the refunding. The 2006 Series Bonds maturing on or before October 1, 2016 are not subject to optional redemption.

The advance refunding of the 2020 through 2029 maturities of the 1999 Series A Bonds was made in order to obtain lower interest rates. The economic gain obtained by this advance refunding is the difference between the present value of old debt service requirements and the new debt service. This refunding resulted in a debt service saving of approximately \$40.8 million and an economic gain of approximately \$25.6 million.

The proceeds of the 2006 Series Bonds related to the refunding were placed in a trust account to provide for all future debt service payments on the 2020 through 2029 maturities of the 1999 Series A Bonds. Approximately \$180 million in funds were deposited into the Escrow Fund accounts. At September 30, 2006, \$162.9 million of defeased 1999 Bonds remained outstanding.

# Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

# **Bonds Payable (continued)**

Debt service requirements at September 30, 2006 were as follows (expressed in thousands):

				overnmental Ac						
			Revenue Bonds Revenue Bonds				Revenue B ond s			
Principal	Interest	Principal	Interest	Principal	I nte re st	Principal	Interest	Principal	I nte re st	
\$ -	\$ 15,821	\$ 11,150	\$ 1,640	\$ 4,470	\$ 714	\$ -	\$ 6,261	\$ 15,620	\$ 24,436	
-	15,821	11,780	1,009	4,750	434	-	6,261	16,530	23,525	
-	15,821	12,455	343	4,915	147	-	6,261	17,370	22,572	
13,135	15,480	-	-	-	-	-	6,107	13,135	21,587	
13,835	14,779	_	_	_	_	_	5,791	13,835	20,570	
81,505	61,562	_	_	_	_	30,095	23,505	111,600	85,067	
· · · ·	· · · · · ·	_	_	_	_	· · ·	,	,	53,727	
		_	_	_	_				17,442	
		_	_	_	_					
\$289,075	\$197,214	\$ 35,385	\$ 2,992	\$ 14,135	\$ 1,295	\$ 106,430	\$ 67,425	\$445,025	\$268,926	
General (	bligation			<u> </u>						
	0	Revenue	Bonds	Tobacc	o Bonds	Garvee	Bonds	Re ven u	e B ond s	
Principal	Interest		Interest	Principal	I nte re st		Interest	Principal	Interest	
		<u> </u>		<u> </u>		<u> </u>				
								. ,	\$ 13,126	
,		,				· · · ·		,	13,004	
,		,	,	1,030		3,475	174	,	12,877	
600	20	6,230	15,951	1,100	672	-	-	3,360	12,746	
_	-	6,580	15,591	1,165	672	_	-	3,495	12,609	
_	-	39,475	71,048	4,005	3,363	_	-	20,090	60,275	
_	_	41,640	46,452	5,410	3,362	_	-	25,840	54,363	
-	-	-	-	_	2,011	-	-	33,270	46,770	
_	_	_	_	8,045	1,810	_	_	64,830	36,779	
_	-	_					_	104,930	8,040	
\$ 3,820	\$ 513	\$ 110,695	\$198,870	\$ 21,665	\$ 13,909	\$ 9,940	\$ 1,010	\$265,145	270,589	
						Total governmental				
		-		in the second seco						
Principal	Interest	Principal	Interest	Principal	Interest	Prin cip al	Interest			
\$ 2.980	\$ 4.658	s –	\$ 5340	\$	s –	\$ 31.035	\$ 65 883			
				<b>4</b> –		- )				
· · · ·	· · ·		,	-	-	· · · ·	,			
,	· · ·	,	,	-	-	· · ·	,			
				-	-					
,	- ,	,	,	-	-	,	,			
· · · ·	· · · · · ·	,	,	-	-	· · · ·	,			
27,020	10,829	29,565	46,006	-	-	229,935	214,739			
27,190	2,946	87,710	31,104	-	-	304,645	100,273			
27,190			7 0 7 1			155,430	46,460			
-	-	82,555	7,871	-	-	155,450	40,400			
-		82,555	/,8/1	48,145	-	153,075	8,040			
				48,145 (40,855)						
	Series           Principal           \$ -           -           -           13,135           13,835           81,505           60,795           119,805           -           \$\$289,075           Gen eral O           Bo           Series           Principal           \$ 1,005           1,075           1,140           600           -           -           -           -           -           -           \$ 1,005           1,075           1,140           600           -	\$ - \$ 15,821 - 15,821 - 15,821 13,135 15,480 13,835 14,779 81,505 61,562 60,795 41,544 119,805 16,386  \$289,075 \$197,214 Gen er al Obligation Bonds Series 1999 A Principal Interest \$ 1,005 \$ 232 1,075 166 1,140 95 600 20       	Series 1998 A         Series 1           Principal         Interest         Principal           \$\$ -         \$\$ 15,821         \$\$ 11,150           -         15,821         \$\$ 11,780           -         15,821         \$\$ 11,780           -         15,821         \$\$ 12,455           13,135         15,480         -           13,835         14,779         -           81,505         61,562         -           60,795         41,544         -           119,805         16,386         -           -         -         -           \$\$ 289,075         \$197,214         \$\$ 35,385           General Obligation Bonds         Revenue Series 1999 A         Series 1           Principal         Interest         Principal           \$\$ 1,005         \$         232         \$           \$\$ 1,005         \$         232         \$           \$\$ 1,005         \$         232         \$           \$\$ 1,005         \$         232         \$           \$\$ 1,005         \$         232         \$           \$\$ 1,005         \$         232         \$           \$\$ 1,005         \$ </td <td>Series 1998 A         Series 1998 C           Principal         Interest         Principal         Interest           \$ -         \$ 15,821         \$ 11,150         \$ 1,640           -         15,821         11,780         1,009           -         15,821         12,455         343           13,135         15,480         -         -           13,835         14,779         -         -           60,795         41,544         -         -           -         -         -         -           5805         16,386         -         -           -         -         -         -           58197,214         \$ 35,385         \$ 2,992           General Obligation Bonds           Beries 1999 A           Principal         Interest           Principal         Interest         Principal         Interest           \$ 1,005         \$ 232         \$ 5,285         \$ 16,921           1,075         166         5,585         16,615           1,140         95         5,900         16,292           6000         20         6,230         15,591           -&lt;</td> <td>Series 1998 A         Series 1998 C         Series           Principal         Interest         Principal         Interest         Principal           \$          -         \$             15,821         \$             11,780         1,009         4,750           -         15,821         12,455         343         4,915           13,135         15,480         -         -         -           -         13,835         14,779         -         -         -           60,795         41,544         -         -         -         -           119,805         16,386         -         -         -         -           -         -         -         -         -         -           S289,075         \$197,214         \$         35,385         \$         2,992         \$         14,135           General Obligation           Bonds         Revenue Bonds         Tobacc           Series         1999 A         Series         910           1,140         95         5,200         16,292         1,030           600         20         6,230         15,591         1,100           <t< td=""><td>Series 1998 A         Series 1998 C         Series 1998 D           Principal         Interest         Principal         Interest         Principal         Interest           \$          -         \$ 15,821         \$ 11,150         \$ 1,640         \$ 4,470         \$ 7,14           -         15,821         11,780         1,009         4,750         434           -         15,821         12,455         343         4,915         147           13,135         15,480         -         -         -         -         -           81,505         61,562         -         -         -         -         -         -           19,805         16,386         -         -         -         -         -         -         -         -           \$ 289,075         \$197,214         \$ 35,385         \$ 2,992         \$ 14,135         \$ 1,295          General Obligation         Bonds         Series 1999 A         Series 1999 A         Series 2001 A           Principal         Interest         Principal         Interest         Principal         Interest           \$ 1,005         \$ 232         \$ 5,285         \$ 16,615         910         673</td><td>Series 1998 A         Series 1998 C         Series 1998 D         Series 1998 D           Principal         Interest         Principal         Interest         Principal         Interest         Principal           \$          -         \$15,821         \$11,150         \$1,640         \$4,470         \$714         \$-           -         15,821         \$11,1780         \$1,009         \$4,750         \$434         -           -         15,821         \$12,455         \$343         \$4,915         \$147         -           -         13,135         \$14,779         -         -         -         -         -           31,935         \$14,779         -         -         -         -         30,065           \$119,805         \$16,386         -         -         -         -         -           \$289,075         \$197,214         \$35,385         \$2,992         \$14,135         \$1,295         \$106,430           General Obligation         Bonds         Series 1999 A         Series 1999 A         Series 2001 A         Series           Principal         Interest         Principal         Interest         Principal         Series 2001 A           \$1,005         \$2</td><td></td><td></td></t<></td>	Series 1998 A         Series 1998 C           Principal         Interest         Principal         Interest           \$ -         \$ 15,821         \$ 11,150         \$ 1,640           -         15,821         11,780         1,009           -         15,821         12,455         343           13,135         15,480         -         -           13,835         14,779         -         -           60,795         41,544         -         -           -         -         -         -           5805         16,386         -         -           -         -         -         -           58197,214         \$ 35,385         \$ 2,992           General Obligation Bonds           Beries 1999 A           Principal         Interest           Principal         Interest         Principal         Interest           \$ 1,005         \$ 232         \$ 5,285         \$ 16,921           1,075         166         5,585         16,615           1,140         95         5,900         16,292           6000         20         6,230         15,591           -<	Series 1998 A         Series 1998 C         Series           Principal         Interest         Principal         Interest         Principal           \$          -         \$             15,821         \$             11,780         1,009         4,750           -         15,821         12,455         343         4,915           13,135         15,480         -         -         -           -         13,835         14,779         -         -         -           60,795         41,544         -         -         -         -           119,805         16,386         -         -         -         -           -         -         -         -         -         -           S289,075         \$197,214         \$         35,385         \$         2,992         \$         14,135           General Obligation           Bonds         Revenue Bonds         Tobacc           Series         1999 A         Series         910           1,140         95         5,200         16,292         1,030           600         20         6,230         15,591         1,100 <t< td=""><td>Series 1998 A         Series 1998 C         Series 1998 D           Principal         Interest         Principal         Interest         Principal         Interest           \$          -         \$ 15,821         \$ 11,150         \$ 1,640         \$ 4,470         \$ 7,14           -         15,821         11,780         1,009         4,750         434           -         15,821         12,455         343         4,915         147           13,135         15,480         -         -         -         -         -           81,505         61,562         -         -         -         -         -         -           19,805         16,386         -         -         -         -         -         -         -         -           \$ 289,075         \$197,214         \$ 35,385         \$ 2,992         \$ 14,135         \$ 1,295          General Obligation         Bonds         Series 1999 A         Series 1999 A         Series 2001 A           Principal         Interest         Principal         Interest         Principal         Interest           \$ 1,005         \$ 232         \$ 5,285         \$ 16,615         910         673</td><td>Series 1998 A         Series 1998 C         Series 1998 D         Series 1998 D           Principal         Interest         Principal         Interest         Principal         Interest         Principal           \$          -         \$15,821         \$11,150         \$1,640         \$4,470         \$714         \$-           -         15,821         \$11,1780         \$1,009         \$4,750         \$434         -           -         15,821         \$12,455         \$343         \$4,915         \$147         -           -         13,135         \$14,779         -         -         -         -         -           31,935         \$14,779         -         -         -         -         30,065           \$119,805         \$16,386         -         -         -         -         -           \$289,075         \$197,214         \$35,385         \$2,992         \$14,135         \$1,295         \$106,430           General Obligation         Bonds         Series 1999 A         Series 1999 A         Series 2001 A         Series           Principal         Interest         Principal         Interest         Principal         Series 2001 A           \$1,005         \$2</td><td></td><td></td></t<>	Series 1998 A         Series 1998 C         Series 1998 D           Principal         Interest         Principal         Interest         Principal         Interest           \$          -         \$ 15,821         \$ 11,150         \$ 1,640         \$ 4,470         \$ 7,14           -         15,821         11,780         1,009         4,750         434           -         15,821         12,455         343         4,915         147           13,135         15,480         -         -         -         -         -           81,505         61,562         -         -         -         -         -         -           19,805         16,386         -         -         -         -         -         -         -         -           \$ 289,075         \$197,214         \$ 35,385         \$ 2,992         \$ 14,135         \$ 1,295          General Obligation         Bonds         Series 1999 A         Series 1999 A         Series 2001 A           Principal         Interest         Principal         Interest         Principal         Interest           \$ 1,005         \$ 232         \$ 5,285         \$ 16,615         910         673	Series 1998 A         Series 1998 C         Series 1998 D         Series 1998 D           Principal         Interest         Principal         Interest         Principal         Interest         Principal           \$          -         \$15,821         \$11,150         \$1,640         \$4,470         \$714         \$-           -         15,821         \$11,1780         \$1,009         \$4,750         \$434         -           -         15,821         \$12,455         \$343         \$4,915         \$147         -           -         13,135         \$14,779         -         -         -         -         -           31,935         \$14,779         -         -         -         -         30,065           \$119,805         \$16,386         -         -         -         -         -           \$289,075         \$197,214         \$35,385         \$2,992         \$14,135         \$1,295         \$106,430           General Obligation         Bonds         Series 1999 A         Series 1999 A         Series 2001 A         Series           Principal         Interest         Principal         Interest         Principal         Series 2001 A           \$1,005         \$2			

Notes to Basic Financial Statements (continued)

### **10. Long-Term Liabilities (continued)**

### **Conduit Debt**

In February 2004, the PFA issued private activity bonds amounting to \$50.6 million to finance costs of construction of a coker plant for a refinery on the island of St. Croix. The bonds are limited obligations of PFA and will be payable solely from and are secured by a pledge and assignment of the amounts payable under the loan agreement between PFA and the refinery. The refinery is responsible for all debt service payments of the private activity bonds. The Government is not obligated for the repayment of the bonds. The bonds are not reported as liabilities in the Government's basic financial statements.

### **Notes Payable**

On September 7, 2006, PFA issued the Subordinate Lien Revenue Notes, Series 2006 (Virgin Islands Gross Receipts Taxes Loan Note) in the aggregate amount of \$4 million (the "Series 2006 Notes"). The Series 2006 Notes accrue interest monthly at a rate of 4% for 36 months. The proceeds of the Series 2006 Notes were loaned to the PG under the same terms, for the purposes of (i) financing the acquisition of fire fighting, fire suppression and fire safety equipment, (ii) training of firefighters, (iii) renovations and repairs to fire stations, and (iv) pay certain costs of issuing the Series 2006 Notes. The PG has pledged gross receipts taxes for the payment of the Notes.

Debt service requirements for the Series 2006 Notes at September 30, 2006 were as follows (expressed in thousands):

Year	
2007 2008 2009	\$ 1,269 1,332 1,399
Total	\$ 4,000

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

#### **Notes Payable (continued)**

On September 7, 2005, PFA issued the Subordinate Lien Revenue Notes, Series 2005 (Virgin Islands Gross Receipts Taxes Loan Note) in the aggregate amount of \$6.35 million (the "Series 2005 Notes"). The Series 2005 Notes accrue interest monthly at a rate of 4% for 36 months. The proceeds of the Series 2005 Notes were loaned to the PG under the same terms, for the purposes of (i) financing the acquisition of a fleet of vehicles for the Virgin Islands Police Department, and (ii) paying certain costs of issuing the Series 2005 Notes. On September 22, 2005 the PFA made a prepayment on the loan balance in the amount of \$500 thousand, from unexpended loan proceeds. The Government has pledged gross receipts taxes for the payment of the Notes.

Debt service requirements for the Series 2005 Notes at September 30, 2006 were as follows (expressed in thousands):

Year	
2007 2008	\$ 2,145 1,443
Total	\$ 3,588

On November 20, 2002, WICO consolidated and refinanced its notes payable and obtained an additional \$2 million in financing for infrastructure improvements. The consolidated loan amounted to \$22.5 million at a fixed rate of 4.5% for the first four years of the 20-year term of the loan, until November 20, 2006. On June 6, 2006, WICO refinanced the outstanding loan back to the maximum of \$22.5 million, at an effective interest rate of 6.2% per annum, effective November 20, 2006. This refinancing created additional working capital of approximately \$2.7 million dollars to fund cruise ship pier upgrades to accommodate mega cruise ships. Subsequent to November 20, 2006, WICO will have the option (not to be exercised more than once every two years) to fix the interest rate at one of the following three options: a) prime rate plus 75 basis points, b) 1 year Libor plus 200 basis points, or c) 3 year Treasury notes plus 125 basis points. The loan will be repaid in 240 consecutive monthly payments of \$164 thousand (representing principal and interest) and a final payment of the outstanding principal balance plus

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Notes Payable (continued)**

any unpaid interest accrued to the date of the final payment. The loan may be prepaid, in whole or in part, at any time without penalty. The revenue and lease agreements of WICO are pledged for the payment of principal and interest on the loan. WICO paid approximately \$938 thousand in interest expense during fiscal year 2006.

Debt service requirements for the WICO loan at September 30, 2006 were as follows (expressed in thousands):

Year	
2007	\$ 654
2008	625
2009	664
2010	706
2011	752
2012 - 2016	4,590
2017 - 2021	6,665
2022 - 2024	6,063
Total	\$ 20,719

### **Fiduciary Funds – Notes Payable**

On December 30, 2002, the pension trust fund entered into a line-of-credit agreement with a bank to provide working capital. The pension trust fund obtained a line-of-credit of \$10 million, which accrues interest at a fixed interest rate of 4.8% calculated on a 360-day basis and is due and payable quarterly in arrears commencing on the first day of the fourth calendar month following the closing of the loan. The terms of the line-of-credit require the pension trust fund to repay the line-of-credit in a period of 30 consecutive days during each 12-month period. The bank retains a certificate of deposit in the amount of \$10 million as security on the note payable. As of September 30, 2006, the outstanding balance on the line-of-credit agreement was \$10 million.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Component Units – Bonds Payable**

Bonds payable of discretely presented component units are those liabilities that are paid out of resources pledged by such entities. These revenue bonds do not constitute a liability or debt of the PG. Bonds payable, outstanding at September 30, 2006, are as follows (expressed in thousands):

Bonds Payable	Final Maturity	Interest Rates (%)	Ē	Balance
University of the Virgin Islands:				
General obligation bonds of 2004	2035	2.02 - 5.38	\$	20,980
General obligation bonds of 1999	2029	4.75 - 5.95		22,805
Virgin Islands Water and Power				
Authority (Electric System)				
Revenue bonds of 2003	2023	4.00 - 5.00		69,960
Revenue bonds of 1998	2021	4.25 - 5.30		83,415
Virgin Islands Water and Power				
Authority (Water System)				
Revenue bonds of 1998	2017	4.90 - 5.50		33,555
Virgin Islands Port Authority				
Series A Revenue bonds of 2003	2023	5.00 - 5.25		18,005
Series B Revenue bonds of 2003	2015	3.73 - 5.43		13,145
Series C Revenue bonds of 2003	2023	4.40		10,417
Virgin Islands Housing Finance				
Authority:				
Revenue bonds of 1995	2025	5.50 - 6.50		2,100
Revenue bonds of 1998	2028	4.10 - 5.25		2,545
Subtotal				276,927
Plus unamortized premium				5,084
Less unamortized discount				(788)
Less deferred amount on debt				
refunding and reacquisition costs				(4,406)
Bonds payable, net				276,817
Less amount due within one year				(10,975)
Bonds payable, due in more	than one year		\$	265,842

Notes to Basic Financial Statements (continued)

#### **10.** Long-Term Liabilities (continued)

#### **Component Units – Bonds Payable (continued)**

Following is a schedule of changes in long-term debt for discretely presented component units for fiscal year 2006 (expressed in thousands):

	Beginning Balance	Additions	Reduc tions	Ending Balanc e	A mounts Due Within One Y ear	A mounts Du e Thereafter
Bonds payable:						
University of the Virgin Islands	\$ 43,791	\$ –	\$ (553)	\$ 43,238	\$ 600	\$ 42,638
Virgin Islands Water and Power Authority:						
Electric System	159,802	-	(4,268)	155,534	6,555	148,979
Water System	33,313	-	(1,691)	31,622	2,090	29,532
Virgin Islands Port Authority	42,034	1,274	(1,530)	41,778	1,625	40,153
Virgin Islands Housing Finance Authority	4,745	_	(100)	4,645	105	4,540
Total bonds payable, net	283,685	1,274	(8,142)	276,817	10,975	265,842
Loans payable:						
Virgin Islands Economic Development						
Authority	848	_	(58)	790	58	732
Virgin Islands Water and Power Authority:			. ,			
Electric System	5,600	11,000	_	16,600	_	16,600
Virgin Islands Port Authority	910	550	_	1,460	1,460	_
Virgin Islands Housing Finance Authority	1,229	_	(185)	1,044	190	854
University of the Virgin Islands	1,736		(55)	1,681	59	1,622
Total loans payable	10,323	11,550	(298)	21,575	1,767	19,808
Other long-term liabilities:						
University of the Virgin Islands	28	16	_	44	_	44
Virgin Islands Housing Authority	3,883	-	(200)	3,683	_	3,683
Virgin Islands Economic Development						
Authority	9,575	1,226	_	10,801	_	10,801
Juan F. Luis Hospital	23	-,	(23)		_	
Roy L. Schneider Hospital	1,318	191	(25)	1,509	633	876
Virgin Islands Housing Finance Authority	14,114	164	_	14,278	-	14,278
Total other long-term liabilities	\$ 28,941	\$ 1,597	\$ (223)	\$ 30,315	\$ 633	\$ 29,682

On December 1, 1999, the University issued the 1999 Series A Bonds. The University issued these bonds to finance a portion of the construction, furnishing, and equipping of various facilities of the University, to refund the 1994 Series A bonds issued by the University, to fund a debt service reserve fund for the 1999 Series A Bonds, and to pay certain costs issued under and secured by an indenture of trust dated. The 1999 Series A Bonds maturing on or after December 1, 2010 are subject to redemption prior to maturity at the option of the University, as a whole or in part of any date, on and after December 1, 2009, at redemption prices ranging between 100% and 102% of their principal amount plus accrued interest to the date fixed for redemption. As of September 30, 2005, the 1994 Series A Bonds were retired.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Component Units – Bonds Payable (continued)**

In fiscal year 2004, the University of the Virgin Islands General Obligation Improvement Bonds, 2004 Series A (the 2004 Series A Bonds) were issued in the amount of \$21.2 million under and secured by the Indenture of Trust dated as of December 1, 1999 and a First Supplemental Indenture of Trust dated as of June 1, 2004, between the University and the trustees. The Bonds were used to finance the costs of construction, furnishings, and equipping of various facilities of the University, to fund the debt service reserve fund and to pay the cost of issuance.

In June 2003, the Virgin Islands Water and Power Authority (Electric System) issued the Electric System Revenue Bonds, Series 2003, amounting to \$69.9 million. The proceeds from the bonds were used to finance capital improvements, repay \$18 million of then outstanding lines-of-credit, cover underwriters' costs, and establish a debt service fund.

In June 1998, the Electric System issued \$110.9 million of 1998 Series A Electric System Revenue and Refunding Bonds. The proceeds from the bonds, and approximately \$14 million in funds from the existing debt service and debt service funds, were used to repay outstanding line-of-credit balances, to provide for approximately \$30 million in funds for the construction of certain capital projects, and to pay underwriters discount and issuance costs of approximately \$1.7 million. The remaining proceeds were used to purchase direct obligations of the U.S. government which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining \$69 million principal amount of the 1991 Series A Electric System Revenue Bonds.

Under the terms of the Bond Resolution relating to the Electric System Revenue and Refunding Bonds, payment of the principal and interest is secured by an irrevocable lien on the Electric System's net revenue, (exclusive of any funds that may be established pursuant to the Bond Resolution for certain specified purposes), including the investments and income, if any, thereof.

The Bond Resolution contains certain restrictions and commitments, including the Electric System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net electric revenue, as defined, that will be at least 125% of aggregate annual principal and interest. The Electric System's net electric revenue for the fiscal year ended June 30, 2006 was 176% of the aggregate debt service as defined in the Bond Resolution.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Component Units – Bonds Payable (continued)**

The Series 2003 Bonds maturing on or after July 1, 2013 are subject to redemption prior to their stated maturity date, at the option of the Electric System, on or after July 1, 2013, as a whole or in part at any time, at a redemption price equal to the principal amount thereof plus accrued interest thereon to the date fixed for redemption.

