guzmán torres & co., psc
certified public accountants & business advisors

PUERTO RICO METROPOLITAN BUS AUTHORITY

(A Component Unit of the Commonwealth of Puerto Rico)

AUDITED FINANCIAL STATEMENTS
YEARS ENDED JUNE 30, 2010 AND 2009

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PUERTO RICO METROPOLITAN BUS AUTHORITY

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INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying statements of net assets of Puerto Rico Metropolitan Bus Authority (the Authority), a component unit of the Commonwealth of Puerto Rico, as of June 30, 2010 and 2009, and the related statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Puerto Rico Metropolitan Bus Authority at June 30, 2010 and 2009 and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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

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As described in Note 12 to the financial statements, the Authority received operating assistance from the Commonwealth of Puerto Rico to assist in the financing of the Authority's operations. The amount of such assistance indicates that the Authority may require continued assistance in order to operate at its current level an as a going concern.

Guzmán Torres & Co., P.S.C.

CERTIFIED PUBLIC ACCOUNTANTS
September 28, 2010

Stamp #2579087_
was affixed to
the original of
this report.

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

MANAGEMENT DISCUSSION AND ANALYSIS
YEARS ENDED JUNE 30, 2010 AND 2009

The following discussion and analysis of the financial performance and activity of the Puerto Rico Metropolitan Bus Authority ("the Authority") provides an introduction and understanding of the basic financial statements of the Authority for the fiscal years ended June 30, 2010 and 2009. This discussion was prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

Financial Highlights for 2010

- Net assets deficiency totaled $12.7million at June 30, 2010.
- Net assets deficiency decreased by $6.8 million in 2010, as compared to an increase of approximately $21.5 million in 2009.
- Net capital assets totaled $64.6 million at June 30, 2010
- Net capital assets increased by 13% at June 30, 2010, when compared with the balance at June 30, 2009 of $51.5 million.

Financial Highlights for 2009

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

The Financial Statements

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

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

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

Overview of the Financial Statements for Business-Type Activities

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

Statement of Net Assets

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

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

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

- *Unrestricted Net Assets* - this component includes all net assets that do not meet the definition of net assets invested in capital assets.

Statement of Revenues, Expenses, and Changes in Net Assets

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

Statement of Cash Flows

The statement of cash flows discloses net cash provided by or used for operating activities, investing activities, noncapital financing activities, and from capital and related financing activities. This statement also portrays the health of the Authority in that current cash flows are sufficient to pay current liabilities.

Notes to Financial Statements

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

Financial Analysis of the Authority's Business-Type Activities

Statements of Net Assets

The following table reflects a condensed summary of assets, liabilities, and net assets of the Authority as of June 30, 2010, 2009, and 2008:

	June 30,		
	2010	**2009**	**2008**
ASSETS			
Current assets	$ 31,217,692	$ 10,712,321	$ 21,785,936
Capital assets	64,555,810	51,519,173	58,688,677
Other assets	542,071	267,071	267,886
Total assets	$ 96,315,573	$ 62,498,565	$ 80,742,499
LIABILITIES			
Current liabilities	$ 73,379,949	$ 44,656,321	$ 39,719,492
Long-term liabilities	35,689,966	37,409,974	39,129,982
Total liabilities	109,069,915	82,066,295	78,849,474
NET ASSETS			
Invested in capital assets, net of related debt	47,417,211	51,519,173	58,688,677
Deficiency in unrestricted net assets	(60,171,553)	(71,086,903)	(56,795,652)
Total net assets	(12,754,342)	(19,567,730)	1,893,025
Total liabilities and net assets	$ 96,315,573	$ 62,498,565	$ 80,742,499

June 30, 2010

Current assets increased by 191.4% to $31.3 million. The change in current assets is primarily due to an increase in the amount due by federal government related to capital contributions received after June 30, 2010.

Capital assets increased by 13% to $64.6 million principally for the acquisition of transportation equipment net of related depreciation for the year. Capital assets are funded with the proceeds from operations and operating and capital grants from the Commonwealth of Puerto Rico. In addition, the Authority is a recipient of certain funds under Federal program 20.507 "Urban Mass Transportation Capital and Operating Assistance Formula Grant" granted by the Federal Transit Administration which is used to finance the acquisition of capital assets. Total capital grants received during fiscal year 2010 from the Commonwealth of Puerto Rico and the Transit Administration amounted to approximately $22.9 million.

Current liabilities increased by 64.3% to $73.3 million. This increase consists principally of an increase in accounts and accrued expenses payable. Accounts payable include approximately $16 million for the acquisition of transportation equipment that will be paid with the capital contributions received from the Federal government after June 30, 2010.

