

**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES
ÁREA DE ASESORAMIENTO, REGLAMENTACIÓN E INTERVENCIÓN FISCAL
ÁREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE CATAÑO
AUDITORÍA 2010-2011
30 DE JUNIO DE 2011**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION
YEAR ENDED JUNE 30, 2011**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
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Fiscal Year Ended June 30, 2011**

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INDEPENDENT AUDITOR'S REPORT

**To the Honorable Mayor and the
Municipal's Assembly Members
Municipality of Cataño
Cataño, Puerto Rico**

I have audited the accompanying financial statements of the Governmental Activities, each major fund and the aggregate remaining fund information of the Municipality of Cataño, Puerto Rico, as of and for the year ended June 30, 2011 which collectively comprise the Municipality of Cataño basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the Municipality's of Cataño Management. My responsibility is to express an opinion on these financial statements based on my audit.

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

The Municipality does not maintain adequate accounting records for recording its financial transactions. Although the accounting records currently used by the Municipality contain substantially all financial events, such records do not provide on a timeliness basis adequate financial reports. The effects on the general purpose financial statements of this condition are not reasonably determinable.

In my opinion, except for the effect of such adjustments, if any, as might have been determined to be necessary had I been able to satisfy myself as to the adequacy of the accounting records by other auditing procedures, as explained in the preceding

paragraph, the statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each mayor fund and the aggregate remaining fund information of the Municipality of Cataño, Puerto Rico, as of June 30, 2011, and the respective changes in financial position and the respective budgetary comparison for the General Fund and the Mayor Special Revenue Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, I have also issued my report dated March 27, 2012 on my consideration of the Municipality of Cataño internal control over financial reporting and on my tests of its compliance with certain provisions of laws, regulations, contracts, and grants. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in assessing the results of my audit.

The accompanying Management's Discussion and Analysis and the Budgetary Comparison Schedule are required part of the basic financial statements referred to above but are supplementary information required by accounting principles generally accepted in the United States of America. I have applied certain limited procedures, which consisted principally of inquires of management regarding the methods of measurement and presentation of the required supplementary information. However, I did not audit the information and express no opinion on it.

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Cataño financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the basic financial statements of the Municipality of Cataño. The Schedule of Expenditures of Federal Awards has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as whole.


Ramon L. Marrero, CPA

Lic. # 3305

March 27, 2012

Bayamón, Puerto Rico



NOTE: Stamp No. 2639573 of the Puerto Rico State Society of Certified Public Accountants was affixed to the original of this report.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2011**

This discussion and analysis of the Municipality of Cataño (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2011. This Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. Besides, this document includes comparative data with prior year as this information was available for the fiscal year ended on June 30, 2010. This MD&A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

1. a broader basis in focusing important issues;
2. acknowledgement of an overview of the Municipality's financial activities;
3. provides for an evaluation of its financial condition as of the end of fiscal year 2010-2011 compared with prior year results;
4. identification of uses of funds in the financing of the Municipality's variety of activities and;
5. assess management's ability to handle budgetary functions.

FINANCIAL HIGHLIGHTS

The financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2011 constitute factual evidence of the Municipality's economic strength by the end of such year. The following comments deserve special mention:

1. Total assets of the Municipality amounted to \$155,381,414 which represents a decrease of 1% compared to prior fiscal year.
2. At the end of fiscal year 2011, total liabilities amounted to \$85,401,269. Out of said amount, \$59,506,493 corresponded to long-term liabilities of which \$50,883,000 represented the outstanding balance of bonds and notes issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues.
3. Total net assets of the Municipality amounted to \$69,980,145 which represents an increase of 12% compared to prior fiscal year.
4. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$49,001,267, derived from the following sources: \$328,520 from charges for services; \$4,063,498 from operating grants and contributions; \$705,937 from capital grants and contributions; and \$43,903,312 from general revenues available.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

FINANCIAL HIGHLIGHTS (CONTINUED)

5. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$41,556,364, a decrease of 11% compared with previous year.
6. As reflected in the Statement of Activities, the current fiscal year operations contributed to an increase in the Net Assets figure by \$7,444,906.
7. As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$5,894,042.
8. In the fund financial statements, the governmental activities revenue increased \$1,930,752 (or 4%), nevertheless governmental activities expenditures increased \$1,278,686 (or 2%).
9. As the end of the current fiscal year, the Municipality's general fund balance amounted to (\$5,843,839) compared to a fund balance of (\$5,937,683) in the prior fiscal year.
10. The actual General Fund budgetary activities resulted in an unfavorable balance of (\$4,486,533).

FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The new approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2011. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

Under the aforementioned approach, assets and liabilities are recognized using the accrual basis of accounting which is similar to the method used by most private enterprises. This means that current year's revenues and expenses are accounted for regardless of when cash is received or paid.

FINANCIAL STATEMENTS COMPONENTS

The basic financial statements consist of the government wide financial statements, the major funds financial statements and the notes to the financial statements which provide details, disclosure and description of the most important items included in said statements.

The Statement of Net Assets reflects information of the Municipality as a whole on a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

USING THIS ANNUAL REPORT

This annual report consists of a series of new financial statements with a change in the focus from previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

GOVERNMENT - WIDE FINANCIAL STATEMENTS

The Government-Wide Financial Statements are designed to provide users of the financial statements with a broad overview of the Municipality's finances in a manner similar to private-sector companies.

The Statement of Net Asset presents information on all of the Municipality's assets and liabilities, with the difference between both reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

The Statement of Activities presents information showing how the Municipality's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the Statement of Activities that will only result in cash flows in future fiscal periods. The Statement of Activities is focused on both the gross and net cost of various activities, which are provided by the government's general tax and other revenues. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

FUND FINANCIAL STATEMENTS

The Fund Financial Statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only one kind of fund which is the governmental fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government Wide Financial Statements. However, unlike the Government Wide Financial Statements, Government Fund Financial Statements, focus on near term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

FUND FINANCIAL STATEMENTS (CONTINUED)

Because the focus of governmental funds is narrower than that of the government wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government wide financial statements. By doing so, users of the basic financial statements may better understand the long-term impact of the Municipality's near term financial decisions. Both of the Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

INFRASTRUCTURE ASSETS

Historically, a government's largest group of assets (infrastructure-roads, bridges, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in government financial statements. GASB 34 requires that these assets be valued and reported within the Governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the modified approach) which periodically (at least every third year), by category, measures and demonstrated its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statement users in evaluating a local government and its performance over time.

According to the requirements of GASB 34, the government must elect to either (a) depreciate the aforementioned assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery to near perpetuity. If the government develops the asset management system, (the modified approach) which periodically (at least every three years), by category, measures and demonstrate its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. In this particular respect, the Municipality has elected the use of recognizing depreciation under the useful life method and it contemplates to continue this treatment on said basis.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

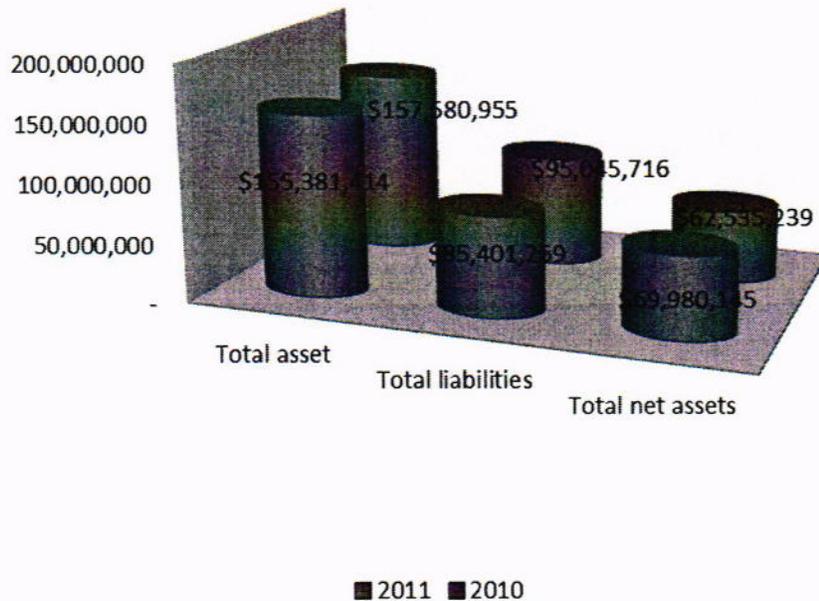
Net Assets

The Statement of Net Assets serves as an important indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Cataño, primary government assets exceeded total liabilities by \$69,980,145 at the end of 2011, as compared with \$62,535,239 as restated which reflect an increase of \$7,444,906 over previous fiscal year. The following condensed Statement of Net Assets of the Primary Government shows on a comparative basis the most important components of the \$7,444,906 increase reflected in the Net Assets figure.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Condensed Statement of Net Assets	2011	2010	Change	%
Current and other assets	\$ 30,102,376	\$ 39,708,046	\$ (9,605,670)	(24%)
Capital assets	125,279,038	117,872,909	7,406,129	6%
Total assets	155,381,414	157,580,955	(2,199,541)	(1%)
Current and other liabilities	25,894,776	30,145,811	(4,251,035)	(14%)
Long-term liabilities	59,506,493	64,899,905	(5,393,412)	(8%)
Total liabilities	85,401,269	95,045,716	(9,644,447)	(10%)
Invested in capital assets, net of related debt	74,261,179	70,780,727	3,480,452	5%
Restricted	11,737,881	16,389,085	(4,651,204)	(28%)
Unrestricted deficit	(16,018,915)	(24,634,573)	8,615,658	35%
Total net assets	\$ 69,980,145	\$ 62,535,239	\$ 7,444,906	12%



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Changes in Net Assets

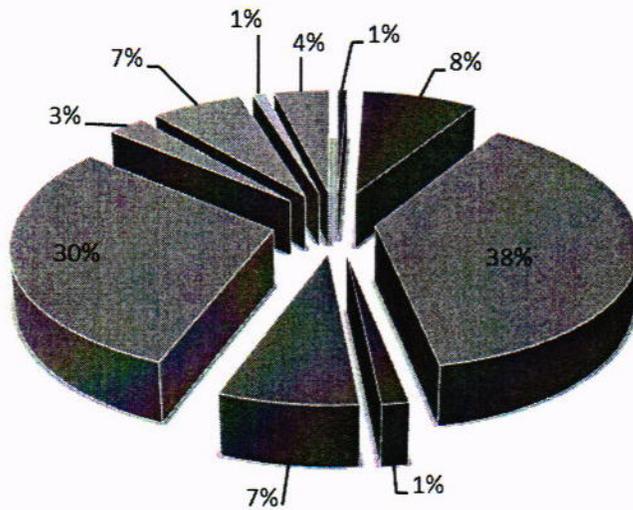
The Municipality's net assets increased by \$7,444,906. Approximately seventy eight percent (78%) of the Municipality's total revenue came from taxes, while sixteen (16%) resulted from grants and contributions, including federal aid. Charges for Services provided (1%), Interest and Investment earnings (1%) and miscellaneous (4%) of total revenues. The Municipality's largest expenses included items such as general government, health and welfare services, public works, community development and public safety. The following table and graphic presentation includes in absolute and relative terms, the composition of revenues and expenses for the fiscal years ended on June 30, 2011 and 2010. Such analysis helps the reader to evaluate the Municipal administration performance in the administration of its current financial operations.

Condensed Statement of Activities	2011	2010	Change	%
Program revenues:				
Charges for services	\$ 328,520	\$ 453,882	\$ (125,362)	(28%)
Operating grants and contributions	4,063,498	2,728,880	1,334,618	49%
Capital grants and contributions	705,937	-	705,937	100%
General revenues:				
Property taxes	18,573,025	17,963,430	609,595	3%
Municipal license tax	14,682,292	13,803,585	878,707	6%
Municipal sales and use tax	3,644,320	3,864,120	(219,800)	(6%)
Construction excise tax	1,339,452	1,465,236	(125,784)	(9%)
Grants and contributions not restricted to specific programs	3,243,206	5,550,753	(2,307,547)	(42%)
Interest and investment earnings	468,383	271,376	197,007	73%
Miscellaneous	1,952,634	969,253	983,381	101%
Total revenues	49,001,267	47,070,515	1,930,752	4%
Expenses:				
General government	19,174,723	26,303,031	(7,128,308)	(27%)
Public safety	2,925,251	3,004,311	(79,060)	(3%)
Urban and economic development	8,167,763	2,913,063	5,254,700	180%
Health and sanitation	5,375,315	4,680,972	694,343	15%
Public housing and welfare	3,211,446	2,987,141	224,305	8%
Culture, recreation and education	189,578	4,211,301	(4,021,723)	(95%)
Interest on long term debt	2,512,285	2,589,733	(77,448)	(3%)
Total expenses	41,556,361	46,689,552	(5,133,191)	(11%)
Change in net assets	7,444,906	380,963	7,063,943	1,854%
Net assets, beginning of year (as restated)	\$ 62,535,239	\$ 62,154,276	380,963	1%
Net assets, end of year	\$ 69,980,145	\$ 62,535,239	\$ 7,444,906	12%

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

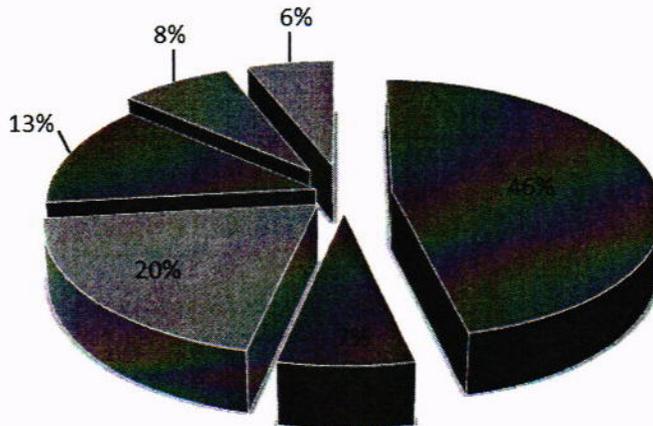
FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Revenues 2011



- Charges for services
- Operating grants and contributions
- Property taxes
- Capital grants and contributions
- Municipal sales and use tax
- Municipal license tax
- Construction excise taxes
- Grants and contributions not restricted to specific programs
- Interest and investment earnings
- Miscellaneous

Expenses 2011



- General government
- Urban and economic development
- Public housing and welfare
- Public Safety
- Health and sanitation
- Interest on long-term debt

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

As noted earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance related legal requirements.

Governmental Funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances amounting to \$5,894,042, which represents a decrease of \$4,557,360 when compared with the prior year. There are reservations of fund balance amounting to \$11,862,881. Out of the indicated balance, \$125,000 were classified as nonspendable. The combined fund balance also includes restricted fund balance amounting to \$11,659,840. This is the portion of fund balance that reflects resources that are subject to externally enforceable legal restrictions 1) to pay for specific program purposes (\$1,149,262), 2) to pay for capital projects (\$8,589,019), 3), to pay debt services (\$1,921,559). There are committed fund balance amounting to \$78,041 that can only be used pursuant to constraint formally imposed by the Municipal Legislature by ordinances and resolutions, the \$78,041 are completely to pay for specific programs purpose.