The 1998 Series Electric System Revenue and Refunding Bonds are subject to redemption on or after July 1, 2008, as a whole or in part at any time, at a redemption price of 101% in 2008, 100.5% in 2009, and 100% thereafter. The Electric System Revenue Bonds are subject to mandatory redemption if (i) any significant part of the Electric System was damaged, destroyed, taken, or condemned, or (ii) any for-profit nongovernmental investor shall acquire an ownership interest in some or all of the assets of the Electric System.

In December 1998, the Virgin Islands Water and Power Authority (Water System) issued the 1998 Water System Revenue and Refunding Bonds amounting to \$44.1 million. The proceeds from the bonds were used to repay the 1990 Series A Water System Revenue Bonds at a redemption price of 100% and to refund the 1992 Series B Water System Revenue Bonds, repay outstanding lines of credit balances, pay underwriters' costs, provide funding for a Renewal and Replacement Reserve Fund, and to purchase obligations of the United States Government, which were placed in an irrevocable trust with an escrow agent to provide all future debt service on the remaining principal amount of the 1992 Series B Bonds. At June 30, 2006, \$33.6 million of the original principal amount of the defeased 1992 Series B Bonds remained outstanding.

Payment of principal and interest of the 1998 Series Bonds is secured by an irrevocable lien on the Water System's net revenues (exclusive of any funds that may be established pursuant to the Bond Resolution for certain other specified purposes) and funds established under the Bond Resolution, including investment securities. To provide additional security, the Water System has conveyed to the bond trustee, a subordinate lien and security interest in the Water System's General Fund. The Water System is also required to make deposits in a debt service reserve fund in accordance with the Bond Resolution.

The Bond Resolution contains certain restrictions and commitments, including the Water System's covenant to establish and maintain reasonable rates, fees, rentals, and other charges to produce net water revenue, as defined, that will be at least 125% of aggregate annual principal and interest payments. The Water System's net water revenue for the fiscal year ended June 30, 2006 was 126% of the aggregate debt service.

Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

### **Component Units – Bonds Payable (continued)**

The 1998 Series Bonds maturing on or after July 1, 2010 are subject to redemption prior to their stated maturity date, at the option of the Water System, as a whole or in part at any time, at a redemption price of 101% during July 1, 2009 through June 30, 2010 and 100% thereafter. The Water System Revenue Bonds are subject to mandatory redemption if (i) any significant part of the water system shall be damaged, destroyed, taken, or condemned or (ii) any for-profit non-governmental investor shall acquire an ownership interest in some or all assets of the Water System.

On January 16, 2003, VIPA issued the Marine Revenue Bonds Series 2003A (AMT) and 2003B (federally taxable) with principal amounts of approximately \$18 million and \$17.4 million, respectively. VIPA is using the proceeds of the bonds to finance the dredging, rehabilitation, and construction of berthing piers for seagoing vessels and cruise ships and mixed use commercial facilities on the island of St. Thomas.

On October 20, 2003, VIPA issued the Marine Revenue Bonds Series 2003C (non-AMT), in the amount of \$3 million with an authorized principal amount not to exceed approximately \$10.8 million. VIPA is using the proceeds of the bonds to finance the completion of several projects of rehabilitation and construction of berthing piers and dredging for cruise and seagoing vessels on the island of St. Thomas.

The bonds' indentures contain certain account restrictions and funding covenants to cover interest, debt service, maintenance, and other costs as specified in the corresponding bond indentures.

The bonds' indentures also specify certain debt service coverage requirements determined from net available revenue of the Rohlsen Terminal, Airport System and the Marine Division. The provisions of each of the bonds' indentures require that rates and fees charged for the use of each facility should be sufficient to generate enough revenue to pay all operation and maintenance expenses, exclusive of depreciation and certain noncash charges, of the respective facilities, plus: (i) at least 125% of the principal and interest and redemption account sinking fund deposit requirement of each of the bonds becoming due during such year; (ii) the amount of the debt service reserve fund deposit requirement for such period; (iii) the deposit required to the Renewal and Replacement Fund; and (iv) the amount of the capital improvements appropriations for such period. The Management of VIPA asserts that VIPA has complied with all bond indenture requirements.

### Notes to Basic Financial Statements (continued)

### **10.** Long-Term Liabilities (continued)

#### **Component Units – Bonds Payable (continued)**

VIHFA issued the 1995 A Revenue Bonds in the amount of \$6.2 million, and the 1998 A Revenue Bonds, in the amount of \$3 million, for the purpose of building single-family housing. The indenture agreements for the bonds require the VIHFA to deposit with the trustee the full amount of the bond proceeds, to purchase Government National Mortgage Association (GNMA) certificates. The servicer is obligated to pay the principal and interest due on the GNMA certificates to the trustee in an amount equal to the scheduled principal and interest payments of the underlying mortgages. All mortgage loans issued by the VIHFA must be originated by the participants and secured by a first priority mortgage lien on the applicable single-family residences.

Fixed maturities required to pay principal and interest on discretely presented component units' bonds payable with fixed maturities at September 30, 2006 are as follows (expressed in thousands):

Year	F	rincipal	]	Interest	Total		
2007	\$	10,975	\$	14,179	\$	25,154	
2008		11,518		14,132		25,650	
2009		12,093		13,582		25,675	
2010		12,718		12,991		25,709	
2011		13,369		11,795		25,164	
2012 - 2016		65,284		49,008		114,292	
2017 - 2021		72,495		29,457		101,952	
2022 - 2026		41,550		14,440		55,990	
2027 - 2031		25,580		6,027		31,607	
2032 - 2035		11,345		1,272		12,617	
Total		276,927	\$	166,883	\$	443,810	
Plus unamortized premium		5,084					
Less unamortized discount		(788)					
Less deferred amount on debt refunding and reacquisition costs		(4,406)					
Bonds payable, net	\$	276,817					

Notes to Basic Financial Statements (continued)

### **11. General Tax Revenue**

For the year ended September 30, 2006, general tax revenue of the PG consisted of the following (expressed in thousands):

		General Fund		FA Debt vice Fund	A Capital rojects	Gov	Other ernmental Funds	 Total
Income taxes Real property taxes Gross receipts taxes Other taxes	\$	507,061 16,570 	\$	- 139,912 47,131	\$ 2,250	\$	- 19,916 250 9,383	\$ 507,061 36,486 142,412 175,627
Tax revenue	\$	642,744	\$	187,043	\$ 2,250	\$	29,549	861,586
Tax revenue not recogni	zed on the	e modified acc	rual ba	isis				 10,522
Total tax revenue - g	overnmen	t-wide						\$ 872,108

### **12.** Commitments and Contingencies

### **Primary Government**

The current labor relations environment of the Government is defined by 13 distinct labor organizations subject to approximately 26 collective bargaining agreements. Fourteen bargaining units are without collective bargaining agreements. As specific disciplines are not grouped under a single pay plan, it is common to have clerical and nonprofessional workers in different departments throughout the Government, represented by different unions. Of the approximately 9,600 government workers, including employees of the executive branch of the Government, approximately 7,200 belong to unions. The present collective bargaining statute requires binding arbitration for certain classified employees in the event of an impasse during salary negotiations between the Government and any union. Under this process, each side chooses an arbitrator and a third impartial arbitrator is selected by the chosen arbitrators. The arbitration panel investigates and reviews the issues in dispute and renders a final and binding decision. For other classified employees, the Government must decide to go to impasse or to enjoin any strike. The Government has contractual liabilities for retroactive union arbitration salary increases estimated at \$272 million accruing from fiscal years 1993 through 2006. Pursuant to Title 24 of the V.I. Code Section 374(h), no such contractual amount is due until appropriation of funds is made

Notes to Basic Financial Statements (continued)

### 12. Commitments and Contingencies (continued)

### **Primary Government (continued)**

by the Legislature. Upon action of the Legislature, the General Fund will have the responsibility to satisfy the obligations arising from the retroactive wages. Until such time, the liability is recorded as a long-term debt in the governmental activities column in the government-wide financial statements.

The Government receives financial assistance from the federal government in the form of loans, grants, and entitlements. Loans received are described in note 9(c). Monetary and nonmonetary federal financial assistance amounted to approximately \$121.1 million and \$25.3 million, respectively, for the year ended September 30, 2006.

Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of resources for eligible purposes. Substantially, all grants are subject to audit under OMB Circular A-133. Disallowances as a result of these audits may become liabilities of the Government.

Management of the Government believes that the future outcome of any changes in federal financial assistance programs will not have a material effect on the basic financial statements.

On September 23, 2002, the Government entered into a three-year compliance agreement with the U.S. Department of Education requiring that the Government develop integrated and systemic solutions to problems in managing its federally funded education programs. The compliance agreement focuses on the areas of program design and evaluation, financial management, human capital, and property management and procurement. The compliance agreement expired on September 23, 2005. The Government had not fully complied with all terms and conditions of the compliance agreement. The U.S. Department of Education subsequently implemented a special condition for the Government to designate a third-party fiduciary to administer U.S. Department of Education grants. The terms and conditions of the original compliance agreement have been extended until the Government is in full compliance with the agreement.

Notes to Basic Financial Statements (continued)

### 12. Commitments and Contingencies (continued)

### **Primary Government (continued)**

The Government is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Title 33, Section 3411(c) of the V.I. Code, no judgment shall be awarded against the Government in excess of \$25,000 for tort claims filed under Government statutes. In cases involving several survivors, each award must be construed separately for purposes of applying the limitation upon recovery imposed by the Tort Claims Act. Under Title 27, Section 166(e) of the V.I. Code, the Government's waiver of immunity is expanded to \$250,000 for medical malpractice actions, including actions for wrongful death based on malpractice. Under certain circumstances, as provided in Title 33, Section 3414 of the V.I. Code, the Government may assume the payment of a judgment entered against an officer or employee who acted reasonably and within the scope of his employment. The Government may pay up to a maximum amount of \$100,000 of the settlement. With respect to pending and threatened litigation, the Government has accrued a provision for legal claims and judgments of approximately \$16 million for awarded and anticipated unfavorable judgments as of September 30, 2006. Management believes that the ultimate liability in excess of amounts provided would not be significant.

Changes in the reported estimated litigation payable resulted from the following activity (expressed in thousands):

	Fis	Beginning Fiscal Year Liability		ims and anges in timates	Claim syments	Ending Fiscal Year Liability	
2005 - 2006	\$	23,043	\$	(7,209)	\$ (1,813)	\$	14,021

Notes to Basic Financial Statements (continued)

### 12. Commitments and Contingencies (continued)

### **Primary Government (continued)**

The breakdown of the estimated litigation payable at September 30, 2006 is as follows (expressed in thousands):

<b>Governmental Activities</b>	
Current portion of estimated litigation payable	\$ 450
Long-term portion of estimated litigation payable	13,571
	\$ 14,021

As of September 2002, the Government was a defendant in a lawsuit regarding the assessment of property taxes. Under the lawsuit, taxpayers asserted that properties should be assessed at actual value in accordance with the Organic Act of 1933. The U.S. District Court agreed with the plaintiffs and, in May 2003, imposed an injunction on the collection of real property taxes for years subsequent to 1998. The Government complied with the Court order to develop a plan to implement the new valuation method, and the injunction was lifted in August 2003. Revised property assessments were mailed to taxpayers in June 2007.

State and federal laws and regulations require the Government to place a final cover on its landfill sites when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although closure and post-closure care costs will be paid only near or after the date that the landfill stops accepting waste, the Government reports a portion of these closure and post-closure care costs as an operating expense in each period based on landfill capacity used as of each balance sheet date. The \$32.7 million reported as landfill closure and post-closure care liability at September 30, 2006, represents the cumulative amount recorded to date based on the use of the estimated capacity of each landfill. The Government will recognize the remaining estimated cost of closure and post-closure care of \$8 million as the remaining estimated capacities are filled. These amounts are based on what it would cost to perform all closure and post-closure care in 2006.

Notes to Basic Financial Statements (continued)

### 12. Commitments and Contingencies (continued)

### **Primary Government (continued)**

The estimated used capacity and expected closure of each of the Government landfills is as follows:

Landfill	Estimated Used Capacity	Estimated Closure Date
Bovoni	61%	2020
Angilla	88%	2010
Susannaberg	100%	1993

Actual cost may be higher due to inflation, changes in technology, or changes in regulations. The Government is required by state and federal laws and regulations to make annual contributions to a trust to finance closure and post-closure care. The Government began making annual contributions to a trust in fiscal year 2007 to finance closure and post-closure costs. The Government expects that future inflation costs will be paid from interest earnings on these annual contributions. However, if interest earnings are inadequate or additional post-closure care requirements are determined (due to changes in technology or applicable laws or regulations, for example), these costs may need to be covered by charges to future landfill users.

Since 1985, the Government has been subject to a consent decree issued by the Virgin Islands District Court, governing the operation of its wastewater treatment plants. The consent decree was amended in 1996 and further modified with the 2002 Stipulation to the Amended Consent Decree (the Stipulation) to establish deadlines for the construction of new secondary treatment facilities, including the replacement of the existing St. Croix and Airport Lagoon (Charlotte Amalie) wastewater treatment plants. The Stipulation requires that the new St. Croix wastewater treatment plants be completed by the end of 2005 and the new Charlotte Amalie wastewater treatment plants be completed by the end of 2006. The cost of both facilities is estimated at approximately \$50 million. The Stipulation also establishes certain interim deadlines and performance standards that must be met by the Government pending completion of the new facilities. In addition, the Stipulation establishes specified penalties for violation of any of the deadlines or performance standards set forth therein. As of the date of the basic financial statements, the Government is current on all of its outstanding obligations pursuant to the

Notes to Basic Financial Statements (continued)

### 12. Commitments and Contingencies (continued)

### **Primary Government (continued)**

Stipulation. In January 2004, the Government's Legislature authorized the creation of the Virgin Islands Waste Management Authority (WMA) for the purpose of meeting environmental requirements of waste treatment in the U.S. Virgin Islands. In December 2004, the PFA issued revenue bonds amounting to \$94 million for the purpose of constructing and rehabilitating wastewater treatment plants noted above.

On August 21, 2002, the Government and the United States Environmental Protection Agency (EPA) entered into a memorandum of understanding documenting the EPA's agreement to support the renewal of the Territorial Pollutant Discharge Elimination System permit for its St. Croix distillery operations provided that the Government make certain funding available to (i) conduct treatability studies regarding the Virgin Islands Rum Industries, Ltd. effluent and the means to mitigate its potential environmental effects in the vicinity of the discharge, (ii) identify practicable, available, reliable, and cost-effective potential mitigation measures, and (iii) implement (or assist in the implementation of) such mitigation measures in the event such measures are determined by the V.I. Department of Planning and Natural Resources after consultation with EPA to be necessary and appropriate. Pursuant to the memorandum of understanding, the Government's obligation to fund such activities is limited to \$6 million in the aggregate, commencing on October 13, 2003. In June 2004, the Government entered into a three years contract with a locally licensed environmental consulting firm to facilitate the Government's commitments with the memorandum of understanding with the EPA.

In September 2004, the Government became a defendant in a lawsuit regarding the assessment of franchise taxes. Under the lawsuit, taxpayers asserted that franchise taxes should be assessed in accordance with Title 13 Virgin Islands Code Section 531(a). The plaintiff taxpayers interpret the definition of "capital stocks used in conducting business in the Virgin Islands" in the V.I. Code as tax collected only on the par value of the stock, while the Government's position is that the amount allocated should be over the par value and additional paid-in capital upon a subsequent reorganization. The Government also imposed a six-year statute of limitations on tax refund claims against the Government. Management believes that the ultimate liability of this case would not have a material adverse impact on the Government's overall financial position as reported in the government-wide financial statements.

Notes to Basic Financial Statements (continued)

#### **12.** Commitments and Contingencies (continued)

#### **Discretely Presented Component Units**

In September 1989, WAPA electric facilities were damaged by Hurricane Hugo. WAPA reconstructed the facilities with proceeds from insurance and FEMA. Subsequent to the receipt of funds, FEMA deobligated approximately \$7.9 million in questioned costs. Approximately \$2.6 million of these questioned costs related to an oil spill that was subsequently settled with FEMA. During 1998, WAPA submitted a second appeal for \$4.4 million of the remaining questioned costs, and agreed to refund approximately \$900 thousand. During 1999, FEMA denied the second appeal and formally closed the disaster claim. WAPA has recorded a liability for \$5.3 million related to the questioned costs. FEMA has not made a formal request for repayment of the funds.

In September 2004, WAPA electric facilities sustained damages amounting to \$1.3 million due to Tropical Storm Jeanne. WAPA reported \$978 thousand as a FEMA claim receivable for the year ended June 30, 2006.

WAPA estimates that capital expenditures in connection with continuing capital improvements will be approximately \$82.8 million for the Electric System and \$7.2 million for the Water System during the year ended June 30, 2007.

The VIHA terminated a development contract in September 2001 pursuant to a clause in the contract that provided for termination for convenience. The other party has sued and claims damages in excess of \$7 million. The Authority has filed a counterclaim. It is not possible to predict the eventual outcome of this case nor estimate any amount or range of potential loss in the event of an unfavorable outcome.

Several former employees have individually filed suits against the VIHA for wrongful discharge over the period 1997 through 2002. None of the cases are resolved and it is not possible to predict the eventual outcome, nor estimate the amount or range of potential loss in the event of an unfavorable outcome.

A subcontractor has sued the VIHA for nonpayment for work done in 2000. It is not possible to predict the eventual outcome nor estimate the amount or range of potential loss in the event of an unfavorable outcome.

Notes to Basic Financial Statements (continued)

#### 12. Commitments and Contingencies (continued)

#### **Discretely Presented Component Units (continued)**

In 2002, the Federal Aviation Administration (FAA) conducted an on-site wildlife evaluation of the St. Croix landfill, which is located next to the St. Croix airport. The FAA determined that the landfill posed an environmental and navigational threat to the airport due to flocks of birds that reside in the landfill area. The FAA may require VIPA to repay \$9.3 million in federal grants and has refused further discretionary grants for the airport until VIPA shows progress toward closing the landfill. The landfill is under the jurisdiction of the PG. The PG has negotiated a remediation plan with FAA to close the landfill within the next four years. FAA accepted the plan, if such measures are implemented.

In connection with the purchase of lands adjacent to the airport, VIPA was awarded federal financial assistance in 2002 amounting to \$8 million under a Real Property Acquisition Relocation Assistance Program. VIPA is in noncompliance with certain federal requirements of the assistance program. Noncompliance with requirements of federal financial assistance programs may result in a refund of the funds granted. VIPA management believes that noncompliance instances should not materially affect VIPA's financial position.

In 2006, the JFL Medical Center entered into an agreement for the construction of a Cancer Institute on the island of St. Croix. As of September 30, 2006, the Medical Center had outstanding contracts and commitments of \$13 million.

WAPA, VIPA, and other discretely presented component units are presently a defendant or codefendant in various lawsuits. The financial managers of the component units have advised the PG that any adverse outcome involving a material claim is expected to be substantially covered by insurance. Government property is exempt from lien, levy, or sale as a result of any judgment under the Virgin Islands Code.

Notes to Basic Financial Statements (continued)

### **13. Retirement Systems**

#### **Plan Description**

GERS is the administrator of a cost-sharing multiple-employer defined-benefit pension plan established as of October 1, 1959 by the Government to provide retirement, death, and disability benefits to its employees. The following description of the plan is provided for general information purposes only. Refer to the actual text of the retirement law in the V.I. Code, Title 3, Chapter 27 for more complete information. Regular employees are eligible for a full-service retirement annuity when they have completed 30 years of credited service or have attained the age of 60 with at least 10 years of credited service. Members who are considered "safety employees," as defined in the V.I. Code, are eligible for full retirement benefits when they have earned at least 20 years of government service or have reached the age of 55 with at least 10 years of credited service. Regular employees who have attained the age of 50 with at least 10 years of credited service are early with a reduced benefit. Senators and members of the Legislature may receive a retirement annuity when they have attained the age of 50 and completed six years of credited service or earned at least six years of credited service as a member of the Legislature.

The monthly annuity benefit payment is determined by applying a stipulated benefit ratio to the member's average compensation. Average compensation is determined by averaging the three highest years of salary the member earned within the last 10 years of service. The maximum annual salary that can be used in this computation is \$65,000 except for senators and judges, whose annual salary is used. The annuity payment to retirees 60 years or older increases by 1.5% of the original amount on July 1 of each year after the first year of payments.

GERS is a blended component unit included in the financial reporting entity and is presented as a pension trust fund of the PG. GERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Employees' Retirement System of the Government of the Virgin Islands, 3438 Kronprindsens Gade, Veterans Drive, St. Thomas, VI 00802.

#### **Funding Policy**

Contributions to GERS are made by the Government and the members. Government and members contributions are not actuarially determined but are set by statute. The Government and members' contributions together with the income of GERS should be sufficient to provide an adequate actuarially determined reserve for the benefits prescribed by the VI Code.

Notes to Basic Financial Statements (continued)

#### 13. Retirement Systems (continued)

#### **Funding Policy (continued)**

The contributions required to fund GERS on an actuarial reserve basis are calculated periodically by the GERS actuarial consultant. The actuarial valuation as of September 30, 2003, performed on an entry age basis, indicates that the current combined statutory employer and employee contribution rates are not sufficient to meet the cost of GERS on an actuarial basis, as required by law.

The Government's required contribution for the year ended September 30, 2006 was 14.5% of the members' annual salary. Since April 1, 1991, required member contributions are 8% of annual salary for regular employees, 9% for senators, 11% for judges, and 10% for Act 5226 eligible employees. Through September 30, 2000, member contributions were refundable without interest upon withdrawal from employment before retirement. Effective June 29, 2000, legislation was passed that provided for 4% annual interest on refunded contributions. The Government's contractually required contributions, actual contributions made, and percentage contributed to the plan for the years ended September 30, 2006, 2005, and 2004, have been estimated based on the 2003 actuarial valuation as follows (expressed in thousands):

	Re	tractually equired tributions	tributions Made	Percentage Contributed
2004	\$	54,085	\$ 54,085	100%
2005	\$	51,542	\$ 51,542	100%
2006	\$	65,061	\$ 65,061	100%

In August 1994, legislation providing an early retirement incentive was passed. The legislation was subsequently amended on October 13, 1994, December 30, 1994, and December 5, 1995. Among other matters, the legislation allows a member of GERS who has a combined aggregate number of years of credited service plus number of years of age, equal to at least 75 years as of the date of the legislation, to retire without reduction of annuity. Members, who have attained the age of 50 with at least 10 but less than 30 years of credited service, may add an additional three years to their age for this computation. Members with 30 years of service or who can retire without penalty under the V.I. Code shall have their average compensation increased by four percentage points.

Notes to Basic Financial Statements (continued)

### 13. Retirement Systems (continued)

#### **Funding Policy (continued)**

For each employee electing to retire pursuant to Section 8(a) of the Early Retirement Act of 1994 (the Act), the Government contributes to GERS, on a quarterly basis, an amount equal to the employer and employee contributions that would have been made until the employee reached the age of 62 had the employee not elected to retire under this provision.

For employees electing to retire under Section 8(b) of the Act, the Government contributes to GERS a sum equal to the additional contribution the employer and employee would have made had the employee received a salary 4% higher during the three years used to compute the employee's average compensation figure plus a sum of \$5,000. Based on this calculation, the amount was \$26.3 million as of September 30, 2006. As of September 30, 2006, GERS has received \$25.9 million of such amount.

The actuaries of GERS have determined that the specific funding provided under the Act is inadequate to cover the costs of the program. GERS is seeking to recover any unfunded costs of the program under a newly enacted provision of the retirement law, which provides that the Primary Government will compensate GERS for the costs of any special early retirement program.

The University has two retirement plans in which all eligible employees are required to participate. The Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF) is a defined-contribution pension plan covering participating, full-time faculty members and other exempt employees, under which the contributions, including employees' contributions, are used to purchase annuities. There are no unfunded past service costs, and vested benefits are equal to the annuities purchased under TIAA-CREF. As of September 30, 2006, 241 faculty members and other employees were TIAA-CREF participants. The number of active participants from the University participating in GERS as of September 30, 2006 was 275. Total contributions made by the University to TIAA-CREF and GERS participant accounts amounted to \$1.9 million and \$1.2 million, respectively.

