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Grant Thornton

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Financial Statements and Report of  
Independent Certified Public Accountants

Puerto Rico Council on Higher Education  
(A Component Unit of the Commonwealth of Puerto Rico)

Single Audit Package - June 30, 2011

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Y SECRETARIO

**Puerto Rico Council on Higher Education**  
**(A Component Unit of the Commonwealth of Puerto Rico)**

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**Report of Independent Certified Public Accountants**

**The Board of Trustees of the  
Puerto Rico Council on Higher Education  
San Juan, Puerto Rico**

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We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregated remaining fund information of the Puerto Rico Council on Higher Education (the Council), a component unit of the Commonwealth of Puerto Rico, as of and for the year ended June 30, 2011, which collectively comprise the Council's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Council's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregated remaining fund information of the Puerto Rico Council on Higher Education as of June 30, 2011, and the changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report, dated October 14, 2011, on our consideration of the Council's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 9 and 27 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquires of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquires, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Council's financial statements as a whole. 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, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. The financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

As discussed in Note (9) to the accompanying financial statements, effective July 1, 2011, the Council merged with the Puerto Rico Council on General Education under the Reorganization Plan No. 1 of July 26, 2010 covered by Act 182 of December 17, 2009, known as "Act of Reorganization and Modernization of the Executive Branch of the Government of Puerto Rico of 2009".

Kevane Grant Thornton LLP

San Juan, Puerto Rico,  
October 14, 2011.



# Puerto Rico Council on Higher Education

## Management's Discussion and Analysis Year Ended June 30, 2011

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### Nature of organization

The Puerto Rico Council on Higher Education (the Council) is the governmental entity that sets policy in higher education and administers student aid funds for postsecondary students. The Council's mission is to promote higher education that allows the development of highly qualified human resources to the social, economic and cultural well-being of Puerto Rico to increase their competitiveness. The Council is governed by a board of trustees, which is comprised of eight Governor-appointed members and the Puerto Rico's Secretary of Education, who are not compensated; each serves six year terms. The Council holds scheduled monthly meetings.

Among the duties and responsibilities of the Council are:

- a) Authorize all higher education institutions the license to operate.
- b) Authorize higher education institutions to offer education programs in Puerto Rico.
- c) Administer the state student financial aid program of postsecondary education institutions, with the exception of the University of Puerto Rico.
- d) Promote research and investigation in areas relative to higher education matters.
- e) Manage the Integrated Postsecondary Education Data System (IPEDS).
- f) Manage the postsecondary education component of Puerto Rico's Federal No Child Left Behind Program (Title II, Part A, subpart 3).

The Council has an Executive Director, who is a full time employee responsible of the coordination of the Council matters, three (3) Programmatic Directors (License and Accreditation, Education Support Program and Research and Documentation on Higher Education) and one Administration and Finance Director.

### Governmental activities

The Council's basic services include: (1) the authorization of licenses to operate higher education institutions (public and private) in Puerto Rico, (2) the administration of the state student financial aid program of the higher level, (3) administration of the Integrated Postsecondary Education Data System (IPEDS), and (4) administration of the postsecondary education component of Puerto Rico Federal No Child Left Behind Program. During fiscal year 2011, the Commonwealth of Puerto Rico's General Fund financed in part some of the first three activities.

# Puerto Rico Council on Higher Education

## Management's Discussion and Analysis Year Ended June 30, 2011

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### Management's discussion and analysis

Our discussion and analysis of the Council's financial performance provides an overview of the Council's financial activities for the fiscal year ended June 30, 2011 and identifies changes in the Council's financial position. Use this section in conjunction with the Council's financial statements. GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, establish new reporting requirements for state and local governments.

### Overview of financial statements

This discussion and analysis is intended to serve as an introduction to the Council's basic financial statements. The Council's basic financial statements include three components: government - wide financial statements, fund financial statements, and notes to the financial statements. This report also contains supplemental information in addition to the basic financial statements themselves.

### Basic financial statements

The basic financial statements include two kinds of financial statements that present different views -the governmental wide financial statements and the fund financial statements. These statements also include the notes to the financial statements.

This annual report presents the Council's financial activities in two parts: Management's Discussion and Analysis (*this section*) and the Basic Financial Statements required by GASB No. 34. The first group of basic financial statements is the government wide financial statements.

The government-wide financial statements are designed to present an overall picture of the financial position of the Council. These statements consist of:

- a) Statement of Net Assets
- b) Statement of Activities

These statements are prepared using the economic resources measurement focus and the accrual basis of accounting. This means that all current year's revenues and expenses are included regardless of when cash is received or paid, producing a view of financial position similar to that presented by the 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. This statement includes all of the Council's assets and liabilities. Net Assets is the difference between the Council's assets and liabilities, and represents one measure of the Council's financial health. An increase or decrease in the Council's net assets from one year to the next is an indicator of whether its financial health is improving or deteriorating.

# Puerto Rico Council on Higher Education

## Management's Discussion and Analysis Year Ended June 30, 2011

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The Statement of Activities focus on both the gross and net cost of various activities, (governmental and other). These costs are paid by appropriations from the Central Government, charges to institutions and other general revenues. This statement summarizes the costs of providing specific government services, and includes all current year revenues and expenses.

The second group of basic financial statements is comprised of the Governmental Funds that include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances.

### **Reporting on the Council's most significant funds**

Funds financial statements present financial information in a form more familiar to experienced users of governmental financial statements. However, these statements now focus on the most significant funds. A fund is a separate accounting entity with a self-balancing set of accounts. The Council uses funds to keep track of sources of funding and spending related to specific activities. Use these statements to find more detailed information about the Council's most significant activities.

#### *Governmental Funds*

A majority of the Council activities are reported in governmental funds. Reporting of these funds focuses on how money flows into and out of those funds and the balances left at year-end that are available for future spending. Governmental funds are accounted for using the modified accrual method of accounting, which measures cash and other assets that can be readily converted to cash. The governmental funds statements provide a detailed short-term view of the agency's general governmental operations and the basic services it provides. The information should help you determine whether there are more or less resources available for the Council's programs. The General Fund and Special Financial Aid Fund were reported as major funds.

### **Financial analysis of the Council as a whole**

Total assets of the Council as of June 30, 2011, were \$11.2 million, compared with \$10.2 million at June 30, 2010. The total liabilities were approximately \$1.7 million at June 30, 2011, and \$840 thousands as of June 30, 2010. Total net assets amounted to \$9.5 million at June 30, 2011 versus \$9.4 million at June 2010.