As of June 30, 2011, the General Fund, which is the main operating fund of the Municipality, reflected an unassigned fund balance of (\$5,968,839).

GENERAL FUND BUDGETARY HIGHLIGHTS

During fiscal year 2010-2011, the Municipal Legislature approved revisions to the operational budget which resulted in further increases in revenues and current expenditures which represented transactions detected during the normal course of business. Despite these budgets readjustments and as previously stated, the Municipal administration of Cataño was able to maintain a balanced budget as required by law as reflected in exhibit, Budgetary Comparison Schedule- General Fund attached here to, budgetary analysis reflected a deficiency of (\$4,486,533) of total operating revenues over current expenses.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2011, amounted to \$185,368,718 which upon deduction of accumulated depreciation in the amount of \$60,224,539 produced a net book value attributable to capital assets in the amount of \$125,144,179. Said investment includes land, construction in progress, buildings, improvements, equipment, infrastructure, furnishing, computers and vehicles. Infrastructure assets are composed of items such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)

The total increase in the Municipality's investment in capital assets for the current fiscal year represented approximately six (6%) of net book value. Depreciation charges for the year totaled \$4,983,468

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2011, the Municipality has \$8,589,019 of proceeds from bond and notes issuances and other restricted assignments that are mainly committed to future construction activities in the Capital Project Fund- Local, State and Federal Grants.

Debt Administration

The Puerto Rico Legislative Assembly has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged. The applicable law also requires that in order for a Municipality to be able to issue additional general obligation bonds and notes, such Municipality must have sufficient "payment capacity" as defined in Act No. 64. Such Act requires a Municipality must has sufficient "payment capacity" to incur additional general obligation debt if its deposits in the Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, is sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt.

The Municipality is required under prevailing applicable law to levy a Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general obligation municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. In the particular case of the Municipality of Cataño, it has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available, but the revenue can be also predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2010-2011.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)
YEAR ENDED JUNE 30, 2011**

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer.

Commonwealth of Puerto Rico
Municipality of Cataño
Statement of Net Assets
June 30, 2011

	<u>Governmental Activities</u>
Assets	
Current assets:	
Cash and cash equivalents	\$ 11,273,657
Cash with fiscal agent	14,839,613
Accounts receivable:	
Municipal license tax	37,241
Property taxes	3,470,235
Sales and use taxes	95,588
Construction excise taxes	71,213
Intergovernmental grants and contributions	47,059
Federal grants	142,771
Inventories and other assets	125,000
Total current assets	<u>30,102,377</u>
Noncurrent assets:	
Capital assets, net of depreciation	125,144,179
Deferred charges, net of accumulated amortization	134,859
Total noncurrent assets	<u>125,279,038</u>
Total assets	<u>\$ 155,381,415</u>
Liabilities	
Current liabilities:	
Accounts payable and accrued liabilities	7,320,632
Due to other governmental entities	3,503,723
Deferred revenues:	
Municipal license tax	9,140,168
Federal grant revenues	337,348
Matured interest due and payable	2,592,800
Current portion of long-term obligations	5,183,442
Total current liabilities	<u>28,078,113</u>
Noncurrent liabilities (excluding current portion):	
Bonds payable	45,980,000
Notes payable	4,903,000
Obligations under capital leases	-
Compensated absences	6,322,299
Due to other governmental entities	7,484,636
Less: Amount reported as current portion	(5,183,442)
Total noncurrent liabilities	<u>59,506,493</u>
Total liabilities	<u>87,584,606</u>
Net Assets	
Invested in capital assets, net of related debt	74,261,179
Restricted for:	
Capital projects	8,317,379
Debt service	1,921,559
Federal and state funded programs	1,227,303
Unrestricted (deficit)	(17,930,611)
Total net assets	<u>\$ 67,796,809</u>

Commonwealth of Puerto Rico
Municipality of Cataño
Statement of Activities
For the Year Ended June 30, 2011

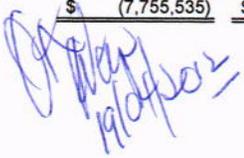
Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	19,174,723	\$ 302,499	\$ 209,163	\$ -	\$ (18,663,061)
Public safety	2,925,251	26,021	99,604		(2,799,626)
Urban and economic development	8,439,403		3,087,965	600,000	(4,751,438)
Health and sanitation	5,375,315		12,324		(5,362,991)
Public housing and welfare	3,211,446		648,524		(2,562,922)
Culture, recreation and education	189,578		25,918	105,937	(57,723)
Interest on long-term debt	2,512,285				(2,512,285)
Total governmental activities	\$ 41,828,001	\$ 328,520	\$ 4,083,498	\$ 705,937	\$ (36,710,046)
General revenues:					
Property taxes					18,573,025
Municipal license tax					14,682,292
Municipal sales and use tax					3,644,320
Construction excise taxes					1,339,452
Grants and contributions not restricted to specific programs					3,243,206
Interest and investment earnings					468,383
Miscellaneous					1,952,634
Total general revenues					43,903,312
Change in net assets					7,193,266
Net assets - beginning, as restated					60,603,543
Net assets - ending					\$ 67,796,809

Commonwealth of Puerto Rico
Municipality of Cataño
Balance Sheet
Governmental Funds
June 30, 2011

	General Fund	Debt Service Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
Assets					
Cash and cash equivalents	\$ 7,615,996	\$ -	\$ 1,977,228	\$ 1,680,433	\$ 11,273,657
Cash with fiscal agent		7,342,034	7,419,056	78,523	14,839,613
Accounts receivable:					
Municipal license tax	37,241				37,241
Property taxes	2,800,910	669,325			3,470,235
Municipal sales and use taxes	95,588				95,588
Construction excise taxes	71,213				71,213
Intergovernmental grants and contributions				47,059	47,059
Federal grants				142,771	142,771
Fines and forfeitures					-
Rent of Property					-
Due from other funds	189,830			171,536	361,366
Interest					-
Inventories and other assets	125,000				125,000
Total assets	\$ 10,935,778	\$ 8,011,359	\$ 9,396,284	\$ 2,120,322	\$ 30,463,743
Liabilities and Fund Balances					
Liabilities :					
Accounts payable and accrued liabilities	\$ 5,875,886	\$ -	\$ 1,078,905	\$ 365,841	\$ 7,320,632
Due to other governmental entities	3,503,723				3,503,723
Due to other funds	171,536			189,830	361,366
Deferred revenues:					
Municipal license tax	9,140,168				9,140,168
Federal grant revenues				337,348	337,348
Matured bonds due and payable		3,497,000			3,497,000
Matured interest due and payable		2,592,800			2,592,800
Total liabilities	18,691,313	6,089,800	1,078,905	893,019	26,753,037
Fund balances:					
Nonspendable	125,000				125,000
Restricted		1,921,559	8,317,379	1,149,262	11,388,200
Committed				78,041	78,041
Unassigned	(7,880,535)				(7,880,535)
Total fund balances	(7,755,535)	1,921,559	8,317,379	1,227,303	3,710,706
Total liabilities and fund balances	\$ 10,935,778	\$ 8,011,359	\$ 9,396,284	\$ 2,120,322	\$ 30,463,743

Commonwealth of Puerto Rico
Municipality of Cataño
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2011

	General Fund	Debt Service Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
Revenues					
Property taxes	\$ 13,841,108	\$ 4,731,917	\$ -	\$ -	\$ 18,573,025
Municipal sales and use tax	3,001,248	643,072			3,644,320
Municipal license taxes	14,682,292				14,682,292
Construction excise taxes	1,339,452				1,339,452
Intergovernmental grants and contributions	3,243,206		705,937	910,446	4,859,589
Interest	468,383				468,383
Charge for services	328,520				328,520
Federal grants				3,173,052	3,173,052
Miscellaneous	1,952,634				1,952,634
Total revenues	\$ 38,856,843	\$ 5,374,989	\$ 705,937	\$ 4,083,498	\$ 49,021,267
Expenditures					
Current:					
General government	21,037,525			170,481	21,208,006
Public safety	2,944,636			56,137	3,000,773
Urban and economic development	7,048,378		1,439,533	3,155,232	11,643,143
Health and sanitation	5,334,861				5,334,861
Public housing and welfare	1,933,661		446,878	825,203	3,205,742
Culture, recreation and education	3,575,457				3,575,457
Debt service:					
Principal		3,370,000			3,370,000
Interest		2,512,285			2,512,285
Total expenditures	41,874,518	5,882,285	1,886,411	4,207,053	53,850,267
Excess (deficiency) of revenues over (under) expenditures	(3,017,675)	(507,296)	(1,180,474)	(123,555)	(4,829,000)
Other financing sources (uses)					
Long-term debt issued					-
Bond issuance costs					-
Transfers in	4,871,640		1,740,498	19,623	6,631,761
Transfers out	(1,760,121)		(4,871,640)		(6,631,761)
Total other financing sources (uses)	3,111,519	-	(3,131,142)	19,623	-
Net changes in fund balances	93,844	(507,296)	(4,311,616)	(103,932)	(4,829,000)
Fund balance beginning, as restated	(7,849,379)	2,428,855	12,628,995	1,331,235	8,539,706
Fund balance, ending	<u>\$ (7,755,535)</u>	<u>\$ 1,921,559</u>	<u>\$ 8,317,379</u>	<u>\$ 1,227,303</u>	<u>\$ 3,710,706</u>



 19/06/2011

Commonwealth of Puerto Rico
Municipality of Cataño
Reconciliation of the Balance Sheet - Governmental Funds
to the Statement of Net Assets
For the Year Ended June 30, 2011

Total Fund Balances - Governmental Funds \$ 3,710,706

Amounts reported for Governmental Activities in the statement of Net Assets
are different because:

Capital Assets used in governmental activities are not financial resources and therefore,
are not reported in the funds. In the current period, these amounts are:

Non Depreciable Capital Assets	\$	35,889,062	
Depreciable Capital Assets		149,479,656	
Accumulated Depreciation		<u>(60,224,539)</u>	
Total Capital Assets			125,144,179

Debt issued by the Municipality has associated costs (debt issuance costs) that are paid from
current available financial resources in the governmental funds. However, these costs are
deferred in the statement of net assets and reported net of accumulated amortization. 134,859

Long term liabilities are not due in the current fiscal year, therefore, are not reported in the
governmental funds, less current maturity which is considered in the governmental funds. (61,192,935)

Total Net Assets of governmental activities \$ 67,796,809

Commonwealth of Puerto Rico
Municipality of Cataño
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2011

Net Change in Fund Balances - Total Governmental Funds **\$ (4,829,000)**

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays (\$12,552,267) exceed depreciation expense (\$4,983,468) 7,568,799

Amortization of deferred charges reported in the statement of activities does not require the use of current financial resources, therefore, are not reported as expenditures in the governmental funds. (24,323)

Disposal of capital assets require removal of cost of the capital assets from the capital asset account on the Government-Wide Statement of Net Assets, resulting in a loss on disposal of capital assets on the Government-Wide Statement of Activities and Change in Net Assets. (138,347)

Bonds and notes proceeds provide current financial resources to Governmental Funds. Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long -term liabilities in the Government-Wide Statement of Net Assets. This is the amount by which the debt proceeds exceed debt service principal payments. 3,370,000

Some expenses, net, reported in the statement of activities do not require the use of current financial resources, therefore, are not reported as expenditures in the governmental funds, including the net change in accrued compensated absences in the current year. 1,246,137

Net changes in net assets reported for governmental activities **\$ 7,193,266**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2011**

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Cataño (the Municipality) is a local municipal government constituted in 1927 in the Commonwealth of Puerto Rico (the Commonwealth). The Municipality has full legislative, fiscal and all other governmental powers and responsibilities expressly assigned by Public Act No. 81 of August 30, 1991 .as amended, known as Autonomous Municipalities Act of the Commonwealth of Puerto Rico (Act No. 81). The Municipality is one of seventy eight municipalities legally separated from the Commonwealth's government.

The Commonwealth's Constitution provides for the separation of powers of the executive, legislative and judicial branches of the Commonwealth and the municipalities. However, the Municipality's governmental system consists of executive and legislative branches only. A Mayor, elected every four years by the citizens, exercises the executive power of the Municipality. The legislative power of the Municipality is exercised by the Municipal Legislature, whose members are also elected every four years. The judiciary power is exercised by the General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality.

The Municipality assumes either full or shared responsibility for providing services to its citizens related to public housing, welfare, public safety, health, sanitation, education, culture, recreation, education, urban development, economic development, and many other fiscal, general and administrative services.

A. Financial Reporting Model

The accompanying basic financial statements present the financial position and the results of operations of the Municipality as a whole, and its various governmental funds as of and for the fiscal year ended June 30, 2011, in conformity with Generally Accepted Accounting Principles as applied to local governmental units in the United States Of America (US GAAP).

According to the financial reporting model established by GASB Statement No. 34, *Basic Financial Statements -and Management's Discussion and Analysis -for State and Local Governments* (GASB No. 34), the required basic financial statement presentation applicable to the Municipality is composed of the following elements: (1) government wide financial statements (GWFS), (2) governmental fund financial statements (GFFS), (3) notes to basic financial statements, and (4) required supplementary information (RSI).

RSI, consisting of a Management's Discussion and Analysis (MD&A), is information presented along with, but separate from, Municipality's basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

MD&A is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the fiscal year ended June 30, 2011, based on the Municipality's knowledge of the transactions, events and conditions reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

Other supplementary information presented in this report for purposes of additional analysis consists of: (1) combining and individual non-major governmental fund financial statements, (2) budgetary comparison schedule - debt service fund, and (3) schedules of capital assets used in the operations of governmental funds, as listed in the accompanying table of contents.

The Municipality adopted the provisions of GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* (GASB No. 55), and GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards* (GASB No. 56).

GASB No. 55 incorporated the hierarchy of USGAAP for state and local governments into the Governmental Accounting Standards Board's (GASB) authoritative literature. The requirements in this Statement codify all USGAAP for state and local governments so that they derive from a single source.

GASB No. 56 incorporated into the Governmental Accounting Standards Board's (GASB) authoritative literature certain accounting and financial reporting guidance presented in the American Institute of Certified Public Accountants' *Statements on Auditing Standards*. This Statement addressed three issues not included in the authoritative literature that establishes accounting principles-related party transactions, going concern considerations, and subsequent events.

In the current year, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which modified the interpretations of certain terms within the definition of special revenue funds and the types of activities the Municipality may choose to report in those funds. GASB No. 54 also clarified the capital projects fund type definition for better alignment with the needs of preparers and users. Definitions of other governmental fund types were also modified for clarity and consistency.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The following is a summary of the significant accounting policies of the Municipality:

The Municipality follows the provisions of GASB Statement No. 14, *The Financial Reporting Entity* (GASB No. 14) and GASB Statement No. 39; *Determining Whether Certain Organizations are Component Units - an Amendment of GASB Statement No. 14* (GASB No. 39) to determine its financial reporting entity.

The accompanying basic financial statements include all departments, agencies and municipal operational units that are under the legal and administrative control of the Mayor, and whose financial resources are under the legal custody and control of the Municipality's Director of Finance and Budget, as prescribed by Act No. 81.

