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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA**

**BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED
JUNE 30, 2008**

ORTIZ, RIVERA, RIVERA & CO.

CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

Suite 152, PO Box 70250, San Juan, P.R. 00936-7250 • Phone (787) 756-8524, Fax (787) 274-0562

**COMMONWEALTH OF PUERTO RICO
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BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

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PART I - FINANCIAL SECTION

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Services Division

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
Municipal Legislature
Municipality of Guánica
Guánica, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Guánica, as of and for the year ended June 30, 2008, which collectively comprise the Municipality's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material 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. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Guánica as of June 30, 2008, and the respective changes in financial position, thereof and the respective budgetary comparison for the general fund and debt services fund for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated December 23, 2008 on our consideration of the Municipality's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grants, agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the

results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 3 through 15 is not a required part of the basic financial statements, but is supplementary information required by the accounting principles generally accepted in the United States of America. We 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, we did not audit the information and express no opinion on it.

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

San Juan, Puerto Rico
December 23, 2008

Ortiz, Rivera, Rivera & Co.

The stamp 2386835 was affixed
to the original of this report.



COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

Our discussion and analysis of the Municipality of Guánica financial performance provides an overview of the Municipality's financial activities for the fiscal year ended June 30, 2008. Because this MD&A is designed to focus on the current year activities, resulting changes and currently known facts, we encourage reader to consider the information presented in this MD&A in conjunction with the additional information furnished in the accompanying basic financial statements.

FINANCIAL HIGHLIGHTS

- The Municipality has reported assets amounting to \$27.07 million in the accompanying statement of net assets, of which most significant are capital assets and cash and cash equivalents amounting to \$19.078 million and \$6.33 million respectively.
- The Municipality's capital assets increase as a result of this year's operations. Capital assets as of June 30, 2008 are \$19.078 million, as compared to \$18.43 million for the year ended June 30, 2007, for a 3.5% of increase.
- The assets of the Municipality exceeded its liabilities by \$9.43 million at June 30, 2008, represented as "net assets" in the accompanying statements of net assets. Restricted and unrestricted (deficit) net assets amounted to \$7.11 million and \$(8.31) million, respectively. Net assets invested in capital assets amounted \$10.63 million.
- During the year, the Municipality reported revenues of \$8.67 million in the General Fund of total revenues restricted and unrestricted of \$13.31 million.
- Long term liabilities principal payments were \$.704 million. During the year ended June 30, 2008, the Municipality issued \$3.995 million on bonds payable.
- The Municipality has reported total expenses amounting to \$12.97 million in the accompanying statement of activities.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statement of Net Assets and the Statement of Activities provide information about the activities of the Municipality as a whole and present a long-term view of the Municipality's finances. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the Municipalities' operations in more detail than the government-wide statements by providing information about the Municipality's most significant funds. Both perspectives 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

Overview of the Basic Financial Statements

The Municipality's financial statements include three components:

1. the government-wide financial statements
2. the fund financial statements
3. notes of the financial statements

These components are described below:

Government-wide financial statement: Are designed to provide reader with a broad of the Municipality's operations and finance as whole in a manner similar to Private-sector business. These statements provide short-term and long-term information about the Municipality's financial position, which assist the Municipality's management to determine the economic condition at the end of the fiscal year. These financial statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. The governmental-wide financial statements include; the statement of net assets and the statement of activities.

The Statement of Net Assets and the Statement of Activities

The Statement of Net Assets and the Statement of Activities report information about the Municipality as a whole and about its activities. These statements include *all* assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Municipality's *net assets* and changes in them. You can think of the Municipality's net assets, the difference between assets and liabilities, as one way to measure the Municipality's financial health, or *financial position*. Over time, *increases or decreases* in the Municipality's net assets are one indicator of whether its *financial health* is improving or deteriorating. You will need to consider other non-financial factors, however, such as changes in the Municipality's property tax base and the condition of the roads, to asses the *overall health* of the Municipality of Guánica.

In the Statement of Net Assets and the Statement of Activities, we divide the Municipality into:

- Governmental activities – Most of the Municipality's basic services are reported here, including the municipal police, public works, garbage disposal, public energy and health services, and general administration. Property taxes, municipal license tax, state and federal grants finance most of these activities.

Reporting the Municipality's Most Significant Funds

Fund Financial Statement: Report the financial position and results of operations of the Municipality's governmental funds. The Fund Financial statement components are the Balance Sheet-government funds and the Statements of Revenues, Expenditures and Changes in Fund Balance. The Fund financial statements provide detailed information about the most significant funds, not the Municipality as a whole. Some funds are required to be established by bond covenants.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

The Municipality's basic services are reported in the governmental funds, that uses an accounting approach which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called *modified accrual* accounting, which measures cash and all other *financial* assets that can readily be converted to cash. The governmental fund statements provide a detailed *short-term view* of the Municipality's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs. We describe the relationship (or differences) between governmental *activities* (reported in the Statement of Net Assets and the Statement of Activities) and governmental *funds* in a reconciliation on this report.