Notes to Basic Financial Statements (continued)

#### 14. Liquidity

At September 30, 2006, the Government had an unrestricted net deficit in the governmental activities amounting to \$330.1 million, mostly attributable to approximately \$1.6 billion in long-term debt that was issued to provide resources for working capital and other noncapital related purposes. The Government has initiated specific actions to improve its liquidity and cash flows through the issuance of long-term debt, engaging a consulting firm to assist in its efforts to develop a series of detailed revenue enhancement and expenditure reduction initiatives and the enactment of certain laws directed toward improving the Government's financial situation.

In 1999, the Government and the U.S. Department of Interior (DOI) entered into a memorandum of understanding (the MOU) whereby the Government agreed to use its best efforts to undertake certain deficit reduction initiatives. The Department of Interior agreed to provide additional financial assistance and financial incentives if the initiatives were successfully implemented. The deficit reduction measures were not implemented to the satisfaction of the Department of Interior as noted in an audit report released by DOI in January 2003. Subsequent negotiations to extend the MOU were not successful and the agreement lapsed in fiscal year 2006.

In April 2000, the Economic Recovery Task Force submitted the five-year operating and strategic financial plan to the Governor for action. The plan provides over 200 recommendations that propose to reduce and eventually eliminate the structural budget deficit by restructuring and reforming Government operations and forging a partnership with the private sector intended to result in sustained growth.

#### **15. Restatements of Net Assets and Fund Balances**

#### **Primary Government – Governmental Funds**

The beginning fund balance of the General Fund was restated by \$62.9 million due to the recognition of an allowance for component unit receivables amounting to \$30.9 million and the reclassification of certain revolving funds amounting to \$32 million eliminated in prior years for financial reporting.

Notes to Basic Financial Statements (continued)

#### 15. Restatements of Net Assets and Fund Balances (continued)

#### **Primary Government – Governmental Funds (continued)**

The beginning fund balance of the General Fund was adjusted for transfers to component units from certain revolving funds of the Government (in thousands):

General Fund	As Previously Reported	Adjustments	As Restated
Fund balance	\$ 180,102	\$ (62,872)	\$ 117,230

Beginning net assets of governmental funds were restated to correct: (1) an error in the accrued union arbitration liability calculation that resulted in a reduction of \$132.7 million, (2) an error in the accrued federal questioned grant expenditures that resulted in a reduction of \$6 million, (3) a reclassification of certain funds for financial reporting resulting in a decrease in net assets of \$62.9 million and (4) a duplication of capital assets recorded in a discretely presented component units of \$89.6 million, for a net adjustment of \$13.8 million as follows:

	Beginn	ing Net Asse	ets
	As		
	Previously		As
	Reported Ad	justments	Restated
Net deficit	\$ (192,332) \$	(13,768)	\$ (206,100)

#### **Primary Government – Business Type Funds**

Beginning net assets of other business-type funds were restated due to the elimination of a revolving fund deficit amounting to \$8.4 million, which should have been included in the general fund.

Beginning net assets of the Virgin Islands Unemployment Insurance Fund (VIESA) was restated due to identification of Reed Act revenues from prior years amounting to \$2.2 million, which had been deferred and should have been recognized as revenues in prior years.

Notes to Basic Financial Statements (continued)

#### 15. Restatements of Net Assets and Fund Balances (continued)

#### **Primary Government – Business Type Funds (continued)**

Beginning net assets of business-type funds of the Government were restated to follows (in thousands):

	As		
	Previously		As
Business-Type Funds	Reported	Adjustments	Restated
Other business-type funds: Funds reclassified for financial reporting	\$ 2,294	\$ 8,401	\$ 10,695
Unemployment insurance: Reed Act grants expended	\$ 30,046	\$ 2,161	\$ 32,207
Business-type activities	\$ 64,892	\$ 10,562	\$ 75,454

#### **Component Units**

Beginning net assets of four discretely presented component units were restated in accordance with financial accounting standard APB No. 20, to correct material errors identified in prior years as follows (expressed in thousands):

Component Unit	As reviously leported	Ad	justment	R	As Restated
Virgin Islands Housing Authority	\$ 63,818	\$	6,577	\$	70,395
Virgin Islands Housing Finance Authority	27,179		9,097		36,276
Roy L Schneider Medical Center	72,429		(315)		72,114
Magens Bay Authority	3,878		(43)		3,835
Waste Management Authority	_		3,169		3,169
Other component units	 493,205		_		493,205
Net Assets	\$ 660,509	\$	18,485	\$	678,994

Notes to Basic Financial Statements (continued)

#### **16. Subsequent Events**

#### **Primary Government**

In August 2006, the PG entered into a contract with an independent contractor to serve as a thirdparty administrator of federal education grants. This administration of grants began October 1, 2006. The contract is the result of an agreement with the U.S. Department of Education, following the conclusion of a three year compliance agreement which expired in September 2005.

In November 2006, the U.S. Department of the Treasury issued final regulations determining residency for U.S. territories and possessions as required by the American Jobs Creation Act passed in October 2004. The PG continues to pursue further revisions to these regulations.

In December 2006, the PG entered into a marketing agreement with local rum makers. Under the terms of the agreement, rum makers will make an initial investment of \$61 million to promote Virgin Islands rum products. The PG committed to pay 35 percent (35%) of additional excise tax revenues received from the federal government resulting from the marketing campaign.

In December 2006, the federal government passed a two-year extension of the PG's rum tax rebate provision. Under the terms of the extension, the per proof gallon rebate of \$13.25 will be retroactive to January 1, 2006 and continue through December 31, 2007. In November 2007 the rebate provision was again extended through December 2009.

In March 2007, the PG authorized an extension of a \$104 million private activity bond allocation used to upgrade capital infrastructure at the Hovensa oil refinery located on the island of St. Croix.

In June 2007, the President signed legislation providing authority to the PG to administer the territorial property tax system.

In July 2007, the US District Court ruled the four percent (4%) personal use tax assessed on items valued at more than \$1,000 and shipped to the territory as unconstitutional. The PG is contesting this ruling.

Notes to Basic Financial Statements (continued)

## **16.** Subsequent Events (continued)

### **Primary Government (continued)**

In January 2008, the PFA approved the issuance of \$108 million dollars in private activity bonds to be issued on behalf of the HOVENSA oil refinery. These bonds will be issued utilizing the 2007 and 2008 annual tax exempt cap for the PFA

In February 2008, the federal government passed an Economic Stimulus Act providing taxpayer rebates ranging from \$300 to \$1,200 depending on taxpayer income and filing status. Under the terms of the Act, the PG will be reimbursed by the federal government for rebates provided to taxpayers. Payments to taxpayers were sent out beginning in June 2008.

In March 2008, the PG passed legislation introducing new property tax rates. Property tax assessments for 2006, and for 2007, have been delayed pending this legislation.

### **Component Units**

In June 2007, the Virgin Islands Water and Power Authority (WAPA) issued the Electric System Subordinated Revenue Series 2007A Bonds amounting to \$57.6 million for capital improvement projects.



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# 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

The Honorable Governor of the Government of the United States Virgin Islands:

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Government of the United States Virgin Islands (the Government) as of and for the year ended September 30, 2006, which collectively comprise the Government's basic financial statements, and have issued our report thereon dated March 16, 2009. Our report was modified to include a reference to other auditors. In addition, the scope of our audit work was not sufficient to enable us to express, and we did not express, an opinion on the business-type activities and aggregate remaining fund information as of September 30, 2006, and the changes in financial position for the year then ended, because of the matters discussed below:

- a. The effects of the adjustments as might have been determined to be necessary, had the other auditors been able to able to obtain sufficient audit evidence to determine whether capital assets of \$305 thousand, accounts receivable of \$1 million, and due to the general fund of \$4.5 million in the financial statements of the Virgin Islands Lottery (VI Lottery) were fairly stated.
- b. The basic financial statements do not include a liability for workers' compensation claims and, accordingly, the Government has also not recorded an expense for the current period change in that liability. The Government's records do not permit, nor is it practical to extend our auditing procedures sufficiently to determine the extent by which the business-type activities and aggregate remaining fund information may have been affected by this condition.

In addition, our auditors' report for opinion units other than business-type activities, based on our audit and the reports of other auditors, was qualified for the following:

• The effect of the adjustments, if any, as might be determined to be necessary, had the other auditors been able to obtain sufficient audit evidence to determine whether 1) land held for sale amounting to \$25 million in the financial statements of VIHFA and 2) loan receivables of \$2.1 million in the financial statements of VIEDA, were fairly stated, as described in paragraphs four and five of the Report of Independent Auditors.



Except as described above, we conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Other auditors audited the financial statements of the Virgin Islands Public Finance Authority (PFA), the West Indian Company, the Tobacco Settlement Financing Corporation, Virgin Islands Housing Authority (VIHA), Virgin Islands Public Television System, Virgin Islands Lottery (VI Lottery), Virgin Islands Economic Development Authority (VIEDA), Magens Bay Authority, Virgin Islands Government Hospital and Health Facilities Corporation (Roy L. Schneider Hospital and Juan F. Luis Hospital and Medical Center), Employees' Retirement System of the Government of the Virgin Islands (GERS), and the Virgin Islands Housing Finance Authority (VIHFA), as described in our report on the Government's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the PFA, Juan Luis Hospital and Medical Center, Magens Bay Authority, Tobacco Settlement Financing Corporation, Waste Management Authority, and Employees' Retirement System of the Government of the Virgin Island were not audited in accordance with Government Auditing Standards.

#### Internal Control over Financial Reporting

In planning and performing our audit, we considered the Government's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Government's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 06-01 through 06-05.



A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. We consider items 06-01 through 06-05 to be material weaknesses.

#### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Government'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 an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and that is described in the accompanying schedule of findings and questioned costs as item 06-02.

This report is intended solely for the information and use of management, others within the entity, 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.

Ernst + Young LLP

March 16, 2009

# Single Audit Report Section



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# Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control over Compliance in Accordance with OMB Circular A-133

The Honorable Governor of the Government of the United States Virgin Islands:

#### Compliance

We have audited the compliance of the Government of the United States Virgin Islands (the Government) with the types of compliance requirements described in the US Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major Federal programs for the year ended September 30, 2006. The Government'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 Government's management. Our responsibility is to express an opinion on the Government's compliance based on our audit.

The Government's basic financial statements include the operations of the discretely presented component units (as defined in the notes to the Government's basic financial statements) some of which received Federal awards, which are not included in the Schedule of Expenditures of Federal Awards during the year ended September 30, 2006. Our audit described below did not include the operations of the aforementioned component units because the component units engaged other auditors to perform an audit in accordance with OMB Circular A-133.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States; 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 Government's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Government's compliance with those requirements.



The Government did not comply with the types of compliance requirements that are applicable to each major Federal program as described in the accompanying schedule of findings and questioned costs and referenced by finding number below:

CFDA Number	Major Program	Compliance Requirement	Finding Reference
10.555, 10.559	Child Nutrition Cluster	Reporting	06-06, 06-07
84.027	Special Education – State Grant Program	Activities Allowed or Unallowed Allowable Costs/Cost Principles Cash Management Equipment and Real Property Management Period of Availability of Federal Funds	06-16 06-16 06-16 06-17 06-16
84.298	Innovative Education Program Strategies	Activities Allowed or Unallowed Allowable Costs/Cost Principles Cash Management Equipment and Real Property Management Period of Availability of Federal Funds	06-18 06-18 06-18 06-19 06-18
93.563	Child Support Enforcement	Activities Allowed or Unallowed Allowable Costs/Cost Principles Cash Management Period of Availability of Federal Funds	06-20 06-20 06-21 06-20
93.778	Medical Assistance Program	Reporting Eligibility Special Tests and Provisions	06-22 06-23 06-24, 06-25

Compliance with such requirements is necessary, in our opinion, for the Government to comply with the requirements applicable to those programs.

In our opinion, because of the effects of the noncompliance described in the table above, the Government did not comply, in all material respects, with the requirements referred to above that are applicable to the following major programs: Child Nutrition Cluster (CFDA No. 10.555 and CFDA No. 10.559), Special Education – State Grant Program (CFDA No. 84.027), Innovative Education Program Strategies (CFDA No. 84.298), Child Support Enforcement (CFDA No. 93.563), and Medical Assistance Program (CFDA No. 93.778) for the year ended September 30, 2006.



The Government did not comply with the types of compliance requirements that are applicable to the major Federal program as described in the accompanying schedule of findings and questioned costs and referenced by the finding numbers below:

CFDA Number	Major Program	<b>Compliance Requirement</b>	Finding Reference
66.605	Performance Partnership Grants	Activities Allowed or Unallowed	06-13
		Allowable Costs/Cost Principles	06-13
		Cash Management	06-13
		Equipment and Real Property Management	06-14
		Period of Availability of Federal Funds	06-13

Compliance with such requirements is necessary, in our opinion, for the Government to comply with the requirements applicable to this program.

Also, in our opinion, except for the noncompliance described in the table above, the Government complied, in all material respects, with the requirements referred to that are applicable the following major program: Performance Partnership Grants (CFDA No. 66.605), for the year ended September 30, 2006.

Moreover, in our opinion, the Government complied, in all material respects, with the requirements referred to in the first paragraph, that are applicable to each of its major Federal programs other than those major programs referred to in the two preceding paragraphs for the year ended September 30, 2006.

The results of our auditing procedures also disclosed other instances of non-compliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 06-08, 06-09 and 06-12.

#### Internal Control over Compliance

The management of the Government 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 the Government's internal control over compliance with requirements that could have a direct and material effect on a major Federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.



We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Government's ability to administer a major Federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 06-06 through 06-26.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major Federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 06-06, 06-07, 06-10, 06-11, 06-13, 06-14, 06-15, 06-16, 06-17, 06-18, 06-19, 06-20, 06-21, 06-22, 06-23, 06-24, 06-25, and 06-26, to be material weaknesses.

This report is intended solely for the information and use of the Honorable Governor of the Government of the United States Virgin Islands, 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.

Ernst + Young LLP

March 11, 2009

# Schedule of Expenditures of Federal Awards

# Year Ended September 30, 2006

Federal CFDA		Federal
Number	Federal grantors/Program or cluster title	Expenditures
	U.S. Department of Agriculture	
10.025	Plant and Animal Disease, Pest Control, and Animal Care	\$ 354,280
10.555	National School Lunch Program	6,061,264
10.559	Summer Food Service Program for Children	520,601
	Child Nutrition Cluster total	6,581,865
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children	5,047,959
10.558	Child and Adult Care Food Program	45,068
10.560	State Administrative Expenses for Child Nutrition	312,630
10.551	Food Stamps	20,591,784
10.561	State Administrative Matching Grants for Food Stamp Program (a)	4,571,391
	Food Stamps total	25,163,175
10.568	Emergency Food Assistance Prgram (Administrative Costs)	28,661
10.574	Team Nutrition Grants	14,561
10.664	Cooperative Foresty Assistance	316,955
10.911	Watershed Surveys and Planning	154,040
		38,019,194
	<b>U.S Department of Commerce</b>	
11.302	Economic Development Support for Planning Organizations	53,208
11.407	Interjudisdictional Fisheries Act of 1986	10,047
11.419	Coastal Zone Management Administration Awards	1,201,155
11.426	Financial Assistance for National Centers for Coastal Ocean Science	77,643
11.433	Marine Fisheries Initiative	41,315
11.434	Cooperative Fisheries Statistics	163,325
11.435	Southeast Area Monitoring and Assessment Program	15,676
11.441	Regional Fishery Management Councils	12,945
11.463	Habitat Conservation	11,210
		1,586,524
	<b>U.S Department of Defense</b>	
12.401	National Guard Military Operations nad Maintenance (O&M) Projects	2,851,324
	U.S Department of Housing and Urban Development	
14.218	Community Development Block Grants/ Entitlement Grants	1,612,346
14.225	Community Development Block Grants/ Special Purpose Block	
	Grants/Insular Areas	146,492
14.246	Community Development Block Grants/Economic Development Initiative	697
		1,759,535

Federal CFDA		Federal
Number	Federal grantors/Program or cluster title	Expenditures
	<b>U.S Department of the Interior</b>	
15.605	Sport Fish Restoration	540,917
15.611	Wildlife Restoration	158,189
	Fish and wildlife cluster total	699,106
15.612	Rare and Endangered Species Conservation	200,522
15.608	Fish and Wildlife Managmenet Assistance	119,351
15.615	Cooperative Endangered Species Conservation Fund	5,735
15.625	Wildlife Conservation and Restoration	12,366
15.633	Landower Incentive	37,049
15.875	Economic, Social, and Political Development of the Territories	2,206,795
15.904	Historic Preservation Fund Grants - In-Aid	366,291
15.616	Clean Vessel Act	13,420
		3,660,635
	<b>U.S Department of Justice</b>	
16.200	Community Relations Service	122,949
16.202	Offender Re-Entry Program	156,083
16.523	Juvenile Accountability Incentive Block Grants	383,846
16.540	Juvenile Justice and Deliquency Prevenion - Allocation to States	199,947
16.549	Part E State Challenge Activities	15,000
16.554	National Criminal History Improvement Program (NCHIP)	187,558
16.572	State Criminal Alien Assistance Program	6,654
16.575	Crime Victim Assistance	698,611
16.579	Edward Byrne Memorial Formula Grant Program	1,674,561
16.585	Drug Court Discretionary Grant Program	43,677
16.586	Violent Offender Incarceration and Truth in Sentencing Initiative Grants	21,760
16.588	Violence Against Women Formula Grants	656,904
16.592	Local Law Enforcement Block Grants Program	309,324
16.593	Residential Substance Abuse Treatment for State Prisoners	183,707
16.595	Community Capacity Developmetn Office	93,954
16.606	State Criminal Alien Assistance Program	107,028
16.710	Public Safety Partnership and Community Policing Grants	1,149,659
		6,011,222

Federal CFDA		Federal
Number	Federal grantors/Program or cluster title	Expenditures
	U.S Department of Labor	*
17.207	Employment Service/Wagner-Peyser Funded Activities	1,658,226
17.258	WIA Adult Program	2,320,022
17.259	WIA Youth Activities	570,361
	Workforce Investment Act cluster total	2,890,383
17.002	Labor Force Statistics	398,625
17.225	Unemployment Insurance	7,380,053
17.235	Senior Community Service Emplyment Program	863,058
17.503	Occupational Safety and Health State Program	203,289
17.504	Consultation Agreements	7,439
		13,401,073
	<b>U.S Department of Transportation</b>	
20.205	Highway Planning and Construction	5,929,898
20.218	National Motor Carrier Safety	394,764
20.500	Federal Transit - Capital Investment Grants	53,298
20.509	Formula Grants for Other than Urbanized Areas	331,957
20.513	Capital Assistance Program for Elderly Persons and Persons with Disabilities	244,190
20.600	State and Community Highway Safety - Highway Safety Cluster	375,527
		7,329,634
	National Foundation on the Arts and Humanities	
45.025	Promotion of Arts - Partnership Agreements	246,820
45.310	Grants to States - State Library Program	137,550
		384,370
	<b>U.S Enviromental Protection Agency</b>	
66.034	Surveys, Studies, Investigations, Demostrations and Special Purpose	
	Activities Relating to the Clean Air Act	27,093
66.418	Construction Grants for Watewater Treatment Works	981,159
66.454	Water Quality Management Planning	44,483
66.461	Regional Wetland Program Development Grants	10,392
66.468	Capitalization Grants for Drinking Water State Revolving Fund	555,825
66.472	Beach Monitoring and Notification Program Implementation Grants	250,927
66.474	Water Protection Grants to States	2,973

Federal CFDA Number	Federal grantors/Program or cluster title	Federal Expenditures
66.605	Performance Partnership Grants	2,459,081
66.606	Surveys, Studies, Investigations, and Special Purpose Grants	276,010
66.608	Environmental Information Exchange Network Grant Program and Related	270,010
00.000	Assistance	24,908
66.700	Consolidated Pesticide Enforcement Cooperative Agreements	28,509
66.805	Leaking Underground Storage Tank Trust Fund	48,766
66.817	State and Tribal Response Program Grants	111,594
00.017		4,821,720
	U.S Department of Energy	4,021,720
81.041	State Energy Program	636,611
011011		
	<b>U.S Department of Education</b>	
84.002	Adult Education - State Grant Program	891,199
84.027	Special Education - Grants to States	10,012,737
84.041	Impact Aid	123,197
84.048	Vocational Education - Basic Grants to States	720,495
84.126	Rehabilitation Services - Vocational Rehabilitation Grants to States	429,762
84.169	Independent Living - State Grants	175
84.177	Rehabilitation Services - Independent Living Services for Older Individuals	
	Who Are Blind	18,556
84.181	Special Education - Grants for Infants and Families with Disabilities	510,086
84.185	Byrd Honors Scholarships	60,000
84.186	Safe and Drug-Free Schools and Communities State Grants	276,192
84.187	Supported Employment Services for Individuals with Severe Disabilities	240
84.265	Rehabilitation Training State Vocational Rehabilitation Unit In-Service	9,350
84.298	State Grants for Innovative Programs	7,630,275
84.330	Advanced Placement Program	167,203
84.346	Vocational Education - Occupational and Employment Information State	10,704
84.357	Reading First State Grants	1,272,094
84.375	Academic Competitiveness Grants	240,930
84.998	Educational Improvement PartnershipsNational Programs Arts in Education	640
		22,373,835

Federal CFDA		Federal
Number	Federal grantors/Program or cluster title	Expenditures
1 (uniber	U.S. Department of Health and Human Services	Expenditures
93.003	Public Health and Social Services Emergency Fund	180,831
93.006	State and Territorial and Technical Assistance Capacity Development	,
	Minority HIV/AIDS Demonstration Program	10,824
93.045	Special Programs for the Aging-Title III, Part C-Nutrition Services	25,579
93.110	Maternal and Child Health Federal Consolidated Programs	89,160
93.116	Project Grants and Cooperative Agreements for Tuberculosis Control	96,692
93.127	Emergency Medical Services for Children	64,29
93.130	Primary Care Services Resource Coordination and Development	24,47
93.136	Injury Prevention and Control Research and State and Community Based	
	Programs	20,96
93.153	Coordinated Services and Access to Research for Women, Infants, Children,	
	and Youth	196,07
93.217	Family Planning-Services	812,85
93.224	Consolidated Health Centers (Community Health Centers, Migrant Health	
	Centers, Health Care for the Homeless, Public Housing Primary Care, and	
	School Based Health Centers)	161,46
93.235	Abstinence Education Program	34,00
93.243	Substance Abuse and Mental Health Services-Projects of Regional and	
	National Significance	717,26
93.256	State Planning Grants Health Care Access for the Uninsured	3,00
93.268	Immunization Grants	967,68
93.283	Centers for Disease Control and Prevention-Investigations and Technical	
	Assistance	1,179,22
93.558	Temporary Assistance for Needy Families	2,974,55
93.563	Child Support Enforcement	3,243,73
93.575	Child Care and Development Block Grant	1,919,58
93.597	Grants to States for Access and Visitation Programs	92,012
93.600	Head Start	9,830,89
93.617	Voting Access for Individuals with Disabilities-Grants to States	30,02
93.667	Social Services Block Grant	5,893,65
93.767	State Children's Insurance Program	2,078,81
93.778	Medical Assistance Program	5,815,224

# Schedule of Expenditures of Federal Awards (continued)

Federal CFDA		Federal
Number	Federal grantors/Program or cluster title	Expenditures
93.782	Medicare Transitional Drug Assistance Program for Territories	7,441
93.917	HIV Care Formula Grants	555,905
93.919	Cooperative Agreements for State-Based Comprehensive Breast and Cervical	
	Cancer Early Detection Programs	1,178
93.938	Cooperative Agreements to Support Comprehensive School Health Programs	
	to Prevent the Spread of HIV and Other Important Health Problems	1,056
93.943	Epidemiologic Research Studies of Acquired Immunodeficiency Syndrome	
	(AIDS) and Human Immunodeficiency Virus (HIV) Infection in Selected	
	Population Groups	510,299
93.944	Human Immunodeficiency Virus (HIV)/Acquired Immunodeficiency Virus	
	Syndrome (AIDS) Surveillance	234,021
93.958	Block Grants for Community Mental Health Services	140,252
93.959	Block Grants for Prevention and Treatment of Substance Abuse	520,070
93.977	Preventive Health Services-Sexually Transmitted Diseases Control Grants	233,747
93.988	Cooperative Agreements for State-Based Diabetes Control Programs and	
00.001	Evaluation of Surveillance Systems	141,965
93.991	Preventive Health and Health Services Block Grant	130,885
93.994	Maternal and Child Health Services Block Grant to the States	1,640,551
		40,580,255
	<b>Corporation for National and Community Service</b>	
94.002	Retired and Senior Volunteer Program	37,101
94.011	Foster Grandparent Program	230,300
		267,401
	Department of Homeland Security	
97.003	Agricultural Inspection	39,544
97.004	State Domestic Preparedness Equipment Support Program	2,387,976
97.042	Emergency Management Performance Grants	633,129
97.012	Boating Safety Financial Assistance	281,027
97.036	Disaster Grants - Public Assistance (Presidentally Declared Disasters)	868,935
97.039	Hazard Mitigation Grant	37,700
97.044	Assistance to Firefighters Grant	252,744
97.052	Emergency Operations Centers	1,440
97.053	Citizen Corps	961
		4,503,456
	Total expenditures of Federal awards	\$ 148,186,789

See accompanying notes.