As of June 30, 2011, \$258,074 of the Council's net assets were invested in capital assets.

### **Changes in net assets**

The Council had total revenues of \$30 million and \$30.9 million for the years ended June 30, 2011 and 2010, respectively. The Council's expenses were approximately \$30 million each year, of which \$26 million and \$25.9 million were incurred in providing student financial aid and manage the higher education component of Puerto Rico's Federal No Child Left Behind Program during the years ended June 30, 2011 and 2010, respectively. As a result, there is an increase in net assets of \$125,423 and \$868,411 for years ended June 30, 2011 and 2010, respectively.

# Puerto Rico Council on Higher Education

## Management's Discussion and Analysis Year Ended June 30, 2011

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### Changes in Net Assets

	<u>Governmental Activities June 30, 2011</u>	<u>Governmental Activities June 30, 2010</u>
<b>Revenues:</b>		
<b>Program revenues</b>		
Charges for licenses	\$ 514,000	\$ 427,124
Commonwealth appropriations	2,737,520	3,645,719
Special revenue grants	26,706,061	26,745,880
<b>Total program revenues</b>	<u>29,957,581</u>	<u>30,818,723</u>
<b>General revenues</b>		
Interest income	37,199	31,078
Other income	75,538	48,527
Services income	11,232	6,456
<b>Total general revenues</b>	<u>123,969</u>	<u>86,061</u>
<b>Total revenues</b>	<u>30,081,550</u>	<u>30,904,784</u>
<b>Expenses:</b>		
General and administrative	3,705,442	4,069,107
Student financial aid and other grants	26,250,685	25,967,266
<b>Total expenses</b>	<u>29,956,127</u>	<u>30,036,373</u>
<b>Increase in net assets</b>	125,423	868,411
Other financing sources (uses)		
Transfer in	-	-
Transfer out	-	-
<b>Total other financing sources (uses)</b>	<u>-</u>	<u>-</u>
<b>Net changes in net assets</b>	<u>\$ 125,423</u>	<u>\$ 868,411</u>

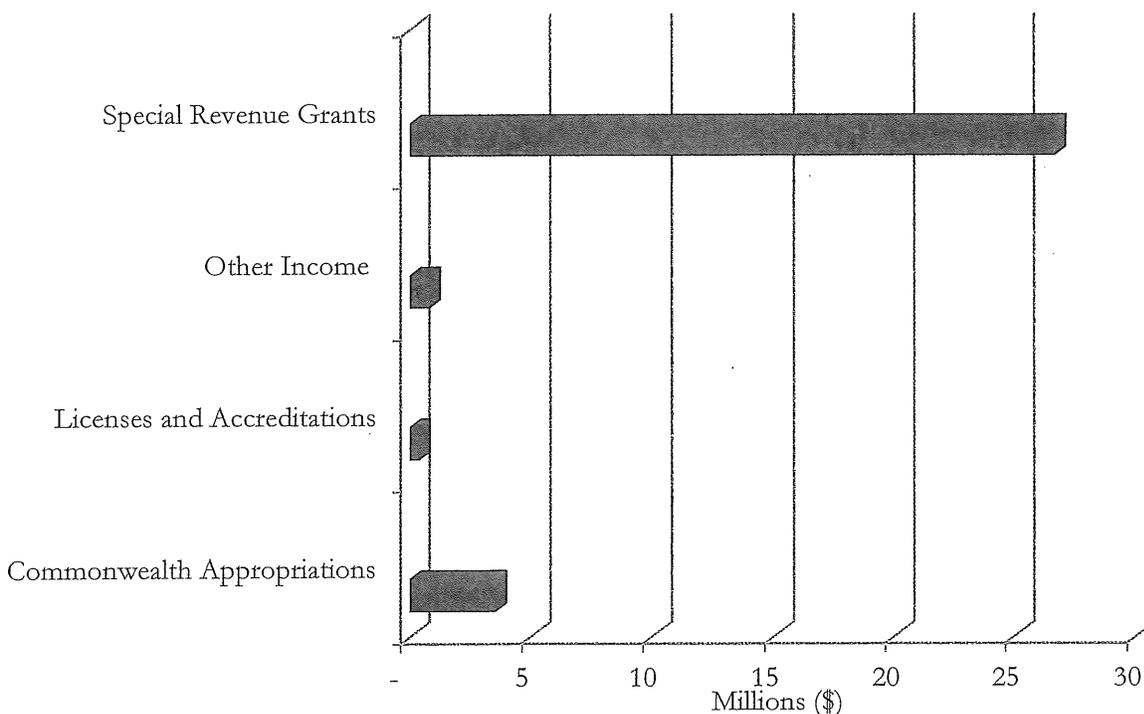
# Puerto Rico Council on Higher Education

## Management's Discussion and Analysis Year Ended June 30, 2011

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### Governmental activities

The Governmental Activities Program Revenues are \$30 million including charges for licenses and accreditations of \$514 thousands, Commonwealth appropriations of \$2.8 million and \$26.7 million in Special Revenue Grants (No Child Left Behind and State Financial Aid Programs). Total General Revenues amounted to \$123,969 corresponding to interest and other income. The total 2011 revenues are approximately \$807 thousands less than 2010 revenues.



	Commonwealth Appropriations	Licenses and Accreditation	Other Income	Special Revenue Grants
Revenues	\$ 2,737,520	\$ 514,000	\$ 123,969	\$ 26,706,061

# Puerto Rico Council on Higher Education

## Management's Discussion and Analysis Year Ended June 30, 2011

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### Financial analysis of the Council funds

The General Fund balance increased during fiscal year 2011 by approximately \$266,000. The general fund main source of revenue is legislative appropriations, which amounted to approximately \$2.7 million. Also, the general fund received income from academic transcript fees, photocopies charges, credentials fees and license fees of approximately \$514 thousands. General and administrative expenses allocated to this fund amounted to approximately \$3 million.

The Special Financial Aid Fund Balance increased by approximately \$424 thousands. The principal source of revenues for this fund corresponds to legislative appropriations, which amounted to \$25 million. Expenses of this fund are related to educational aid distributed to students, which for the year ended June 30, 2011 amounted to approximately \$24.6 million.