The Municipality's management has considered (all potential component units (whether governmental, not-for-profit, or profit-oriented) for which it may be financially accountable, and other legally separate organizations for which the Municipality is not financially accountable but the nature and significance of their relationship with the Municipality may be such that exclusion of their basic financial statements from those of the Municipality would cause the accompanying basic financial statements to be misleading or incomplete. Accordingly, a legally separate organization would be reported as a component unit of the Municipality if all of the following criteria are met:

The Mayor appoints a voting majority of an organization's governing body and, either (1) the Municipality has the ability to impose its will on that organization or (2) the organization has the potential to provide specific financial benefits to, or impose specific financial burdens on, the Municipality.

The economic resources, for which the Municipality is entitled, either received or held by the separate organization, are entirely or almost entirely for the direct benefit of the Municipality or its constituents

The Municipality's management has concluded that, based on the aforementioned criteria, there are no legally separate entities or organizations that should be reported as component units of the Municipality for the fiscal year ended June 30, 2011.

B. Government-wide and fund financial statements

Financial information of the Municipality is presented in this report as follow:

1. Management's discussion and analysis introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all activities of the Municipality and its component units, if any. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, if any, which rely to a significant extent on fees and charges for support. Interfund activity has been removed from these statements to minimize the duplicating effect on assets and liabilities within the governmental activities.

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

Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. Pursuant to the provisions set forth by GASB No. 54, the Municipality reported the following governmental funds in the accompanying GFFS:

General Fund – is the Municipality main operating fund used to account for and report all financial and reported resources and governmental activities, except for those required to be accounted for in another fund. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) USGAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund. Its revenues consist mainly of taxes, licenses and permits, intergovernmental, charges for services and other.

Debt Service Fund – is a major governmental fund used to account for and report for the accumulation of financial resources that are restricted for, and the payment of, principal and interest for: (1) bonds payable for which debt service payments are legally mandated to be accounted for in a debt service fund and (2) certain special long-term obligations for which the Municipality is been accumulating financial resources in advance to pay principal and interest payments maturing in future years.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital Project Funds – is a major governmental fund used to account for and report financial resources that are restricted or committed to expenditure for capital outlays, including the acquisition or construction of major capital facilities, including those outlays financed by the general obligation bond proceeds (other than those financed by proprietary funds or in trust funds for individuals, private organizations, or other governments). The use of the capital projects funds has been limited to only for major capital acquisitions, construction or improvement activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalizable assets (such as furniture, office equipment, vehicles and other minor capital assets or improvements) have been reported in the governmental fund from which financial resources were used for the payment.

The other governmental funds of the Municipality account for grants and other resources whose use is restricted to a particular purpose.

The Municipality periodically undertakes a comprehensive evaluation of its fund structure to ensure that it complies with all aspects that are of importance to users of general purpose external financial reports.

Consequently, all superfluous funds and some internal funds currently used by the Municipality in the day-to-day accounting procedures have not been reported as individual governmental funds in the accompanying fund financial statements. Accordingly, the accompanying fund financial statements include only the minimum number of funds consistent with legal and operating requirements and, consequently, certain types of similar internal funds have been combined into single funds in the accompanying fund financial statements.

The various capital improvement bond issues outstanding have been reported as a single major capital projects fund, the capital improvements bond fund.

Numerous less significant capital project and special revenue funds have been combined into single non major capital project and special revenue funds, respectively. These funds are reported as supplementary information in the accompanying combining and individual non-major governmental fund financial statements.

Program-specific capital grants awarded by the Legislature of the Commonwealth of Puerto Rico have been combined into a single non major capital projects fund, the legislative joint resolutions fund.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The accompanying GFFS are accompanied by the following schedules required by GAAP: (1) the reconciliation of the balance sheet - governmental funds to the statement of net assets, and (2) the reconciliation of the statement of revenues, expenditures and changes in fund balances (deficits) - governmental funds to the statement of activities.

3. The notes to the financial statements provide information that is essential to a user's understanding of the basic financial statements.
4. Required supplementary information such as the budgetary comparison schedule-general fund and other types of data required by GASB.
5. Notes to the budgetary comparison schedule-general fund.

The accompanying statement of activities presents the Municipality's results of operations by showing how the Municipality's net assets changed during the fiscal year ended June 30, 2011, using a net (expense) revenue format.

This statement presents the cost of each function/program as well as the extent to which each of the Municipality's functions, programs or other services either contributes to or draws from the Municipality's general revenues (such as property taxes, municipal license taxes, construction excise taxes, etc.).

The statement of activities demonstrates the degree to which program revenues offset direct expenses of a given function/program or segments. Direct expenses are those that are clearly identifiable with a specific function, segment or operational unit. This statement reports revenues in two broad categories: (1) program revenues and (2) general revenues.

Program revenues are generated directly from a program itself or may come from parties outside the Municipality's taxpayers or citizens. In the statement of activities, program revenues reduce the costs (expenses) of the function/program to arrive at: (1) the net cost of the function/program that must be financed from the Municipality's general revenues or (2) the net program revenue that contributes to the Municipality's general revenues. The accompanying statement of activities reports the following categories of program revenues for the fiscal year ended June 30, 2011:

Charges for services - These revenues generally consist of exchange or exchange-like transactions involving charges to customers or applicants who purchase, use or directly benefit from the goods, services or privileges provided, or are otherwise directly affected by the services.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

These revenues include fees charged for specific services, charges for licenses and permits, and fines and forfeitures, among others.

Program-specific operating and capital grants and contributions - These revenues consist of transactions that are either mandatory or voluntary non-exchange transactions with other governments, organizations, or individuals that restrict the resources for use in a particular program. Operating grants and contributions consist of resources that are required to be used to finance the costs of operating a specific program or can be used either for operating or capital purposes of a specific program. Capital grants and contributions consist of revenues or resources that are restricted for capital purposes to purchase, construct or renovate capital assets associated with a specific program. Restricted operating and capital grants and contributions are program revenues because they are specifically attributable to a program and reduce the net expense of that program to the Municipality. They are reported net of estimated uncollectible amounts.

General revenues are the default category for revenues. It includes all revenues and gains that do not meet the definition of program revenues.

Property taxes, municipal license taxes, municipal sales and use taxes and construction excise taxes are reported as general revenues. All other nontax revenues (including unrestricted interest on deposits, grants and contributions not restricted for specific programs and miscellaneous revenues) that do not meet the definition of program revenues are classified as general revenues. Resources that are dedicated internally by the Municipality are reported as general revenues rather than as program revenues. All general revenues are reported net of estimated uncollectible amounts, which are recorded as reduction of revenues rather than as expenses.

The general government function/program reported in the accompanying statement of activities includes expenses that are, in essence, indirect or costs of other functions/programs of the Municipality.

Even though some of these costs have been charged to certain funds in the GFFS as indirect cost allocations permitted under some federal programs, the Municipality has reported these indirect costs as direct expenses of the general government function. Accordingly, the Municipality generally does not allocate general government (indirect) costs to other functions.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The effects of all inter-fund governmental activities (revenues, expenditures and other financing sources/uses among governmental funds) have been removed from the accompanying statements of net assets and activities.

The Municipality classifies all of its activities as governmental activities in the accompanying GWFS. These are activities generally financed through taxes, intergovernmental revenues and other non-exchange revenues that can be used to support the Municipality's programs or services. These governmental activities are also generally reported in the GFFS.

The Municipality has no fiduciary activities, which are those in which the Municipality would be holding or managing net assets for specific individuals or other external parties in accordance with trust agreements or other custodial arrangements. In addition, the Municipality has no operations or activities that are financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public (expenses, including depreciation) is financed primarily through user charges; or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

C. Governmental Fund Financial Statements

The accounts of the Municipality are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Fund types are as follows:

Special Revenue Fund - Federal Grants - Special Revenue Funds are used to account for revenues derived from federal grants. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund - Local and State Grants - Special Revenue Funds are used to account for revenues derived from local funds, state grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Debt Service Fund- Debt Service Funds are used to account for the accumulation of resources for and the payment of, general long-term debt principal, interest, and related costs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital Projects Funds - Local, State and Federal Grants - Capital Project Funds are used to account for financial resources used for the acquisition or construction of major capital facilities

Other Governmental Funds - The other governmental funds are non-major governmental funds used by the Municipality to account for revenues derived from grants, contributions or other revenue sources that are either self-restricted by the Municipality or legally restricted by outside parties for use in specific purposes.

D. Measurement focus, basis of accounting and financial presentation

Government-wide financial statements - The accompanying GWFS are prepared using the economic resources measurement focus and the accrual basis of accounting. Subject to the additional rules and limitations detailed below, revenues (including interest on deposits and investments) are generally recorded when earned and expenses are generally recorded when a liability is incurred, regardless of the timing of related cash flows.

All revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are generally recorded when the exchange takes place. In exchange transactions, each party to the transaction receives and gives up essentially equal values. An exchange-like transaction is one in which there is an identifiable exchange and the values exchanged, though related, may not be quite equal. Nevertheless, the exchange characteristics of the exchange-like transaction are strong enough to justify treating it as an exchange for accounting purposes (examples include fees for licenses and permits, charges for services, and miscellaneous revenues, which are recorded as revenues when collected because they are generally not measurable until actually received).

All revenues, expenses, gains, losses and assets resulting from non-exchange transactions are recorded using the criteria set forth by GASB Statement No. 33, Accounting and Financial Reporting for Non-exchange Transactions (GASB No. 33). GASB No. 33 established accounting and reporting standards for non-exchange transactions involving cash and financial or capital resources (for example, most taxes, grants and private donations). In a non-exchange transaction, the Municipality gives (or receives) value without directly receiving (or giving) equal value in return. This is different from an exchange transaction, in which each party receives and gives up essentially equal values. According to GASB No. 33, the Municipality groups its non-exchange transactions into the following four classes in the accompanying basic financial statements: (a) derived tax revenues, (b) imposed non exchange revenues, (c) government mandated non-exchange transactions, and (d) voluntary non-exchange transactions.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In the case of derived tax revenue transactions, which result from assessments the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred.

In the case of imposed non-exchange revenue transactions (such as property taxes and municipal license taxes), which result from assessments made by the Municipality on non-governmental entities, including individuals, other than assessments on exchange transactions, receivables are generally recorded in the period when an enforceable legal claim has arisen. Property taxes and municipal license are generally recorded as revenues (net of amounts considered not collectible) in the fiscal year when resources are required to be used or the first fiscal year that the use of the resources is permitted.

Government-mandated non-exchange transactions (such as grants and contributions) result when a government at one level (such as the federal or state government) provides resources to the Municipality and the provider government requires the Municipality to use those resources for a specific purpose or purposes established the provider's enabling legislation. In these type of transactions, receivables and revenues are generally recorded when all eligibility requirements imposed by the provider have been met. For the majority of grants, the Municipality must expend resources on the specific purpose or project before the provider reimburses any amounts. Revenue is, therefore, generally recognized as qualifying reimbursable expenditures are incurred.

Voluntary non-exchange transactions (such as donations and certain grants and entitlements) result from legislative or contractual agreements, other than exchanges, willingly entered into by two or more parties. In these types of transactions, receivables and revenues are generally accounted for in the same manner as government-mandated non-exchange transactions discussed above. Events that are neither exchange nor non-exchange transactions are recorded when it is probable that a loss has been incurred and the amount of loss is reasonably estimable.

Receipts of any type of revenue sources collected in advance for use in the following fiscal year are recorded as unearned (deferred) revenues.

According to GASB No. 34, all general capital assets and the un-matured long-term liabilities are recorded only in the accompanying statement of net assets. The measurement focus and the basis of accounting used in the accompanying GWFS differ significantly from the measurement focus and basis of accounting used in the preparation of the accompanying GFFS. Therefore, the accompanying GFFS include reconciliations, as detailed in the accompanying table of contents, to better identify the relationship between the GWFS and the GFFS.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Governmental fund financial statements- The accompanying GFFS are reported using the current financial resources measurement focus (flow of current financial resources) and the modified accrual basis of accounting. Revenues are generally recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current fiscal year or soon enough thereafter to pay liabilities of the current fiscal year. For this purpose, the Municipality generally considers most revenues (municipal licenses taxes, construction excise taxes, sales and use taxes, interests on deposits, intergovernmental grants and contributions and certain charges for services) to be available if collected within sixty (60) days after June 30, 2011. At June 30, 2011, all revenues sources met this availability criterion.

Property taxes are all considered susceptible to accrual if commonly collected within sixty (60) days following the end of the fiscal period, unless unusual circumstances justify a greater period.

Other revenue sources considered susceptible to accrual include municipal license taxes, sales and use taxes, construction excise taxes, intergovernmental grants and contributions, interests on deposits and charges for services. These principal revenue sources meet both measurability and availability criteria in the accompanying GFFS.

In a manner similar to the GWFS, but subject to and limited by the availability criteria discussed above, all revenues, expenses, gains, losses, assets and liabilities resulting from exchange, exchange-like transactions are also generally recorded when the exchange takes place while all revenues, expenses, gains, losses, and assets resulting from non-exchange transactions are recorded when an enforceable legal claim arises or when all eligibility requirements imposed by the provider have been met, applicable.

Interests on deposits are recorded when earned since these revenues are considered both measurable and available at June 30, 2011.

Pursuant to the provisions of GASB Interpretation No.6, "*Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*" (GASBI. No. 6; in the absence of an explicit requirement (i.e., the absence of an applicable modification, discussed below), the Municipality generally accrues a governmental fund liability and expenditure (including salaries, professional services, supplies, utilities, etc.) in the period in which the government incurs the liability, to the extent that these liabilities are normally expected to be liquidated in a timely manner and in full with current available financial resources.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

GASB No. 6 modified the recognition criteria for certain expenditures and liabilities reported under the modified accrual basis of accounting prior to GASB No. 34, and clarified a number of situations in which the Municipality should distinguish between governmental fund liabilities and general long-term liabilities. Therefore, the accompanying balance sheet governmental funds generally reflect only assets that will be converted into cash to satisfy current liabilities. Long-term assets and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying balance sheet governmental funds. At the same time, long-term liabilities (generally, those un matured that will not require the use of current financial resources to pay them) are not accounted for in the accompanying balance sheet governmental funds.

Modifications to the accrual basis of accounting in accordance with GASBI No.6 include:

Principal and interest on bonds payable are recorded when they mature (when payment is due), except for principal and interest of bonds due on July 1, 2010, which are recorded as governmental fund liabilities at June 30, 2010 which is the date when resources were available in the debt service fund.

Notes payable, obligations under capital leases, compensated absences, and legal claims and judgments are recorded only when they mature (when payment is due).

Certain accounts payable intergovernmental payables and other accrued liabilities not due and payable (no matured) or not normally expected to be liquidated in full and in a timely manner with available and expendable financial resources, are recorded in the accompanying statement of net assets. Such liabilities are recorded in the governmental funds when they mature. Executory purchase orders and contracts are recorded as a reservation of fund balance in the GFFS.