# Notes to Schedule of Expenditures of Federal Awards

Year Ended September 30, 2006

#### **1. Basis of Presentation**

For purposes of complying with the Single Audit Act Amendments of 1996, the Government of the United States Virgin Islands (the Government or GVI) is defined in a manner consistent with the entity defined in the basic financial statements as of and for the year ended September 30, 2006, except that the component units (as defined in the notes to the aforementioned basic financial statements) are excluded. Accordingly, the accompanying Schedule of Expenditures of Federal Awards (the Schedule) presents the Federal financial assistance programs administered by the Government for the year ended September 30, 2006, excluding the component units.

#### 2. Basis of Accounting

The accompanying schedule was prepared using the modified accrual basis of accounting, except for nonmonetary programs, which are presented based on the fair value of the food stamps (CFDA #10.551 in the amount of \$20,591,784) and the food commodities (CFDA #10.555 in the amount of \$300,000) distributed during the year. The Government's accounting system provides the primary information from which the schedule is prepared.

#### 3. Matching Costs

Matching costs, such as the nonfederal share of certain program costs, are not included in the accompanying Schedule, except Unemployment Insurance (CFDA No. 17.225), as indicated in Note 8.

#### 4. Relationship to Federal Financial Reports

The regulations and guidelines governing the preparation of Federal financial reports vary by Federal agency and among programs administered by the same agency. Accordingly, the amounts reported in the Federal financial reports do not necessarily agree with the amounts reported in the accompanying schedule, which is prepared on the basis explained in Notes 1 and 2.

Office of Management and Budget (OMB) Circular A-133 requires that Federal financial reports and claims for advances and reimbursements contain information that is supported by the books and records from which the basic financial statements have been prepared. The Government's departments prepare the Federal financial reports and claims for advances and reimbursements primarily based on information from the internal accounting records of the respective Federal

# Notes to Schedule of Expenditures of Federal Awards (continued)

#### 4. Relationship to Federal Financial Reports (continued)

program Departments. However, these records do not agree with the accounting records of the Government's accounting system in all instances. The Government's departments, in various instances, do not prepare a reconciliation of the internal accounting records of the Federal programs with the Government's accounting system. See Finding No. 06-05.

#### **5.** Consolidated Block Grants

The Government was granted a consolidated grant award under Title V of Public Law 95-134. The consolidated grant to insular areas permits the consolidation of two or more authorized programs under one application to provide for simplified reporting procedures and flexibility in allocating funds to meet educational needs. The most significant programs under which the Virgin Islands' Department of Education used and administered the funds and the cash disbursements for each program for the fiscal year ended September 30, 2006 are the following:

Federal CFDA Number	Program Title	Expenditures
84.002	Adult Education -State Grant Program	\$ 891,199
84.027	Special Education -Grants to States	10,012,737
84.048	Vocational Education -Basic Grants to States	720,495
84.298	State Grants for Innovative Programs	7,630,275
		\$19,254,706

#### 6. Subrecipients

Of the Federal expenditures presented in the schedule, the Government provided Federal awards to subrecipients related to major programs as follows:

		Amount
Federal CFDA Number	Program Title	Provided to Subrecipients
93.667	Social Services Block Grant	\$374,351

# Notes to Schedule of Expenditures of Federal Awards (continued)

#### 7. Unemployment Insurance Expenditures

OMB Circular A-133 Compliance Supplement requires the Unemployment Insurance (CFDA No. 17.225) to include the state funds as well as the Federal funds in the total expenditures of the program. Consequently, the total amount of expenditures presented in the accompanying schedule is composed of the following:

Federal fund expenditures	\$2,402,690
State fund expenditures	4,977,363
Total expenditures	\$7,380,053

# Schedule of Findings and Questioned Costs

September 30, 2006

# Part I – Summary of Auditors' Results

### **Financial Statement Section**

Type of auditor's report issued on the basic financial statements:

Opinion Unit	Type of Report
Governmental activities	Unqualified
Business-type activities	Disclaimer
Discretely presented component units	Qualified
General fund	Unqualified
PFA debt service fund	Unqualified
PFA capital projects fund	Unqualified
West Indian Company fund - enterprise fund	Unqualified
Unemployment Insurance fund - enterprise fund	Unqualified
Aggregate remaining fund information	Disclaimer
Internal Control over Financial Reporting Reportable conditions identified that are not considered to be n	naterial weaknesses? <u>Yes</u>
Non-compliance material to financial statements noted?	<u>Yes</u>
Federal Award Section	
Internal control over major programs:	
Material weaknesses identified?	<u>Yes</u>
Reportable conditions identified that are not considered to be n	naterial weaknesses? <u>Yes</u>

# Schedule of Findings and Questioned Costs (continued)

# Part I – Summary of Auditors' Results (continued)

#### Federal Award Section (continued)

Type of auditor's report issued on compliance for major programs:

CEDA Normhan	Malan Dua anan	Type of Report Issued
CFDA Number	Major Program	on Compliance
10.551, 10.561	Food Stamps Cluster	Unqualified
10.555, 10.559	Child Nutrition Cluster	Adverse
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children	Unqualified
17.225	Unemployment Insurance	Unqualified
66.605	Performance Partnership Grants	Qualified
84.027	Special Education -Grants to States	Adverse
84.298	Innovative Education Program Strategies	Adverse
93.563	Child Support Enforcement	Adverse
93.600	Head Start	Unqualified
93.667	Social Services Block Grant	Unqualified
93.778	Medical Assistance Program	Adverse
93.600 93.667 93.778 Any audit fir	Head Start Social Services Block Grant	Unqualified Unqualified Adverse

# Identification of Major Programs

CFDA Number	Major Program
10.551, 10.561	Food Stamps Cluster
10.555, 10.559	Child Nutrition Cluster
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children
17.225	Unemployment Insurance
66.605	Performance Partnership Grants
84.027	Special Education -Grants to States
84.298	State Grants for Innovative Programs
93.563	Child Support Enforcement
93.600	Head Start
93.667	Social Services Block Grant
93.778	Medical Assistance Program

# Schedule of Findings and Questioned Costs (continued)

Part I – Summary of Auditors' Results (continued)

# Identification of Major Programs (continued)

Dollar threshold used to distinguish between Type A and Type B programs:	<u>\$3 million</u>
Auditee qualified as low-risk auditee:	<u>Nc</u>

## Schedule of Findings and Questioned Costs

For the Year Ended September 30, 2006

# Part II – Financial Statements Findings Section

This section identifies the reportable conditions, material weaknesses, fraud, illegal acts, violations of provisions of contracts and grant agreements, and abuse related to the financial statements for which *Government Auditing Standards* require reporting in a Circular A-133 audit.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-01

### Topic

The Government has control deficiencies in its internal control structure, accounting and financial management systems, budgetary controls and financial reporting practices. Due to their nature and magnitude, these deficiencies are considered to be a material weakness.

### Category

Internal Control

### Criteria

Auditees must prepare their financial statements in accordance with accounting principles generally accepted in the United States (GAAP). OMB Circular A-133 section 310, states that the auditee shall prepare financial statements that reflect its financial position, results of operations or changes in net assets, and, where appropriate, cash flows for the fiscal year audited.

GASB Codification Section 1100, *Summary Statement of Principles*, states that a governmental accounting system must make it possible both: (a) to present fairly and with full disclosure the funds and activities of the governmental unit in conformity with GAAP, and (b) to determine and demonstrate compliance with finance-related legal and contractual provisions.

GASB Codification Section 1300, *Fund Accounting*, states that governmental accounting systems should be organized and operated on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts to record cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.

GASB Codification Section 1900, states that governmental entities should prepare interim and year-end financial statements and reports of financial position, operating results, and other pertinent information to facilitate management control of financial operations, legislative oversight, and for external reporting purposes.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-01 (continued)

### **Criteria** (continued)

OMB Circular A-102 Subpart C, Section 20, states that a state must expend 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 permit preparation of reports required by this part and the statutes authorizing the grant, and permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restriction and prohibitions of applicable statutes. The financial management systems must meet the following standards:

- 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.
- Accounting records: grantees and subgrantees must maintain records that 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.
- 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.
- Budget control: actual expenditures or outlays must be compared with budgeted amounts for each grant or subgrant. Financial information must be related to performance or productivity data, including the development of unit cost information whenever appropriate or specifically required in the grant or subgrant agreement. If unit cost data are required, estimates based on available documentation will be accepted whenever possible.
- Allowable cost: applicable OMB cost principles, agency program regulations, and the terms of grant and subgrant agreements will be followed in determining the reasonableness, allowability, and allocability of costs.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

## Finding Number: 06-01 (continued)

#### Criteria (continued)

- Source documentation: accounting records must be supported by such source documentation as canceled checks, paid invoices, payrolls, time and attendance records, contract and subgrant award documents, etc.
- Cash management: procedures for minimizing the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by grantees and subgrantees must be followed whenever advance payment procedures are used. Grantees must establish reasonable procedures to ensure the receipt of reports on subgrantees' cash balances and cash disbursements in sufficient time to enable them to prepare complete and accurate cash transactions reports to the awarding agency. When advances are made by letter-of-credit or electronic transfer of funds methods, the grantee must make drawdowns as close as possible to the time of making disbursements.

In addition to the above requirements, the Government's internal control system must provide for reconciliation of amounts reflected in control accounts with subsidiary records and the reconciliation of transactions and balances between different departments and agencies.

#### **Condition Found**

The Government has inadequate internal controls and has not established accounting policies, procedures, and financial reporting practices necessary to conform to generally accepted accounting principles, (GAAP), as applicable to governmental entities. Significant deficiencies noted are as follows:

• There is a lack of effective internal controls to reasonably assure compliance with the requirements of Federal laws, regulations and program compliance requirements. The Government has deficiencies in internal control such as the absence of sufficient level of control consciousness throughout all of the Government's separate administrative operations, the absence of an appropriate segregation of duties, the absence of appropriate management review and approval of transactions, accounting entries and financial and other reporting.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

## Finding Number: 06-01 (continued)

### **Condition Found (continued)**

• There are inadequate procedures for appropriately assessing and applying accounting principles, inadequate provisions for the safeguarding of assets, the absence of an accounting procedures manual and the absence of many controls considered appropriate for an entity of this size and type.

Due to their nature and magnitude, these control deficiencies are considered to be a material weakness.

#### **Known Questioned Costs**

Not applicable.

### **Underlying Cause**

The Government's management has not adopted and enforced internal control policies and procedures over its accounting and financial management, budgetary practices and financial reporting.

#### Effect

The Government's ineffective internal controls are conducive to many deficiencies as described in the numerous findings contained in this report. The continued existence of these deficiencies could result in significant cost disallowances by the Federal awarding agencies due to unsupported or inappropriate costs or ultimately; in the reduction or elimination of Federal awards received by the Government.

#### Recommendation

The Government should implement internal controls to provide reasonable assurance that:

• Transactions are properly recorded and accounted for to permit the preparation of reliable financial statements and Federal reports, maintain accountability over assets; and demonstrate compliance with laws, regulations, and other compliance requirements

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

## Finding Number: 06-01 (continued)

#### **Recommendation** (continued)

• Funds, property, and other assets are safeguarded against loss from unauthorized use or disposition.

#### Management's Response

U.S. Department of Finance (DOF) concurs with Ernst & Young findings and recommendations.

To begin the process of addressing the findings noted in 06-01 above, the Government implemented the Tyler-Munis Enterprise Resource Planning (ERP) financial management system, effective October 1, 2006. While an assessment with respect to the effectiveness and efficiency of the ERP financial management system throughout the Government can be reasonably measured over a three to five year time horizon, the incremental impact of these attributes has been immediate, albeit with a variety of latent and patent challenges identified along the way. Nonetheless, the GVI recognizes that the ERP financial management system by itself does not equate to credibility unless updated policies and procedures surrounding the internal control structure is not well documented, communicated, consistently followed and fully embraced by the separate administrative operations throughout the Government.

The initial implementation of the ERP financial management system commenced with several "core" modules (i.e., Purchasing/Requisitions, Accounts Payable, Cash Receipts, Treasury Management, General Ledger, Budgeting and Fixed Assets) which have served to gradually minimize the ineffectiveness of the internal control structure of the Government. These core modules, which conform to generally accepted accounting principles (GAAP), along with the training of Government personnel to utilize the capabilities of the ERP financial management system and documented policies and procedures, have improved the effectiveness of the Government's internal control structure dramatically.

For example, to address the deficiency in locating supporting documentation underlying each transaction that is eventually posted to the general ledger; all transactions are electronically attached with the necessary supporting documentation and stored within the ERP financial management system for proper review and/or retrieval. Moreover, through the embedded levels of workflow approval within the ERP financial management system, which is decentralized at

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-01 (continued)

### Management's Response (continued)

the departmental/agency by specific staff (i.e., segregation of duties) that have limited access to accounts for their respective department/agency through permissions and security; there is a low probability that a transaction will be approved by a Department/Agency Head (i.e., management review and approval) prior to being forwarded to the Department of Property and Procurement (P&P) for procurement review and funding availability approval and finally to the DOF for final review and subsequent payment. Note that, both P&P and DOF also have mutually exclusive workflow approval processes that serve to minimize (or eliminate) the likelihood of missing supporting documentation, as well as to further enhance management review and approval of transactions, as well as accounting entries and financial and other reporting.

Although the ERP financial management system has enabled the Government to make significant improvements in the proper recording and accounting of transactions to permit the preparation of reliable financial statements and Federal reports, the reconciliation of these transactions to ensure compliance with laws, regulations and other compliance requirements will require additional effort and oversight by department/agencies, the V.I. Office of Management and Budget (OMB) and DOF.

The first step in accomplishing this task is to provide department/agencies with a set of standard reports that should be reviewed on a monthly basis for completeness prior to the DOF's established cut-off dates for closing monthly periods. These standard reports emanating from the ERP financial management system, along with the policies and procedures supporting them, will be communicated to agencies/departments as the "official" set of records/reports that should be leveraged in the preparation of external Federal reports. These Federal reports will then be reviewed at departmental/agency level by the appropriate Program Manager responsible for external Federal reporting leveraging the "official" set of records/reports from the ERP financial management system as the supporting documentation. Once this review is complete, it will be forwarded to the Department/Agency Certifying Officer and Agency Head prior to submission to OMB for final review and dissemination from OMB to external Federal reporting entities. In order to achieve success in this regard, once the Government has moved past the initial challenges of implementing the ERP financial management system, a strong focus on reconciliation and review at each of the aforementioned levels, as well as through the established channels will be embraced, enforced and consistently followed to eliminate this deficiency.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-01 (continued)

#### Management's Response (continued)

Finally, ensuring that funds, property and other assets are safeguarded against loss from authorized use or disposition is partially mitigated by the ERP financial management system. Aside from the well-established inter/intra-workflow approval process that exists to manage, review and approve transactions, from a funding standpoint, the "allotment lever" utilized by the OMB within the core Budgeting module, serves as a strong mechanism to safeguard and control the flow of funds from unauthorized use by departments/agencies at the outset of initiating a transaction. The funding controls are further strengthened via a multi-level review at P&P, as well as the DOF (i.e., Accounting and Treasury Divisions). Conversely, the control environment surrounding property has been improved through the implementation and oversight of the Fixed Asset Module by P&P, as well as the ancillary policies and procedures that permit the Government to cross-reference the detailed items resident within the ERP financial management system.

Schedule of Findings and Questioned Costs

Part II - Financial Statements Findings Section (continued)

### Finding Number: 06-02

#### Topic

The Government did not comply with the established due date for the submission of the required Single Audit Report.

#### Category

Internal Control and Compliance

#### Criteria

OMB Circular A-133, Subpart C, Section 320a establishes that all audits shall be completed and submitted to the cognizant agency within the earlier of 30 days after receipt of the auditor's report or nine (9) months after the end of the audit period.

#### **Condition Found**

The Government did not comply with the required submission date of the Single Audit for the fiscal year ended September 30, 2006. The due date for this report was no later than June 30, 2007.

#### **Known Questioned Costs**

Not applicable.

#### **Underlying Cause**

Due to the failure to ensure that adequate accounting records exist and that the timely and accurate closing of books occurs, management did not comply with the requirements established in OMB Circular A-133.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-02 (continued)

#### Effect

The Government could be exposed to a reduction or elimination of funding by the Federal awarding agencies.

#### Recommendation

The Government should establish monthly closing schedules and improve its year-end closing procedures to allow for the timely performance of the Single Audit and enable the Government to comply with the reporting requirements established by applicable regulations.

#### Management's Response

The Department of Finance (DOF) concurs with Ernst & Young findings and recommendations.

To begin the process of addressing the findings noted in 06-02 above, the Government implemented the Tyler-Munis Enterprise Resource Planning (ERP) financial management system, effective October 1, 2006. Although the DOF has fully communicated to departments/agencies the establishment of monthly closing schedules to effectuate the timely issuance of the Single Audit, the enforcement of this policy cannot be fully achieved until the outstanding audits for fiscal year 2007 and fiscal year 2008 is completed.

More specifically, the ERP financial management system is meant to accommodate having two (2) fiscal periods open at a time to ensure that monthly closings are performed. The implication of having more than two fiscal periods open obviates the institution of monthly closings for the Government because the system will remain in a "soft close" mode (rather than "hard close") until all final adjustments are included. Given the unenviable position of having more than two fiscal periods open and its direct correlation to other anomalies in the ERP financial management system, the Government's resolve has strengthened to become more timely in meeting the criteria under OMB Circular A-133, Subpart C, § 320 of the Uniform Administrative Requirements for Grants Agreements.

# Schedule of Findings and Questioned Costs

# Part II – Financial Statements Findings Section (continued)

#### Finding Number: 06-02 (continued)

#### Management's Response (continued)

As such, the Government has embarked on an approach to addressing the timeliness of financial statement issuance within the 270 day criteria outlined in OMB Circular A-133, by endeavoring toward the completion of the fiscal year 2007 and fiscal year 2008 outstanding audits within a timeframe that allows for full performance of the monthly closing schedules in fiscal year 2010.

# Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

#### Finding Number: 06-03

#### Topic

The Government's lack of control over the financial statement close process led to significant adjustments in the financial statements which are considered to be material weaknesses.

#### Category

Internal Control

#### Criteria

A fundamental element of a sound system of internal controls is an effective financial statement close process. Such a process is essential in enabling companies to prepare timely and accurate financial statements. This process helps us ensure that all financial transactions are properly recorded, appropriately supported, and subjected to supervisory review. The financial statement close process begins with accounting data recorded in the Government's general ledger and culminates in the preparation of the Government's financial statements, including identification and documentation of relevant disclosures that are required under generally accepted accounting principles.

#### **Condition Found**

During our audit we noted deficiencies in the Government's financial statement close process, including the following:

- Management's judgmental estimates were not entirely supported, including tax receivables allowance, accrued questioned costs, and retroactive pay liability, resulting in significant audit adjustments. Lack of documentation and support over accrued questioned costs and retroactive pay liability resulted in prior period errors.
- Lack of controls over accounts payable reconciliation has made it difficult for the Government to establish its accounts payable sub-ledger. This resulted in significant adjustments to the financial statements.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-03 (continued)

#### **Condition Found (continued)**

• Inappropriate accounting treatment over deferred revenues, capital assets, and fund classification resulted in prior period errors related to understatement of revenues, duplication of capital assets, and understatement in bank balances, respectively.

#### **Known Questioned Costs**

Not applicable.

#### **Underlying Cause**

The Government's financial statements have grown in complexity. Additionally, supervisory review of the closing process was not effective in all instances.

#### Effect

The lack of supervisory review led to significant adjustments in the Government's financial statements, some of which were related to prior year errors.

#### Recommendation

The Government's management should be more closely involved in the monitoring and review of the financial statement close process. Management should consider performing this process on a quarterly basis in order to detect and correct errors on at timely basis, while enhancing the Government's knowledge over its financial condition.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-03 (continued)

#### Management's Response

Concur with Ernst & Young findings and recommendations.

The ERP financial management system is meant to only accommodate having two (2) fiscal periods open at a time to ensure that monthly closings are performed. The implication of having more than two fiscal periods open obviates the institution of monthly and/or quarterly closings for the Government because the system will remain in a "soft close" mode (rather than "hard close") until all final adjustments are included. Given the unenviable position of having more than two fiscal periods open (i.e., fiscal year 2007: Hard Closed; fiscal year 2008: Soft Closed; fiscal year 2009: Open) and its direct correlation to other anomalies in the ERP financial management system, the Government's resolve has strengthened to meet strict monthly closing processes that will allow for the detection and correction of errors on a timely basis. Moreover, this process improvement will lay the foundation for the GVI to meet the criteria under OMB Circular A-133, Subpart C, § 320 of the Uniform Administrative Requirements for Grants Agreements.

As such, the Government has embarked on an approach to addressing the timeliness of financial statement issuance within the 270 day criteria outlined in OMB Circular A-133, by endeavoring toward the completion of the fiscal year 2007 and fiscal year 2008 outstanding audits within a timeframe that allows for full performance of monthly closing processes during fiscal year 2010.

In anticipation of implementing these procedures during fiscal year 2010, the Government has begun the process of developing a monthly closing checklist that will improve the completeness of transactions that must be accounted for as part of the overall financial statements for the Government. Although the development of the checklist is currently underway, a partial depiction of the "draft" monthly closing checklist can be found below:

Completed (Y/N)	Initials	Date	Action	
			Verify a complete back-up of the database has been	
			completed	
			Verify that all batches are proofed and posted	

# Schedule of Findings and Questioned Costs

# Part II - Financial Statements Findings Section (continued)

# Finding Number: 06-03 (continued)

Completed				
(Y/N)	Initials	Date	Action	
			Verify all open requisitions and purchase orders are	
			posted	
			Verify that no un-posted contracts exist in the	
			contracts management module	
			Verify that all funds are in the segment table	
			Verify each entry in the fund attribute table actually	
			exists in the GL Master	
			Verify the fund of each Due To/ Due From is in the	
			segment table	
			Verify account of Due To/ Due From is in the GL	
			Master	
			Verify accounts in allocation table are in GL Master	
			Verify accounts in the budget roll-up are in the GL	
			master	
			Verify that each record in the chart of accounts has	
			the proper account type. ("B","E", OR "R")	
			Verify that all balance sheet accounts in the master	
			have the proper balance type ("A", "L" or "U")	
			Verify that the fund is in the segment table for each	
			account	
			Verify that the object is in the object table for each	
			account	

# Schedule of Findings and Questioned Costs

# Part II - Financial Statements Findings Section (continued)

# Finding Number: 06-03 (continued)

Completed					
(Y/N)	Initials	Date	Action		
			Verify that the project is in the project table for each		
			account		
			Verify that the org is in the org table for each		
			account		
			Verify that each account's fund matches the fund of		
			the org to which it belongs.		
			Verify that the remaining segments in each chart of		
			account match the remaining segments in each chart		
			of account.		
			Match the remaining segments for the org to which		
			they belong.		
			Verify that the reference/org/project for an account		
			is in the GL Master.		
			Verify that the trial balance is in balance by fund by		
			verifying the sum of actual balances by account in a		
			fund equals 0.00		
			Verify trial balance is in balance by period by fund		
			by verifying the sum of a month's close for all		
			accounts in fund equals 0.00.		
			Verify that the period amounts sum to the master		
			amounts by adding all 14 monthly amounts and		
			comparing that to the current year actual balance in		
			the master		
			Verify by fund by period revenue detail versus		
			control master		

# Schedule of Findings and Questioned Costs

# Part II - Financial Statements Findings Section (continued)

# Finding Number: 06-03 (continued)

Completed					
(Y/N)	Initials	Date	Action		
			Verify by fund by period expense detail versus		
			control master		
			Verify 14 master balance records exist for each		
			account in the GL master		
			Each account in the hold table must exist in the GL		
			master		
			Verify current year hold file is in balance by fund,		
			by journal		
			Verify the sum of expense account entries in the		
			current year hold file equal the expenditure control		
			entry in the hold file by fund, by journal		
			Verify the sum of the revenue account entries in the		
			current year hold file equal the revenue control		
			entry in the hold file by fund, by journal		
			Verify there are no transactions in the hold file that		
			have been through a month end closing for periods		
			that should have already been closed, as the current		
			year/period would be the next one to finish closing		
			Verify there are no transactions in the transaction		
			proof file for periods that should have already been		
			closed as the current year/period would be the next		
			one to finish closing		

# Schedule of Findings and Questioned Costs

# Part II - Financial Statements Findings Section (continued)

# Finding Number: 06-03 (continued)

Completed (Y/N)	Initials	Date	Action
			Verify accounts currently in the transaction proof exist in the GL master
			Verify that no un-posted purchase orders exist in the purchasing module

# Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

#### Finding Number: 06-04

#### Topic

Performance and review of the bank reconciliation process has not been timely.