The Other Special Revenue Fund consists of federal grants received under the No Child Left Behind Program. The majority of the amounts granted were expended in supporting professional development activities for teachers. Federal grants for the year ended June 30, 2011 and the corresponding expenses amounted approximately to \$1.7 million.

### General fund budgetary highlights and economic factors

The Council prepares an annual operating budget for all governmental funds. For fiscal year 2011-12 the Commonwealth of Puerto Rico approved \$3,578,000 for operations and \$394,000 for the promotion of research in matters relative to higher education.

The Council ceased operations on June 30, 2011, as a result of its merge with the Puerto Rico Council on General Education, and effective on July 1, 2011, a new organization was created. As a consequence, all the assets and liabilities of the Council were transferred to the new organization, the Puerto Rico Council on General Education. This transaction was supported by the Reorganization Plan No. 1 of July 26, 2010, under Act 182 of December 17, 2009.

# Puerto Rico Council on Higher Education

## Management's Discussion and Analysis Year Ended June 30, 2011

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### Capital assets

At the end of fiscal year 2011 the Council had \$258,074 (net of accumulated depreciation) invested in 4 categories of capital assets, including computer and peripheral equipment see table below).

	<b>Governmental Activities June 30, 2011</b>	<b>Governmental Activities June 30, 2010</b>
Furniture and equipment	\$ 643,106	\$ 692,039
Motor vehicles	44,158	63,636
Computer and peripherals	460,858	560,614
Leasehold improvements	475,750	475,750
<b>Total capital assets</b>	<b>1,623,872</b>	<b>1,792,039</b>
Less: Accumulated depreciation and amortization	1,365,798	1,496,212
<b>Total capital assets, net</b>	<b>\$ 258,074</b>	<b>\$ 295,827</b>

More detailed information about the Council's capital assets is presented in Note (4) to the basic financial statements.

### Contacting the Council's financial management

This financial report is designed to provide our citizens, taxpayers, customers, students and creditors with a general overview of the Council's finances and to demonstrate the Council's accountability for the funds it receives. If you have questions about this report, or need additional financial information, contact the Former Acting Director of the Finance and Administration Office at Hato Rey Center Building, 15 Floor, Ponce de León Ave. #268, Hato Rey, P.R. 00918.

Puerto Rico Council on Higher Education  
(A Component Unit of the Commonwealth of Puerto Rico)

Statement of Net Assets  
June 30, 2011

<u>Assets</u>	<u>Governmental Activities</u>
<b>Current assets:</b>	
Cash and cash equivalents	\$ 3,883,500
Accounts receivable --	
Institutions and others	60,648
Investments	<u>6,991,995</u>
Total current assets	<u>10,936,143</u>
Capital assets, net of accumulated depreciation and amortization of \$1,365,798	<u>258,074</u>
Total assets	<u>11,194,217</u>
<b><u>Liabilities and Net Assets</u></b>	
<b>Current liabilities:</b>	
Accounts payable and accrued liabilities	512,321
Voluntary termination benefits, current portion	<u>69,869</u>
Total current liabilities	<u>582,190</u>
<b>Non-current liabilities -</b>	
Voluntary termination benefits, net of current portion	526,377
Compensated absences	<u>545,539</u>
Total non-current liabilities	<u>1,071,916</u>
Total liabilities	<u>1,654,106</u>
<b>Net assets:</b>	
Investment in capital assets	258,074
Restricted	8,573,303
Unrestricted	<u>708,734</u>
Total net assets	<u>\$ 9,540,111</u>

**Puerto Rico Council on Higher Education**  
(A Component Unit of the Commonwealth of Puerto Rico)

**Statement of Activities**  
Year Ended June 30, 2011

	Program Revenues				Net Revenue and Change in Net Assets
	Expenses	Licenses and Accreditations	Commonwealth Appropriations	Special Revenue Grants	
<b>Governmental activities:</b>					
Operations	\$ 3,705,442	\$ 514,000	\$ 2,737,520	\$ -	\$ (453,922)
Student financial aid fund	26,250,685	-	-	26,706,061	455,376
Total governmental activities	<u>\$ 29,956,127</u>	<u>\$ 514,000</u>	<u>\$ 2,737,520</u>	<u>\$ 26,706,061</u>	<u>1,454</u>
<b>General revenues:</b>					
Services revenues					11,232
Interest income					37,199
Other income					75,538
Total general revenues					<u>123,969</u>
Change in net assets					<u>125,423</u>
Other financial sources (uses)					-
Transfer in					-
Transfer out					-
Net other financial sources (uses)					-
<b>Net change in net assets</b>					<u>125,423</u>
<b>Net assets at beginning of the year</b>					<u>9,414,688</u>
<b>Net assets at end of year</b>					<u>\$ 9,540,111</u>

The accompanying notes are an integral part of this financial statement.

**Puerto Rico Council on Higher Education**  
(A Component Unit of the Commonwealth of Puerto Rico)

Balance Sheet - Governmental Funds  
June 30, 2011

	General Fund	Special Financial Aid Fund	Other Special Revenue	Total
<b>Assets:</b>				
Cash and cash equivalents	\$ 3,087,116	\$ 796,384	\$ -	\$ 3,883,500
Accounts receivable -				
Institutions and others	13,409	14,442	32,797	60,648
Other governmental funds	441,355	-	-	441,355
Investments	-	6,991,995	-	6,991,995
<b>Total assets</b>	<b>\$ 3,541,880</b>	<b>\$ 7,802,821</b>	<b>\$ 32,797</b>	<b>\$ 11,377,498</b>
<b>Liabilities:</b>				
Accounts payable and accrued liabilities	\$ 463,010	\$ 17,441	\$ 31,870	\$ 512,321
Voluntary termination benefits	69,869	-	-	69,869
Payable to other governmental funds	440,428	-	927	441,355
<b>Total liabilities</b>	<b>973,307</b>	<b>17,441</b>	<b>32,797</b>	<b>1,023,545</b>
<b>Fund balances:</b>				
Restricted	-	7,785,380	-	7,785,380
Assigned	813,874	-	-	813,874
Unassigned	1,754,699	-	-	1,754,699
<b>Total fund balances</b>	<b>2,568,573</b>	<b>7,785,380</b>	<b>-</b>	<b>10,353,953</b>
<b>Total liabilities and fund balances</b>	<b>\$ 3,541,880</b>	<b>\$ 7,802,821</b>	<b>\$ 32,797</b>	<b>\$ 11,377,498</b>

The accompanying notes are an integral part of this financial statement.