The measurement focus of the GFFS is on decreases of net financial resources (expenditures) rather than expenses. Most expenditures are measurable and are recorded when the related governmental fund liability is incurred. Allocation of costs, such as depreciation and amortization are recorded in the accompanying statement of activities, but are not recorded in the accompanying GFFS.

E. Assets, liabilities and net assets

- 1. Cash and cash equivalents, and cash with fiscal agent-** The Municipality's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash with fiscal agent in the debt service fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law. Also, cash with fiscal agent consists of unused proceeds of bonds and notes issued for the acquisition of equipment and construction of major capital improvements.

2. Receivables and payables- Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables in the General Fund represent mostly contributions from the Puerto Rico Electric Power Authority, which contribute a specific percentage of their revenues as payment in lieu of taxes. Intergovernmental receivable in the special revenue fund represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs.

3. Inventories- Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net assets.
4. Capital assets- Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. The Municipality defines capital asset as assets with an initial, individual cost of more than \$25 and an estimated useful life in excess of one year. Such assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital assets of the Municipality are depreciated using the straight-line method over the following estimated useful lives:

<u>Description</u>	<u>Useful Life</u>
Land improvements	20 years
Buildings and site improvements	30 to 50 years
Infrastructure	20 to 50 years
Vehicles	8 years
Furniture and fixtures	5 to 20 years
Machinery and equipment	3 to 5 years

5. Deferred revenues – In the GFFS, deferred revenues arises when one of the following situations occur:

- a. Potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period (unavailable revenue). As previously discussed, available is defined as due (or past due) at June 30, 2011 and collected within 60 days thereafter to pay obligations due at June 30. In subsequent periods, when both criteria are met, the liability for deferred revenue is removed and revenue is recognized.
- b. The Municipality receives resources before it has a legal claim to them (unearned revenue). In subsequent periods, when the revenue recognition criterion is met, the liability for deferred revenue is removed and revenue is recognized.

Deferred revenues at the government-wide level arise only when the Municipality receives resources before it has a legal claim to them.

6. Long-term obligations- The liabilities reported in the government-wide financial statements included general and special obligation bonds and notes, and other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities and landfill closure and post closure care costs.

In the fund financial statements, governmental fund types recognize bond issuances cost, during the current period. The face amount of debt issued is reported as other financing sources, while bond issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the general fund.

Non-interest bearing notes payable are accounted for under the provisions of Opinion No. 21, *Interest on Receivables and Payables*, issued by the Accounting Principles Board (APB No. 21).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

According to APB No. 21, the Municipality has recorded such notes at present value with an imputed interest rate that approximates the rate that would have been used, using the same terms and conditions, if it had been negotiated by an independent lender. In the accompanying statement of net assets, such notes payable are reported net of the applicable unamortized discount, which is the difference between the present value and the face amount of the notes. The discount is amortized over the life of the notes using the effective interest method. Amortization of the notes discount is recorded as part of interest expense in the statement of activities. In the GFFS, notes discount is recognized as other financing uses during the current period.

7. Leases- The Municipality classifies its lease agreements either as operating or capital leases according to Statement No.13, *Accounting for Leases*, issued by FASB (FASB No. 13). Capital lease agreements are generally non-cancelable and involve substance over form, the transfer of substantially all benefits and risks inherent in the ownership of the leased property, while operating leases do not involve such transfer. Accordingly, a capital lease involves the recording of an asset and a related lease obligation at the inception of the lease. According to FASB No. 13, the Municipality classifies a lease agreement as a capital lease if at its inception the lease meets one or more of the following four criteria:

By the end of the lease term, ownership of the leased property is transferred to the Municipality.

The lease agreement contains a bargain purchase option.

The lease term is substantially equal (75 percent or more) to the estimated useful life of the leased property.

At the inception of the lease, the present value of the minimum lease payments, with certain adjustments, is 90 percent or more of the estimated fair value of the leased property.

Although the Municipality is prevented legally from entering into obligations extending beyond one fiscal year, most capital lease agreements entered by the Municipality contain fiscal funding clauses or cancellation clauses that make the continuation of the agreements subject to future appropriations. Leases that meet at least one of the aforementioned four criteria and have a fiscal funding or a cancellation clause have been recorded as capital leases in the accompanying GWFS since the likelihood of invoking the provision is considered remote. The Municipality's lease agreements do not include contingent rental payments or escalation clauses.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In the GWFS, the obligation under capital leases is recorded at the lesser of the estimated fair value of the leased property or the present value of the minimum lease payments, excluding any portion representing executory costs and profit thereon to be paid by the lessor. A portion of each minimum lease payment is allocated to interest expense and the balance is applied to reduce the lease obligation using the effective interest method.

In the GFFS the net present value of the minimum lease payments at the inception of the capital lease is recorded simultaneously as: (1) expenditures and (2) other financing sources. Minimum lease payments are recorded as expenditures in the GFFS.

8. **Compensated absences-** Employees accumulate vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. All vacation pay is accrued when incurred in the government-wide financial statements. Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality. All sick leave pay and salary related benefits are accrued when incurred in the governmental-wide financial statements when the employee meets such criteria.
9. **Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund when the liability is incurred.
10. **Fund balances-** In the current year, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which enhanced the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied. This statement establishes fund balance classifications that comprise a hierarchy upon the use of the resources reported in governmental funds.

Pursuant to the provisions of GASB No. 54, the accompanying GFFS report fund balance amounts that are considered restricted, committed, assigned, and unassigned, based on the relative strength of the constraints that control how specific amounts can be spent, as described as follows:

- a. **Nonspendable** – Represent resources that cannot be spent readily with cash or are legally or contractually required not to be spent, including but not limited to inventories, prepaid items, and long term balances of interfund loans and accounts receivable.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- b. *Restricted* – Represent resources that can be spent only for the specific purposes stipulated by constitutional provisions, external resource providers (externally imposed by creditors or grantors), or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
- c. *Committed* – Represent resources used for specific purposes, imposed by formal action of the Municipal’s highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by a similar law, ordinance or resolution, no later than the end of fiscal year.
- d. *Unassigned* – Represent the residual classification for the Municipality’s general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

Negative fund balance amounts are assigned amounts reduced to the amount that will raise the fund balance to zero. Consequently, negative residual amounts in restricted, committed and assigned fund balance classifications have been reclassified to unassigned fund balances.

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely. However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balances amounts as of for the fiscal year ended June 30, 2011.

In situations when expenditure is made for a purpose for which amounts are available in multiple fund balance classifications, the Municipality generally spends committed resources first, and then unrestricted resources.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Within unrestricted resources, the Municipality generally spends committed resources first, followed by assigned resources, and then unassigned resources.

11. Net Assets

Restricted net assets have been reported pursuant to the provisions of GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation* (GASB No. 46). Those net assets consist of net resources restricted by external parties (such as debt covenants, creditors, grantors, contributions, laws or regulations of other governments, etc.), or net assets for which constraints are imposed by the constitutional provisions or enabling legislation.

Enabling legislation consists of legislation that authorizes the Municipality to assess, levy, charge or otherwise mandate payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation. A legally enforceable enabling legislation restriction is one that a party external to the Municipality (such as citizens, public interest groups, or the judiciary) can compel the Municipality to honor. The Municipality periodically reevaluates the legal enforceability of an enabling legislation to determine if any of the resources raised by the enabling legislation are used for a purpose not specified by the enabling legislation or if the Municipality has other cause for consideration.

The classification of restricted net assets identifies resources that have been received or earned by the Municipality with an explicit understanding between the Municipality and the resource providers that the resources would be used for specific purposes. Grants, contributions and donations are often given under those kinds of conditions. Bond indentures also often limit the use of bond proceeds to specific purposes.

Internally imposed designation of resources, including earmarking, are not reported as restricted net assets. These designations consist of management's plans for the use of resources, which are subject to change at the discretion of the Municipal Legislature.

In the government-wide statements, net assets are segregated into three categories:

- a. *Invested in capital assets, net of related debt*: Consist of capital asset balances net of accumulated depreciation and outstanding balances of any bonds, notes and other borrowings that are attributable to the acquisition, construction, or improvement of those assets. This category should not include cash that is restricted to capital assets acquisition or construction (unspent bond proceeds) and any unamortized debt issue costs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- b. *Restricted net assets*: Represent net assets that are subject to restrictions beyond the Municipal's control. These include restrictions that are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or restrictions imposed by the law through constitutional provisions or enabling legislation (including enabling legislation passed by the government itself).
- c. *Unrestricted net assets*: Represent net assets that do not meet the definition of net assets invested in capital assets, net of related debt or restricted. Unrestricted assets are often designated to indicate that management does not consider them to be available for general operations. These types of constraints are internal and management can remove or modify them. Designations are not reported on the face statement of net assets.

12. Accounting for Pension Costs- On July 1, 2007, the Municipality adopted the provisions of GASBS No. 50, *Pension Disclosure*, which amended GASBS No.27, *Accounting for Pensions by State and Local Government Employers*, by requiring disclosure of how the contractually required contribution rate is determined by governments participating in multi-employer cost-sharing pension plans.

The Municipality accounts for pension costs from the standpoint of a participant in a multi-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

For the purpose of applying the requirements of GASBS No. 27, the state Government of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multi-employer cost-sharing define benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate. The Municipality is considered a participant, and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Government of Puerto Rico and the basic financial statements of such retirement systems are part of the financial reporting entity of the Government of Puerto Rico.

13. Interfund and intra-entity transactions- The Municipality has the following types of transactions among funds:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- a. **Operating Transfers-** Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
- b. **Intra-Entity Transactions-** Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.

14. Risk financing

The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the CRIM for the year ended June 30, 2011 to \$440,209. The current insurance policies have not been cancelled or terminated.

The Municipality carries insurance coverage for death and bodily injuries caused by the automobile accidents. The insurance is obtained through the Automobile Accidents Compensation Administration (AACA), a component unit of the Commonwealth of Puerto Rico. This insurance is compulsory for all licensed vehicles used on public roads and highways in Puerto Rico. The annual premium is \$35 per licensed motor vehicle, which is paid directly to AACA.

The Municipality obtains workers' compensation insurance through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth of Puerto Rico. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center (CRIM) for the year ended June 30, 2011 amounted to \$709,678.

The Municipality obtains unemployment compensation, non-occupational disability, and drivers' insurance coverage for its employees through various insurance programs administered by the Commonwealth of Puerto Rico's Department of Labor and Human Resources (DOL). These insurance programs cover workers against unemployment and provide supplementary insurance coverage for temporary disability, or death because work or employment-related accidents or non-occupational disability and drivers' insurance premiums are paid directly to DOL on a cost reimbursement basis.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Under Act No. 63 of June 21, 2010, the Legislative Assembly of the Commonwealth of Puerto Rico, authorized the municipalities to procure and manage at their own discretion all insurance policies, including those related to health plans been provided to the municipal employees. The Municipality also obtains medical insurance coverage from one health insurance company for its employees. Different health coverage and premium options are negotiated each year by the Municipality. Premiums are paid on a monthly basis directly to the insurance company.

15. Use of Estimates

The preparation of financial statements in conformity with USGAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual amounts could differ from those estimates.

2. CASH AND CASH EQUIVALENTS

The Municipality maintains its deposits in various commercial banks located in Puerto Rico and Government Development Bank for Puerto Rico (GDB). Proceeds from bonds and funds related to certain grant awards are required by law to be held with GDB.

The Municipality adopted the provisions of GASB Statement No. 40 (GASB No. 40), *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. This statement requires that state and local governments disclose essential risk information about deposits and investments. The disclosure requirements cover four main areas: (1) credit risk, (2) interest rate risk, (3) custodial credit risk, (4) foreign exchange exposure.

Credit risk – This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial and credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2011.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

2. CASH AND CASH EQUIVALENTS (CONTINUED)

Interest rate risk - This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investment portfolio at June 30, 2011, (2) limiting the weighted average maturity of its investments to three months or less, and (3) keeping most of its bank deposits in interests bearing accounts generating interests at prevailing market rates. At June 30, 2011, the Municipality's investments in certificates of deposits are recorded at cost, which approximates their fair value. Therefore, the Municipality's management has concluded that at June 30, 2011, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

Custodial credit risk - In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico* the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$250,000 per depositor.

In addition, public funds deposited in commercial banks by the Municipality are fully securities pledged as collateral are held, in the Municipality's name, by the agents of the Commonwealth's Secretary of Treasury. Deposits with GDB are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2011. Therefore, the Municipality's management has concluded that at June 30, 2011 the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

Foreign exchange risk - The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, the Municipality is prevented from investing in foreign securities or any other types of investments in which foreign exchange risk exposure may be significant.

Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2011.

Under Commonwealth of Puerto Rico statutes public funds deposited in commercial banks 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 Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

2. CASH AND CASH EQUIVALENTS (CONTINUED)

Description	<u>Major Governmental Funds</u>				Total
	General Fund	Debt Service Fund	Capital Improvement Bond Fund	Other Governmental Funds	
Cash and cash equivalents commercial banks	\$7,615,996	\$ -	\$1,977,228	\$ 1,680,433	\$11,273,657
Cash with fiscal	-	7,342,034	7,419,056	78,523	14,839,613
Total carrying amount of deposits	<u>\$7,615,996</u>	<u>\$7,342,034</u>	<u>\$9,396,284</u>	<u>\$1,758,956</u>	<u>\$26,113,270</u>

3. RECEIVABLES

a. **Municipal License Tax** - The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2011, the tax rates were as follows:

1. Financial business- 1.50% of gross revenues
2. Other organizations- 0.50% of gross revenues

Any taxpayers that have been granted with a partial tax exemption under any of the tax incentive acts of the Commonwealth ultimately pay municipal license taxes at reduced tax rates, generally between 60 percent and 90 percent under standard rates.

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable of \$37,241 represents filed municipal license tax returns that were uncollected as of June 30, 2011, net of allowance for uncollectible accounts.

Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year is recorded as deferred revenues.

- b. **Property Taxes** - Property taxes receivable recorded in the general and debt service fund amounted to \$2,800,910 and \$669,325 respectively.
- c. **Municipal sales and use taxes** - Municipal sales and use tax receivable of \$95,588 represents filed municipal sales and use tax returns that were uncollected as of June 30, 2011.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

3. RECEIVABLES (CONTINUED)

d. *Intergovernmental Receivables* - Intergovernmental receivables and payables recorded in the accompanying GWFS and GFFS are as follows:

<u>Program Description:</u>	<u>Amount</u>
Law No. 52	
OMEB (Information Network Infrastructure)	\$ 34,751
TAPI - ("Transportación Alternativa Personas con Impedimentos")	12,193
	<u>115</u>
Total	<u>\$ 47,059</u>

e. *Federal Grants Receivable*- Federal grants receivable in other governmental funds represents expenditures incurred not yet reimbursed by the pass-through grantor.