Long-Term Debt consists principally of amounts due to Scotia Bank of Puerto Rico related to a long-term financing obtained in prior years. The loan with Scotia Bank is payable in monthly principal installment of $143,334 plus interests at fixed rate of 5.43% plus a spread as defined in the loan agreement (6.68% at June 30, 2010) due in February 12, 2012.

Net assets deficiency decreased 35% to a net deficiency of $12.8 million. This decrease was the result of an excess of revenues (operating and non-operating) over expenses (operating and non-operating) and capital grants of $6.8 million. The largest portion of the Authority's net assets represents its investment in capital assets net of related debt outstanding used to acquire those capital assets.

June 30, 2009

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

Capital assets decreased by 12% to $51.5 million due to the retirement and disposition of transportation equipment that reached the end of their useful life. Capital assets are funded with the proceeds from operations and operating and capital grants from the Commonwealth of Puerto Rico. In addition, the Authority is a recipient of certain funds under Federal program 20.507 "Urban Mass Transportation Capital and Operating Assistance Formula Grant" granted by the Federal Transit Administration which is used to finance the capital improvement program. Total capital grants received during fiscal year 2010 from the Commonwealth of Puerto Rico and the Transit Administration amounted to approximately $2.5 million.

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

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

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

The following table reflects a condensed summary of the revenues, expenses, and changes in net assets for the three years ended June 30, 2010:

	Years Ended June 30,		
	2010	**2009**	**2008**
Operating revenues	$ 6,313,102	$ 24,403,044	$ 31,535,689
Operating expenses	85,153,876	85,542,546	85,353,134
Operating loss	(78,840,774)	(61,139,502)	(53,817,445)
Non-operaing revenues:			
Operating grants	66,952,499	42,193,592	46,863,505
Interest income (expense), net	(4,131,901)	(5,014,845)	(3,931,421)
Total non-operating revenues	62,820,598	37,178,747	42,932,084
Loss before capital contributions	(16,020,176)	(23,960,755)	(10,885,361)
Capital contributions	22,833,564	2,500,000	10,225,283
Change in net assets	6,813,388	(21,460,755)	(660,078)
Net assets deficit at beginning of year	(19,567,730)	1,893,025	2,553,103
Net assets deficit at end of year	$ (12,754,342)	$ (19,567,730)	$ 1,893,025

***Year Ended June 30,* 2010**

Operating revenues which consisted principally of fares for transportation and other services, decreased by 74.1% to $6.3 million. This decrease is due to a decrease in patronage during fiscal year 2010 as a result of general economic conditions. The Authority had a service contract with the Puerto Rico Highways and Transportation Authority (PRHTA) in which PRHTA paid the Authority a total of $13.6 million for certain transportation services during the year ended June 30, 2009. This contract was cancelled effective February 2009. No amount was received under this contract during the year ended June 30, 2010.

Operating expenses, which consisted principally of salaries and employees benefits, depreciation and amortization, repairs and maintenance, diesel, insurance, professional services and general and administrative decreased by .45% to $85.2 million.

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

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

***Year Ended June 30,* 2009**

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

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

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

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

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At June 30, 2010, the Authority had invested approximately $64.6 million in capital assets (net of related depreciation) including transportation equipment, land and buildings and machinery and equipment used in the operations. At June 30, 2009, the Authority had invested approximately $51.5 million in capital assets.

Major capital assets events during the years ended June 30, 2010 and 2009 include the acquisition and repairs of transportation equipment which were funded principally by capital contributions received.

Debt Administration

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

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

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

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

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

STATEMENTS OF NET ASSETS
JUNE 30, 2010 AND 2009

	2010	2009
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 625,576	$ 1,169,682
Accounts receivable	23,962,847	3,416,436
Inventory	3,868,099	3,671,850
Prepaid expenses	2,761,170	2,454,353
Total current assets	31,217,692	10,712,321
CAPITAL ASSETS	64,555,810	51,519,173
OTHER ASSETS	542,071	267,071
TOTAL	$ 96,315,573	$ 62,498,565
LIABILITIES AND NET ASSETS (DEFICIT)		
CURRENT LIABILITIES:		
Borrowings under line of credit	$ 3,000,000	$ 3,000,000
Accounts payable	34,382,733	13,509,957
Accrued expenses payable	32,038,054	24,207,141
Deferred revenue	2,239,154	2,219,215
Current portion of long-term debt	1,720,008	1,720,008
Total current liabilities	73,379,949	44,656,321
LONG-TERM DEBT		
Notes payable, net of current portion	35,689,966	37,409,974
NET ASSETS (DEFICIT):		
Invested in capital assets, net of related debt	47,417,211	51,519,173
Unrestricted deficit	(60,171,553)	(71,086,903)
Net assets (deficit)	(12,754,342)	(19,567,730)
TOTAL	$ 96,315,573	$ 62,498,565