**Puerto Rico Council on Higher Education**  
**(A Component Unit of the Commonwealth of Puerto Rico)**

**Reconciliation of the Balance Sheet of Governmental Funds to  
the Statement of Net Assets**

**June 30, 2011**

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Total fund balance of governmental funds	\$	10,353,953
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets used in governmental activities are not financial resources, therefore, are not reported in governmental funds balance sheet.		258,074
Long-term liabilities are not due and payable in the current period, and therefore, are not reported in governmental funds balance sheet.		<u>(1,071,916)</u>
Total net assets of governmental activities	\$	<u><u>9,540,111</u></u>

**Puerto Rico Council on Higher Education**  
(A Component Unit of the Commonwealth of Puerto Rico)

**Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds**  
**Year Ended June 30, 2011**

	General Fund	Special Financial Aid Fund	Other Special Revenue	Total
<b>Revenues:</b>				
Legislative appropriations	\$ 2,737,520	\$ 25,000,001	\$ -	\$ 27,737,521
Federal grants	-	-	1,706,060	1,706,060
Licenses and accreditations	514,000	-	-	514,000
Interest income	5,543	31,656	-	37,199
Services income	11,232	-	-	11,232
Other income	21,050	54,488	-	75,538
	<u>3,289,345</u>	<u>25,086,145</u>	<u>1,706,060</u>	<u>30,081,550</u>
Total revenues				
<b>Expenditures:</b>				
Current:				
General and administrative	2,983,652	6,549	111,388	3,101,589
Educational aid	-	24,656,013	1,594,672	26,250,685
Capital expenditures	39,629	-	-	39,629
	<u>3,023,281</u>	<u>24,662,562</u>	<u>1,706,060</u>	<u>29,391,903</u>
Total expenditures				
Excess of revenues over expenditures	266,064	423,583	-	689,647
Other financing sources (uses):				
including transfers				
Transfers in	-	-	-	-
Transfers out	-	-	-	-
	<u>266,064</u>	<u>423,583</u>	<u>-</u>	<u>689,647</u>
Net change in fund balances				
Fund balances at beginning of year	2,302,509	7,361,797	-	9,664,306
	<u>\$ 2,568,573</u>	<u>\$ 7,785,380</u>	<u>\$ -</u>	<u>\$ 10,353,953</u>
Fund balances at end of year				

**Puerto Rico Council on Higher Education**  
**(A Component Unit of the Commonwealth of Puerto Rico)**

**Reconciliation of the Statement of Revenues, Expenditures and Changes  
in Fund Balances of Governmental Funds to the Statement of Activities  
Year Ended June 30, 2011**

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Net change in fund balances - total governmental funds	\$ 689,647
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation and amortization exceed capital outlays in the current period.	(38,285)
Some expenses reported in the statement of activities do not require the use of current financial resources and are not reported as expenditures in governmental funds.	<u>(525,939)</u>
Change in net assets of governmental activities	<u>\$ 125,423</u>

**Puerto Rico Council on Higher Education**  
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Financial Statements  
June 30, 2011

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(1) Organization and summary of significant accounting policies:

(a) Organization -

The Puerto Rico Council on Higher Education (the Council) was created through the enactment of Law No. 17 of June 16, 1993 (Council on Higher Education Act), to develop the higher education and to administer student aid funds for those institutions in the Commonwealth of Puerto Rico (the Commonwealth). Law No. 170 of August 22, 2002 gave the Council direct responsibility of student aid funds and Law No. 213 of August 1, 2003 created the Center for Study and Documentation of Puerto Rico Higher Education, ascribed to the Council. The Council is a component unit of the Commonwealth of Puerto Rico and accordingly, is included in the general -purpose financial statements of the Commonwealth. The Council's Board of Trustees is composed of the Secretary of Education, an ex-officio member, and eight additional members appointed by the Governor of Puerto Rico with the consent of the Senate. The Directors are not compensated and the appointment is for six years.

On June 30, 2011, the Council ceased operations. See note (10) for related information.

(b) Summary of significant accounting policies-

(i) Government-wide and fund financial statements-

Government-wide financial statements - include the statement of net assets and the statement of activities. These statements report financial information of the Council as a whole. The effect of interfund activity has been removed from these government wide financial statements.

The statement of activities reports the expenses of a given function offset by program revenues directly connected with the functional program. A function is an assembly of similar activities and may include portions of a fund or summarize more than one fund to capture the expenses and program revenues associated with a distinct functional activity. Program revenues include: (1) charges for services and other revenue, (2) appropriations from the Commonwealth of Puerto Rico and (3) US Department of Education grant contributions.

Fund financial statements- are provided for governmental funds. Major individual governmental funds are reported in separate columns with composite column for non major funds.

(ii) Measurement focus and basis of accounting -

The government-wide financial statements were prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The governmental fund financial statements were prepared using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they are both measurable and available. Available means collectible with the current period or soon enough thereafter to pay current liabilities. The Council considers revenues to be

**Puerto Rico Council on Higher Education**  
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Financial Statements  
June 30, 2011

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available if they are collected within 60 days of the end of the fiscal year. Expenditures are recorded when the related fund liability is incurred. However, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

Fund Types and Major Funds:

Governmental Funds -- The Council reports the following major governmental funds:

- General Fund -- Reports as the primary fund of the Council. This fund is used to account for all financial resources not reported in other funds.
- Student Financial Aid Fund -- This Special Revenue fund is used to account for the Commonwealth appropriations distributed as financial aids to Puerto Rican students.
- Other Governmental Funds -- Accounts for federal grants received under the Title II, Part A, Subpart 3 of the No Child Left Behind Program.

(iii) Cash and cash equivalents -

The Council considers as cash and cash equivalents all highly liquid investments with original or remaining maturities at the date of purchase of three months or less.

As of June 30, 2011, cash and cash equivalents consists of deposits and investments in banks and are categorized following the "Guide to Implementation of GASB Statement No. 3 on Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements", as amended.

(iv) Investments -

The Council classifies certificates of deposits as investments if they have a maturity greater than three months when acquired. Investments are reported at fair value and income generated is reported as interest income in the accompanying financial statements.

(v) Capital assets:-

Cost basis-

Capital assets are recorded at historical cost or estimated historical cost. The cost of property and equipment includes costs for furniture, office equipment, computer and peripheral equipment, vehicles, and leasehold improvements.