#### Category

Internal Control

#### Criteria

Performance and review bank reconciliations should be performed within a period of 30 to 45 days after month end.

#### **Condition Found**

During our audit, we noted that bank reconciliations were not being performed and reviewed within a reasonable period. Most bank reconciliations were completed, reviewed and approved after 365 days.

#### **Known Questioned Costs**

Not applicable.

#### **Underlying Cause**

The Government has numerous bank accounts and its process for performing bank reconciliations is, for the most part, performed manually.

#### Effect

The lack of timely performance and review of bank reconciliations had led to adjustments not being identified on a timely basis. In addition, this has prevented the Government from performing monthly closing procedures, which is necessary for timely financial reporting.

Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding Number: 06-04 (continued)

#### Recommendation

The Government should automate its bank reconciliation process and consolidate unnecessary bank accounts. This will allow for the Government's personnel to be more efficient and effective in detecting errors and provide the Government more timely and accurate financial information.

#### Management's Response

Concur with Ernst & Young findings and recommendations.

To begin the process of addressing the findings noted in 06-04 above, the Government implemented the Tyler-Munis Enterprise Resource Planning (ERP) financial management system, effective October 1, 2006. While an assessment with respect to the effectiveness and efficiency of the ERP financial management system throughout the Government can be reasonably measured over a three to five year time horizon, the incremental impact of these attributes has been immediate, albeit with a variety of latent and patent challenges identified along the way. Nonetheless, the Government recognizes that the ERP financial management system by itself does not equate to credibility unless updated policies and procedures surrounding the internal control structure is well documented, communicated, consistently followed and fully embraced by the separate administrative operations throughout the Government.

As part of the ERP, an integral component in automating the bank reconciliation functions within the DOF's Treasury Division lay in the bank reconciliation application, which resides in the Treasury Management Module (TMM). The TMM was used to reconcile all Government bank accounts as of September 30, 2007 and began in earnest as a monthly reconciliation tool throughout fiscal year 2008 and henceforth. While the TMM has been instrumental in improving the overall reconciliation process and the controls surrounding cash, it has revealed the necessity to reduce the amount of excess bank accounts utilized throughout the Government. It is our expectation that many of these excess bank accounts will be closed prior to September 30, 2009. Moreover, in maximizing the benefits of the TMM, the Government will move towards increased efficiency and effectiveness through consolidation of existing bank accounts, while leveraging the full suite of available on-line financial tools (e.g., inter- and intra-bank ACH transactions) prior to September 30, 2009.

# Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

#### Finding No. 06-05

#### Topic

Errors were identified in the Schedule of Expenditures and Federal Awards (SEFA).

#### Category

Internal Control

#### Criteria

Recipients of Federal awards are to maintain adequate controls over their books and records in order to prepare appropriate financial statements, including the Schedule of Expenditures of Federal Awards (OMB Circular A-133, Section .300(d)).

#### **Condition Found**

The Schedule of Expenditures of Federal Awards (SEFA) is to provide total Federal awards expended for each individual Federal program. Errors were identified in the preparation of the September 30, 2006 Schedule of Expenditures of Federal Awards.

# Schedule of Findings and Questioned Costs

## Part II – Financial Statements Findings Section (continued)

#### Finding No. 06-05 (continued)

#### **Condition Found (continued)**

As part of our compliance testing, items were identified that were not properly recorded in the September 30, 2006 Schedule of Expenditures of Federal Awards according to the definition of expenditures per OMB Circular A-133. The September 30, 2006, SEFA was not corrected. The September 30, 2006 SEFA reflected additional expenditures of \$4,724,138 over amounts reported and requested for reimbursement. Differences identified between expenditures reported in the SEFA and actual expenditures were as follows:

CDFA #	Program	Expenditures per SEFA	Expenditures Reported	Difference
10.551, 10.561	Food Stamp Cluster	\$25,163,175	\$25,010,766	\$ 152,409
10.555, 10.559	Child Nutrition Cluster	\$ 6,581,865	\$ 5,159,834	1,422,031
10.557	Special Supplemental Nutrition			
	Program for Women, Infants and			
	Children	\$ 5,047,959	\$ 5,410,234	(362,275)
17.225	Unemployment Insurance	\$ 7,380,053	\$ 6,483,896	896,157
66.605	Performance Partnership Grants	\$ 2,459,081	\$ 2,869,407	(410,326)
93.600	Head Start	\$ 9,830,889	\$ 7,513,848	2,317,051
93.667	Social Services Block Grant	\$ 5,893,652	\$ 5,857,905	35,747
93.778	Medical Assistance Program		. , ,	,
	(Medicaid-Title XIX)	\$ 5,815,224	\$ 6,162,352	(347,128)
			· · ·	\$3,703,666

#### **Known Questioned Costs**

No questioned costs for the year ended September 30, 2006, as the expenditures reported and requested for reimbursements were based on local programs records and not on the records in accounting system that are the basis for the SEFA.

# Schedule of Findings and Questioned Costs

Part II – Financial Statements Findings Section (continued)

### Finding No. 06-05 (continued)

#### **Underlying Cause**

Inadequate internal controls over reporting resulted in errors in the preparation of the Schedule of Expenditures of Federal Awards. Lack of reconciliation between Federal grant expenditures recorded in the Government's records with the amounts accounted for in its accounting system.

#### Effect

The September 30, 2006, SEFA was overstated by the above amounts in the above programs.

#### Recommendation

The Government should implement additional procedures and internal controls to ensure its Schedule of Expenditures of Federal Awards is prepared properly to include all Federal expenditures applicable to the reporting period. The Government should ensure proper reconciliation between accounting system and Federal expenditures at program level is timely performed and discrepancies are investigated.

#### Management's Response

DOF concurs. Although the ERP financial management system has enabled the Government to make significant improvements in the proper recording and accounting of transactions to permit the preparation of reliable financial statements and Federal reports, the reconciliation of these transactions to ensure compliance with laws, regulations and other compliance requirements will require additional effort by department/agencies, the V.I. Office of Management and Budget (OMB), and DOF.

The first step in accomplishing this task is to provide department/agencies with a set of standard reports that should be reviewed on a monthly basis for completeness prior to DOF's established cut-off dates for closing monthly periods. These standard reports emanating from the ERP financial management system, along with the policies and procedures supporting them, will be communicated to agencies/departments as the "official" set of records/reports that should be leveraged in the preparation of external Federal reports. These Federal reports will then be

# Schedule of Findings and Questioned Costs

## Part II – Financial Statements Findings Section (continued)

#### Finding No. 06-05 (continued)

#### Management's Response (continued)

reviewed at departmental/agency level by the appropriate Program Manager responsible for external Federal reporting leveraging the "official" set of records/reports from the ERP financial management system as the supporting documentation. Once this review is complete, it will be forwarded to the Department/Agency Certifying Officer and Agency Head, with a copy to OMB, for final review and dissemination to external Federal reporting entities. In order to achieve success in this regard, once the Government has moved past the initial challenges of implementing the ERP financial management system, a strong focus on reconciliation and review at each of the aforementioned levels, as well as through the established channels will be embraced, enforced and consistently followed to eliminate this deficiency. As such, a suggested standard format that could be adopted by the Government or specific programs to reconcile federal reports (e.g., SF 269) is depicted as follows:

#### Fiscal Year 20XX Expenditures Reconciliation

<u>Per ERP</u> Grant F1000T Federal Expenditures per ERP	1,000,000	
	-	
Total Program FY 20XX Federal expenditures per ERP	1,000,000	
<u>Per Federal reports (i.e. SF269, CMS64, etc.)</u>		
SF269 Q1 (federal outlays for the quarter, or other)	250,000	
reporting period		
SF269 Q2	200,000	
SF269 Q3	240,000	
SF269 Q4	270,000	
Total Program FY 20XX Federal expenditures per federal	reports _	960,000

# Schedule of Findings and Questioned Costs

# Part II - Financial Statements Findings Section (continued)

#### Finding No. 06-05 (continued)

### Management's Response (continued)

Differences to be Reconciled**	40,000
Current year payroll cost coded with prior year grant award (to be reversed F1100S Prior year expenditures not posted timely	(15,000) (20,000)
Federal expenditures funded from general fund loan	(5,000)
	-

### Drawdowns Reconciliation

Program FY 20XX federal drawdowns per ERP	1,002,000
Program FY 20XX federal drawdowns per program records	1,100,000
Differences to be Reconciled **	(98,000)

\*\*Differences and corrections to be explained, if necessary.

## Schedule of Findings and Questioned Costs

For the Year Ended September 30, 2006

### Part III - Federal Awards Findings and Questioned Costs Section

This section identifies reportable conditions, material weaknesses, and instances of noncompliance, including questioned costs, as well as any abuse findings involving awards that are material to a major program related to the audit of major Federal programs as required to be reported by OMB Circular A-133, Section .510a.

Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## **U.S. Department of Agriculture - Child Nutrition Cluster**

(CFDA Nos. 10.555 and 10.559)

The objectives of the child nutrition cluster programs are to: (1) assist States in administering food services that provide healthful, nutritious meals to eligible children in public and non-profit private schools, residential child care institutions, and summer recreation programs; and (2) encourage the domestic consumption of nutritious agricultural commodities. Total Child Nutrition Cluster expenditures for the fiscal year ended September 30, 2006 amounted to \$6,581,865.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-06

#### Program

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA Nos. 10.555 and 10.559

#### Topic

Discrepancies between meals reported and meals served.

#### Category

Compliance/Internal Control

#### **Compliance Requirement**

Reporting

#### Criteria

In accordance with 7 CFR 210.7(C)(1)(iii,iv), the school food authority shall, at a minimum, base Claims for Reimbursement on lunch counts, taken daily at the point of services, which correctly identify the number of free, reduced price and paid lunches served to eligible children and correctly record, consolidate and report those lunch and supplement counts on the Claims for Reimbursement.

#### **Condition Found**

Based on our compliance testing on the following districts, we note the following findings due to discrepancies between the meal service forms and the meals reported on the FNS 418, *Report of the Summer Food Service Program for Children*.

Month	School/Sponsor	Program	
1. June	Agape	Breakfast	
2. June	Agape	Lunch	
3. June	Wesley	Breakfast	
4. June	Wesley	Lunch	

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-06 (continued)

#### Program

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA Nos. 10.555 and 10.559

#### **Condition Found (continued)**

Month	School/Sponsor	Program
5. June	St. Thomas	Breakfast/Lunch/Snack
6. June	St. Croix	Breakfast/Lunch/Snack
7. August	St. Thomas	Breakfast/Lunch/Snack
8. August	St. Croix	Breakfast/Lunch/Snack

These reports are filed during the summer months (June to August). We tested 2 out of 3 months for all six districts. Discrepancies were noted in four districts for both months tested and were noted in 16 out of 25 meals tested.

#### **Known Questioned Costs**

None.

#### **Underlying Cause**

The program does not have proper controls in place to ensure the accuracy, flow, and consolidation of meals served between the supporting worksheets and the claims for reimbursement.

#### Effect

The program is not in compliance with the requirements of 7 CFR 210.7 (c)(1)(iii,iv,v). This could result in reimbursement being made for meals provided to ineligible students.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-06 (continued)

#### Program

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA Nos. 10.555 and 10.559

#### Recommendation

We recommend the Government strengthen current procedures to ensure that all claims for reimbursement are supported by accurate meal counts and that the underlying supporting documentation is consolidated correctly.

#### Management's Response

V.I. Department of Education (VIDE) concurs with this finding. After careful review of the document we found that second meals served were erroneously omitted. As a result sponsors were under paid. The State Agency will revise the FNS-418 and submit them to USDA to reinstitute the funds for payment to the sponsors.

VIDE has put in place procedures where the meal counts and reimbursement claims will be reconciled by the Nutrition Programs Specialist and two other State Agency staff. Additionally, all meal counts will be recorded on a spreadsheet as a record of accountability and supportive documents will be attached and filed.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-07

#### Program

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA Nos. 10.555 and 10.559

#### Topic

The V.I. Department of Education did not reconcile Federal financial reports with its financial records (FMS).

### Category

Compliance/Internal Control

#### **Compliance Requirement**

Reporting

#### Criteria

Pursuant to 7 CFR 301.6.2(b)(6), accurate, current, and complete disclosure of the financial results of the financially assisted activities must be made in accordance with the financial reporting requirements of the grant.

#### **Condition Found**

The V.I. Department of Education, through its state agency, prepares Federal financial reports based on information from the accounting records of the program. The program receives Federal funds based on the number of meals served plus actual expenditures incurred in the administration of the program. However, we were unable to compare the amount of expenditures per the Government's Financial Management System (FMS) with the program records because the program did not properly track expenditures incurred.

The state agency also does not prepare a reconciliation of the program's records with the FMS. Timely reconciliation is necessary to ensure accurate reporting to the U.S. Department of Agriculture.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

### Finding No. 06-07 (continued)

#### Program

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA Nos. 10.555 and 10.559

#### **Condition Found (continued)**

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA No. 10.555 and No. 10.559

As a result of the above matters, we were unable to validate the completeness and accuracy of the amounts reported on the quarterly reports.

A similar situation was included in the 2005 OMB Circular A-133 Report as Finding No. 05-08.

### **Known Questioned Costs**

For St. Thomas, amounts reported in SF-269 are overstated by \$124,416 when compared to supporting internal records, while for St. Croix, amounts reported in SF-269 are overstated by \$326,112 when compared to supporting internal records. Unsupported amount requested for reimbursement totals \$450,528.

#### **Underlying Cause**

Current procedures do not include timely reconciliation of the program's records with FMS, and adequate records are not maintained to support the amounts reported to the U.S. Department of Agriculture.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-07 (continued)

#### Program

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA Nos. 10.555 and 10.559

#### Effect

The lack of timely reconciliation of the program records with the FMS and the lack of adequate supporting documentation may result in incorrectly posted transactions not be promptly detected and corrected. This may also lead to incorrect financial information presented in the reports submitted to the Federal government, as well as reimbursement being made for unallowable costs and meals being provided to ineligible students.

#### Recommendation

We recommend that the V.I. Department of Education, through its state agency, monitor program expenditures, and maintain adequate supporting documentation. In addition, we recommend that through its state agency, the V.I. Department of Education implement procedures to provide for the reconciliation of Federal expenditures between program records and the Government's FMS/ERP system.

#### Management's Response

VIDE concurs with this finding. VIDE will:

- 1. Initiate an invoice, requisition or any form of purchase order;
- 2. the district will send purchase order to Business Office for processing, and enter the relevant information into the ERP System;
- 3. the district will check the ERP System to ascertain payment has been made to vendor;
- 4. the districts will print a copy of the transaction from the ERP system showing the vendor's name, account code, amount paid, and check number;
- 5. the district will forward a copy to the State Office, requesting a draw be made for those payments;

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-07 (continued)

#### Program

U.S. Department of Agriculture - Child Nutrition Cluster - CFDA Nos. 10.555 and 10.559

#### Management's Response (continued)

- 6. the State Office will make the necessary draw to match the payments made;
- 7. after the draw is made and funds received into the bank account, the Department of Finance informs the State Office via telephone, e-mail and/or fax of the wire transfer revenue transactions;
- 8. the State Office will proceed to enter the revenue into the ERP System in the appropriate accounts for those payments made;
- 9. the State Office will coordinate with both districts and the Business Office to verify expenditures, and obligations prior to entering the information on the SF-269 for submittal to USDA.

Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

### U.S. Department of Agriculture – Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) CFDA No. 10.557

The objective of the Special Supplemental Nutrition Program for Women, Infants and Children (WIC) is to provide supplemental nutritious foods, nutrition education, and referrals to health care for low-income persons during critical periods of growth and development. Such persons include pregnant women, breast-feeding women up to one year postpartum, non-breast-feeding women up to six months postpartum, infants (persons under one year of age), and children under age five determined to be at nutritional risk. Intervention during the prenatal period improves fetal development and reduces the incidence of low birth weight, short gestation, and anemia. Total WIC expenditures for the fiscal year ended September 30, 2006 amounted to \$5,047,959.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-08

#### Program

U.S. Department of Agriculture - Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) – CFDA No. 10.557

#### Topic

Required compliance investigation on vendors was not performed.

#### Category

Compliance/Internal Control

#### **Compliance Requirement**

Special Tests and Provisions: Compliance Investigation of High-Risk Vendor.

#### Criteria

Pursuant to 7 CFR 246.12(j)(4)(i) through (iii), a State agency operating a retail food delivery system must conduct compliance investigations, which consist of inventory audits and/or compliance buys, on a minimum of 5 percent of the vendors authorized as of October 1 of each year. A State agency must conduct compliance investigations on its high-risk vendors up to the 5 percent minimum. High-risk vendors are identified at least once annually using criteria developed by FNS, and/or other statistically based criteria developed by the State agency and approved by FNS.

#### **Condition Found**

Although the Program has no designated high-risk vendors, they did not perform the required compliance investigation on authorized vendors during the fiscal year. One annual required investigation from a total population of 11 authorized vendors should have been performed.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-08 (continued)

#### Program

U.S. Department of Agriculture - Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) – CFDA No. 10.557

#### **Known Questioned Costs**

None

#### **Underlying Cause**

Due to either lack of controls in place to ensure required investigations are performed or trained staff.

#### Effect

The lack of performance of these required investigations, could lead to undetected vendor noncompliance with program requirements and high-risk designation.

#### Recommendation

Appropriate controls need to be in place to ensure these investigations are performed during the year.

#### Management's Response

As of September 30, 2008, the matter had been addressed and staff was assigned to carry out the duties of a vendor monitor. During fiscal year 2008, vendor training, compliance buys and monitoring activities were conducted.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-09

#### Program

U.S. Department of Agriculture - Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) – CFDA No. 10.557

#### Topic

The V.I. Department of Human Services (VIDHS) has deficiencies in its property management procedures.

#### Category

Compliance/Internal Control

#### **Compliance Requirement**

Equipment and Real Property Management

#### Criteria

OMB Circular A-102 requires that equipment be used in the program for which it was acquired or, when appropriate, other Federal programs. Equipment records shall be maintained, a physical inventory of equipment shall be taken at least once every two years and reconciled to the equipment records, an appropriate control system shall be used to safeguard equipment, and equipment shall be adequately maintained.

#### **Condition Found**

Although the program keeps an inventory listing of equipment purchased with Federal funds, the program has not registered its equipment with the V.I. Department of Property and Procurement. Therefore, we were unable to observe V.I. Department of Property and Procurement official tags to determine appropriate equipment safeguards and accountability.

In addition, no official records certifying the performance of a physical inventory of property within the past two years was provided to us.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-09 (continued)

#### Program

U.S. Department of Agriculture - Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) – CFDA No. 10.557

#### **Known Questioned Costs**

Could not be determined

#### **Underlying Cause**

The V.I. Department of Health did not follow procedures in place to maintain appropriate records for acquisition and control of property acquired with Federal fund and/or lack of knowledge of Federal requirements regarding property acquired with Federal funds.

#### Effect

Inappropriate recordkeeping of equipment could lead to misappropriation of assets and noncompliance with Federal regulations.

#### Recommendation

The Department of Health should perform a physical inventory of equipment purchased with Federal funds and include unrecorded assets with V.I. Property and Procurement Office.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-09 (continued)

#### Program

U.S. Department of Agriculture - Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) – CFDA No. 10.557

#### Management's Response

DOH-WIC concurs that its equipment was not registered with the Department of Property and Procurement (P&P). However, although not registered with P&P, except for chairs, all computers equipment, desks, etc. are tagged. DOH-WIC was advised by P&P that chairs were no longer considered equipment. Further, by September 30, 2009, DOH-WIC will have its inventory updated and signed by the Program Director and the Systems Analyst, in order to certify/validate performance of a physical inventory.

Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## **U.S. Department of Agriculture - Food Stamps Cluster**

### CFDA Nos. 10.551 and 10.561

The objective of the Food Stamp Program is to help low-income households buy the food they need for good health. Total Food Stamps Cluster expenditures for the fiscal year ended September 30, 2006 amounted to \$25,163,175.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-10

#### Program

U.S. Department of Agriculture - Food Stamps Cluster - CFDA Nos. 10.551 and 10.561

#### Topic

The Virgin Islands' Department of Human Services (VIDHS) did not reconcile Federal financial reports with the program's accounting records.

### Category

Internal Control

#### **Compliance Requirement**

Reporting

#### Criteria

In accordance with 7 CFR 3016.20 (b)(1) on financial reporting states that 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.

#### **Condition Found**

The Financial Status Reports (SF 269) did not agree with the program's internal accounting records as follows:

Program accounting records	\$4	,153,737
SF269 (Federal outlays - line 10(k))	4,138,667	
Difference	\$	15,070

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-10 (continued)

### Program

U.S. Department of Agriculture - Food Stamps Cluster - CFDA Nos. 10.551 and 10.561

### **Known Questioned Costs**

None. Amounts disbursed by the Department were in excess of amounts claims.

#### **Underlying Cause**

Current internal controls for the Food Stamp Program are not operating effectively with regards to providing the proper reconciliation of accounting records/information.

### Effect

Inaccurate financial reports could affect future federal grant awards.

#### Recommendation

The V.I. Food Stamp Program should ensure that periodic reconciliations between federal financial reports and the program's accounting records are performed.

#### Management's Response

Department of Human Services concurs and will review/research the difference to reflect the necessary corrections and take appropriate action(s) deemed necessary to address it.

Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## U.S. Department of Labor - Unemployment Insurance

## CFDA No. 17.225

The regular Unemployment Insurance (UI) program, also referred to as Unemployment Compensation (UC), Unemployment Compensation for Federal Employees (UCFE), and Unemployment Compensation for Ex-Service Members (UCX) programs provide benefits to unemployed workers for periods of involuntary unemployment and help stabilize the economy by maintaining the spending power of workers while they are between jobs. UC programs cover almost all wage and salaried workers. During periods of high unemployment, the Extended Benefits (EB) program pays EB for an additional (or extended) period of time to eligible unemployed workers who have exhausted their entitlement to UC, UCFE, or UCX. Total Unemployment Insurance expenditures for the fiscal year ended September 30, 2006 amounted to \$7,380,053.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-11

### Program

U.S. Department of Labor - Unemployment Insurance - CFDA No. 17.225

### Topic

The U.S.V.I. Department of Labor did not reconcile Federal financial reports with the Government's financial records (FMS).

### Category

Internal Control

### **Compliance Requirement**

Reporting

### Criteria

29 CFR 97.20(b)(6) requires that internal controls be maintained to ensure that Federal transactions are properly recorded and accounted for in the recipient's books and records so as to enable the recipient to prepare reliable Federal reports.