The accompanying notes are integral part of the financial statements

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

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS JUNE 30, 2010 AND 2009

	2010	2009
OPERATING REVENUES		
Passenger fares	$ 5,815,007	$ 10,120,615
Service contract with Puerto Rico Highways and Transportation Authority	-	13,654,545
Advertising and other	498,095	627,884
Total operating revenues	6,313,102	24,403,044
OPERATING EXPENSES		
Salaries and employee benefits	59,759,351	57,428,968
Diesel, gasoline, oil and lubricants	5,407,602	6,266,897
Depreciation and amortization	10,030,500	9,675,690
Materials, spare parts and repairs and maintenance	3,433,832	5,912,733
Utilities	1,354,164	1,607,215
Professional services	1,631,423	2,208,325
General and administrative	3,537,004	2,442,718
Total operating expenses	85,153,876	85,542,546
OPERATING LOSS	(78,840,774)	(61,139,502)
NON-OPERATING REVENUES (EXPENSES)		
Gasoline, diesel, petroleum and tax oil revenues	10,029,234	8,777,138
Operarting grants:		
Commonwealth of Puerto Rico operating grant	42,616,745	19,277,374
Federal Transit Administration	14,306,520	14,139,080
Interest and other financing expenses	(4,132,395)	(5,041,703)
Interest income	494	26,858
Total non-operating revenues	62,820,598	37,178,747
LOSS BEFORE CAPITAL CONTRIBUTIONS	(16,020,176)	(23,960,755)
CAPITAL CONTRIBUTIONS	22,833,564	2,500,000
CHANGE IN NET ASSETS	6,813,388	(21,460,755)
NET ASSETS DEFICIENCY AT BEGINNING OF YEAR	(19,567,730)	1,893,025
NET ASSETS DEFICIENCY, AT END OF YEAR	$ (12,754,342)	$ (19,567,730)

The accompanying notes are integral part of the financial statements

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

STATEMENTS OF CASH FLOWS
YEARS JUNE 30, 2010 AND 2009

	2010	2009
OPERATING ACTIVITIES:		
Cash received from customers and users	$ 6,220,673	$ 24,256,985
Cash payments to suppliers for goods and services	(11,703,486)	(18,287,009)
Cash payments to employees for services	(52,410,651)	(53,692,947)
Net cash used in operating activities	(57,893,464)	(47,722,971)
NON-CAPITAL FINANCING ACTIVITIES:		
Operating grants received from:		
Federal Transit Administration	12,136,872	19,203,315
Commonwealth of Puerto Rico	51,520,183	32,533,977
Interest paid	(4,354,610)	(4,148,737)
Payment of notes payable	(1,720,008)	(1,720,008)
Net cash provided by non-capital financing activities	57,582,437	45,868,547
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition of capital assets	(5,928,538)	(3,867,038)
Capital contributions	5,694,965	2,500,000
Net cash used by capital and related financing activities	(233,573)	(1,367,038)
INVESTING ACTIVITIES:		
Interest received	494	26,858
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(544,106)	(3,194,604)
CASH AND CASH EQUIVALENTS, at beginning of year	1,169,682	4,364,286
CASH AND CASH EQUIVALENTS, at end of year	$ 625,576	$ 1,169,682

The accompanying notes are integral part of the financial statements

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

STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2010 AND 2009

	2010	2009
RECONCILIATION OF OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES:		
Operating loss	$ (78,840,774)	$ (61,139,502)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization	10,030,500	9,675,690
Loss on disposition of capital assets	-	1,360,852
Changes in operating assets and liabilities:		
Accounts receivable	(92,429)	(146,059)
Inventory	(196,249)	241,744
Prepaid expenses	(306,817)	266,498
Other assets	(275,000)	815
Accounts payable	3,734,177	(2,866,790)
Accrued expenses payable	8,053,128	4,883,781
Net cash used in operating activities	$ (57,893,464)	$ (47,722,971)
SCHEDULE OF NON-CASH TRANSACTIONS:		
Accounts payable incurred in the acquisition of capital assets	$ 17,138,599	$ -

The accompanying notes are integral part of the financial statements

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

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

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

Use of Estimates

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

Cash and Cash Equivalents

In the statement of cash flows, cash equivalents are defined as short-term, highly liquid investments that are readily convertible to known amounts of cash and are so near to their maturity that they present insignificant risk of changes in value because of changes in

interest rates. In particular, they include cash on hand and on deposit and short-term investments with maturities of three months or less.