Capitalization policy-

The Council capitalization policy is to capitalize items having a unit value greater than or equal to \$300. The cost of normal maintenance and repairs that do not add value to the assets or materially extend assets lives are not capitalized.

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Depreciation of capital assets-

Depreciation is provided using the straight-line method over an estimated useful life of three years for computers and peripheral equipment, and five years for furniture, office equipment and vehicles. Amortization is provided, over leasehold improvements, using the straight-line method over an estimated useful life of fifteen years.

Impairment of capital assets-

The Council has implemented GASB No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. The objective of GASB No. 42 is to establish accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. This statement also clarifies and establishes accounting requirements for insurance recoveries.

Governments are required to evaluate prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. Such events or changes in circumstances that may be indicative of impairment include evidence of physical damage, enactment or approval of laws or regulations or other changes in environmental factors, technological changes or evidence of obsolescence, changes in the manner or duration of use of a capital asset, and construction stoppage among others.

The Council evaluated its capital assets as required by GASB No. 42 and no impairment was identified during the year ended June 30, 2011.

(vi) Net assets -

Net assets is the difference between assets and liabilities. Net assets invested in capital assets are capital assets net of accumulated depreciation. Restricted net assets are net assets less related debt that are subject to constraints on their use by creditors, grantors, contributors, legislation, and other parties. All other net assets are reported as unrestricted.

(vii) Fund balance classifications -

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which the Council is bound to honor constraints on the specific purposes for which amounts in the respective governmental funds can be spent. The classifications used in the governmental fund financial statements are as follows:

- Restricted - This classification includes amounts for which constraints have been placed on the use of the resources either (a) externally imposed by creditors (such as through debt covenant), grantors, contributors, or laws or regulations of other governments, or (b) imposed by law through constitutional provisions or enabling legislation.
- Committed - This classification includes amounts that can be used only for specific purposes pursuant to constraints imposed by formal action of the Board of Trustees. These amounts cannot be used for any other purpose unless the Board of Trustees removes or changes the specified use by taking the same type of action (ordinance or

**Puerto Rico Council on Higher Education**  
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resolution) that was employed when the funds were initially committed. This classification also includes contractual obligations to the extent that existing resources have been specifically committed for use in satisfying those contractual requirements. The Council did not have any committed resources as of June 30, 2011.

- Assigned - This classification represents amounts that are constrained by the government's intent to be used for a specific purpose. Assigned fund balance classifications are not actively used by the entity. Remaining fund balances are reported as unassigned.
- Unassigned - This classification includes the residual fund balance for the General Fund. The Unassigned classification also includes negative residual fund balance of any other governmental fund that cannot be eliminated by offsetting of Assigned fund balance amounts.

The Council typically use Restricted fund balances first, followed by Committed resources, and then Assigned resources, as appropriate opportunities arise, but reserves the right to selectively spend Unassigned.

**(viii) Compensated absences (vacation and sick leave) -**

The employees of the Council are entitled to 2.5 days per month for vacation and 1.5 days per month for sick leave. Vacation and sick leave can be accumulated up to a maximum of 60 and 90 days, respectively. Any excess over the maximum of accumulated sick leave is paid to the employees during March of the next fiscal year. Any excess over the maximum of accumulated vacations is liquidated to the employees on or before December 31<sup>st</sup> of the next fiscal year. Sick leave is payable to the employee upon retirement. As per the executive order 2006-27 any excess over the maximum of accumulated vacations have to be liquidated by the employer on or before December 31<sup>st</sup> of the next fiscal year and accrued as a current liability and expenditure in the fund financial statements as of June 30, 2011.

Effective March 9, 2009 the Council entered into the Phase II of Act. No. 7 (The Act) which states that the accumulated sick leave and vacation's excess will not be liquidated for a period of two years. This requirement was extended until June 30, 2011, with the Collective Resolution No. 66 of July 2, 2010. The sick leave excess over 90 days as of December 31, 2010 should be used on or before June 30, 2011. The vacation excess over 60 days should be used on or before December of each fiscal year.

The accrued amount of up to 60 days of vacation is recorded as a long-term liability in the government – wide statements. The long-term payable is segregated as follows:

Unrestricted net assets	\$ 519,588
Restricted net assets	25,951
	\$ 545,539

See related Note (5).

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June 30, 2011

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(ix) Revenue recognition –

General fund - includes Commonwealth appropriations and license and accreditation fees. Revenue is recognized when received.

Special financial aid fund –includes revenues received for restricted grants distributions and federal grants which are recorded when expenditures are incurred.

Other special revenue fund – includes revenues for federal grants received under Title II, Part A, Subpart 3 of the No Child Left Behind Program. Grants are recorded when expenditures are incurred.

(x) Use of estimates -

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

(2) Budget policy and practice:

The Council prepares an annual operating budget request for all governmental funds. The budget is incorporated into the Commonwealth's consolidated budget project submitted by the executive body to the legislature. Public hearings and discussions are held toward the legal enactment of the consolidated budget project on or before the commencement of the fiscal year for which the budget project was prepared (the first of July of each fiscal year). Once the budget project is approved, legally adopted, and in effect, the Council's management can request the transfer of budgeted and approved amounts. The Constitution of the Commonwealth of Puerto Rico requires that budgeted expenditures be balanced with estimated revenues. The budget has been prepared in accordance with accounting principles generally accepted in the United States of America. The comparison of actual results of operations to the governmental fund budget is presented for analytical purposes only.

(3) Deposits and investments:

Cash and investments as of June 30, 2011 are composed as follows:

Cash and cash equivalents	\$	2,485,073
Restricted cash and cash equivalents		1,398,427
Restricted investments		6,991,995
Total	\$	<u>10,875,495</u>

Restricted cash and cash equivalents and restricted investments as of June 30, 2011 represent funds for the sole purpose of special financial aid and research.

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**June 30, 2011**

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The Council is authorized to deposit cash only in institutions approved by the Department of Treasury of the Commonwealth of Puerto Rico, and such deposits are maintained in separate accounts in the name of the Council.

Custodial credit risk – deposits

For deposits, custodial credit risk is the risk that in the event of bank failure, the Council's deposits may not be returned to it. Under Puerto Rico statutes public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. The bank balance of the Council's deposit at June 30, 2011 amounts to \$3,908,798.