Following is a detail of the federal grants receivable:

<u>Governmental Entity</u>	<u>Amount</u>
Child Care - SENDEC	\$ 112,505
Even Start Program	17,876
American Recovery and Reinvestment Act - Child Care	3,850
Traffic Safety Commission	<u>8,540</u>
Total	<u>\$ 142,771</u>

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2011 are summarized as follows:

a. Due from/to other fund:

<u>Fund</u>	<u>Receivable Fund</u>	<u>Payable Fund</u>
General Fund	\$ 189,830	\$ 171,536
Other Governmental Fund	<u>171,536</u>	<u>189,830</u>
Total	<u>\$ 361,366</u>	<u>\$ 361,366</u>

b. Transfer in/out to other fund

Following is a summary of interfund transfers for the year:

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Capital Projects Fund	Transfers funds to cover capital projects and improvements	\$ 1,740,498
General Fund	Other Governmental Funds	Transfers funds to cover payroll and related expenses.	19,623
Capital Projects Fund	General Fund	Transfers funds to cover operating expenses	4,871,640
Total			<u>\$ 6,631,761</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

5. CAPITAL ASSETS

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2011, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

<u>Governmental Activities:</u>	<u>Balance July 1, 2010</u>	<u>Additions</u>	<u>Retirements/ Reclassifications</u>	<u>Balance June 30, 2011</u>
Capital asset, not being depreciated:				
Construction in progress	\$ 20,791,215	\$ 2,934,604	\$ (135,712)	\$ 23,590,107
Land	<u>12,298,955</u>	<u>-</u>	<u>-</u>	<u>12,298,955</u>
Total capital assets not being depreciated	<u>33,090,170</u>	<u>2,934,604</u>	<u>(135,712)</u>	<u>35,889,062</u>
Capital assets, being depreciated:				
Buildings and building improvements	57,385,920	7,538,081	-	64,924,001
Infrastructure and Infrastructure improvements	71,996,608	1,674,707	-	73,671,315
Machinery, Equipment and furniture	5,358,545	248,871	(25,063)	5,582,353
Computers	231,925	5,762	-	237,687
Vehicles	<u>5,286,363</u>	<u>150,243</u>	<u>(372,306)</u>	<u>5,064,300</u>
Total capital assets being depreciated	<u>140,259,361</u>	<u>9,617,664</u>	<u>(397,369)</u>	<u>149,479,656</u>
Less accumulated depreciation for:				
Buildings and building improvements	(18,483,468)	(1,918,974)	-	(20,402,442)
Infrastructure and Infrastructure improvements	(27,500,500)	(2,563,190)	-	(30,063,690)
Machinery, Equipment and furniture	(4,669,210)	(273,632)	22,427	(4,920,415)
Computers	(189,158)	(17,610)	-	(206,768)
Vehicles	<u>(4,793,468)</u>	<u>(210,062)</u>	<u>372,306</u>	<u>(4,631,224)</u>
Total accumulated depreciation	<u>(55,635,804)</u>	<u>(4,983,468)</u>	<u>394,733</u>	<u>(60,224,539)</u>
Total capital assets being depreciated, net	<u>84,623,557</u>	<u>4,634,196</u>	<u>(2,636)</u>	<u>89,255,117</u>
Governmental activities capital assets, net	<u>\$117,713,727</u>	<u>\$ 7,568,800</u>	<u>\$ (138,348)</u>	<u>\$125,144,179</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

5. CAPITAL ASSETS (CONTINUED)

Depreciation expense was charged to functions/programs of the Municipality as follows:

<u>Governmental activities:</u>	<u>Amount</u>
General government	\$ 2,084,086
Public safety	30,690
Urban and economic development	1,712,444
Health and sanitation	40,454
Public housing and welfare	49,680
Culture, recreation and education	<u>1,066,114</u>
 Total depreciation expense-governmental activities	 <u>\$ 4,983,468</u>

6. PROPERTY TAXES

The personal property tax is self assessed by the taxpayer on a return which is to be filed by May 15 of each year with the Municipal Revenue Collection Center (CRIM), a governmental entity created by the government of Puerto Rico as part of the Municipal Governmental Autonomous Law of August 1991. Real property tax is assessed by the CRIM on each piece of real estate and on each building.

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections, as modified by the quarterly revisions of estimates required law. The CRIM is required by law to prepare a liquidation statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This preliminary liquidation has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final liquidation made not later than six months after year-end, subject to the verification by its Independent Auditors. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. The CRIM issued the preliminary liquidation noting that the advances exceeded collections by \$480,744 on an alleged inadequate procedure for the estimate of revenues applicable to the CRIM liquidation. In the government-wide financial statements, the entire amount has been recognized as long term debt.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

6. PROPERTY TAXES (CONTINUED)

On January 26, 2000, Public Law No. 42 was enacted, which authorized the CRIM to obtain a loan up to \$200,000,000, and for a term not to exceeding 10 years, to allow for the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year ended June 30, 2000.

The amounts that the Municipalities will collect from additional property taxes resulting from increases in the subsidy from the Commonwealth of Puerto Rico to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238, enacted on August 15, 1999. On October 11, 2001, Public Law No. 146 was enacted to amend Public Law No. 42, to extend the loan amortization period up to 30 years. Also, on October 11, 2002, Public Law No. 172 was enacted, to provide as an option for the Municipalities to include the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections for the fiscal year ended June 30, 2001 with the loan authorized through Public Law No. 42 enacted on January 26, 2000.

On June 26 1997, Public Law No. 21 was enacted, which authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owed property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable or equivalent in money. Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law No. 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables.

The Municipality is authorized by Act No. 81 to impose and collect property taxes from any natural or legal person that, at January 1 of each calendar year: (1) is engaged in trade or business and is the owner of personal or real property used in trade or business or (2) owns residential real property with a value in excess of \$15,000 (at 1957 market prices).

Personal property taxes are self-assessed by taxpayers every year using the book value of personal property assets owned by the taxpayer at January 1 (lien; levy date) and reporting such taxable value through a personal property tax return filed on May 15 (due date and collection date) subsequent to the assessment date. The total personal property tax rate in

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

6. PROPERTY TAXES (CONTINUED)

force at June 30, 2011 was 6.83 percent (of which taxpayers pay 6.63 percent and the remaining 0.20 percent is paid by the Department of Treasury, as a subsidy).

Real property taxes are assessed every January 1 (lien; levy date) and are based on estimated current values of the property, deflated to 1957 market prices. Real property taxes are due and collectible on January 1 and July of every fiscal year. The total real property tax rate in force at June 30, 2011 was 8.83 percent (of which 8.63 percent is paid by taxpayers and the remaining 0.20 percent is also paid by the Department of Treasury, as a subsidy).

Residential real property occupied by its owner (not engaged in trade or business) is exempt from property taxes only on the first \$15,000 of the assessed value (at 1957 market prices).

For exempt amounts, the Department of Treasury assumes the payment of the basic tax (4.00 percent and 6.00 percent for personal and real property, respectively), except for property assessed for less than \$3,500 (at 1957 market prices), for which no payment is made by the Department of Treasury.

Included within the total personal and real property tax rates of 6.83 percent and 8.83 percent, respectively, there is a portion of the tax rate in the amount of 1.40 percent that is restricted for the Municipality's debt service requirements on bonds. Such amounts are recorded in the Municipality's debt service fund.

Property tax revenues in the general and debt service funds amounted to \$13,841,108 and \$4,731,917, respectively, for the fiscal year ended June 30, 2011.

7. MUNICIPAL SALES AND USE TAX

The Municipality imposes a sales and use tax pursuant to the provisions of the Puerto Rico Internal Revenue Code, as amended. The tax consists of one percent (1.0%) on the sales price of taxable items or on the purchase prices of all usage, storage, or consumption of taxable items, excluding wholesales. The sales and use tax is a self-assessed tax collected by the Municipality through monthly tax returns due on the twentieth day of the immediate following month. The tax returns are filed by the respective businesses that are required by law to withhold the tax from consumers on each taxable product or service.

Sales and use tax revenues in the general fund amounted to \$3,001,248 for the fiscal year ended June 30, 2011.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

7. MUNICIPAL SALES AND USE TAX (CONTINUED)

The Commonwealth of Puerto Rico imposes a separate state sales and use tax of 0.5%, which is imposed and collected by the Puerto Rico Treasury Department (PRTD) through monthly tax returns due on the twentieth day of the immediate following month. This 0.5% tax is administered by the Government Development Bank for Puerto Rico for the following purposes: (1) 0.2% is deposited in the new "Municipal Debt Service Fund", strictly for granting loans to the municipalities of Puerto Rico, (2) 0.2% for the creation of the "Municipal Development Fund" % which will be distributed among all municipalities pursuant to a statutory formula, and (3) 0.1 % for the creation of the "Permanent Improvements Fund", to be distributed by the Legislature of the Commonwealth of Puerto Rico to carry out public works and permanent improvement projects in the municipalities of Puerto Rico.

Accordingly, during the fiscal year ended June 30, 2011, the Municipality recorded intergovernmental grants and contributions revenues in the debt service fund amounting to \$643,072, which represents the contributions collected from PRTD arising from the 0.2% portion of the state sales tax to be used to cover future debt service payments of the Municipality's bonds.

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2011 are summarized as follows:

Description	General Fund	Debt Service Fund	Capital Projects Fund	Other Governmental Fund	Total
Accounts payable	\$ 4,499,798	\$ -	\$ 1,078,905	\$ 365,841	\$ 5,944,544
Accrued liabilities	<u>1,376,088</u>	-	-	-	<u>1,376,088</u>
Total	<u>\$ 5,875,886</u>	<u>\$ -</u>	<u>\$ 1,078,905</u>	<u>\$ 365,841</u>	<u>\$ 7,320,632</u>

9. DUE TO OTHER GOVERNMENTAL ENTITIES

The amounts due to other governmental entities in the general fund include the following:

Governmental Entity	Amount
General Services Administration	\$ 625
Retirement System Administration	312,420
Puerto Rico Telephone Company	9,565
Puerto Rico Aqueduct and Sewer Authority	860,894
Department of Labor-Unemployment Program	57,673
State Insurance Fund Corporation	124,509
Puerto Rico Treasury Department	2,058,828
Commonwealth of Puerto Rico Employee Association	<u>79,209</u>
Total	<u>\$ 3,503,723</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

10. DEFERRED REVENUES

- A. Municipal License Tax- The deferred revenues of \$9,140,168 in the general fund relates to municipal license tax collected in fiscal year 2010-11 that will be earned in fiscal year 2011-12.
- B. Federal Grants- The deferred revenues presented in other governmental funds represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Federal Program	\$ 3,299
Federal Transit Administration	287
Food Program	192,372
Community Development Block Grant	65,290
Even Start	14,984
Community Service Block Grant	3,777
Emergency Shelter	9,782
Child Care (SENDEC)	47,557
Total	<u>\$ 337,348</u>

11. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2011, was as follows:

Description	Beginning Balance, as restated	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds Payable	\$ 49,035,000	\$ -	\$ (3,055,000)	\$ 45,980,000	\$3,405,000
Notes Payable	5,218,000	-	(315,000)	4,903,000	92,000
Capital leases	3,400	-	(3,400)	-	-
LIMS Repayment Plan	153,756	-	(100,994)	52,762	52,762
Property tax debt	2,044,895	480,744	(1,264,457)	1,261,182	780,438
Advances from CRIM - Law No. 42	6,305,466	-	(134,774)	6,170,692	143,242
Compensated Absences	6,483,555	548,225	(709,481)	6,322,299	710,000
Total	<u>\$69,244,072</u>	<u>\$1,028,969</u>	<u>\$(5,583,106)</u>	<u>\$64,689,935</u>	<u>\$5,183,442</u>

1. Legal Debt Margin- The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment of property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds payable, is paid with unrestricted funds.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

11. LONG-TERM LIABILITIES (CONTINUED)

2. Bonds and notes payable- The Municipality issues general and special obligation bonds and notes to provide funds for the acquisition and construction of major capital facilities. Bonds and notes payable outstanding at June 30, 2011 are as follows:

Description	Balance at June 30, 2011
1995 Public improvements bond for the construction of a capital asset with an original amount of \$14,520,000 due in installments of \$315,000 to \$1,370,000 through July 1, 2014, with interest ranging from 6.11% to 7.71%	\$ 4,900,000
1998 General obligation bond for infrastructure construction with an original amount of \$18,825,000 due in installments of \$260,000 to \$1,635,000 through July 1, 2022, with interest ranging from 4.86% to 8.00%	13,285,000
2000 General obligation bond for construction or acquisition of capital assets with an original amount of \$11,850,000 due in installments of \$315,000 to \$1,170,000 through July 1, 2018, with interest ranging from 2.70% to 6.13%	7,270,000
2001 General obligation bond for construction or acquisition of capital assets with an original amount of \$7,240,000 due in installments of \$195,000 to \$715,000 through July 1, 2019, with interest ranging from 2.70% to 5.19%	4,820,000
2004 General obligation bond for construction or acquisition of capital assets with an original amount of \$10,450,000 due in installments of \$315,000 to \$800,000 through July 1, 2024, with interest ranging from 4.17% to 5.28%	8,300,000
2008 Special obligation note for construction or acquisition of capital assets with an original amount of \$5,067,000 due in installments of \$79,000 to \$407,000 through July 1, 2033, with interest ranging from 1.53% to 7.00%	4,903,000
2009 General obligation bond for operational expenses with an original amount of \$7,405,000 due in installments of \$125,000 to \$610,000 through July 1, 2034, with interest ranging from 5.00% to 7.00%	<u>7,405,000</u>
Total	<u>\$ 50,883,000</u>

These bonds are payable from the special ad valorem property tax of 1.75% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

The special obligation note of \$5,067,000 for the construction of various projects, due annual principal installments ranging from \$79,000 to \$407,000, plus interest due in semiannual installments at variable rates (1.5% to 7.0%) through July 1, 2033. This note is payable with the revenues generated from the collection of the .03% of the municipal sales and use tax imposed by the Municipality and collected by the Puerto Rico Treasury Department.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

11. LONG-TERM LIABILITIES (CONTINUED)

Annual debt service requirements to maturity for bonds and notes payable are as follows:

Year Ending June 30,	Principal	Interest
2012	\$ 3,497,000	\$ 2,592,800
2013	3,763,000	2,747,179
2014	4,045,000	2,513,023
2015	4,352,000	2,259,529
2016	3,210,000	2,040,856
2017-2021	16,614,000	7,297,511
2022-2026	8,595,000	3,365,763
2027-2031	3,470,000	1,807,750
2032-2035	3,337,000	444,505
Total	<u>\$ 50,883,000</u>	<u>\$ 25,068,916</u>

3. **Capital leases-** The Municipality is obligated under capital leases with third parties that expire through 2011 for the acquisition of machinery and equipment. At June 30, 2011, the amount of \$3,400 related to the leased machinery and equipment, is accounted for as long-term liabilities.
4. **LIMS Repayment Plan-** During the fiscal year 2000-2001 the Municipality authorized the CRIM to retain the corresponding portion for the financing project of Land Information Management System- LIMS, contracted by the CRIM. A total of \$810,183 is to be retained in ten years period at an interest rate of 5.95% until November 28, 2011. At June 30, 2011, the outstanding balance is \$52,762.
5. **Property Taxes Debts-** These amounts represents the balance owned to the Treasury Department and to the Municipal Revenue Collection Center ("CRIM") at June 30, 2011 as described in Note 6.
6. **Advances from CRIM-** This amount represents the balance owed to the CRIM at June 30, 2011 will be repaid through a financing obtained by the CRIM with GDB.
7. **Compensated Absences-** The government-wide statement of net assets includes approximately \$4,114,931 of accrued sick leave benefits, and approximately \$2,207,368 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

12. PENSION PLAN

The Employee's Retirement System of the Commonwealth and its Instrumentalities (the Retirement System) is a cost-sharing multiple defined benefit pension plans sponsored by,

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

12. PENSION PLAN (CONTINUED)

and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Municipality under 55 years of age at the date of employment become members of the Retirement System as a condition to their employment.