#### **Condition Found**

The V.I. Department of Labor prepares federal financial reports based on information obtained from the program records. However, these records do not agree with supporting records as follows:

Federal Receipts		Federal Expenditures			
ETA 2112	\$ 1,270,678	SF 269	\$ 1,506,533		
Program records	1,337,557	Program records	1,503,314		
Difference	<u>\$ (66,879)</u>	Difference	<u>\$ 3,219</u>		

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-11 (continued)

### Program

U.S. Department of Labor - Unemployment Insurance - CFDA No. 17.225

#### **Condition Found (continued)**

Furthermore, the program did not prepare a reconciliation of its accounting records with amounts reported. Timely reconciliations are necessary to ensure accurate reporting to the U.S. DOL.

#### **Known Questioned Costs**

None. Amounts paid by VIDOL were in excess of amounts requested for reimbursements.

### **Underlying Cause**

Current procedures do not include a reconciliation of the program's records with amounts reported to Federal agency.

#### Effect

The lack of timely reconciliation of the program's records with amounts reported to Federal agency may result in incorrectly recorded transactions not being promptly detected and corrected. This may also lead to incorrect financial information presented in reports submitted to the Federal government.

#### Recommendation

The V.I. Department of Labor and the V.I. Department of Finance should prepare reconciliations between the V.I. Department of Labor records and FMS.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-11 (continued)

### Program

U.S. Department of Labor - Unemployment Insurance - CFDA No. 17.225

### **Management's Response**

DOL – VI concurs with the finding. Members of the VI staff have been designated to resolve the differences. New reconciliation procedures were implemented. This process change also involved creation of a monthly Statement of Appropriations, Outlays, and Obligation file which is the internal form 500-99.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-12

### Program

U.S. Department of Labor - Unemployment Insurance - CFDA No. 17.225

## Topic

The U.S.V.I. Department of Labor could not provide us with evidence supporting expenditures.

## Category

Compliance/Internal Control

## **Compliance Requirement**

Activities Allowed or Unallowed, Allowable Costs/Cost Principles, Eligibility, Period of Availability, and Special Tests and Provisions: Employer Experience Rating

### Criteria

The 29 CFR 97.20(b)(2) states that grantees and sub grantees shall retain and allow access to records, supporting documents, statistical records and other records that are otherwise reasonably considered as pertinent to program regulations. The program is required to maintain complete and accurate employer's employment history related to the calculation of experience rating.

### **Condition Found**

We identified a lack of internal controls over the record keeping function within the USVI Department of Labor. Controls in place over maintaining and safeguarding records related to employer files and claimant files.

One (1) out of seventy (70) claimant files selected out of a universe of approximately 11,000 files was unable to be provided as a result of the control deficiency. Four (4) out of twenty (20) employer files selected out of a universe of 215,000 files were unable to be provided.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-12 (continued)

### Program

U.S. Department of Labor - Unemployment Insurance - CFDA No. 17.225

#### **Known Questioned Costs**

\$3,095

### **Underlying Cause**

The USVI Department of Labor does not maintain adequate controls to ensure records are maintained and safeguarded as evidenced with the requested sample items backup support being unavailable.

#### Effect

Doubts may be raised by regulators over the completeness and accuracy of the underlying information within the computer system, including but not limited to: (1) labor statistics; (2) the employer's employment records within the computer system; and (3) records and statistics calculated within the computer system.

Doubts may also arise as to the existence of employers and claimants being reported due to the lack of supporting records.

#### Recommendation

The USVI Department of Labor should redesign and implement a new method of maintaining and safeguarding records of employers and claimants. Backup documentation applicable to drawdown requests should be maintained and safeguarded.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-12 (continued)

### Program

U.S. Department of Labor - Unemployment Insurance - CFDA No. 17.225

#### Management's Response

Missing employer files: 4 of 20 employer files requested for verification of employer registrations were unable to be provided.

• DOL – UI concurs. Although files were located for the four (4) employers, the particular document, the Employer Registration that was being searched for could not be found. The employers will be contacted to secure updated Employer Registration.

Missing claim files: 1 of 70 claims files requested was unable to be provided.

• DOL –UI concurs. Due to office space restrictions, most of these files had been placed in retention at an opposite location. DOL-UI will secure more file cabinets to be kept on the premises to allow for three full years of claimant closed files.

Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## U.S. Environmental Protection Agency – Performance Partnership Grants CFDA No. 66.605

Performance Partnership Grants (PPGs) are the cornerstone of the National Environmental Performance Partnership System (NEPPS)- EPA's strategy to strengthen partnerships and build a results-based management system. PPGs are innovative grant delivery tools that allow states and tribes to combine up to 20 eligible program grants into a single grant with a single budget. PPGs can reduce administrative transaction costs, provide the flexibility to direct resources toward the highest priority environmental problems, and support cross-media approaches and initiatives. EPA's overarching goal is to optimize the leveraging power of PPGs to strategically focus on the joint priorities of EPA, states and Tribes. Total Performance Partnership Grants expenditures for the fiscal year ended September 30, 2006 amounted to \$2,459,081.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-13

### Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

## Topic

The U.S.V.I. Department of Planning and Natural Resources could not provide us with evidence supporting expenditures.

## Category

Compliance/Internal Control

### **Compliance Requirement**

Activities Allowed or Unallowed, Allowable Costs/Cost Principles, Cash Management and Period of Availability

## Criteria

In accordance with 40 CFR 31.20 (6), OMB Circular A-87 Attachment C. Accounting Records must be supported by source documentation such as cancelled checks, paid bills, payrolls, time and attendance records, contract and subgrant award documents, etc. at the time of audit.

### **Condition Found**

During our testing of vendor and payroll expenditure selections totaling \$176,248 out of a universe of \$2,459,081, we noted the following (see table below):

Vendor Selections							
	Check No.	. Date		Amount	Test	Comments	
1	9180858	8/10/2006	\$	3,640	Internal Control	А	
2	9180431	9/11/2006		1,895	Internal Control	А	
3	9162841	11/28/2005		26,154	Compliance	А	
4	9171733	5/8/2006		1,970	Compliance	А	
5	5446792	4/18/2006		1,312	Compliance	А	
100(272			\$	34,971			

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

### Finding No. 06-13 (continued)

### Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

#### **Condition Found (continued)**

			Charged to		
#	Employee No.	Period Ending	Grant	Test	Comments
1	78984	11/26/2005	\$ 2,966	Compliance	В
2	60216	8/5/2006	N/A	Compliance	С
3	26948	7/22/2006	N/A	Compliance	С
4	78752	8/5/2006	N/A	Compliance	С
5	88476	8/5/2006	N/A	Compliance	С
			\$ 2,966		

### Comments:

- A. The drawdown request was not available for testing.
- B. Timesheet for employee was not available for testing.
- C. Time charged on employee timesheets did not agree to time charged on the Payroll Distribution Report. As a result, amounts charged to the grant do not agree to the amounts expended.

### **Known Questioned Costs**

\$37,937

### **Underlying Cause**

Current internal controls in the Department of Planning and Natural Resources (DPNR) are not operating effectively with regard to providing for the proper maintenance of accounting records.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-13 (continued)

### Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

### Effect

As a result, funds may be expended for unallowable costs.

#### Recommendation

The V.I. Department of Planning and Natural Resources and the Department of Finance should coordinate their efforts to maintain proper accounting records.

### Management's Response

- A. The Department of Planning and Natural Resources concurs with this finding. However, the actually attachment for the compliance testing that was made, resulted in difficulty in sorting the actual amount in the lump sum drawdown; since drawdowns are done in large volumes. Presently, the Program has now implemented procedures which call for printing figures/checks from the Enterprise Resource Planning to coincide with the draws.
- B. The Department of Planning and Natural Resources concurs with this finding. Procedures have now been put in place to ensure this deficiency does not recur. A memorandum was circulated to all employees indicating that the absence of the time distribution sheet will result in non-payment of bi-weekly salary.
- C. The Department of Planning and Natural Resources does not concur with this finding. Time per report and actual timesheet will not reconcile. Since the paycheck is cut from one account as seen on the Financial Management System and employees are paid under various grants both figures will not agree. Adjustments have to be made in each fund either up or down, resulting in the 2080 sheet.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-13 (continued)

## Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

### **Auditor's Conclusion**

For all cases in reference C, no such adjustments to the funds were provided to us. Therefore, the finding remains as stated.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-14

### Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

## Topic

The Department of Planning and Natural Resources could not provide us with evidence supporting equipment additions.

## Category

Compliance/Internal Control

### **Compliance Requirement**

Equipment and Real Property Management

### Criteria

In accordance with 40 CFR 31.20 (6), OMB Circular A-87 Attachment C, G-5.

Accounting Records must be supported by source documentation such as cancelled checks, paid bills, payrolls, time and attendance records, contract and subgrant award documents, etc. at the time of audit.

### **Condition Found**

During our testing of 6 equipment addition selections we noted the following: (See table below)

	Asset#	<b>Description</b>	Amount	Test	Reference
1	402196	Computer	\$ 1,861	Internal Control	А
2	Unavailable	Computer	1,895	Internal Control	А
3	Unavailable	Computer	 2,310	Compliance	A, B
			\$ 6,066		

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-14 (continued)

### Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

## **Condition Found (continued)**

### <u>Reference:</u>

A. The purchase order and invoice were not available for testing.

B. The item could not be agreed to Inventory Listing of Property conducted on September 30, 2006.

Our testing selections represent \$35,960 of the \$38,685 of equipment additions made by the Program for 2006.

### **Known Questioned Costs**

\$6,066

### **Underlying Cause**

Current internal controls in the Department of Planning and Natural Resources (DPNR) are not operating effectively with regard to providing for the proper maintenance of accounting records.

### Effect

As a result, funds may be expended for unallowable costs.

### Recommendation

The V.I. Department of Planning and Natural Resources and the Department of Finance should coordinate their efforts to maintain proper accounting records.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-14 (continued)

### Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

### **Management's Response**

Presently there are written procedures in place for proper maintenance of all documents by grant awards. Additionally, there are written procedures in place to update inventoried items as they occur. The effect that as a result funds may be expended for unallowable cost did not exist. All requests for purchase from EP Awards are approved for allowable and unallowable cost and the availability of funds before processing in the system. Management will ensure that employees comply with procedures in place in this regard.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-15

### Program

U.S. Environmental Protection Agency - Performance Partnership Grants - CFDA No. 66.605

## Topic

The Department of Planning and Natural Resources did not keep proper evidence supporting allocation of payroll costs.

## Category

Internal Control

### **Compliance Requirement**

Activities Allowed or Unallowed, Allowable Costs/Cost Principles, Cash Management and Period of Availability

### Criteria

In accordance with 40 CFR 31.20 (3) on internal control states that 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.

### **Condition Found**

During our testing of 40 payroll related expenditure selections, we noted that none of the timecards examined indicated that a review and approval of a supervisor was conducted.

### **Known Questioned Costs**

Not determinable.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-15 (continued)

### Program

U.S. Environmental Protection Agency – Performance Partnership Grants – CFDA No. 66.605

### **Underlying Cause**

Current internal controls in the Department of Planning and Natural Resources (DPNR) are not operating effectively with regard to providing for the evidence of review and approval of employee timesheets.

### Effect

Lack of review and approval of employee time may result in the inappropriate allocation of personnel charges to Federal grants.

### Recommendation

The V.I. Department of Planning and Natural Resources require that supervisors review and approve employee timesheets prior to submission for payment. To ensure compliance with internal control rules, timesheets should not be processed for payment until a supervisor's signature indicating approval is present.

### Management's Response

It is a requirement and procedures are in place that requires the supervisor and the employee to both sign-off on the employee's timesheets before transmitting them to payroll for processing. Management will reiterate once again to all supervisors that these procedures be followed to the letter.

Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## U.S. Department of Education - Special Education - Grants to States CFDA No. 84.027

The purposes of the Individuals with Disabilities Education Act (IDEA) are to: (1) ensure that all children with disabilities have available to them a free appropriate public education (FAPE) which emphasizes special education and related services designed to meet their unique needs; (2) ensure that the rights of children with disabilities and their parents or guardians are protected; (3) assist States, localities, educational service agencies and Federal agencies to provide for the education of all children with disabilities; and (4) assess and ensure the effectiveness of efforts to educate children with disabilities. The Assistance for Education of All Children with Disabilities Program (Special Education – Grants to States - IDEA, Part B) provides grants to States to assist them in meeting these purposes (20 USC 1400 et seq.). Total Special Education – Grants to States expenditures for the fiscal year ended September 30, 2006 amounted to \$10,012,737.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-16

### Program

U.S. Department of Education - Special Education - Grants to States - CFDA No. 84.027

## Topic

The U.S.V.I. Department of Education could not provide us with evidence supporting payroll expenditures.

## Category

Compliance/Internal Control

### **Compliance Requirement**

Activities Allowed or Unallowed, Allowable Costs/Cost Principles, Cash Management and Period of Availability

## Criteria

In accordance with 34 CFR 80.20 (b)(6) Accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and subgrant award documents, etc.

In addition, in accordance with OMB Circular A-87, Attachment B, sections 8(h)(3) and 8(h)(4) related to support of salaries and wages requires the following: Employees that are expected to work solely on a single Federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications will be prepared at least semi-annually and will be signed by the employee or supervisory official having first hand knowledge of the work performed by the employee. Furthermore, where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-16 (continued)

### Program

U.S. Department of Education - Special Education - Grants to States - CFDA No. 84.027

### **Criteria** (continued)

documentation which meets the standards in subsection (5) (see below) unless a statistical sampling system or other substitute system has been approved by the cognizant Federal agency. Such documentary support will be required where employees work on:

- (a) More than one Federal award,
- (b) A Federal award and a non-Federal award,
- (c) An indirect cost activity and a direct cost activity,
- (d) Two or more indirect activities which are allocated using different allocation bases, or
- (e) An unallowable activity and a direct or indirect cost activity.

Subsection (5): Personnel activity reports or equivalent documentation must meet the following standards:

- (a) They must reflect an after-the-fact distribution of the actual activity of each employee,
- (b) They must account for the total activity, for which each employee is compensated,
- (c) They must be prepared at least monthly and must coincide with one or more pay periods, and
- (d) They must be signed by the employee.

### **Condition Found**

During our testing of payroll related expenditures, we noted 3 out of 25 transactions tested with no certification of amount of time spent on the program, as listed below. The sample population was \$806,049 and the universe of payroll expenditures was \$6,421,881.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-16 (continued)

### Program

U.S. Department of Education - Special Education - Grants to States - CFDA No. 84.027

### **Condition Found (continued)**

In addition, we were unable to reconcile payroll amounts charged to the program in the submitted report by the third party fiduciary to the payroll records and Notice of Personnel Action forms (NOPA) for all selected payroll expenses.

Employee #	District	% Payroll Allocable to Federal Grant	Charged to Grant	
43736	STX	0.60%	\$	353
94382	STX	100%		24,470
94840	STX	6.70%		1,647
			\$	26,470

### **Known Questioned Costs**

\$26,470. However, likely questioned costs could be significantly higher due to the condition described above related to not being able to reconcile amounts charged to the program with NOPA.

### **Underlying Cause**

Current internal controls are not operating effectively with regards of providing the evidence of proper review and approval of employee time worked on the Federal program.

### Effect

The lack of evidence supporting review and approval of employee time may result in the inappropriate allocation of personnel charges to Federal grants, leading to reimbursement being made for unallowable costs.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-16 (continued)

### Program

U.S. Department of Education - Special Education - Grants to States - CFDA No. 84.027

#### Recommendation

The V.I. Department of Education should ensure that evidence of proper review and approval of employee time spent working on each program is maintained.

#### Management's Response

VIDE does not concur with this finding. The Third Party Fiduciary conducted a payroll audit which resulted in the determination for USDE reimbursement to the VIDE.

### **Auditor's Conclusion**

Requirements established by the cited criteria were not complied with. The fact that a third-party fiduciary conducted a payroll audit and that the USDE reimbursed VIDE for these costs are not by themselves evidence of these compliance violations being waived. Therefore, the finding remains as stated.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-17

### Program

U.S. Department of Education - Special Education - Grants to States - CFDA No. 84.027

## Topic

No physical inventory of equipment acquired with Federal funds has been performed for two years.

## Category

Compliance/Internal Control

### **Compliance Requirement**

Equipment and Real Property Management

### Criteria

In accordance with 34 CFR 80.32(d)(2) A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years; also, in accordance with OMB Circular A-87, Appendix B to Part 225, 11 f(3)h, physical inventories must be taken at least once every two years (a statistical sampling approach is acceptable) to ensure the assets exist and are in use.

### **Condition Found**

During our testing of equipment and real property management, we noted that a physical inventory of the property had not been performed within the past two years. We also noted that no purchase of new equipment and real property was made throughout the year.

### **Known Questioned Costs**

N/A

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-17 (continued)

### Program

U.S. Department of Education - Special Education - Grants to States - CFDA No. 84.027

### **Underlying Cause**

The V.I. Department of Education's internal controls over property and equipment purchased with Federal funds are not effective.

#### Effect

The V.I. Department of Education is exposed to the risk of possible unauthorized use and disposition of equipment due to the lack of internal controls. The lack of proper inventory controls for equipment acquired with Federal funds could result in disallowed costs.

#### Recommendation

The V.I. Department of Education should implement effective internal control procedures to ensure that the requirements of property acquired with the Federal funds are met.

#### Management's Response

VIDE concurs with this finding. As part of its Standard Operating Procedures, VIDE has implemented inventory procedures that address deadlines for physical inventories and policies on equipment distribution and location, transfers, dispositions, stolen, missing and damaged equipment and all applicable forms. Training with schools and activity center Inventory Managers will begin March 2009.

Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## U.S. Department of Education - Innovative Education CFDA No. 84.298

This former Title VI program was reauthorized by the No Child Left Behind Act (NCLB Act), Pub. L. No. 107-110, as Title V, Part A of the Elementary and Secondary Education Act (ESEA). The objectives of Title V, Part A are to: (1) support local educational reform efforts that are consistent with and support statewide education reform efforts; (2) provide funding to enable State Educational Agencies (SEAs) and Local Educational Agencies (LEAs) to implement promising educational reform programs and school improvement programs based on scientifically based research; (3) provide a continuing source of innovation, and educational improvement, including support programs to provide library services and instructional and media materials; (4) meet the educational needs of all students, including at-risk youth; and (5) develop and implement education programs to improve school, student, and teacher performance, including professional development activities and class size reduction programs (Title V, Part A, Section 5101(a) of the ESEA (20 USC 7201(a))). Total State Grant for Innovative Programs expenditures for the fiscal year ended September 30, 2006 amounted to \$7,630,275.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-18

### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

## Topic

The Department of Education could not provide us with evidence supporting payroll expenditures.

## Category

Compliance/Internal Control

### **Compliance Requirement**

Activities Allowed or Unallowed, Allowable Costs/Cost Principles, Cash Management and Period of Availability

## Criteria

In accordance with 34 CFR 80.20 (b)(6) Accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and subgrant award documents, etc.

In accordance with OMB Circular A-87, Attachment B, sections 8(h)(3) and 8(h)(4) related to support of salaries and wages. Employees are expected to work solely on a single Federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications will be prepared at least semi-annually and will be signed by the employee or supervisory official having first hand knowledge of the work performed by the employee. Furthermore, where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation which

## Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

### Finding No. 06-18 (continued)

### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

### **Criteria** (continued)

meets the standards in subsection (5) (see below) unless a statistical sampling system or other substitute system has been approved by the cognizant Federal agency. Such documentary support will be required where employees work on:

- (a) More than one Federal award,
- (b) A Federal award and a non-Federal award,
- (c) An indirect cost activity and a direct cost activity,
- (d) Two or more indirect activities which are allocated using different allocation bases, or
- (e) An unallowable activity and a direct or indirect cost activity.

Subsection (5)-Personnel activity reports or equivalent documentation must meet the following standards:

- (a) They must reflect an after-the-fact distribution of the actual activity of each employee,
- (b) They must account for the total activity for which each employee is compensated,
- (c) They must be prepared at least monthly and must coincide with one or more pay periods, and
- (d) They must be signed by the employee.

### **Condition Found**

During our internal control and compliance testing of payroll related expenditures, we noted that the following 23 out of 23 payroll amounts charged to the grant selected for testing had no evidence of the time and effort allocated to this program. Total payroll costs charged to the program amounted to \$2,292,002.

Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

### Finding No. 06-18 (continued)

### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

## **Condition Found (continued)**

In addition, we were unable to reconcile payroll amounts charged to the program in the submitted report by the third party fiduciary to the payroll records and Notice of Personnel Action forms (NOPA) for all selected payroll related expenditures.

	Employee			<b>Federal Grant</b>			
#	Number	Test	Option	Allocation %	A	Amount	
1	19294	Internal Control	940	16.70%	\$	34,498	
2	68358	Internal Control	818	71.60%		55,277	
3	70797	Internal Control	819	1.40%		252	
4	64492	Internal Control	819	1.50%		266	
5	39426	Internal Control	819	0.60%		504	
6	42791	Internal Control	819	2.10%		504	
7	15104	Internal Control	819	1.00%		660	
8	71533	Internal Control	819	2.60%		645	
9	88381	Internal Control	819	2.60%		435	
10	95627	Internal Control	819	100.00%		1,563	
11	63466	Internal Control	819	71.60%		59,221	
12	59881	Internal Control	822	1.20%		324	
13	11522	Internal Control	822	2.20%		748	
14	62188	Internal Control	822	3.20%		1,138	
15	46753	Internal Control	822	2.00%		1,592	
16	20406	Internal Control	822	5.20%		1,620	
17	75523	Internal Control	822	4.10%		1,656	
18	Unavailable	Internal Control	822	3.00%		1,764	
19	52156	Internal Control	822	6.20%		2,052	
20	66640	Internal Control	822	7.10%		3,016	
21	63300	Internal Control	822	5.60%		3,091	
22	87166	Internal Control	822	96.90%		43,636	
23	47333	Compliance	822	5.40%		2,565	
				Total	\$	217,028	

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-18 (continued)

### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

### **Known Questioned Costs**

\$217,028. However, likely questioned costs could be significantly higher due to the condition described above related to not being able to reconcile amounts charged to the program with NOPA.

#### **Underlying Cause**

Current internal controls are not operating effectively with regards to providing for the evidence of proper review and approval of employee time charged to the program.

#### Effect

The lack of evidence supporting review and approval of employee time may result in the inappropriate allocation of personnel charges to Federal grants, leading to reimbursement being made for unallowable costs.

#### Recommendation

The V.I. Department of Education should demonstrate that evidence of proper review and approval of employee time charged to each program is maintained.

#### Management's Response

VIDE does not concur with the findings. The Third Party Fiduciary conducted a payroll audit which resulted in the determination for USDE reimbursement to the VIDE.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-18 (continued)

### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

#### **Auditor's Conclusion**

Requirements established by the cited criteria were not complied with. The fact that a third-party fiduciary conducted a payroll audit and that the USDE reimbursed VIDE for these costs are not by themselves evidence of these compliance violations being waived. Therefore, the finding remains as stated.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-19

### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

#### Topic

No physical inventory of equipment acquired with Federal funds has been performed for two years.

### Category

Compliance/Internal Control

### **Compliance Requirement**

Equipment and Real Property Management

### Criteria

In accordance with 34 CFR 80.32(d)(2) A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years; also, in accordance with OMB Circular A-87, Appendix B to Part 225, 11 f(3)h, physical inventories must be taken at least once every two years (a statistical sampling approach is acceptable) to ensure the assets exist and are in use.

### **Condition Found**

During our testing of equipment and real property management, we noted that a physical inventory of the property had not been performed within the past two years. Furthermore, a list of equipment and real property for the program was not provided for us to test.

#### **Known Questioned Costs**

Could not be determined

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-19 (continued)

#### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

### **Underlying Cause**

The V.I. Department of Education's internal controls over property and equipment purchased with Federal funds are not effective.

#### Effect

The V.I. Department of Education is exposed to the risk of possible unauthorized use and disposition of equipment due to the lack of internal controls.

#### Recommendation

The V.I. Department of Education should implement effective internal control procedures to ensure that the requirements of property acquired with the Federal funds are met.