As of June 30, 2011, the Council's custodial credit risk was approximately \$3,896,540, which is the bank balance of cash deposited, at the Government Development Bank (the Trustee). These deposits are exempt from the collateral requirement established by the Commonwealth.

Custodial credit risk - investments

For an investment, custodial credit risk is the risk that in the event of failure of the counter party, the Council will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The investments held by the Council are certificates of deposits with an original or remaining maturity over three months.

Interest rate risk – investments

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value is to changes to market interest rate. At year end, the average maturities of investments are as follows:

Restricted cash and investments with Trustee at June 30, 2011 consist of:

<u>Investment</u>	<u>Percentage of Total Portfolio</u>	<u>Weighted Average Maturity</u>
Certificates of Deposits - Restricted	100%	98 days

Puerto Rico Council on Higher Education  
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Notes to Financial Statements  
June 30, 2011

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(4) Capital assets:

The following schedule summarizes the capital assets held by the Council as of June 30, 2011:

	<u>Balance at June 30, 2010</u>	<u>Additions</u>	<u>Retirements/ Adjustments</u>	<u>Balance at June 30, 2011</u>
Furniture and equipment	\$ 692,039	\$ 21,089	\$ (70,022)	\$ 643,106
Vehicles	63,636	-	(19,478)	44,158
Computer and peripheral equipment	560,614	19,072	(118,828)	460,858
Leasehold improvements	<u>475,750</u>	<u>-</u>	<u>-</u>	<u>475,750</u>
Total	1,792,039	40,161	(208,328)	1,623,872
Less accumulated depreciation and amortization	<u>1,496,212</u>	<u>77,914</u>	<u>(208,328)</u>	<u>1,365,798</u>
	<u>\$ 295,827</u>	<u>\$ (37,753)</u>	<u>\$ -</u>	<u>\$ 258,074</u>

Depreciation expense amounted to \$77,914 for the year ended June 30, 2011, and is included within the operations governmental activities in the accompanying Statement of Activities.

**Puerto Rico Council on Higher Education**  
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**Notes to Financial Statements**  
**June 30, 2011**

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**(5) Restricted and unrestricted net assets:**

As of June 30, 2011, the restricted and unrestricted net assets are composed as follows:

<u>Purpose</u>	<u>Amount</u>
Restricted net assets:	
Restricted fund balance	\$ 7,785,380
Assigned fund balance	813,874
Long-term debt for vacations	<u>(25,951)</u>
Restricted net assets	<u>\$ 8,573,303</u>
Unrestricted net assets:	
Unassigned fund balance	\$ 1,824,568
Voluntary termination benefits	(596,246)
Long-term debt for vacations	<u>(519,588)</u>
Unrestricted net assets	<u>\$ 708,734</u>

**(6) Pension plans:**

Employees of the Council participate in one of the two pension plans available at the Council, as follows:

- i. The Council's employees that were employed by the University of Puerto Rico (University) before the Council's creation participate in the University of Puerto Rico Retirement System.
- ii. The employees that became part of the Council after its creation participate in the Employees Retirement System of the Government of Puerto Rico (the System) and its instrumentalities.

Additional information on the University of Puerto Rico Retirement System is provided in its financial statements for the years ended June 30, 2011 and 2010, a copy of which can be obtained from the UPR Retirement System Administrator, P. O. Box 21769, UPR Station, San Juan, Puerto Rico 00931. For more information on the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities, refer to its financial statements, a copy of which can be obtained from the Administrator of Retirement System Administration, P. O. Box 42003, San Juan, Puerto Rico 00949.

Total payroll covered during the year ended June 30, 2011 amounted to approximately \$1,248,495.

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**June 30, 2011**

University of Puerto Rico Retirement System (UPRRS)

The UPRRS provides retirement, disability, and death benefits. Cost-of-living adjustments are provided at the discretion of the UPRRS's Board of Trustees. Benefits vest after completion of a given number of years of credited service based on age. Benefits are determined by the application of stipulated benefit ratios of the members' average compensation.

Funding Policy University employees are required to contribute 4% to 11% of their annual salary to the UPRRS, depending on certain qualifications. The University was required to contribute 10.9% of applicable payroll in 2007. The contribution made was 13%. The contributions are established by law, and are not actuarially determined. Although the University has not expressed any intent to terminate the Plan administered by the UPRRS, it may do so at any time. In the event of termination, the right of participants and beneficiaries are non-forfeitable to the extent funded.

Total contributions (rounded) to the UPRRS for the Council for the years ended June 30, 2011, 2010 and 2009 were approximately as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Employees	\$ 33,400	\$ 35,300	\$ 40,500
Employer	75,400	76,500	95,200
Total	<u>\$ 108,800</u>	<u>\$ 111,800</u>	<u>\$ 135,700</u>

Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS)

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

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

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

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Notes to Financial Statements  
June 30, 2011

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

Total contributions (rounded) for the years ended June 30, 2011, 2010 and 2009 were approximately as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Employees	\$ 56,300	\$ 89,800	\$ 117,800
Employer	<u>62,500</u>	<u>105,000</u>	<u>131,000</u>
Total	<u>\$ 118,800</u>	<u>\$ 194,800</u>	<u>\$ 248,800</u>

(7) **Voluntary termination benefits:**

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

The financial impact resulting for the benefits granted to participants on this program was the recognition of a liability in the statement of net assets and a charge in the statement of activities in the amount of \$596,246 as of and for the year ended June 30, 2011, respectively. At June 30, 2011, unpaid long-term benefits granted on this program were discounted at 3.29%.

Puerto Rico Council on Higher Education  
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Financial Statements  
June 30, 2011

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(8) **Risk management:**

To minimize its risk of loss the Council purchases insurance coverage for public liability, hazard, property, natural disasters and directors and officers automobile, crime and bonding as well as medical and workmens' insurance for employees. The selection of the insurer must be approved by the Commonwealth Treasury Department's insurance office. Insurance coverage's for fiscal years 2011 and 2010 remained similar to those of prior years. For the last three years insurance settlements have not exceeded the amount of coverage. Claims and liabilities are accounted for when it is probable that a claim has occurred and the amount of loss can be reasonably estimated. At June 30, 2011 and 2010, there are no outstanding claims.

(9) **Commitments and contingencies:**

Lease commitments

The Council leased office facilities under an operating non-cancelable lease agreement expiring in 2012. Rent expense for leased facilities for the year ended June 30, 2011 amounted to \$428,229.