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

Members who have attained 55 years of age and have completed at least 25 years of creditable service, members who have attained 58 years of age and have completed ten years of creditable service or policemen and firemen members who have attained 50 years of age and have completed at least 25 years of creditable service, are entitled to an annual benefit payable monthly for life.

Members are eligible for monthly benefit payments determined by the application of the stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a member is eligible, is limited to a minimum of \$300 per month and a maximum of 75 percent of the average compensation.

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 Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions during the year ended June 30, 2011 amounted to approximately \$1,303,197 this amount represented 100% of the required contribution.

On September 24, 1999, an amendment to Act. No. 447 of May 15, 1951, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employee's participation in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Municipality on or after January 1, 2000, 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 ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

12. PENSION PLAN (CONTINUED)

The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. 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. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

If at the time of retirement accumulated benefits amount to \$10,000 or less may elect to receive a lump sum distribution up to the accumulated benefits. Under the new program the retirement age is reduced from 65 to 60 for those employees who joined the current plan on or after April 1, 1990.

Funding Policy

The authority under which the funding policy and the obligations to contribute to the ERS and System 2000 by the plans' members, employers and other contributing entities (state and municipal contributions), are established or may be amended by law.

Contribution requirements are established by law and are as follows:

Municipality	9.275% of gross salary
Employees:	
Hired on or before March 31, 1990	5.775% of gross salary up to \$6,600
	8.275% of gross salary over \$6,600
Hired on or before April 1, 1990	8.275% of gross salary

Annual Contribution

The Municipality contributions during those years are recognized as total pension expenditures/expenses in the category of administration as follows:

<u>Fiscal year</u>	<u>Law No. 447</u>	<u>System 2000</u>
2011	\$ 653,958	\$ 649,239
2010	\$ 562,933	\$ 552,160

These amounts represented the 100% of the required contribution for the corresponding year. Additionally, changes made in the types and amounts of benefits offered by special

COMMONWEALTH OF PUERTO RICO
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YEAR ENDED JUNE 30, 2011

12. PENSION PLAN (CONTINUED)

laws and cost of living adjustments, led to a one-time recommended contribution to fund the retroactive adjustment related to the changes.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2011, a copy of which can be obtained from the Retirement System, Minillas Station, PO Box 42004, San Juan, PR 00940.

13. RISK MANAGEMENT

The Property Division of the Municipality is responsible of assuring that the Municipality's property is properly insured. Annually, the Property Division compiles the information of all property owned and its respective market value. After evaluating this information, the Property Division submits the data regarding the Municipality's properties to the Area of Public Insurance at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities. Settled claims have not exceeded commercial coverage in any of the past three fiscal years.

14. FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

The GASB has issued the following statements that have effective dates after June 30, 2011:

- a. GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements* (GASB 60). The requirements of this statement are effective for the fiscal year commencing on July 1, 2011.
- b. GASB Statement No. 61, *The Financial Reporting Entity* (GASB 61). The requirements of this statement are effective for the fiscal year commencing after June 15, 2012.
- c. GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA pronouncements* (GASB 62). The requirements of this statement are effective for the fiscal year commencing on July 1, 2012.
- d. GASB Statement No. 63, *Financial Reporting Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. The requirements of this statement are effective for the fiscal year commencing on December 15, 2011.
- e. GASB Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provision (amendment to GASB Statement No. 53)*. The requirements of this statement are effective for the fiscal year commencing on June 15, 2011.

The impact of these statements on the Municipality's basic financial statements has not yet been determined.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

14. Fund Balance (Deficit)

As of June 30 2011, fund balance (deficit) is comprised of the following:

Fund Balance (Deficit)	General Fund	Debt Service Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
Nonspendable:					
Inventories	\$ 125,000	-	-	-	\$ 125,000
Restricted for					
General Government				240,905	240,905
Culture, Recreation and Education			226,760	92,777	319,537
Health and Sanitation			71,780	2,093	73,873
Urban and Economic Development			8,018,839	617,666	8,636,505
Public Housing and Welfare				24,945	24,945
Public Safety				170,876	170,876
Debt Service		1,921,559			1,921,559
Committed:					
General Government				18,972	18,972
Culture, Recreation and Education				10,862	10,862
Health and Sanitation				5,316	5,316
Urban and Economic Development				801	801
Public Housing and Welfare				42,090	42,090
Public Safety					
Unassigned	(7,880,535)				(7,880,535)
Total Fund Balance (Deficit)	\$ (7,755,535)	\$ 1,921,559	\$ 8,317,379	\$ 1,227,303	\$ (3,710,706)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011**

15. COMMITMENTS AND CONTINGENCIES

A. Federal Grants:

The Municipality participates in a number of federal financial assistance programs funded by the Federal Government. Although the Municipality's grant programs have been audited in accordance with the provisions of the Single Audit Act of 1996, through June 30, 2011, these programs are still subject to financial and compliance audits by the granting agencies and the resolution of previously identified questioned costs. The amount, if any, of expenditures which may be disallowed by such audits cannot be determined at this time, although the Municipality management expects such amounts, if any, not to be material.

B. Claims and lawsuits:

The Municipality is a defendant in several legal proceedings that arise in the ordinary course of the Municipality's activities. Certain of these claims are covered by insurance. The administration believes that the ultimate liability, if any, would not be significant. As a result, the accompanying basic financial statements do not include adjustments, if any, that could result from the resolution of these legal proceedings.

16. SUBSEQUENT EVENTS

Act No. 94 issued on June 16, 2011 by the Legislature established an incentive plan for the payment of real and personal property tax dues, beginning on July 14, 2011. This Act provides an amnesty to all property tax payers forgiving all penalties, charges and interests of the unpaid principal of pass-due property tax liability. The period that tax payers have to enjoy for such benefit is for exactly ninety (90) days beginning on July 14 through October 11, 2011. The unpaid property taxes covered under this Act are those related to fiscal year 2009-2010 and earlier (for real property taxes) and for 2008 and earlier for personal property tax.

17. PRIOR PERIOD ADJUSTMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

The following restatements have been made in the governmental fund financial statements, which are reported as an adjustment to the beginning fund balances:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
YEAR ENDED JUNE 30, 2011

17. PRIOR PERIOD ADJUSTMENTS (CONTINUED)

Description	General Fund	Debt Service Fund	Capital Projects Fund	Other Governmental Funds	Total
Fund balance beginning	\$(5,937,683)	\$ 2,428,855	\$ 12,628,995	\$ 1,331,235	\$ 10,451,402
Prior years debts with the Treasury Department related to income taxes	(397,781)	-	-	-	(397,781)
Prior years debts with the Treasury Department related to excise tax debt corresponding to the years 1998-2009	(1,513,915)	-	-	-	(1,513,915)
Fund balance, beginning as restated	<u>\$ (7,849,379)</u>	<u>\$ 2,428,855</u>	<u>\$ 12,628,995</u>	<u>\$ 1,331,235</u>	<u>\$ 8,539,706</u>

B. GOVERNMENTAL-WIDE FINANCIAL STATEMENTS

The following restatements have been made in the governmental-wide financial statements, which are reported as an adjustment to beginning net assets:

<u>Description</u>	<u>Total</u>
Net assets, beginning	\$ 62,450,239
To restate <i>General Long-term liabilities (Notes Payable)</i>	65,000
To properly presents the <i>Due to other governmental entities (Treasury Department excise tax and income taxes debts corresponding to the years 1998-2009)</i>	(1,911,696)
Net assets, beginning as restated	<u>\$ 60,603,543</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
YEAR ENDED JUNE 30, 2011**

	<u>Budgeted Amount</u>		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 13,801,486	\$ 13,801,486	\$ 13,841,108	\$ 39,622
Municipal license tax	22,002,203	22,002,203	14,682,292	(7,319,911)
Construction excise tax	1,300,000	1,300,000	1,339,452	39,452
Sales and use tax	7,503,500	7,503,500	3,001,248	(4,502,252)
Charges for services	541,386	541,386	328,520	(212,866)
Intergovernmental grants and contributions	5,953,141	5,953,141	3,243,206	(2,709,935)
Interest on deposits and investments	165,000	165,000	468,383	303,383
Miscellaneous	<u>2,371,504</u>	<u>2,371,504</u>	<u>1,952,634</u>	<u>(418,870)</u>
Total revenues	<u>53,638,220</u>	<u>53,638,220</u>	<u>38,856,843</u>	<u>(14,781,377)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
General government	29,211,350	28,607,776	21,037,525	7,570,251
Urban and economic development	8,790,054	7,772,152	6,776,738	995,414
Public safety	3,633,704	3,475,465	2,944,636	530,829
Health and sanitation	5,883,380	5,844,380	5,334,861	509,171
Culture, recreation and education	3,936,062	4,025,783	3,575,457	450,326
Public housing and economic development	2,183,670	2,172,514	1,933,661	238,853
Operating transfer to other funds	-	<u>1,740,498</u>	<u>1,740,498</u>	-
Total expenditures, encumbrances and other financing uses	<u>\$ 53,638,220</u>	<u>\$ 53,638,220</u>	<u>\$ 43,343,376</u>	<u>\$ 10,294,844</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)			<u>\$ (4,486,533)</u>	<u>\$ (4,486,533)</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 38,856,843
Non-budgeted transfer in				<u>4,871,640</u>
Total revenues and other financing sources as reported on the statement of revenues, expenditures and changes in fund balance				<u>43,728,483</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 43,343,376
Differences-budget to GAAP:				
Non-budgeted transfer out				19,623
Non-budgeted expenditures				<u>271,640</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 43,634,639</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
YEAR ENDED JUNE 30, 2011

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Control

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with USGAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

The Municipality prepares its annual budget including the operations of the general fund. For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For USGAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year.

The unencumbered balance of any appropriation at the end of the fiscal year will lapse at the end of such fiscal year. Other appropriations, mainly capital project appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2010 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2011.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF EXPENDITURES AND FEDERAL AWARDS
YEAR ENDED JUNE 30, 2011**

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Pass-through the Office of the Commissioner for Municipal Affairs: Community Development Block Grant - State's Program	14.228		\$ 1,246,185
Pass-through the Office of the Commissioner for Municipal Affairs: Community Development Block Grant State's Program - Recovery Act Funded	14.255	Not Available	244,257
Pass-through the Puerto Rico Family Department: Homelessness Prevention and Rapid Re- Housing Program (Recovery Act Funded)	14.257	Not Available	<u>122,652</u>
Total U.S. Department of Housing and Urban Development			<u>1,613,094</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Puerto Rico Family Department: Child Care and Development Block Grant	93.575	Not Available	267,641
Pass-through the Office of Administration for Children and Families (Family Department): ARRA - Child Care Program and Development Block Grant	93.713	Not Available	<u>58,872</u>
Total U.S. Department of Health and Human Services			<u>326,513</u>
U.S. DEPARTMENT OF EDUCATION:			
Pass-through Puerto Rico Department of Education: Even Start - State Educational Agencies	84.213		<u>338,745</u>
Total U.S. Department of Education			<u>338,745</u>
U.S. DEPARTMENT OF AGRICULTURE:			
Pass-through Puerto Rico Department of Education: Child and Adult Care Food Program	10.558		<u>13,219</u>
Total U.S. Department of Agriculture			<u>13,219</u>

**MUNICIPALITY OF CATAÑO
SCHEDULE OF EXPENDITURES AND FEDERAL AWARDS
YEAR ENDED JUNE 30, 2011**

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF TRANSPORTATION:			
Direct Program:			
Federal Transit – Formula Grants Pass-through the Commonwealth of Puerto Rico – Traffic Safety Commission:	20.507		1,086,533
State and Community Highway Safety	20.600		<u>11,472</u>
Total U.S. Department of Transportation			<u>1,098,005</u>
U.S. DEPARTMENT OF ENERGY:			
Pass-through the Puerto Rico Energy Affairs Administration:			
Energy Efficiency and Conservation Block Grant Program (Recovery Act Funded)	81.128		146,000
Total U.S. Department of Energy			<u>146,000</u>
U.S. ENVIRONMENTAL PROTECTION AGENCY:			
Direct Program:			
Brownfield Training, Research, and Technical Assistance Grants and Cooperative Agreement	66.814		20,000
Total U.S. Environmental Protection Agency			<u>20,000</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 3,555,576</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
NOTES TO THE SCHEDULE OF EXPENDITURES AND FEDERAL AWARDS
YEAR ENDED JUNE 30, 2011

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Cataño and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the fund financial statements. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Other Governmental Funds in the Municipality's fund financial statements. The reconciliation between the expenditures in the funds financial statements and the disbursements in the Schedule of Expenditures of Federal Awards is as follows:

Description	Other Governmental Funds
Per Schedule of Expenditures of Federal Awards	\$ 3,555,576
Non federal programs expenditures	<u>651,478</u>
Total expenditures in the basic financial statements	<u>\$ 4,207,054</u>

Ramón L. Marrero Rosado

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

**To the Honorable Mayor and
the Municipal's Assembly Members
Municipality of Cataño
Cataño, Puerto Rico**

I have audited the financial statements of the governmental activities, each mayor fund and the aggregate remaining fund information of the Municipality of Cataño as of and for the year ended June 30, 2011 which collectively comprise the Municipality of Cataño basic financial statements and have issued my report thereon dated March 27, 2012. I conducted my 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 my audit, I considered the Municipality of Cataño internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Municipality's internal control over financial reporting. Accordingly, I do not express an opinion on the effectiveness of the Municipality's internal control over financial reporting.

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their

assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Municipality's ability to initiate, authorize, record, process, or report financial data reliable in accordance with generally accepted accounting principles, such that there is more than a remote likelihood that a misstatement of the municipality's financial statements that is more than inconsequential will not be prevented or detected by the Municipality's internal control. I consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting as items 11-01 and 11-02.

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

My consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, I consider items 11-01 and 11-02 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality of Cataño financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items 11-04 thru 11-07.

The Municipality of Cataño response to the findings identified in my audit is described in the accompanying schedule of findings and questioned costs. I did not audit Municipality's response and accordingly, I express no opinion on it.

This report is intended for the information of the audit committee, the Municipality's management, the Department of Housing and Urban Development (Cognizant Agency), and federal awarding agencies and pass-through entities. However, since this report is issue in connection with a local government it is a matter of public record and its distribution is not limited.


Ramon L. Marrero, CPA
Lic. #3305

March 27, 2012
Bayamón, Puerto Rico



NOTE: Stamp No. 2639574 of the Puerto Rico State Society of Certified Public Accountants was affixed to the original of this report.