Allowance for Doubtful Accounts

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

Inventories

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

Capital Assets

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

The estimated useful lives of the capital assets follow:

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

The Authority periodically reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. No impairment of capital asset was identified during the years ended June 30, 2010 and 2009. During the years ended 2009 the Authority retired from operations transportation equipment which reached the end of its useful live. A loss of approximately $1,360,000 was recorded as result of such retirements during the year ended 2009 respectively.

Vacation and Sick Leave

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

Net assets

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

Invested in Capital Assets, Net of Related Debt

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

Unrestricted

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

Operating Revenues and Expenses

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

Contributions

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

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

Risk Financing

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

Accrual for legal claims

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

2. CASH AND CASH EQUIVALENTS

Cash and cash equivalents at June 30, 2010 and 2009 consist of cash on hand and on bank deposit.

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

Pursuant to the Investment Guidelines for the Commonwealth adopted by Government Development Bank for Puerto Rico ("GDB"), the Authority may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, repurchase agreements, bankers acceptances, or in pools of obligations of the municipalities of Puerto Rico, among others. There are no investments at June 30, 2010 and 2009.

For deposits, custodial credit risk is the risk that in the event of bank failure, the Authority's deposits may not be returned to it. Under Puerto Rico statutes public funds deposited in commercial bank must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of the Commonwealth of Puerto Rico. The bank balance of the Authority's deposit at June 30, 2010 and 2009, excluding deposits in Government Development Bank for Puerto Rico described below, amounted to approximately $1,345,815 and $1,393,000, respectively, of which $983,852 and $773,000 are insured by Federal Deposit Insurance Corporation at June 30, 2010 and 2009 respectively.

In addition, at June 30, 2010 and 2009, the Authority maintained cash deposited at the Governmental Development Bank for Puerto Rico (GDB), in the amount approximately $92,000 and $71,000, respectively. These amounts are uncollateralized since by law, the governmental banks of the Commonwealth of Puerto Rico are exempt of the requirement of insuring the deposits of funds of the entities of the Commonwealth of Puerto Rico.

3. ACCOUNTS RECEIVABLE

Accounts receivable at June 30, 2010 and 2009 consist of:

	2010	2009
Operating and capital grants:		
Federal Transit Administration	$ 20,918,229	$ 1,590,043
Commonwealth of Puerto Rico	1,322,901	197,105
Puerto Rico Highways and Transportation Authority	1,575,930	1,572,556
Other	528,809	439,754
Total	24,345,869	3,799,458
Less allowance for doubtful accounts	383,022	383,022
Total	$ 23,962,847	$ 3,416,436

Account receivable from Federal Transit Administration consists principally of operating and capital contributions pending to be received at June 30, 2010 and 2009. At June 30, 2010 the amount receivable includes approximately $17 million for capital contributions that are restricted for the payment of liabilities related to the acquisition of capital assets.

The account receivable from the Puerto Rico Highways and Transportation Authority (PRTHA) includes approximately $1,256,000 related to a contract with PRTHA in which the Authority provides transportation services to passengers using the urban train system. Under the term of the contract PRTHA will reimburse the Authority certain amounts specified in the contract for each passenger served. The amount outstanding represents the amount billed to PRTHA for services performed since July 2005 to June 30, 2007. At June 30, 2010 management is in the process of discussing the amounts billed with PRTHA in order to settle the amount outstanding. Management believes that the amount outstanding represents billings for services performed under the term of the contract and that the amount will be collected.

4. INVENTORY

Inventory at June 30, 2010 and 2009 consists of:

	2010	2009
Spare parts	$ 3,542,389	$ 3,361,672
Diesel and gasoline	206,806	187,348
Supplies	118,904	122,830
Total	$ 3,868,099	$ 3,671,850

5. TRANSACTIONS WITH RELATED ENTITIES

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

6. ACCOUNTS AND ACCRUED EXPENSES PAYABLE

Accounts and accrued expenses payable at June 30, 2010 and 2009 include amounts due to other governmental entities in amount of approximately $23.4 million and $15.9 million respectively. These amounts represent liabilities for payroll withholdings, utilities and other related debts.