#### Management's Response

VIDE concurs with the finding. With the implementation of the ERP System, VIDE will:

(1) Manage all public school recordkeeping of all fixed assets such as machinery and equipment: All public school fixed assets such as machinery and equipment are kept in an Excel spreadsheet. All information such as purchase order number, vendor, serial number, model number, property tag number, physical location, federal or local funding, date of service is kept in the Excel spreadsheet, and the information is shared with the Department of Property and Procurement that verifies the information submitted. The Fixed Asset Module in Tyler Munis has not been brought online. It is expected to be online sometime in fiscal year 2009.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

### Finding No. 06-19 (continued)

### Program

U.S. Department of Education - Innovative Education - CFDA No. 84.298

#### Management's Response

- (2) Create asset records from requisitions or directly from invoices: Asset records are created from requisitions and invoices/packing slips. Once a requisition is procured and converted into a purchase order, we receive the items and match them with the purchase order and the corresponding invoice/packing slip. That generates the asset record for that PO and corresponding equipment.
- (3) Implement and integrate barcode tracking system: We are in the process of purchasing barcode scanner. The barcode scanner will assist with the inventory and distribution of equipment. They will improve accuracy and speed in processing equipment and in also tracking the fixed assets.
- (4) Automate inventory counts and manage all inventory accounting automatically including onhand balances and month-to-date (MTD) and year-to-date (YTD) values: The inventory module in Tyler-Munis has not been brought online. It is expected to be online some time in fiscal year 2009. The information is presently being kept in an Excel spreadsheet.

# Schedule of Findings and Questioned Costs

# Part III – Federal Awards Findings and Questioned Costs Section (continued)

## U.S. Department of Health and Human Services - Child Support Enforcement

### CFDA No. 93.563

The objectives of the Child Support Enforcement programs are to: (1) enforce support obligations owed by non-custodial parents, (2) locate absent parents, (3) establish paternity, and (4) obtain child and spousal support. Total Child Support Enforcement expenditures for the year ended September 30, 2006 amounted to \$3,243,733.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-20

### Program

U.S. Department of Health and Human Services - Child Support Enforcement - CFDA No. 93.563

## Topic

The V.I. Department of Justice (VIDOJ) overstated payroll expenditures requested for reimbursement.

## Category

Compliance/Internal Control

### **Compliance Requirement**

Activities Allowed or Unallowed, Allowable Costs/Cost Principles

### Criteria

A cost is allowable for Federal reimbursement only to the extent of benefits received by Federal awards and its conformance with the general policies and principles stated in OMB Circular A-87, Appendix A, Section C1a through h.

The individual operating agencies are responsible for the performance or administration of Federal awards. In order to receive cost reimbursement under Federal awards, the department or agency usually submits claims asserting that allowable and eligible costs (direct and indirect) have been incurred in accordance with OMB Circular A-87.

Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-20 (continued)

## Program

U.S. Department of Health and Human Services - Child Support Enforcement - CFDA No. 93.563

## **Condition Found**

We tested 12 out of the 26 payrolls representing payroll costs charged to the program totaling \$3,168,689 (Federal and state share). Of the 12 payrolls tested of \$2,616,561 (Federal and state share) we noted that 9 of those payrolls overstated payroll expense charged to the program by approximately \$341,000 (Federal share).

#### **Known Questioned Costs**

\$341,000

#### **Underlying Cause**

During management's calculation of the monthly payroll expense, they mistakenly included the total from the Payroll Breakdown report instead of using the gross payroll balance to determine the monthly payroll expense. The total balance listed on the Payroll Breakdown report includes, the employee's gross payroll, insurance, FICA and retirement expenses. Therefore, the gross amount included in the calculation was overstated by the employee's insurance, FICA and retirement expenses.

#### Effect

The Quarterly Reports of Expenditures and Estimates (Form OCSE-396A) that were submitted to the U.S. Department of Health and Human Services for reimbursement were overstated by \$341,000. As such, the Government was reimbursed for an additional \$341,000 over its allowable costs.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-20 (continued)

#### Program

U.S. Department of Health and Human Services - Child Support Enforcement - CFDA No. 93.563

#### Recommendation

Management should initiate an internal control in which a second level review is performed of the payroll expense calculation prior to Quarterly Report of Expenditures and Estimates being submitted to the Federal Government. Further, in order for the control to be effective, the Program should maintain evidence of this process by retaining the payroll expense calculation with appropriate preparer and reviewer sign-offs.

Furthermore, management should make the necessary corrections to restate their 2006 Quarterly Report of Expenditures and Estimates to properly state the Net Federal Share of Expenditures.

#### Management's Response

The Division concurs with this finding. An adjustment was made on the OCSE 396A for the quarter ending September 30, 2008, to correct the overstatement. Internal control measures, already in place to ensure the correctness of calculations prior to submitting reports to the Federal government, have been strengthened to avoid such errors in the future.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-21

#### Program

U.S. Department of Health and Human Services - Child Support Enforcement – CFDA No. 93.563

#### Topic

Lack of adequate controls over cash drawdowns caused noncompliance with the CMIA agreement.

#### Category

Internal Control/Compliance

#### **Compliance Requirement**

Cash Management

#### Criteria

In accordance with the executed Cash Management Improvement Act agreement (CMIA) for the period of October 1, 2005 to September 30, 2007, under the U.S. Department of Treasury regulations at 31 CFR part 205, the Government requires the use of an "average clearance" funding technique for vendor and payroll related costs. Under the "average clearance" funding technique, the Government may submit claims for reimbursement such that the funds are deposited, by ACH on the dollar-weighted average day of clearance, in the Government's bank account on the fourth day following the release of funds for vendor disbursements and on the day in which payroll checks are released for payroll related costs. Furthermore, reimbursement requests shall be for the exact amounts disbursed.

## Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-21 (continued)

#### Program

U.S. Department of Health and Human Services - Child Support Enforcement - CFDA No. 93.563

#### **Condition Found**

We tested 17 out of the 52 drawdowns totaling \$3,498,728 performed during fiscal year 2006. Of the 17 drawdowns tested in the amount of \$1,783,642, 13 of them in the amount of \$1,556,927 were not in compliance with the clearance funding patterns stipulated in the CMIA Agreement according to mail logs maintained by the Department of Finance as follows:

	Drawdown					
Sample	Reimbursement Month Amount	Date Check	Requested	Drawdown	Variance	
Number		Amount	was Released	Date	Receipt Date	(In days)
1	Jul-06	\$258,589	7/11/2006	7/14/2006	7/17/2006	6
2	Sep-06	\$144,607	8/24/2006	9/8/2006	9/11/2006	18
3	Jul-06	\$132,950	7/6/2006	7/21/2006	7/24/2006	18
5	Mar-06	\$131,271	3/7/2006	3/9/2006	3/10/2006	3
6	Jan-06	\$301,400	12/19/2006	1/9/2006	1/10/2006	22
7	Aug-06	\$ 73,857	8/3/2006	8/17/2006	8/18/2006	15
8	Aug-06	\$ 84,120	8/3/2006	8/10/2006	8/11/2006	8
9	Jun-06	\$ 74,702	6/8/2006	6/21/2006	6/22/2006	14
12	Apr-06	\$ 82,997	3/23/2006	4/4/2006	4/5/2006	13
13	Apr-06	\$ 66,455	3/16/2006	4/3/2006	4/4/2006	19
14	May-06	\$ 33,993	5/2/2006	5/5/2006	5/8/2006	6
16	Oct-06	\$102,542	9/29/2005	10/5/2006	10/6/2006	7
17	Mar-06	\$ 68,074	3/2/2006	3/6/2006	3/7/2006	5

In all cases, the noncompliance relates to drawdowns being requested after the specified date as per CMIA Agreement. While this did not lead to drawing funds in advance of CMIA established timing, it is evidence of lack of sufficient or effective internal controls over drawdowns requirements.

#### **Known Questioned Costs**

Not applicable.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-21 (continued)

#### Program

U.S. Department of Health and Human Services - Child Support Enforcement - CFDA No. 93.563

#### **Underlying Cause**

The Department of Finance's policies and procedures are not designed and operating effectively to ensure that all drawdowns are being reviewed to guarantee that they are made within the guidelines established by the CMIA Agreement.

#### Effect

This Department of Finance's control deficiency could adversely affect the Government's ability to comply with the cash management requirement of this Federal program.

#### Recommendation

The Department of Finance should design and implement controls to ensure compliance with the CMIA Agreement. Management should consider periodic monitoring, verification, and reporting of the Department of Finance's progress in implementing the controls.

#### Management's Response

The Division concurs with this finding. PCSD continues to work with Department of Finance to improve compliance with cash management procedures, and has instituted internal control measures to ensure that all drawdowns are made within the guidelines established by the CMIA Agreement.

Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

The objective of the Medical Assistance Program (Medicaid or Title XIX of the Social Security Act, as amended, (42 USC 1396 et seq.)) is to provide payments for medical assistance to low-income persons who are age 65 or over, blind, disabled, or members of families with dependent children or qualified pregnant women or children. Medical Assistance Program expenditures for the fiscal year ended September 30, 2006, amounted to \$5,815,224.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-22

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

## Topic

The Bureau of Health and Insurance and Medical Assistance (the Bureau) did not reconcile Federal financial reports to the Government's financial records (FMS).

## Category

Compliance/Internal Control

#### **Compliance Requirement**

Reporting

#### Criteria

Pursuant to 45 CFR 92.20(b)(1), 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.

#### **Condition Found**

We noted an error in the amounts reported in the Federal financial report (CMS64) certification for the quarter ended September 30, 2006, due to an input error in the prior period adjustment section of form CMS 64.9P, as follows. We selected one of the four quarters to test.

Fourth quarter adjustment, as reported in CMS 64.9P	\$3,642,633
Fourth quarter adjustment, per program records	895,078
	\$2,747,555

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-22 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### **Condition Found (continued)**

As a result, the CMS64 Certification reported an overstated Federal share amount of \$8,169,815, instead of \$5,422,260. (Note: Amounts reported in the CMS 64 Certification includes program expenditures other than Medicaid Title XIX, like SCHIP and Medicaid Part D, not in the scope of our audit procedures)

#### **Known Questioned Costs**

\$2,747,555

#### **Underlying Cause**

Current procedures do not include a proper review of reported information.

#### Effect

Lack of a supervisory review of reports may result in undetected errors in Federal financial reports. These may lead to incorrect financial information presented in reports submitted to the Federal government for reimbursement.

#### Recommendation

The Bureau should establish procedures to ensure Federal financial reports are properly reviewed by trained supervisory personnel.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-22 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### Management's Response

All federal funds drawn were reconciled with the federal system. For the local system, a full reconciliation of draws posted in the FMS was not completed for fiscal year 2006 due to the shortage of staff in the fiscal office. The limited fiscal staff was responsible for the end of the year closeout workload while at the same time preparing for a new computer system (ERP). The fiscal office was and still is in dire need of staff. The reconciliation will be completed to identify draws which make up the difference between the FMS total and the Department of Health – Medicaid total on file for fiscal year 2006.

The fiscal year 2006 fourth quarter CMS 64 Report was revised to reflect the fiscal year 2006 encumbrances that were processed in the first quarter of fiscal year 2007. The error occurred due to lack of adequate training in posting of adjustments in the federal system for the CMS 64 Reports. The total amount for adjustments was combined with the original fourth quarter total to show the revised total expenditure for the fiscal year 2006 fourth quarter. However, the data was entered into the wrong section of the report which resulted in an error. Additional training on how to prepare the many CMS Reports is needed. In the meantime, the revised CMS 64 Report for the fiscal year 2006 fourth quarter amount in the correct section for prior period adjustments.

There is a clear need for an Internal Auditor for a program like Medicaid. With the services of an Internal Auditor many of the discrepancies detected by the Single Audit would be resolved. This is a necessity especially when the fiscal office lacks the manpower to manage the various accounts. Fiscal year 2006 expenditure will be reviewed and the fiscal year 2006 CMS 64 Quarterly Reports will be revised to reflect each of the four quarters based on the local FMS final total.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-23

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

## Topic

The Bureau could not provide us with evidence supporting eligibility of participants.

## Category

Compliance/Internal Control

#### **Compliance Requirement**

Eligibility

#### Criteria

As described in 42 USC 1320b-7(d); 42 CFR sections 435.907 and 435.913, a written application signed under penalty of perjury and inclusion in each applicant's case records facts to support the agency's decision on the application is required.

#### **Condition Found**

During our testing of eligibility for individuals, for 9 out of 25 cases, we were unable to conclude on the eligibility determination of the cases due to the following conditions explained in the table below:

No.	MAP Case Number	Comment
1	6A0310102242101	Α
2	7C0370179203113	Α
3	8A0380045152202	Α
4	8C0380195092112	Α

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-23 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### **Condition Found (continued)**

No.	MAP Case Number	Comment
5	8C0380195592202	Α
6	6C0360136882202	В
7	7C0370181082211	В
8	8C0370096963202	В
9	8C0380191482115	В

#### Comment:

**A**. The application form is missing from the participant file. **B**. The participant file was not provided.

#### **Known Questioned Costs**

Could not be determined.

#### **Underlying Cause**

Although current internal controls provide that eligibility documentation should be maintained in the participant's records, the department responsible for the program was unable to locate the supporting documents of the participant's files selected.

#### Effect

The program may have awarded Federal funds to an individual who is not eligible to participate in the program.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-23 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### Recommendation

The V.I. Department of Health should implement procedures to ensure that all participant files are properly maintained and available.

#### Management's Response

- A. DOH –MAP concurs. Four (4) of (or the four (4) files) were inaccessible due to storage in a room in the St. Croix office which was cordoned off by the EPA because of mold.
- B. Four (4) of the files (or the four files) were inaccessible due to storage in a room in the St. Croix office which was cordoned off by the EPA because of mold.

A mold remediation program has been initiated in the St. Croix building. Further, MAP anticipates scanning patient information in its VIMS (Virgin Islands Medicaid System) in addition to capturing other data and information in the ERP (Enterprise Resource Planning) System.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-24

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

## Topic

The Bureau could not provide us with evidence supporting compliance with requirements for the Special Test and Provision specified below.

## Category

Compliance/Internal Control

#### **Compliance Requirement**

Special Tests and Provisions: Utilization Control and Program Integrity

#### Criteria

The State plan must provide methods and procedures to safeguard against unnecessary utilization of care and services, including long-term care institutions. In addition, the State must have: (1) methods or criteria for identifying suspected fraud cases; (2) methods for investigating these cases; and (3) procedures, developed in cooperation with legal authorities, for referring suspected fraud cases to law enforcement officials (42 CFR parts 455, 456, and 1002).

#### **Condition Found**

The V.I. Bureau of Insurance and Medical Assistance (the Bureau) did not provide supporting documentation to evidence the performance of the procedures throughout the fiscal year of the criteria above.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-24 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### **Known Questioned Costs**

Not applicable

#### **Underlying Cause**

Although the State Plan provides methods and procedures against unnecessary utilization of care and services, the Bureau does not have appropriate controls in place to ensure these procedures are performed.

#### Effect

The lack of internal controls to ensure these procedures are performed may lead to unnecessary utilization of care and services and non-compliance with the program requirements.

#### Recommendation

The Bureau should establish appropriate controls to ensure that procedures to safeguard against unnecessary utilization of care and services are placed in operation.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-24 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### Management's Response

The Bureau hired the required Quality Control staff to implement the program in fiscal year 2007. The Quality Control Chief (a Territorial appointment) as well as the necessary Front End Investigative staff for the districts of St. Thomas and St. Croix were hired. In the case of long term care, Sea View – the Nursing Home Facility must submit a Cost Report annually to Medicaid. This Cost Report is audited by an auditor contracted by Medicaid. Any difference in the costs is calculated at the Average Medicare Rate which is used among the states.

With the necessary staff in place, program personnel can do more reviews, investigations, and site visits in order to increase vigilance against program fraud and waste. The Bureau is currently in the process of acquiring additional office space to include the Quality Control Unit.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-25

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

## Topic

The program did not operate a Medicaid Eligibility Quality Control System, as required.

## Category

Internal Control/Compliance

#### **Compliance Requirement**

Eligibility

#### Criteria

Pursuant to 42 USC 1396b and 42 CFR parts 431.800 through 431.865, states are required to operate a Medicaid Eligibility Quality Control (MEQC) system in accordance with requirements established by the Centers for Medicare and Medicaid Services (CMS). The MEQC system redetermines eligibility for individual sampled cases of beneficiary eligibility made by state Medicaid agencies or their designees.

However, most states are operating MEQC pilots or have been given a waiver from the traditional MEQC program described in regulation. The pilots and waivers differ from the traditional MEQC program by performing special studies, targeted reviews, or other activities that are designed to ensure program integrity or improve program administration.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-25 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### **Condition Found**

During fiscal year 2006, the program did not have a functioning MEQC system or any other alternative procedures in place to perform the required eligibility redeterminations.

A similar situation was included in the 2005 OMB Circular A-133 Report as Finding No. 05-37.

#### **Known Questioned Costs**

None.

#### **Underlying Cause**

The personnel hired to administer this process resigned during fiscal year 2003. The program is in the process of interviewing qualified individuals to fill positions required to administer the MEQC system.

#### Effect

The program is not in compliance with 42 USC 1396b and 42 CFR part 431.800 through 431.865.

#### Recommendation

We recommend that the program develop a MEQC system and perform the required eligibility redeterminations pursuant to 42 USC 1396b and 42 CFR part 431.800 through 431.865.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-25 (continued)

#### Program

U.S. Department of Health and Human Services - Medical Assistance Program (Medicaid-Title XIX) – CFDA No. 93.778

#### Management's Response

With regards to the regulations that required BHIMA to operate a MEQC system, the Territories are not required to have an MEQC system. This requirement does not apply to Puerto Rico, Guam, the Virgin Islands, the Northern Mariana Islands, or American Samoa. However, BHIMA does acknowledge the value of a Quality Control Unit and it is still the program's intention to complete establishment of the unit.

#### **Auditor's Conclusion**

No documentation or specific reference was provided that waives the requirement to the Virgin Islands of the aforementioned CFR. Therefore, this finding remains as stated.

Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26

## Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

## Topic

Inadequate and/or insufficient internal control over Federal expenditures were identified.

## Category

Internal Control

## Criteria

The A-102 Common Rule requires that non-Federal entities receiving Federal awards (i.e., auditee management) establish and maintain internal control designed to reasonably ensure compliance with Federal laws, regulations and program compliance requirements.

The objectives of internal control pertaining to the compliance requirements for Federal programs (Internal Control Over Federal Programs), as found in §\_\_\_\_\_.105 of OMB Circular A-133, are as follows:

- 1. Transactions are properly recorded and accounted for to:
  - i. Permit the preparation of reliable financial statements and Federal reports;

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### **Criteria** (continued)

- ii. Maintain accountability over assets; and
- iii. Demonstrate compliance with laws, regulations, and other compliance requirements;
- 2. Transactions are executed in compliance with:
  - i. Laws, regulations and the provisions of contracts or grant agreements that could have a direct and material effect on a Federal program; and
  - ii. Any other laws and regulations that are identified in the compliance supplements; and
- 3. Funds, property and other assets safeguarded against loss from unauthorized use of disposition.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### **Condition Found**

The Government lacked sufficient procedures and controls over the monitoring of Federal expenditures in the following programs for the following compliance requirements:

CDFA #	Program	Requirement
10.551, 10.561	Food Stamps Cluster	Matching, Level of Effort, Earmarking; Reporting
10.555, 10.559	Child Nutrition Cluster	Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Cash Management; Matching, Level of Effort, Earmarking; Period of Availability of Federal Funds; Procurement, Suspension and Debarment; Reporting; Special Tests and Provisions; Accountability of Commodities

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

#### Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

CDFA #	Program	Requirement
10.557	Special Supplemental Nutrition Program for Women, Infants and Children (WIC)	Equipment and Real Property Management; Reporting; Special Tests and Provisions
17. 225	Unemployment Insurance	Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Cash Management; Eligibility; Matching, Level of Effort, Earmarking; Period of Availability of Federal Funds; Reporting; Special Tests and Provisions: Employer Experience Rating
66.605	Performance Partnership Grants	Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Cash Management; Equipment and Real Property Management; Period of Availability of Federal Funds

#### **Condition Found (continued)**

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

CDFA #	Program	Requirement
84.027	Special Education – State Grant Programs	Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Cash Management; Equipment and Real Property Management; Period of Availability of Federal Funds
84.298	Innovative Education	Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Cash Management; Equipment and Real Property Management; Period of Availability of Federal Funds
93.563	Child Support Enforcement	Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Cash Management

#### **Condition Found (continued)**

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### **Condition Found (continued)**

CDFA #	Program	Requirement
93.778	Medical Assistance Program (Medicaid-Title XIX)	Activities Allowed or Unallowed; Allowable Costs/Cost Principles; Eligibility; Matching, Level of Effort, Earmarking; Period of Availability of Federal Funds; Procurement, Suspension and Debarment; Reporting; Special Tests and Provisions: Utilization Control and Program Integrity

There is a lack of an effective internal control to reasonably assure compliance with the requirements of Federal laws, regulations and program compliance requirements. The Government has deficiencies in internal control such as the absence of sufficient level of control consciousness throughout all of the Government's separate administrative operations, the absence of an appropriate segregation of duties, the absence of appropriate management review and approval of transactions, accounting entries and financial and other reporting.

Due to its nature and magnitude, this significant deficiency is considered to be a material weakness.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### **Known Questioned Costs**

None.

#### **Underlying Cause**

Inadequate internal controls over compliance exist.

#### Effect

Internal controls are not sufficiently designed to detect material noncompliance with Federal laws, regulations and program compliance requirements.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### Recommendation

The Government should implement internal controls to provide reasonable assurance that:

- Transactions are properly recorded and accounted for to permit the preparation of reliable financial statements and Federal reports, maintain accountability over assets; and demonstrate compliance with laws, regulations, and other compliance requirements.
- Transactions are executed in compliance with laws, regulations and the provisions of contracts or grant agreements that could have direct and material effect on a Federal program.
- Supporting documentation should be maintained, organized and filed in a manner to facilitate retrieval.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### **Management's Response**

The Government only partially concurs with this finding. Specific concurrence or lack thereof for specific findings related to compliance requirements referenced under individual programs listed by CFDA numbers can be found in Finding Nos. 06-06 to 06-25.

In general, however, the Government has an Accounting Manual that has been updated over the years through various memorandums. Such procedures, for example, required the use of Miscellaneous Disbursement Vouchers (MDVs) and Miscellaneous Encumbrance Documents (MEDs). An MDV which was used to facilitate a payment on the FMS (Financial Management System) was prepared by one employee and reviewed by at least one other employee. Ultimately the Department Head or his/her designee would receive the document for review and signature prior to forwarding it to the Department of Finance (DOF) for further processing. DOF then instituted its own internal review process prior to finalizing the transaction on the FMS.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### Management's Response (continued)

With the Government's transition from the FMS to the ERP (Enterprise Resource Planning) System there was a requisite need to update its forms and its processes, as applicable. The Office of Management and Budget (OMB) plays a role in monitoring federal expenditures from a budget perspective. Department and agencies complete a Federal Budget Plan form which must be signed by the Department Head and/or his designee prior to submission to OMB. OMB has its internal review process prior to allocating the budget by specific categories. Similarly, in addition to revisions to the budget form, OMB likewise (in conjunction with DOF) updated the indirect cost procedures and related documents. Also to foster the use of Best Business Practices, the Government previously consulted to map out its business processes: "As Is" and "To Be".

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### Management's Response (continued)

Some relevant procedures and/or controls with respect to some of the compliance requirements are as follows:

#### (1) Suspension and Debarment

The template for Professional Services contracts for the Government has been updated to include a clause/provision that addresses this requirement. Also some programs peruse or download such list as applicable. OMB will consult with the Departments of Property and Procurement and Justice regarding accessing and providing a Suspension and Debarment list to departments and agencies on a scheduled basis.

#### (2) Reporting and Reconciliation

Reconciliation was addressed in the response to Finding 06-05. OMB could institute a policy of sending out reminder and/or delinquency notices government-wide, to foster and strongly encourage the timeliness of submitting financial reports upon augmenting its staff.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### Management's Response (continued)

#### (3) Allowable Costs

In general findings related to this requirement resulted due to lack of documentation and/or the timeliness of providing the required substantiation. OMB previously provided departments and agencies with a general guideline/format for structuring a grant file to include, reports, awards/amendments, etc. This however, did not involve capturing all expenditures by documents. Ideally that would be reserved for vendor files. However, we can revisit the format provided to investigate the need for redundancy, as well as the impact that currently scanning supporting documents on the ERP would have.