Ramón L. Marrero Rosado

Certified Public Accountants & Consultants

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

**To the Honorable Mayor and
the Municipal's Assembly Members
Municipality of Cataño
Cataño, Puerto Rico**

✦ Compliance

I have audited the compliance of the Municipality of Cataño with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2011. The Municipality of Cataño major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Municipality of Cataño management. My responsibility is to express an opinion on the Municipality of Cataño compliance based on my audit.

I conducted my audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Governmental Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that I 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 Municipality of Cataño compliance with those requirements and performing such other procedures as I considered necessary in the circumstances. I believe that my audit provides a reasonable basis for my opinion. My audit does not provide a legal

determination of the Municipality of Cataño compliance with those requirements.

As described in items 11-04 thru 11-07 in the accompanying schedule of audit findings and questioned costs, the Municipality of Cataño did not comply with requirements regarding cash management, that are applicable to its awards: Community Development Block Grants, Child Care, Even Start, Food Program, and Federal Transit. Compliance with such requirements is necessary, in my opinion, for the Municipality of Cataño to comply with the requirements applicable to those programs.

In my opinion, except for the noncompliance described in the preceding paragraph, the Municipality of Cataño complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2011.

✦ Internal Control Over Compliance

The management of the Municipality of Cataño, 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 my audit, I considered the Municipality's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine my auditing procedures for the purpose of expressing my opinion on compliance, but not for the purpose of expressing an opinion the effectiveness of the Municipality's internal control over compliance. Accordingly I do not express an opinion on the effectiveness of the Municipality of Cataño internal control over compliance.

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

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by

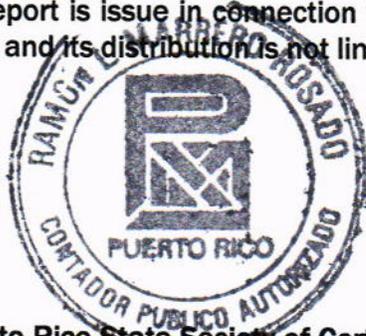
the entity's internal control. I consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, as items 11-01 and 11-02 significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, I consider items 11-01 and 11-02 to be material weaknesses.

The Municipality of Cataño, response to the findings identified in my audit is described in the accompanying schedule of findings and questioned costs. I did not audit Municipality's response and, accordingly, I express no opinion on it.

This report is intended for the information of the audit committee, the Municipality's management, the Department of Housing and Urban Development (Cognizant Agency), and federal awarding agencies and pass-through entities. However, since this report is issued in connection with a local government is a matter of public record and its distribution is not limited.


Ramon L. Marrero, CPA
Lic. #3305



March 27, 2012
Bayamón, Puerto Rico

NOTE: Stamp No. 2639575 of the Puerto Rico State Society of Certified Public Accountants was affixed to the original of this report.

Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Qualified

Internal control over financial reporting:

- Material weakness (es) identified? x yes no
- Reportable condition(s) identified that are not considered to be material weaknesses x yes none reported
- Noncompliance material to financial statements noted? x yes no

Federal Awards

Internal control over major programs:

- Material weakness (es) identified? x yes no
- Reportable condition (s) identified that are not considered to be material weakness (es)? x yes none reported

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

Any audit findings disclosed that are required to be reported in accordance with section 510 9a) of Circular A-133? x yes no

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

Section I - Summary of Auditor's Results - Continued

Identification of major programs:

CFDA #	Name of Federal Programs or Cluster
14.228	CDBG
20.507	Federal Transit Formula Grants

Dollar threshold used to distinguish
between type A and type B programs: \$ 300,000

Auditee qualified as low-risk auditee? yes x_no

**Section II Financial Statements Findings
Reportable Conditions
"Material Weaknesses"**

11-01 Accounting System and Other Accounting Records

Statement of condition

The Uniform Accounting System (UAS) and the accounting records currently used by the Municipality do not have the necessary capabilities, procedures, internal controls and records to ensure accurate financial reporting and to prepare the Municipality's basic financial statements and federal program's reports in conformity with Accounting Principles Generally Accepted in the United States of America for State and Local Governments (GAAP). The UAS is a system promulgated by the Office of the Commissioner of Municipal Affairs of Puerto Rico (OCAM, by its Spanish acronyms), a governmental entity created by law to provide technical assistance to the municipalities of Puerto Rico in several administrative and fiscal matters.

The Municipality's UAS mostly provides for the recording of revenue collections, disbursements and other limited transactions. In addition, the accounting records are not fully integrated, and a double entry system is not generally followed. Accounting records are maintained on the cash basis and budgetary accounting bases (two accounting bases that differ significantly from GAAP) and do not comply with Statement No. 34 of the Governmental Accounting Standards Board (GASB 34), as amended.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

11-01 Accounting System and Other Accounting Records (Continued)

The following specific additional conditions were noted in relation to the UAS of the Municipality:

- Accounting transactions are currently accounted for simultaneously through manual and computerized accounting systems for which no reconciliation procedures are made among them, including the accounting records currently used by federal programs which are not reconciled with the UAS. The balance sheet accounts in the UAS are not reconciled and adjusted to conform them to the Municipality's audited basic financial statements.
- The UAS does not have the capabilities of: (1) distinguish between expenditures (expenses) incurred and encumbered, (2) recording and processing all types of capital asset transactions, principally the accounting of depreciation and amortization expense, (3) recording and processing all transactions related to revenues susceptible to accrual (accounts receivable) and, (4) recording and processing transactions related to long-term debt, including bonds and notes payable, obligations under capital leases, reserves for federal cost disallowances, legal claims and judgments and compensated absences, etc.
- No adequate year-end closing procedures are made to account for all transactions affecting all funds.
- No adequate segregation is made between items representing actual accounts payable and those representing outstanding encumbrances. Accordingly, material amounts of unrecorded liabilities are generally recorded at fiscal year-end.
- The management of the federal programs administered by the Municipality maintains separate accounting records for each federal program, which are not reconciled with the UAS (the official accounting system of the Municipality).
- No adequate and complete accounting records are kept for inter-fund balances and transactions.
- The audit adjustments resulting from Single Audits are not completely posted in the UAS.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

11-01 Accounting System and Other Accounting Records (Continued)

The basic financial statements of the Municipality must be prepared using the financial information obtained from various municipal departments and accounting records outside of the official UAS, and from information obtained from regulators and independent third parties. In addition, the Department of Finance does not maintain accounting records and working papers supporting the balances and disclosures reported in the basic financial statements of the Municipality; principally those related to Government-wide Financial Reporting.

The Finance Department does not maintain accounting records supporting most of the procedures performed during the preparation of the Municipality's basic financial statements as follows:

- ✦ The conversion of accounting records from the cash basis of accounting to the modified accrual basis of accounting used by governmental funds;
- ✦ The conversion of governmental funds from the modified accrual basis to the accrual basis of accounting used by government-wide financial statements; and
- ✦ Working papers and analyses of significant balances reported in the basic financial statements, such as capital assets, accounts receivable (municipal licenses, grants and contributions, etc.), deferred revenues, accounts payable, and long-term obligations (for which the general practice is to rely upon the notifications received from the Government Development Bank for Puerto Rico, the Puerto Rico Treasury Department, the Federal Government and the Municipal Revenue Collection Center for the balance of its outstanding debt and the withholding for its debt service).

Criteria:

Article 8.010(b) of Law No.81 of August 30, 1991, know as the Autonomous Municipalities Act of Puerto Rico (Law No. 81), states that the Municipality must maintain its fund accounting in accordance with Accounting Principles Generally Accepted in the United States of America (GAAP), as promulgated by the Governmental Accounting Standards Board (GASB), the National Committee on Governmental Accounting (NCGA) and the Governmental Accounting, Auditing and Financial Reporting book (commonly know as Blue Book).

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

11-01 Accounting System and Other Accounting Records (Continued)

In addition, Article 8.010 (c) of Law No. 81 states that uniform accounting system used by the Municipality must (1) produce reliable reports and financial statements, (2) provide complete information about the results of operations of the Municipality, and (3) include the necessary internal controls to account all funds, capital assets and other assets of the Municipality.

Furthermore, Section 5 of the Revised Regulation on basic Standards for the Municipalities of Puerto Rico, which were created pursuant to Article 19.011 of law No. 81 and approved by the Office of the Commissioner of Municipal Affairs, state that the accounting system of the Municipality should include:

- ✦ Final entry books that allow for the preparation of month-end summaries of transactions for posting in the original entry records and for the gathering of information needed for the preparation of basic financial statements and other reports;
- ✦ Fiscal procedures for the system's operations, establishing proper internal controls and the prevention of irregularities. These procedures should provide for the timely and accurate performance of operations. It should include the necessary records, files, reconciliations, adjustments, closing entries, reports, and all other necessary documentation to support the basic financial statements.

Due to the conditions referred to above, the preparation of the Municipality's basic financial statements as of and for the fiscal year ended June 30, 2011 was more difficult and less efficient than would have been in ordinary circumstances. A significant amount of adjusting entries had to be made to the financial data and reports processed through the UAS in order to properly account for unrecorded transactions and to correct transactions recorded in the wrong accounting period. Since the accounts and other accounting records of the UAS are not designed to provide all the information necessary to prepare the Municipality's basic financial statements, the Municipality had to obtain and process financial data from several sources outside the UAS. These conditions represent material weaknesses in the Municipality's internal controls over financial reporting.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

11-01 Accounting System and Other Accounting Records (Continued)

Failure to have a complete and adequate accounting system does not allow the Municipality to have timely and accurate financial information for its decision making process. In addition, financial reports prepared may have errors or omissions that will affect future financial decisions. Another effect is the use of inaccurate financial information as a base for the preparation of annual budgets, which, therefore, may result in budgetary compliance problems.

Recommendation:

The Municipality must finally implement a complete uniform accounting system designed to provide main and essentials procedures in compliance with all applicable federal and local laws and regulations and with prescribed requirements regarding internal controls.

Auditee Response:

This condition is similar as in prior years audits. Management accepted the condition and is actually working on the following:

As of May 2011, the Municipality completed the implementation of a Financial Management System, which provides necessary and adequate internal controls, designed to account all daily revenues and disbursements transactions of all municipal funds. This application provides monthly accurate reports about the results of the operations of the Municipality. Essentially, it is a valuable tool to be used in monitoring monthly revenues and disbursements, in reconciliation process and for budgetary purposes.

11-02 Inactive and Unnecessary Funds

Statement of Condition:

During prior years, the Municipality has maintained excessive number of funds pertaining to the special revenue and capital projects funds, many of which were inactive or had insignificant movement or operations. Municipality's management has been working over the intended objective of all these funds, in order to record any required adjustment over the inactive ones.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

11-02 Inactive and Unnecessary Funds (Continued)

Criteria:

Article 8.007(b) of the Law No. 81 of August 30, 1991; known as the Autonomous Municipalities Act of Puerto Rico (Law No. 81), states that funds without specific fiscal years should be closed when the fund's objectives have been completed.

NCGA Statement No. 1, paragraph 4, states that "governmental units should establish and maintain those funds required by law and sound financial administration. Only the minimum number of funds consistent with legal and operating requirements should be established since unnecessary funds result in inflexibility, undue complexity, and inefficient financial administration".

In addition, the recommended practice on "Improving the effectiveness of Fund Accounting" (2004), issued by the Government Finance Officers Association of the United States and Canada (GFOA), states that it is important in this regard to distinguish accounting from financial reporting. Whereas an accounting system must collect all of the data needed to ensure and demonstrate legal compliance, financial reporting is concerned with only those aspects of compliance that are of importance to users of general purpose external financial reports.

This situation occurred because the Municipality did not analyze and close on time inactive funds and bank accounts when the fund's objectives have been met or are no longer relevant. The continued maintenance of these funds and accounts exposed the Municipality to the unauthorized use of funds from inactive accounts for activities not intended to be financed with these funds. The aforementioned conditions represent material weaknesses in the Municipality's internal controls over financial reporting.

Recommendation:

The finance director must develop policies and procedures to continuously analyze these funds in order to prevent occurrences of the above condition again. Inactive and unnecessary funds should be closed after determining that its intended objectives were met. Remaining balances should be disposed of in accordance with local and federal laws and regulations.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

11-02 Inactive and Unnecessary Funds (Continued)

Auditee Response:

This condition is similar as in prior year's audits. The finance directors is aware of its significant effects over the Municipality's financial position and has been working on a process to analyze all inactive accounts with balances to determine whether they are needed or should be closed.

11-03 General Fund Deficit

Statement of Condition:

As more fully explained in Note 17 to the Basic Financial Statements, prior period adjustments and reclassifications to the General Fund increased the deficit presented as of June 30, 2010, as follows:

Fund Balance (Deficit) – as originally presented	(\$5,937,683)
Prior periods (1998-2009) debts recognition	(1,911,696)
	<hr/>
Fund Balance (Deficit) as restated	<u>(\$7,849,379)</u>

Criteria:

Sound management requires proper managing and classifications of General and Special Funds for the effectiveness of Fund Accounting, and for the estimation of balances for budgetary purposes. These balances should be based on facts, tendencies and prior year experiences. Law #81 of 1991 named "Autonomous Municipalities Act" requires that each year a portion of the budget be segregated to cover any budget or fund balance deficit from prior fiscal years. If deficit continues to increase, the portion to be segregated each year will also increase, leaving less balance available to Municipality for expenditures.

Recommendation:

The Finance Director must develop policies and procedures in order to prevent the above condition again. Also, a portion of next fiscal year budget should be segregated to cover prior year fund balance accrued deficit.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

11-03 General Fund Deficit

Auditee Response:

Management agrees with the finding and the recommendation, and established and account, setting aside a portion of the 2011-2012 budget, for prior year adjustments. Effective procedures were developed among the purchase and auction offices, meeting the budgetary requirements.

Section III Federal Awards Programs
Schedule of Findings and Questioned Costs

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

**SBGP 11-04 - FEDERAL CASH MANAGEMENT SYSTEM
CFDA # 14. 228**

Criteria:

Federal regulations require that grantees shall conform to the standards of timing and amounts as applicable to advances by federal agencies. Amounts requested should be limited to the program's immediate cash needs.

Condition:

The Municipality has not established effective cash management procedures.

Effect:

As part of my test, the program had an average cash balance of approximately \$26,903.46 during the fiscal year. There were months which reported balances as high as \$ 132,299.21.

Cause:

Cash balances remained high because usually the funds received during the month are expended during the following months.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdowns of Federal funds as closely as possible to the actual disbursements.

Auditee Response:

The Municipality of Cataño Federal Program Office is aware of all federal and local regulations. Since there was no internal procedures or regulations on how to manage cash from federal sources, the Federal Program Office produced a brief procedure to be follow on all transactions when a drawdown is requested to the different federal or local agencies involving federal cash. The Federal Program Office, together with the Finance Department, will be attending these procedures, which will form part of any other Municipality's internal procedure on cash management activities.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

**Child Care 11-05 - FEDERAL CASH MANAGEMENT SYSTEM
CFDA # 93.575**

Criteria:

Federal regulations require that grantees shall conform to the standards of timing and amounts as applicable to advances by federal agencies. Amounts requested should be limited to the program's immediate cash needs.