During the pre-consolidation process with the Puerto Rico Council on General Education (See Note 10), the Council was required to assume a lease debt of this entity related to an unbudgeted portion of their rent expense from January 2011 through June 2011. As of June 30, 2011, an accrual amounting to \$216,118, was recorded associated with this lease commitment.

Litigation settlement

During the year ended June 30, 2011, the Professional Employees International Union presented a claim to the Labor Relations Commission Public Service (LRCPS) for unjustified dismissal on behalf a former employee, discharged under Act No. 7. On June 22, 2011, the LRCPS determined that the Council was liable of lost wages amounting to \$44,255 and ordered to reinstate the employee. As of June 30, 2011, an accrual related to lost wages was recorded in the accompanying financial statements.

Encumbrances

The Council has commitments related to unperformed contracts of services, amounting to \$349,027, for the year ended June 30, 2011. Those encumbrances are presented in the general fund classified as assigned fund balance.

(10) **Subsequent events:**

On July 1, 2011, the Council consummated a merger with the Puerto Rico Council on General Education covered by the provisions of the Reorganization Plan No. 1, of July 26, 2010 for the, under Act 182 of December 17, 2009 known as "Act of Reorganization and Modernization of the Executive Branch of the Government of Puerto Rico of 2009". A new organization was created; Puerto Rico Council on Education, and all the assets and liabilities of the Council were transferred and assumed by the new Council during the merge.

During the pre-consolidation process with the Puerto Rico Council on General Education, the Council was required to assume a lease debt of this entity related to an unbudgeted portion of their rent expense from January 2011 through June 2011. As of June 30, 2011, an accrual amounting to \$216,118, was recorded associated with this lease commitment.

**Puerto Rico Council on Higher Education**  
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**Required Supplemental Information**  
**Statements of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds**  
**Budget and Actual**  
**Year Ended June 30, 2011**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Positive (Negative)
	Original	Final		
<b>Revenues:</b>				
Commonwealth appropriations	\$ 27,737,521	\$ 27,737,521	\$ 27,737,521	\$ -
Federal grants	-	-	1,706,060	1,706,060
Licenses and accreditations	400,000	127,295	514,000	386,705
Investment income	-	-	37,199	37,199
Other income	-	-	86,770	86,770
<b>Total revenues</b>	<b>28,137,521</b>	<b>27,864,816</b>	<b>30,081,550</b>	<b>2,216,734</b>
<b>Expenditures:</b>				
Current:				
General and administrative:				
Operational Fund	3,145,001	2,970,961	2,958,057	12,904
Licenses and accreditation	-	127,295	143,532	16,237
Sub-total General and Administrative	3,145,001	3,098,256	3,101,589	(3,333)
Educational aid	25,000,000	25,000,000	26,250,685	(1,250,685)
Capital expenditures	8,000	54,744	39,629	15,115
<b>Total expenditures</b>	<b>28,153,001</b>	<b>28,153,000</b>	<b>29,391,903</b>	<b>(1,238,903)</b>
Excess (deficit) of revenues over expenditures	(15,480)	(288,184)	689,647	977,831
Transfers in	-	-	-	-
Transfers out	-	-	-	-
<b>Net change in fund balance</b>	<b>(15,480)</b>	<b>(288,184)</b>	<b>689,647</b>	<b>977,831</b>
Fund balance - at beginning of year	9,664,306	9,664,306	9,664,306	-
Fund balance - at end of year	\$ 9,648,826	\$ 9,376,122	\$ 10,353,953	\$ 977,831

Puerto Rico Council on Higher Education  
(A Component Unit of the Commonwealth of Puerto Rico)

Schedule of Expenditures of Federal Awards  
For the Year Ended June 30, 2011

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<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
<b>U.S. Department of Education:</b>		
Improving Teacher Quality State Grants - SAHES No Child Left Behind Program	84.367B	<u>\$ 1,706,060</u>

Puerto Rico Council on Higher Education  
 (A Component Unit of the Commonwealth of Puerto Rico)

Notes to the Schedule of Expenditures of Federal Awards  
 For the Year Ended June 30, 2011

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1. Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity of Puerto Rico Council on Higher Education (the Council) under programs of the federal government for the year ended June 30, 2011. The information in this schedule is presented in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Because the schedule presents only a selected portion of the operations of the Council, it is not intended to and does not present the financial position, changes in net assets or cash flows of the Council.

2. Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the modified accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-122, *Cost Principles for Non-profit Organizations*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

3. Subrecipients

Of the federal expenditures presented in the Schedule, the Council provided federal awards to subrecipients as follows:

<u>Program Title</u>	<u>Federal CFDA Number</u>	<u>Amount Provided to Subrecipients</u>
Improving Teacher Quality State Grants - SAHES No Child Left Behind Program	84.367B	<u>\$ 1,594,672</u>



**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**

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**The Board of Trustees of the  
Puerto Rico Council on Higher Education  
San Juan, Puerto Rico**

We have audited the financial statements of the Puerto Rico Council on Higher Education (the Council) as of and for the year ended June 30, 2011 and have issued our report thereon dated October 14, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

**Internal Control over Financial Reporting**

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Council's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be a material weakness, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Council'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 no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

We noted certain matters that we reported to management of the Council in a separate letter dated October 14, 2011.

This report is intended solely for the information and use of the Board of Trustees and other charged with governance, management, others within the Council, and the U.S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

*Kevane Grant Thornton LLP*

San Juan, Puerto Rico,  
October 14, 2011.





**Independent Auditor's Report on Compliance with Requirements that could have a Direct and Material Effect on each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133**

**The Board of Trustees of the  
Puerto Rico Council on Higher Education  
San Juan, Puerto Rico**

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**Compliance**

We have audited Puerto Rico Council on Higher Education's (the Council) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on its major federal program for the year ended June 30, 2011. The Council's major federal program is 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 its major federal program is the responsibility of the Council's management. Our responsibility is to express an opinion on the Council's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audit of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Council'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 Council's compliance with those requirements.

In our opinion, Puerto Rico Council on Higher Education complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal program for the year ended June 30, 2011. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item 2011-01.