# Schedule of Findings and Questioned Costs

Part III - Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### Management's Response (continued)

#### (4) Cash Management

OMB has previously requested and received a copy of the Treasury-State Agreement which was distributed to departments and agencies. The programs are cognizant of the clearance pattern and the methodology (e.g., average clearance). In response to Program Managers and Fiscal Officers along with OMB at prior monitoring meetings, DOF updated the FMS to reflect check distributions. This information was invaluable in allowing staff to time draws relative to related expenditures. A similar ERP enhancement would serve the same purpose. Staff also communicated and coordinated with the CMIS Coordinator housed in DOF. This is still an on-going function maintained by DOF.

#### (5) Property Management

The Department of Property and Procurement (P&P) has a manual which has been updated/revised. P&P also communicates often with departments re: documentation for acquisitions and has a point of contact and related forms for approval to address disposal and/or transfer of assets. P&P has also been working diligently in consultation with DOF to bring the Fixed Asset Module (ERP) on-line.

# Schedule of Findings and Questioned Costs

Part III – Federal Awards Findings and Questioned Costs Section (continued)

## Finding No. 06-26 (continued)

#### Program

- U.S. Department of Agriculture: Food Stamp Cluster CFDA Nos. 10.551 and 10.561; Child Nutrition Cluster CFDA Nos. 10.555 and 10.559; Special Supplemental Nutrition Program for Women, Infants and Children CFDA No. 10.557
- U.S. Department of Labor: Unemployment Insurance CFDA No. 17.225
- U.S. Environmental Protection Agency: Performance Partnership Grants CFDA No. 66.605;
- U.S. Department of Education: Special Education-State Grant Programs CFDA No. 84.027; Innovative Education – CFDA No. 84.298
- U.S. Department of Health and Human Services: Child Support Enforcement CFDA No. 93.563; Medical Assistance Program (Medicaid-Title XIX) CFDA No. 93.778

#### Management's Response (continued)

Overall, the Government has procedures that address expenditures irrespective of funding source (e.g., Federal, local). However, some procedures might be outdated, while others have been updated but require more revisions. The ERP Subcommittee that was tasked with reviewing the manuals has reviewed most related to the Financial Module. Upon review and sign-off by the applicable department heads, these manuals can be released formally, but will be subject to constant review and future updates, as required, as we continue to implement the processes and procedures contained therein and learn throughout this process.

Separate and apart from general government procedures and controls. This finding suggests the need for a separate SOP (standard operating procedure) specific to federal funds that at a minimum will address key compliance requirements, especially those related to this and prior audits. OMB anticipates that by fiscal year 2010 it will fully or near fully staff its Federal Grants Management Unit (FGMU) at which time it can move forward with this initiative, and work closely with DOF's Federal Programs Unit, etc., and staff of the major federal programs to facilitate this.

# Summary Schedule of Prior Audit Findings

September 30, 2006

	Finding 05-04
CFDA Number	10.551 and 10.561
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Food Stamps Cluster
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Deputy Commissioner, Fiscal and Administrative
Corrective Action Plan	Operations (FAO) – Department of Human Services
	(DHS)
Status	Corrected
	Finding 05-05
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Allowable Cost/Cost Principles, Period of
	Availability
Amount of Questioned Cost	None
Contact Person Responsible for	Financial Management Specialist, Child Nutrition
Corrective Action Plan	Program – Department of Education (DOE)
Status	DOE did not concur with this finding as
	documentation was and is available in the Federal
	grants and Audit Office. Condition not found during current year audit.
	Finding 05-06
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Activities Allowed or Unallowed, Allowable
	Cost/Cost Principles, Period of Availability
Amount of Questioned Cost	\$60,803

Corrected

State Director, Child Nutrition Program -

Department of Education (DOE)

Amount of Questioned Cost Contact Person Responsible for Corrective Action Plan Status

# Summary Schedule of Prior Audit Findings (continued)

	Finding 05-07
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Procurements, Suspension and Debartment
Amount of Questioned Cost	Could not be determined.
<b>Contact Person Responsible for</b>	Deputy Commissioner of Procurement (DP&P);
<b>Corrective Action Plan</b>	State Director, Child Nutrition Program –
	Department of Education (DOE)
Status	Corrected
	Finding 05-08
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	State Director, Child Nutrition Program –
Corrective Action Plan	Department of Education (DOE)
Status	Recurring (Finding 06-07)
~~~~~~	
	Finding 05-09
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Special Tests and Provisions
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Director, Child Nutrition Program and Director,
Corrective Action Plan	Federal Grants and Audit – Department of
	Education (DOE)
Status	Corrected

# Summary Schedule of Prior Audit Findings (continued)

	Finding 05-10
CFDA Number	10.557
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Special Supplemental Nutrition Program for
0	Women, Infants and Children (WIC)
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	\$227,629
<b>Contact Person Responsible for</b>	Director, Special Supplemental Nutrition Program
Corrective Action Plan	for Women, Infants and Children (WIC) –
	Department of Health (DOH)
Status	Corrected
Status	Concerca
	Finding 05-11
CFDA Number	10.557
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Special Supplemental Nutrition Program for
	Women, Infants and Children (WIC)
Type of Compliance Requirement	Eligibility
Amount of Questioned Cost	\$601
<b>Contact Person Responsible for</b>	Director, Special Supplemental Nutrition Program
<b>Corrective Action Plan</b>	for Women, Infants and Children (WIC) –
	Department of Health (DOH)
Status	Corrected
Status	Contenta
	Finding 05-12
CFDA Number	10.557
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Special Supplemental Nutrition Program for
<u> </u>	Women, Infants and Children (WIC)
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	Director, Special Supplemental Nutrition Program
Corrective Action Plan	for Women, Infants and Children (WIC) –
	Department of Health (DOH)
Status	Corrected

# Summary Schedule of Prior Audit Findings (continued)

	Finding 05-13
CFDA Number	15.875
Federal Agency	U.S. Department of Interior
Name of Federal Program	Economic, Social and Political Development of the Territories and the Freely Associated States
Type of Compliance Requirement	Davis-Bacon Act
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	Associate Director, Federal Grants Manager Unit,
Corrective Action Plan	OMB
Status	The Government did not agree with this finding as
Status	the Davis-Bacon Act does not apply for DOI-DIA
	projects.
	projecto.
	Finding 05-14
CFDA Number	15.875
Federal Agency	U.S. Department of Interior
Name of Federal Program	Economic, Social and Political Development of the
	Territories and the Freely Associated States
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Associate Director, Federal Grants Manager Unit,
<b>Corrective Action Plan</b>	OMB
Status	Corrected
	Finding 05-15
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	Could not be determined.
<b>Contact Person Responsible for</b>	Director, Business and Administration – Department
<b>Corrective Action Plan</b>	of Labor (DOL)
Status	Corrected

7.225 U.S. Department of Labor Unemployment Insurance Deporting Uone Director, Unemployment Insurance (UI) – Department of Labor (DOL) Department of Labor (DOL) Department of Labor T.225 U.S. Department of Labor Unemployment Insurance Deporting
Unemployment Insurance Reporting None Director, Unemployment Insurance (UI) – Department of Labor (DOL) Recurring (Finding 06-11) ding 05-17 7.225 J.S. Department of Labor Unemployment Insurance
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Director, Unemployment Insurance (UI) –
Department of Labor (DOL)

	Finding 05-19
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Special Tests and Provision
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Unemployment Insurance (UI) –
Corrective Action Plan	Department of Labor (DOL)
Status	Corrected
	Finding 05-20
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	All applicable compliance requirements as stated in
	OMB Circular A-133.
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Unemployment Insurance (UI) –
<b>Corrective Action Plan</b>	Department of Labor (DOL)
Status	Corrected
	Finding 05-21
CFDA Number	84.027
Federal Agency	U.S. Department of Education
Name of Federal Program	Special Education – Grants to States
Type of Compliance Requirement	Activities Allowed or Unallowed, Allowable
	Cost/Cost Principles, Period of Availability
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Special Education – Department of
Corrective Action Plan	Education (DOE)

	Finding 05-22
CFDA Number	84.027
Federal Agency	U.S. Department of Education
Name of Federal Program	Special Education – Grants to States
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Special Education – Department of
Corrective Action Plan	Education (DOE)
Status	Corrected
	Finding 05-23
CFDA Number	84.027
Federal Agency	U.S. Department of Education
Name of Federal Program	Special Education – Grants to States
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Special Education – Department of
Corrective Action Plan	Education (DOE)
Status	Corrected
	Finding 05-24
CFDA Number	84.027
Federal Agency	U.S. Department of Education
Name of Federal Program	Special Education – Grants to States
Type of Compliance Requirement	Procurement, Suspension and Debartment
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Property, Procurement and Auxiliary
<b>Corrective Action Plan</b>	Services STT/STX and Director, Business Affairs
	STT/STX – Department of Education (DOE)

	Finding 05-25
CFDA Number	84.027 and 84.298
Federal Agency	U.S. Department of Education
Name of Federal Program	Special Education – Grants to States and State
	Grants for Innovative Programs
Type of Compliance Requirement	Compliance Agreement
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
Corrective Action Plan	Services – Department of Education (DOE)
Status	Corrected
	Finding 05-26
CFDA Number	84.298
Federal Agency	U.S. Department of Education
Name of Federal Program	State Grants for Innovative Programs
Type of Compliance Requirement	Equipment and Real Property Management
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	Director, Property, Procurement and Auxiliary
Corrective Action Plan	Services STT/STX – Department of Education
	(DOE)
Status	Recurring (Finding 06-19)
	Finding 05-27
CFDA Number	84.298
Federal Agency	U.S. Department of Education
Name of Federal Program	State Grants for Innovative Programs
Type of Compliance Requirement	Matching Level of Effort and Earmarking
Amount of Questioned Cost	None
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
Corrective Action Plan	Services – Department of Education (DOE)
Status	Corrected

	Finding 05-28
CFDA Number	84.298
Federal Agency	U.S. Department of Education
Name of Federal Program	State Grants for Innovative Programs
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
<b>Corrective Action Plan</b>	Services – Department of Education (DOE)
Status	Corrected
	Finding 05-29
CFDA Number	93.563
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Child Support Enforcement Research
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Paternity and Child Support Division
<b>Corrective Action Plan</b>	(PCSD) – Department of Justice (DOJ)
Status	Recurring (Finding 06-21)
	Finding 05-30
CFDA Number	93.563
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Child Support Enforcement Research
Type of Compliance Requirement	Special Tests and Provisions
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Paternity and Child Support Division
Corrective Action Plan	(PCSD) – Department of Justice (DOJ)

	Finding 05-31
CFDA Number	93.563
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Child Support Enforcement Research
Type of Compliance Requirement	Procurement, Suspension and Debartment
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Paternity and Child Support Division
<b>Corrective Action Plan</b>	(PCSD) – Department of Justice (DOJ)
Status	Corrected
	Finding 05-32
CFDA Number	93.600
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Head Start
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
<b>Corrective Action Plan</b>	Operations (FAO) – Department of Human Services
	(DHS)
Status	Corrected
	Finding 05-33
CFDA Number	93.667
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Social Services Block Grant
Type of Compliance Requirement	Procurement, Suspension and Debartment
Amount of Questioned Cost	\$460
<b>Contact Person Responsible for</b>	Deputy Commissioner, Fiscal and Administrative
<b>Corrective Action Plan</b>	Operations (FAO) – Department of Human Services (DHS)
Status	Corrected

	Finding 05-34
CFDA Number	93.778
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Medical Assistant
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Executive Director, Health Insurance and Medical
<b>Corrective Action Plan</b>	Assistance, and Administrator, Financial Services –
	Department of Health (DOH)
Status	Corrected
	Finding 05-35
CFDA Number	93.778
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Medical Assistant
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	\$6,418,403
<b>Contact Person Responsible for</b>	Executive Director, Health Insurance and Medical
<b>Corrective Action Plan</b>	Assistance, and Administrator, Financial Services –
	Department of Health (DOH)
Status	Recurring (Finding 06-22)
	Finding 05-36
CFDA Number	93.778
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Medical Assistant
Type of Compliance Requirement	Procurement, Suspension and Debartment
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	Executive Director, Health Insurance and Medical
<b>Corrective Action Plan</b>	Assistance, and Administrator, Financial Services –
<b>a</b>	Department of Health (DOH)
Status	Corrected

	Finding 05-37
CFDA Number	93.778
Federal Agency	U.S. Department of Health and Human Services
Name of Federal Program	Medical Assistant
Type of Compliance Requirement	Eligibility
Amount of Questioned Cost	None
Contact Person Responsible for	Executive Director, Health Insurance and Medical
<b>Corrective Action Plan</b>	Assistance, and Administrator, Financial Services –
	Department of Health (DOH)
Status	Recurring (Finding 06-25)
CEDA Number	Finding 05-38
CFDA Number Federal Agency	Finding 05-38 93.778
Federal Agency	Finding 05-38 93.778 U.S. Department of Health and Human Services
Federal Agency Name of Federal Program	Finding 05-38 93.778 U.S. Department of Health and Human Services Medical Assistant
Federal Agency	Finding 05-38 93.778 U.S. Department of Health and Human Services
Federal Agency Name of Federal Program Type of Compliance Requirement	Finding 05-38 93.778 U.S. Department of Health and Human Services Medical Assistant Matching, Level of Effort and Earmarking None
Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost	Finding 05-38 93.778 U.S. Department of Health and Human Services Medical Assistant Matching, Level of Effort and Earmarking
Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost Contact Person Responsible for	Finding 05-38 93.778 U.S. Department of Health and Human Services Medical Assistant Matching, Level of Effort and Earmarking None Executive Director, Health Insurance and Medical

	Finding 04-04
CFDA Number	10.551 and 10.561
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Food Stamps Cluster
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Deputy Commissioner, Fiscal and Administrative
<b>Corrective Action Plan</b>	Operations (FAO) – Department of Human Services
	(DHS)
Status	Corrected
	Finding 04-05
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Financial Management Specialist, Child Nutrition
<b>Corrective Action Plan</b>	Program (CNP) – Department of Education
Status	Recurring (Finding 06-10)
	Finding 04.06
CFDA Number	Finding 04-06 10.555 and 10.559
Federal Agency Name of Federal Program	U.S. Department of Agriculture Child Nutrition Cluster
Type of Compliance Requirement	Allowable Costs/Cost Principles
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	State Director, Child Nutrition Program (CNP) –
Corrective Action Plan	Department of Education
Status	VIDOE did not concur with this finding. Program's
	position has been accepted by the USDA. Condition not found during current year audit.

	Finding 04-07
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Procurement, Suspension and Debartment
Amount of Questioned Cost	None
Contact Person Responsible for	Deputy Commissioner of Procurement (DP&P);
Corrective Action Plan	State Director, Child Nutrition Program –
	Department of Education (DOE)
Status	Corrected
	Finding 04-08
CFDA Number	10.555 and 10.559
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Child Nutrition Cluster
Type of Compliance Requirement	Special Tests and Provisions
Amount of Questioned Cost	None
Contact Person Responsible for	State Director, Child Nutrition Program (CNP) –
Corrective Action Plan	Department of Education (DOE)
Status	Corrected
/	
	Finding 04-09
CFDA Number	10.557
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Special Supplemental Nutrition Program for
	Women, Infants and Children (WIC)
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Special Supplemental Nutrition Program
<b>Corrective Action Plan</b>	for Women, Infants and Children (WIC) –
	Department of Health (DOH)
Status	Corrective action plan is currently being
	implemented with the new Tyler-Munis Enterprise
	Resource Planning (ERP) System. Condition not
	found during current year audit.

	Finding 04-10
CFDA Number	10.557
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Special Supplemental Nutrition Program for
	Women, Infants and Children (WIC)
Type of Compliance Requirement	Eligibility
Amount of Questioned Cost	\$9,059
Contact Person Responsible for	Director, Special Supplemental Nutrition Program
<b>Corrective Action Plan</b>	for Women, Infants and Children (WIC) –
	Department of Health (DOH)
Status	Corrected
	Finding 04-11
CFDA Number	10.557
Federal Agency	U.S. Department of Agriculture
Name of Federal Program	Special Supplemental Nutrition Program for
-	Women, Infants and Children (WIC)
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Director, Special Supplemental Nutrition Program
Corrective Action Plan	for Women, Infants and Children (WIC) –
	Department of Health (DOH)
Status	Corrected
	Finding 04-12
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Unemployment Insurance (UI) –
Corrective Action Plan	Department of Labor (DOL)
Status	Recurring (Finding 06-11)

# Summary Schedule of Prior Audit Findings (continued)

	Finding 04-13
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Director, Unemployment Insurance (UI) –
<b>Corrective Action Plan</b>	Department of Labor (DOL)
Status	Recurring (Finding 06-11)
	Finding 04-14
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Director, Business and Administration (BA) –
<b>Corrective Action Plan</b>	Department of Labor (DOL)
Status	Corrected
	Finding 04-15
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Eligibility
Amount of Questioned Cost	\$11,779
<b>Contact Person Responsible for</b>	Director, Unemployment Insurance (UI) –
<b>Corrective Action Plan</b>	Department of Labor (DOL)
Status	Recurring (Finding 06-12). New policy and procedure implemented in January 2007.

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	Finding 04-16
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Special Tests and Provision
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Unemployment Insurance (UI) –
Corrective Action Plan	Department of Labor (DOL)
Status	Corrected
	Finding 04-17
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Period of Availability
Amount of Questioned Cost	\$25,026
Contact Person Responsible for	Director, Business and Administration (BA) –
Corrective Action Plan	Department of Labor (DOL)
Status	Corrected
	Finding 04-18
CFDA Number	17.225
Federal Agency	U.S. Department of Labor
Name of Federal Program	Unemployment Insurance
Type of Compliance Requirement	Special Tests and Provision
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Unemployment Insurance (UI) –
Corrective Action Plan	Department of Labor (DOL)

	Finding 04-19
CFDA Number Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost Contact Person Responsible for Corrective Action Plan Status	<ul> <li>17.225</li> <li>U.S. Department of Labor</li> <li>Unemployment Insurance</li> <li>All applicable compliance requirements as stated in</li> <li>OMB Circular A-133.</li> <li>None</li> <li>Director, Unemployment Insurance (UI) –</li> <li>Department of Labor (DOL)</li> <li>Corrected</li> </ul>
	Finding 04-20
CFDA Number Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost Contact Person Responsible for Corrective Action Plan Status	<ul> <li>84.027</li> <li>U.S. Department of Education</li> <li>Special Education – State Grant</li> <li>Cash Management</li> <li>None</li> <li>Deputy Commissioner, Fiscal and Administrative</li> <li>Services – Department of Education (DOE)</li> <li>Corrected</li> </ul>
	Finding 04-21
CFDA Number Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost Contact Person Responsible for Corrective Action Plan Status	<ul> <li>84.027</li> <li>U.S. Department of Education</li> <li>Special Education – State Grant</li> <li>Matching, Level of Effort and Earmarking</li> <li>\$210,578</li> <li>Director, Director, Business Affairs STT/STX and</li> <li>Director, Business Office STX – Department of</li> <li>Education (DOE)</li> <li>DOE is currently working on preparing adjustment</li> <li>documents to correct this finding. Condition not</li> <li>found in current year audit.</li> </ul>

	Finding 04-22
CFDA Number	84.027 and 84.298
Federal Agency	U.S. Department of Education
Name of Federal Program	Special Education – State Grant and State Grants for
	Innovative Programs
Type of Compliance Requirement	Special Tests and Provision
Amount of Questioned Cost	Could not be determined.
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
<b>Corrective Action Plan</b>	Services, Compliance Monitor – Department of
	Education (DOE)
Status	Corrected
	Finding 04-23
CFDA Number	84.298
Federal Agency	U.S. Department of Education
Name of Federal Program	State Grants for Innovative Programs
Type of Compliance Requirement	Equipment and Real Property Management
Amount of Questioned Cost	None
Contact Person Responsible for	Director, Property, Procurement and Auxiliary
<b>Corrective Action Plan</b>	Services – Department of Education (DOE)
Status	Recurring (Finding 06-19)
	Finding 04-24
CFDA Number	84.298
Federal Agency	U.S. Department of Education
Name of Federal Program	State Grants for Innovative Programs
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
Corrective Action Plan	Services – Department of Education (DOE)
Status	Corrected

	Finding 04-25
CFDA Number Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost Contact Person Responsible for Corrective Action Plan Status	<ul> <li>93.563</li> <li>U.S. Department of Heath and Human Services Child Support Enforcement Research Reporting \$17,610</li> <li>Director, Paternity and Child Support Division (PCSD) – Department of Justice (DOJ)</li> <li>PCSD did not agree with finding because audit trails existed in the form of daily collection and disbursement reports. Condition not found in current year audit.</li> </ul>
	Finding 04-26
CFDA Number	93.563
Federal Agency	U.S. Department of Heath and Human Services
Name of Federal Program	Child Support Enforcement Research
Type of Compliance Requirement	Eligibility
Amount of Questioned Cost	None
<b>Contact Person Responsible for</b>	Director, Paternity and Child Support Division
<b>Corrective Action Plan</b>	(PCSD) – Department of Justice (DOJ)
Status	Corrected
	Finding 04-27
CFDA Number	93.563
Federal Agency	U.S. Department of Heath and Human Services
Name of Federal Program	Child Support Enforcement Research
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
Contact Person Responsible for Corrective Action Plan	Director, Operations – Department of Justice (DOJ)
Status	Recurring (Finding 06-21)

	Finding 04-28
CFDA Number	93.600
Federal Agency	U.S. Department of Heath and Human Services
Name of Federal Program	Head Start
Type of Compliance Requirement	Procurement, Suspension and Debartment
Amount of Questioned Cost	\$127,392
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
<b>Corrective Action Plan</b>	Operations (FAO) – Department of Human Services
	(DHS)
Status	Corrected
	Finding 04-29
CFDA Number	93.600
Federal Agency	U.S. Department of Heath and Human Services
Name of Federal Program	Head Start
Type of Compliance Requirement	Matching, Level of Effort and Earmarking
Amount of Questioned Cost	Could not be determined.
<b>Contact Person Responsible for</b>	Assistance Administrator, Pre-School Services –
<b>Corrective Action Plan</b>	Department of Human Services (DHS)
Status	Corrected
	Finding 04-30
CFDA Number	93.667
Federal Agency	U.S. Department of Heath and Human Services
Name of Federal Program	Social Services Block Grant
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
Contact Person Responsible for	Deputy Commissioner, Fiscal and Administrative
Corrective Action Plan	Operations (FAO) – Department of Human Services
Corrective Action I fair	(DHS)
Status	Corrected
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	Finding 04-31
CFDA Number Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost	93.778 U.S. Department of Heath and Human Services Medical Assistance Reporting None
Contact Person Responsible for Corrective Action Plan	Executive Director, Health Insurance and Medical Assistance, and Administrator, Financial Services – Department of Health (DOH)
Status	Recurring (Finding 06-22)
	Finding 04-32
CFDA Number Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost Contact Person Responsible for Corrective Action Plan Status	<ul> <li>93.778</li> <li>U.S. Department of Heath and Human Services Medical Assistance</li> <li>Eligibility</li> <li>Could not be determined.</li> <li>Executive Director, Health Insurance and Medical</li> <li>Assistance – Department of Health (DOH)</li> <li>Recurring (Finding 06-23)</li> </ul>
	Finding 04-33
CFDA Number Federal Agency Name of Federal Program Type of Compliance Requirement Amount of Questioned Cost Contact Person Responsible for Corrective Action Plan Status	93.778 U.S. Department of Heath and Human Services Medical Assistance Eligibility None Executive Director, Medical Assistance Program – Department of Health (DOH) Recurring (Finding 06-23)

	Finding 04-34
CFDA Number	93.778
Federal Agency	U.S. Department of Heath and Human Services
Name of Federal Program	Medical Assistance
Type of Compliance Requirement	Reporting
Amount of Questioned Cost	None
Contact Person Responsible for	Administrator, Financial Services and Executive
Corrective Action Plan	Director, Health Insurance and Medical Assistance
	– Department of Health (DOH)
Status	Recurring (Finding 06-22)
CEDA N L	Finding 04-35
CFDA Number	97.004
Federal Agency	U.S. Department of Home Land Security
Name of Federal Program	Homeland Security Cluster
Type of Compliance Requirement	Cash Management
Amount of Questioned Cost	None
Contact Person Responsible for	
<b>Corrective Action Plan</b>	Director, Financial Management - VITEMA
Status	Corrected

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