Condition:

The Municipality has not established effective cash management procedures.

Effect:

As part of my test, the program had an average cash balance of approximately \$8,756.52 during the fiscal year. There were months which reported balances as high as \$ 11,958.74.

Cause:

Cash balances remained high because usually the funds received during the month are expended during the following months.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdowns of Federal funds as closely as possible to the actual disbursements.

Auditee Response:

The Municipality of Cataño Federal Program Office is aware of all federal and local regulations. Since there was no internal procedures or regulations on how to manage cash from federal sources, the Federal Program Office produced a brief procedure to be follow on all transactions when a drawdown is requested to the different federal or local agencies involving federal cash. The Federal Program Office, together with the Finance Department, will be attending these procedures, which will form part of any other Municipality's internal procedure on cash management activities.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

**Even Start 11-06 – FEDERAL CASH MANAGEMENT SYSTEM
CFDA #84.213**

Criteria:

Federal regulations require that grantees shall conform to the standards of timing and amounts as applicable to advances by federal agencies. Amounts requested should be limited to the program's immediate cash needs.

Condition:

The Municipality has not established effective cash management procedures.

Effect:

As part of my test, the program had an average cash balance of approximately \$16,417.39 during the fiscal year. There were months which reported balances as high as \$ 45,697.63.

Cause:

Cash balances remained high because usually the funds received during the month are expended during the following months.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdowns of Federal funds as closely as possible to the actual disbursements.

Auditee Response:

The Municipality of Cataño Federal Program Office is aware of all federal and local regulations. Since there was no internal procedures or regulations on how to manage cash from federal sources, the Federal Program Office produced a brief procedure to be follow on all transactions when a drawdown is requested to the different federal or local agencies involving federal cash. The Federal Program Office, together with the Finance Department, will be attending these procedures, which will form part of any other Municipality's internal procedure on cash management activities.

**Commonwealth of Puerto Rico
Municipality of Cataño
Schedule of Finding and Questioned Costs
June 30, 2011**

**Food Program 11-07 - FEDERAL CASH MANAGEMENT SYSTEM
CFDA #10. 558**

Criteria:

Federal regulations require that grantees shall conform to the standards of timing and amounts as applicable to advances by federal agencies. Amounts requested should be limited to the program's immediate cash needs.

Condition:

The Municipality has not established effective cash management procedures.

Effect:

As part of my test, the program had an average cash balance of approximately \$142,468.11 during the fiscal year. There were months which reported balances as high as \$ 187,087.42.

Cause:

Cash balances remained high because usually the funds received during the month are expended during the following months.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdowns of Federal funds as closely as possible to the actual disbursements.

Auditee Response:

The Municipality of Cataño Federal Program Office is aware of all federal and local regulations. Since there was no internal procedures or regulations on how to manage cash from federal sources, the Federal Program Office produced a brief procedure to be follow on all transactions when a drawdown is requested to the different federal or local agencies involving federal cash. The Federal Program Office, together with the Finance Department, will be attending these procedures, which will form part of any other Municipality's internal procedure on cash management activities.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

For a II prior year findings and questioned costs the Municipality has filed The Corrective Action Plan.

During the current audit, we inquired about the status of the prior year's audit findings and questioned costs, communicated to the Municipality of Cataño. It was noted that corrective action has been taken, except for certain conditions that still exists.

**SINGLE AUDIT REPORTS FOR THE
YEAR ENDED JUNE 30, 2010**

PROGRAM FINDINGS/NONCOMPLIANCE
All Federal Programs 10-05 - FEDERAL FINANCIAL REPORTS

Statement of Condition:

Reporting requirements:

Accounting records in Federal Programs are not reconciled with those recorded in the Municipality's central accounting department records.

Recommendation:

The Municipality should prepare federal financial Reports based on the programs underlying accounting records.

Current Status:

Corrected

**SBGP 10-06 - FEDERAL CASH MANAGEMENT SYSTEM
CFDA # 14. 228**

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

**SBGP 10-06 – FEDERAL CASH MANAGEMENT SYSTEM (CONTINUED)
CFDA # 14. 228**

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-04

**Child Care 10-07 – FEDERAL CASH MANAGEMENT SYSTEM
CFDA # 93. 575**

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-05

**Even Start 10-08 – FEDERAL CASH MANAGEMENT SYSTEM
CFDA #84. 213**

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

**Even Start 10-08 - FEDERAL CASH MANAGEMENT SYSTEM (CONTINUED)
CFDA #84. 213**

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-06

**Food Program 10-09 - FEDERAL CASH MANAGEMENT SYSTEM
CFDA #10. 558**

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-07

**SINGLE AUDIT REPORTS FOR THE
YEAR ENDED JUNE 30, 2009**

**PROGRAM FINDINGS/NONCOMPLIANCE
All Federal Programs 09-07 - FEDERAL FINANCIAL REPORTS**

Statement of Condition:

Reporting requirements:

Accounting records in Federal Programs are not reconciled with those recorded in the Municipality's central accounting department records.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

PROGRAM FINDINGS/NONCOMPLIANCE
All Federal Programs 09-07 – FEDERAL FINANCIAL REPORTS (CONTINUED)

Recommendation:

The Municipality should prepare federal financial Reports based on the programs underlying accounting records.

Current Status:

Corrected

SBGP 09-07 – FEDERAL CASH MANAGEMENT SYSTEM
CFDA # 14. 228

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-04

Child Care 09-08 – FEDERAL CASH MANAGEMENT SYSTEM
CFDA # 93. 575

Statement of Condition:

The Municipality has not established effective cash management procedures.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

**Child Care 09-08 – FEDERAL CASH MANAGEMENT SYSTEM (CONTINUED)
CFDA # 93.575**

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-05

**Even Start 09-09 – FEDERAL CASH MANAGEMENT SYSTEM
CFDA #84.213**

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-06

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

**Food Program 09-10 – FEDERAL CASH MANAGEMENT SYSTEM
CFDA #10. 558**

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-07

**SINGLE AUDIT REPORTS FOR THE
YEAR ENDED JUNE 30, 2008**

PROGRAM FINDINGS/NONCOMPLIANCE

All Federal Programs 08-07 – FEDERAL FINANCIAL REPORTS

Statement of Condition:

Reporting requirements:

Accounting records in Federal Programs are not reconciled with those recorded in the Municipality's central accounting department records.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011

SINGLE AUDIT REPORTS FOR THE
YEAR ENDED JUNE 30, 2008

PROGRAM FINDINGS/NONCOMPLIANCE

All Federal Programs 08-07 - FEDERAL FINANCIAL REPORTS (CONTINUED)

Recommendation:

The Municipality should prepare federal financial Reports based on the programs underlying accounting records.

Current Status:

Corrected

Child and Care
Food Program
CFDA No. 10.558

08-09 - FEDERAL CASH MANAGEMENT SYSTEM

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-07

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

**Child Care
CFDA No. 93.575**

08-11 - FEDERAL CASH MANAGEMENT SYSTEM

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-05

**SBGP Program
CFDA No. 14.228**

08-12 - FEDERAL CASH MANAGEMENT SYSTEM

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdowns of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-04

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CATAÑO
SCHEDULE OF PRIOR YEARS AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

**SBGP Program
CFDA No. 14.228**

08-14 - INADEQUATE DOCUMENTATION OF PARTICIPANT FILES

Statement of Condition:

Incomplete accounting records.

Still remain 21 files that do not presented for examination the inspection of the rehabilitation work upon completion and 1 file that do not contain evidence of construction material return.

Recommendation:

The Municipality must inspect the rehabilitation work upon completion to assure that it is carried out in accordance with the contract specifications.

Current Status:

Condition still prevail.

**Even Start
CFDA No. 84.213**

08-16 FEDERAL CASH MANAGEMENT SYSTEM

Statement of Condition:

The Municipality has not established effective cash management procedures.

Recommendation:

In accordance with Federal regulations, the Municipality should estimate drawdown of Federal funds as closely as possible to the actual disbursements.

Current Status:

Condition still prevail. Similar finding in current year. See finding 11-06

**Commonwealth of Puerto Rico
Municipality of Cataño
Summary schedule of prior years audit findings
Fiscal year 2006-2007**

The following schedule contains the finding number and title of each of the findings included in the report on compliance and internal control based on the audit of the general purpose financial statements for performed in accordance with government auditing standards for the fiscal year ended June 30, 2007. Under the heading corrective action taken there will be the following:

PR - Partially resolved (indicating the corrective action plan was partially implemented and the finding repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011).

NR - Not resolved yet. Findings repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011.

R - Resolved

Finding Number	Title	Corrective Action Taken
07-01 09-01	Deficiencies in the Uniform Accounting System and other Accounting Records	NR
07-02 09-02	Inactive and Unnecessary Funds	NR
07-03	lack of monitoring and fraud prevention activities	R
07-06	Disbursement test	NR

**Commonwealth of Puerto Rico
Municipality of Cataño
Summary schedule of prior years audit findings
Fiscal year 2006-2007**

The following schedule contains the finding number and title of each of the findings included in the report on compliance with requirements applicable to each major program and internal control over compliance in accordance with OMB Circular A-133 for the fiscal year ended June 30, 2007. Under the heading corrective action taken there will be the following:

R - Resolved

PR - Partially resolved (indicating the corrective action plan was partially implemented and the finding repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011).

NR - Not resolved yet. Some Findings repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011.

Finding Number	Title	Corrective Action Taken
07-09	Federal financial reports	NR
07-11	Equipment and Real Property Management	R
07-13 09-07	Federal cash management system	NR
07-14 09-08	Federal cash management system	NR
07-15 09-09	Federal cash management system	NR
09-10	Federal cash management system	NR
07-17	Inadequate documentation of participant files	NR
07-18	Earmarking Requirement	R

**Commonwealth of Puerto Rico
Municipality of Cataño
Summary schedule of prior years audit findings
Fiscal year 2005-2006**

The following schedule contains the finding number and title of each of the findings included in the report on compliance and internal control based on the audit of the general purpose financial statements for performed in accordance with government auditing standards for the fiscal year ended June 30, 2007. Under the heading corrective action taken there will be the following:

PR - Partially resolved (indicating the corrective action plan was partially implemented and the finding repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011).

NR - Not resolved yet. Some Findings repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011.

Finding Number	Title	Corrective Action Taken
06-01 09-01	Deficiencies in the Uniform Accounting System and other Accounting Records	NR
06-02 09-02	Inactive and Unnecessary Funds	NR
06-03	Lack of monitoring and fraud prevention activities	R
06-06	Personnel files and related payroll procedures	NR

**Commonwealth of Puerto Rico
Municipality of Cataño
Summary schedule of prior years audit findings
Fiscal year 2005-2006**

The following schedule contains the finding number and title of each of the findings included in the report on compliance with requirements applicable to each major program and internal control over compliance in accordance with OMB Circular A-133 for the fiscal year ended June 30, 2007. Under the heading corrective action taken there will be the following:

R - Resolved

PR - Partially resolved (indicating the corrective action plan was partially implemented and the finding repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011).

NR - Not resolved yet. Some Findings repeated in fiscal year 2007-2008, 2008-2009, 2009-2010 and 2010-2011.

Finding Number	Title	Corrective Action Taken
06-09 09-01	Accounting system	NR
06-12 09-07	Federal cash management system	NR
06-13 09-08	Federal cash management system	NR
06-14 09-09	Federal cash management system	NR
09-10	Federal cash management system	NR
06-16	Inadequate documentation of participant files	NR
06-18	Earmarking Requirement	R
06-19	Equipment and Real property Management	R



**COMMONWEALTH OF PUERTO RICO - MUNICIPALITY OF CATAÑO
CORRECTION ACTION PLAN (CAP)**

Audit Report: Reports on Compliance and Internal Control in Accordance with Governmental Auditing Standards and Circular OMB A-133
 Audit Period: July 1, 2010 – June 30, 2011 Fiscal year 2010-2011

Honorable Mayor: José A. Rosario Meléndez.

Contact Person: Mrs. Lisaniz Figueroa Oyola, Internal Auditor Director

Phone: (787) 788-0404 ext. 4157

Program: COMMUNITY DEVELOPMENT BLOCK GRANTS, CHILD CARE, EMERGENCY SHELTER, EVEN START, FOOD PROGRAM, AND
FEDERAL TRANSIT.

Finding Number	Requirement	Finding Narrative	Corrective Action / Planned Actions	Questioned Cost	Status
2011-01	Compliance and Internal Control	<p align="center">ACCOUNTING SYSTEM AND OTHER ACCOUNTING RECORDS</p> <p>The financial Department does not maintain accounting records supporting most of the procedures performed during the preparation of the Municipality's basis financial statement as follows:</p> <ul style="list-style-type: none"> ▪ The conversion of accounting records from the cash basis of accounting to the modified accrual basis of accounting used by governmental funds; ▪ The conversion of governmental funds from the modified accrual basis to the accrual basis of accounting used by government – wide financial statements; and ▪ Working papers and analyses of significant balance reports in the basic financial statement, such as capital assets, accounts receivable (municipal licenses, grants and contributions, etc), deferred revenues, accounts payable, and long-term obligations (for which the general practice is to rely upon the notifications received from the Government Development Bank for Puerto Rico, the P.R. Treasury Dept., the Federal Government and the Municipal Revenue Collection Center for the balance of its outstanding debt and the withholding for its debt service). <p>The continued failure to have an adequate accounting system does not allow the Municipality to have timely and accurate financial information for its decision making process.</p>	<p>Produce accurate monthly reports of accounting transactions of revenues and disbursements in compliance of federal and local laws and regulations; including adequate internal controls to the process.</p>	None	Underway

Finding Number	Requirement	Finding Narrative	Corrective Action / Planned Actions	Questioned Cost	Status
		<p>Auditee Response:</p> <p>This condition is similar as in prior year's audits. Management accepted the condition and is actually working on the following:</p> <p>As of May 2011, the Municipality completed the implementation of a Financial Management System, which provides necessary and adequate internal controls, designed to account all daily revenues and disbursements transactions of all municipal funds. This application provides monthly accurate reports about the results of the operations of the Municipality. Essentially, it is a valuable tool to be used in monitoring monthly revenues and disbursements, in reconciliation process and for budgetary purposes.</p>			
2011-02	Compliance and Internal Control	<p>INACTIVE AND UNNECESSARY FUNDS</p> <p>During prior years, the Municipality has maintained excessive number of funds pertaining to the special revenue and capital projects funds, many of which were inactive or had insignificant movement or operations. Municipality's management has been working over the intended objective of all these funds, in order to record any required adjustment over the inactive ones.</p>	Continue analyzing inactive accounts with balances to determine whether they are needed or should be closed.	None	Underway
2011-03	Compliance and Internal Control	<p>GENERAL FUND DEFICIT</p> <p>The Basic Financial Statements, prior period adjustments and reclassifications to the General Fund increased the deficit presented as of June 30, 2010, as follows:</p> <p>Fund Balance (Deficit) — as originally presented (\$5,937,683) Prior periods (1998-2009) debts recognition (1,911,696) Fund Balance (Deficit) as restated (\$7,849,379)</p>	Set aside a portion of the 2011-2012 budget, for prior year adjustments.	None	Complete