### Internal Control Over Compliance

Management of the Council 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 Council's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Council's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiency in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified a deficiency in internal control over compliance that we consider to be a significant deficiency as described in the accompanying schedule of findings and questioned costs as item 2011-01. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

### Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Council as of and for the fiscal year ended June 30, 2011, and have issued our report thereon dated October 14, 2011, which contained an unqualified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Council's basic financial statements. The 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, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial

statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

The Council's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the Council's response and, accordingly, we express no opinion on the response.

This report is intended solely for the information and use of the Board of Trustees and others charged with governance, management, others within the Council, and the U.S. Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

*Kevane Grant Thornton LLP*

San Juan, Puerto Rico,  
October 14, 2011.



**Puerto Rico Council on Higher Education**  
**(A Component Unit of the Commonwealth of Puerto Rico)**

**Schedule of Findings and Questioned Costs**  
**Year Ended June 30, 2011**

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**Section I - Summary of Auditor's Results**

**Financial Statements -**

Type of auditor's report issued: Unqualified

Internal control over financial reporting:  
 Material weakness(es) identified?  yes  no  
 Significant deficiency(ies) identified that are not considered to be material weaknesses?  yes  None reported

Noncompliance material to financial statements noted?  yes  no

**Federal Awards -**

Internal control over major programs:  
 Material weakness(es) identified?  yes  no  
 Significant deficiency(ies) identified that are not considered to be material weakness(es)?  yes  None reported

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

Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of OMB Circular A-133?  yes  no

**Identification of Major Programs -**

<u>CFDA Number(s)</u>	<u>Name of Federal Program</u>
84.367B	Improving Teacher Quality State Grants - SAHES No Child Left Behind Program

Dollar threshold used to distinguish Between Type A and Type B programs: \$300,000

Auditee qualified as low-risk auditee?  yes  no

**Section II- Financial Statements Findings**

The audit report covering the year ended June 30, 2011, dated October 14, 2011, includes no financial statement findings.

Puerto Rico Council on Higher Education  
(A Component Unit of the Commonwealth of Puerto Rico)

Schedule of Findings and Questioned Costs  
Year Ended June 30, 2011

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Section III- Federal Award Findings and Questioned Costs

A. Activities allowed or unallowed

None.

B. Allowable Costs/Cost Principles

None.

C. Cash Management

**Finding 11-01 (Improving Teacher Quality State Grants – SAHES – 84.367B [No Child Left Behind Program])**

*Condition:*

During our compliance testing procedures, we noted in one (1) instance of twenty-five (25) that the Council did not disburse the funds from its bank account within the seventy-two (72) hours time frame established by Federal agency.

*Criteria:*

When entities are funded on a reimbursement basis, program costs must be paid for by entity funds before reimbursement is requested from the Federal Government. When funds are advanced, recipients must follow procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement.

The requirements for cash management are contained in the A-102 Common Rule (§\_\_\_\_.21), OMB Circular A-110 (2 CFR section 215.22), Treasury regulations at 31 CFR part 205, program legislation, Federal awarding agency regulations, and the terms and conditions of the award.

The Council is required to disburse the funds from its bank account within seventy-two (72) hours of receiving them from the Federal agency.

*Cause:*

The funding technique used by the Council to minimize time elapsed between receipt of Federal funds and actual disbursement is not functioning correctly.

*Effects:*

The Council is not in compliance with the above mentioned requirement which could result in cost disallowances by the Federal awarding agency.

*Questioned Costs:*

None identified.

Puerto Rico Council on Higher Education  
(A Component Unit of the Commonwealth of Puerto Rico)

Schedule of Findings and Questioned Costs  
Year Ended June 30, 2011

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*Recommendation:*

The Council must establish and implement internal controls directly related to minimize the time elapsed between receipt of Federal funds and actual disbursement. The Council should make efforts to limit cash advances to the minimum amounts needed and should time its advances to meet actual immediate cash needs. Also, the Council must determine to work all Federal cash request to be under the reimbursement method funding technique to prevent noncompliance with the Federal compliance requirement.

*Management's Response:*

We accept the auditors' recommendation. Immediately, all the No Child Left Behind Program checks will be send by certified mail within the period established by the regulations.

**D. Davis-Bacon Act**

None.

**E. Equipment and Real Property Management**

None.

**F. Matching, Level of Effort, Earmarking**

None.

**G. Period of Availability of Federal Funds**

None.

**H. Procurement and Suspension and Debarment**

None.

**I. Program Income**

None.

**J. Real Property Acquisition and Relocation Assistance**

None.

**K. Reporting**

None.

Puerto Rico Council on Higher Education  
(A Component Unit of the Commonwealth of Puerto Rico)

Schedule of Findings and Questioned Costs  
Year Ended June 30, 2011

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L. Sub-recipient Monitoring

None.

M. Special Tests and Provisions

None.

**Puerto Rico Council on Higher Education**  
(A Component Unit of the Commonwealth of Puerto Rico)

**Summary Schedule of Prior Year Audit Findings**  
**Year Ended June 30, 2011**

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**Finding 10-02**

*Federal Program:*

CFDA 84.367B Improving Teacher Quality Grants – SAHES (No Child Left Behind Program)

*Compliance Requirement:*

Procurement and Suspension and Debarment

*Condition:*

The Council does not have internal controls established to verify that individuals and entities that received contracts or sub-awards (related to federal programs) are not suspended or debarred for participation in federal programs.

*Status:*

This condition was corrected. The Council immediately implemented an internal control mechanism by adding a new step prior to settling a contract or sub-award, to verify if individuals and entities interested in contracts or sub-awards related to Federal programs are not suspended or disqualified from such participation.

**Puerto Rico Council on Higher Education**  
**(A Component Unit of the Commonwealth of Puerto Rico)**

**Profile of Independent Public Accountants**  
**Year Ended June 30, 2011**

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**CPA FIRM:** Kevane Grant Thornton LLP

**IDENTIFICATION NUMBER:** 66-0563256

**LEAD AUDITORS:** Luis Valenzuela -- Audit Partner  
Kayra Rivera -- Audit Manager

**ADDRESS:** 33 Bolivia St., 4th Floor  
San Juan, Puerto Rico 00917

**TELEPHONE NUMBER:** (787) 754-1915

The audit was performed between July and September 2011, at the Council's facilities, as follows:

<u>Location</u>	<u>Description of Facility</u>	<u>Dates Visited</u>
San Juan, PR	Administration Offices	July through September 2011

Records for the accounting and administration of the Council are located at the above-referenced facility.