7. CAPITAL ASSETS

The following schedule summarizes the capital assets held by the Authority as of June 30, 2010 and 2009:

	Balance at June 30, 2009	Increases	Decreases	Balance at June 30, 2010
Assets not being depreciated:				
Land and improvements	$ 2,569,210	$ -	$ -	$ 2,569,210
Assets being depreciated:				
Buildings and improvements	17,869,096			17,869,096
Terminals	4,100,692			4,100,692
Transportation equipment	76,665,568	19,107,047	(6,669,527)	89,103,088
Machinery and equipment	37,847,948	4,026,983	(869,180)	41,005,751
Total	136,483,304	23,134,030	(7,538,707)	152,078,627
Less accumulated depreciation	87,533,341	10,030,500	(7,471,814)	90,092,027
Capital assets being depreciated, net	48,949,963	13,103,530	(66,893)	61,986,600
Total capital assets, net	$ 51,519,173	$ 13,103,530	$ (66,893)	$ 64,555,810

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

8. BORROWINGS UNDER LINE OF CREDIT

The Authority has an unsecured line of credit with a commercial bank in which the Authority may borrow up to $3,000,000. Borrowings under this of line of credit are by the assignment of diesel tax revenues and bear interest at LIBOR plus a spread as defined in the agreement (1.597% and 1.57% at June 30, 2009 and 2008, respectively).

A summary of the activity in the line of credit during the years ended June 30, 2010 and 2009 follows:

	Balance at 2009	Increases	Decreases	Balance at 2010	Current Portion
Borrowings under line of credit	$ 3,000,000	$ -	$ -	$ 3,000,000	$ 3,000,000

	Balance at 2008	Increases	Decreases	Balance at 2009	Current Portion
Borrowings under line of credit	$ 3,000,000	$ -	$ -	$ 3,000,000	$ 3,000,000

9. LONG-TERM DEBT

Long-term debt at June 30, 2010 and 2009 consist of:

	Balance at 2009	Increases	Decreases	Balance at 2010	Current Portion
Secured note payable to bank	$ 39,129,982	$ -	$ (1,720,008)	$ 37,409,974	$ 1,720,000

	Balance at 2008	Increases	Decreases	Balance at 2009	Current Portion
Secured note payable to bank	$ 40,849,990	$ -	$ (1,720,008)	$ 39,129,982	$ 1,720,008

The note payable to bank is secured by the assignment of diesel tax revenues and is payable in monthly principal installments of approximately $144,000 plus interest at fixed rate of 5.43% plus a spread as defined in the loan agreement (6.68% at June 30, 2010 and 2009).

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

Year ending June 30,	
2011	$ 1,720,000
2012	35,690,000
Total	$ 37,410,000

10. RETIREMENT PLAN

Substantially all the Authority's employees participate in the Retirement System of the Commonwealth of Puerto Rico ("the System"), a cost sharing multi-employer defined benefit pension plan. The payroll for employees covered by the System for the years ended June 30, 2010 and 2009 was approximately $34.8 million and $36.5 million, respectively.

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

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

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

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

Total employer contributions during the years ended June 30, 2010 and 2009 under this plan amounted to approximately $4,744,000 and $3,209,000 respectively.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2010 and 2009, a copy of which can be obtained from the Retirement System Administration, Minillas Station, P.O. Box 42003, San Juan, PR 00940.

11. COMMITMENTS AND CONTINGENT LIABILITIES

Litigation

The Authority is involved in litigation arising in the normal course of operations. Management believes that its ultimate liability, if any, in connection with these matters will not have a material effect on the Authority's financial condition and results of operations. Due to uncertainties in the settlement process, it is at least reasonably possible that management's view of the outcome of these claims will change in the near term. Based on advice of legal counsel, management has recorded an estimated litigation and claim loss of approximately $4,270,000 and $4,490,000 as of June 30, 2010 and 2009, respectively.

Federal Assistance Programs

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

12. OPERATING FINANCIAL ASSISTANCE FROM THE COMMONWEALTH OF PUERTO RICO

As shown in the accompanying financial statements, the Authority has incurred in accumulated losses after operating and capital contributions in the amount of $60.1 million and as of June 30, 2010 the Authority's liabilities exceeded its assets by approximately $12.7 million. In addition, at June 30, 2010 the Authority has a working capital deficiency of approximately $42.2 million making it difficult for the Authority to pay its liabilities in the normal course of business. These facts indicate that the Authority needs the continued support from the Commonwealth of Puerto Rico in the form of operating grants to continue to operate at its present level and to continue as a going concern. The Commonwealth of Puerto Rico has experienced budget constrains during the current and prior years which have resulted in reductions in the operating grants provided to the Authority. Management believes that since the transportation service provided by the Authority is an essential service to the people of Puerto Rico, the Commonwealth of Puerto Rico will continue to fund the operational deficits incurred by the Authority. Any significant reduction in these operating grants and financial support will affect the ability of the Authority to provide the transportation services and to continue as a going concern.