Notes to the Basic Financial Statement: The notes provide additional information that is essential to a full understanding of the data provided in government-wide and the fund financial statements.

THE MUNICIPALITY AS A WHOLE

The Municipality's *combined* net assets increases from a year ago, from \$9.09 million to \$9.43 million. Our analysis below focuses on the net assets (Table 1) and changes in net assets (Table 3) of the Municipality's governmental activities.

Table 1

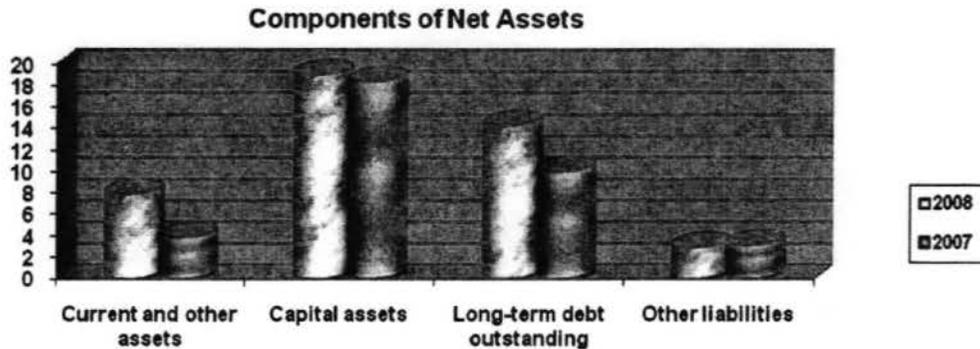
NET ASSETS

(in Million)

Governmental Activities

	2007	2008
Current and other assets	\$3.96	\$7.99
Capital assets	18.43	19.07
Total assets	22.39	26.97
Long-term debt outstanding	(10.08)	(14.34)
other liabilities	(3.22)	(3.02)
Total liabilities	(13.30)	(17.63)
Net assets:		
Invested in capital assets, net of related debt	13.69	10.63
Restricted for:		
Debt services	.23	.45
Capital project	2.87	6.43
Other specified purpose	.03	.02
Unrestricted	(7.71)	(8.31)
Net Assets	\$ 9.09	\$9.43

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008



Net assets of the Municipality's governmental activities increased by \$.34million (\$9.43million Compared to \$9.09 million). *Unrestricted* net assets, the part of net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements, changed from approximately \$(7.71) million at June 30, 2007 to a \$(8.31) million at June 30, 2008. The following is a condensed presentation of the Municipality's results of operations, as reported in the government-wide financial statements:

Comparative Condensed Statement of Activities:

	2007	2008
Revenues:		
Program revenues:		
Operating grants and contributions	\$ 1,675,274	\$1,796,402
Capital grants and contributions		
Charges for services	550,698	264,165
General revenues:		
Property taxes	1,626,687	1,819,208
Municipal license taxes	378,269	363,337
Sales and uses tax		809,669
Construction excise taxes		
Unrestricted intergovernmental contributions and reimbursements	8,042,761	7,277,283
Unrestricted interest on deposit	124,646	120,062
Other	701,084	865,985
Special items-		
Gain on Sale of capital assets		
Total revenues	<u>13,385,577</u>	<u>13,316,111</u>
Expenses:		
General government	5,740,027	6,596,168
Urban and economic development		2,774,006
Public Safety	1,087,949	988,860
Public work and sanitation	2,159,721	
Culture and recreation	546,883	699,316
Health and welfare	2,396,623	1,623,330
Interest and bonds, notes and capital lease obligations	296,311	294,834
Total expenses	<u>12,227,514</u>	<u>12,976,514</u>
Net increase in net assets	1,158,063	339,597
Net assets-at the beginning of the year, as restated	<u>7,934,173</u>	<u>9,092,235</u>
Net assets- at end of the year	<u>9,092,235</u>	<u>9,431,832</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

Financial analysis of the Municipality's Governmental Funds

The Municipality uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the Municipality's governmental fund is to provide information on near-term inflow, outflow, and balance of spendable resources. Such information is useful in assessing the Municipality's financial requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of fiscal year. The following is a condensed presentation of the Municipality's balance sheet and results of operations of government fund:

	2007	2008
Comparative Condensed Balance Sheet-Governmental funds:		
Total assets-major funds	5,538,928	9,866,611
Total assets-nonmajor funds	1,021,407	1,35,658
Total assets	6,560,335	11,222,269
Total liabilities:		
Total liabilities-major funds	4,239,179	5,520,694
Total liabilities-nonmajor funds	1,150,272	1,307,226
Total liabilities	5,389,451	6,827,920
Fund Balances:		
Reserved-major funds	3,075,212	7,142,068
Reserved-nonmajor funds	205,454	
Unreserved-major funds	(1,791,347)	(2,796,151)
Unreserved-nonmajor funds	(318,455)	48,432
Total fund balances	1,170,884	4,394,346
Comparative Condensed Statement of Operations-Governmental funds:		
Total revenues-major funds	11,902,463	10,500,547
Total revenues-nonmajor funds	2,492,002	2,815,564
Total revenues	14,394,465	13,316,111
Total expenditures:		
Total expenditures-major funds	12,262,867	11,995,797
Total expenditures-nonmajor funds	2,682,778	2,384,173
Total expenditures	14,945,645	14,379,970
Other Financial Sources-major funds(excluding operating transfers among funds)	335,000	4,287,324
Special items, net		
Net changes in fund balances	(216,180)	3,223,465

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

Governmental Activities

Programs revenues of Municipality's governmental activities decrease by (\$.17million) while total expenses increased by (\$.75million). The Municipality of Guánica took the following major actions this year to improve the financial position:

- The Mayor of the Municipality of Guánica still has a Finance Auxiliar Director to improve the collections of municipal licensed tax and property tax revenues; supervise the operations of the official and auxiliary collector of the Municipality.
- In the budget respect the administration of the Municipality received the estimated of expenses by each department, and the Budget Director and the Mayor performed the evaluation to those expenses and determine the needed of each one, looking for the reduction of those unnecessary expenses without affecting the daily operations.

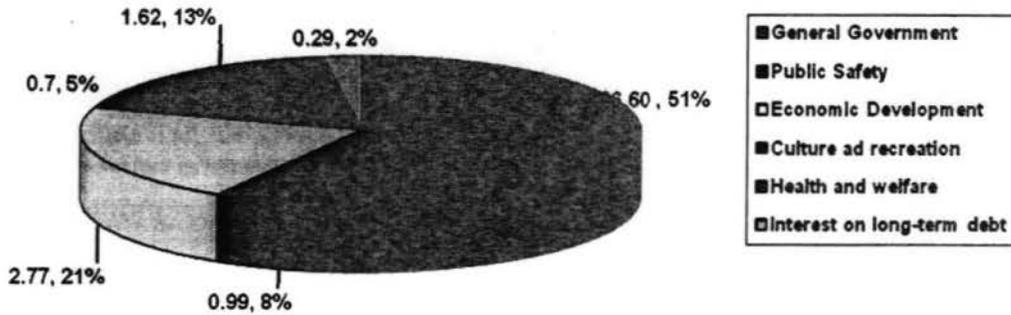
Expenses during the fiscal year ended June 30, 2008, was substantially related to the following:

Table 2
Governmental Activities
(in Million)

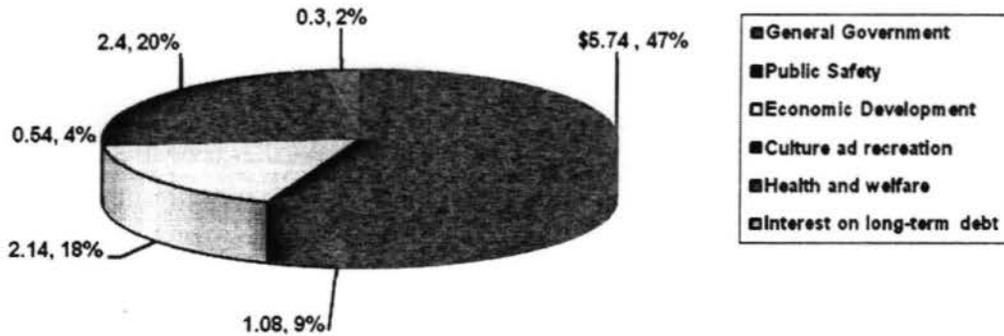
	Total expenses	
	2007	2008
General Government	\$5.74	\$6.60
Public Safety	1.08	.99
Economic Development	2.14	2.77
Culture, recreation and education	.54	.70
Health and welfare	2.40	1.62
Interest on long term debt	.30	.29
Totals	\$12.22	\$12.97

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
 Management Discussion and Analysis
 June 30, 2008

Total Expense 2008



Total Expense 2007



The cost of all governmental activities this year was \$12.97 million compared to \$12.22 million last year. Table 2 presents the cost of each of the Municipality of Guanica's largest programs.

The major sources of general revenue are property taxes, municipal license taxes, sales tax and grant and contributions not restricted, which in total represent \$10.27 (91%) and \$ 10.03 (91%) of all revenues in 2008 and 2007, respectively.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

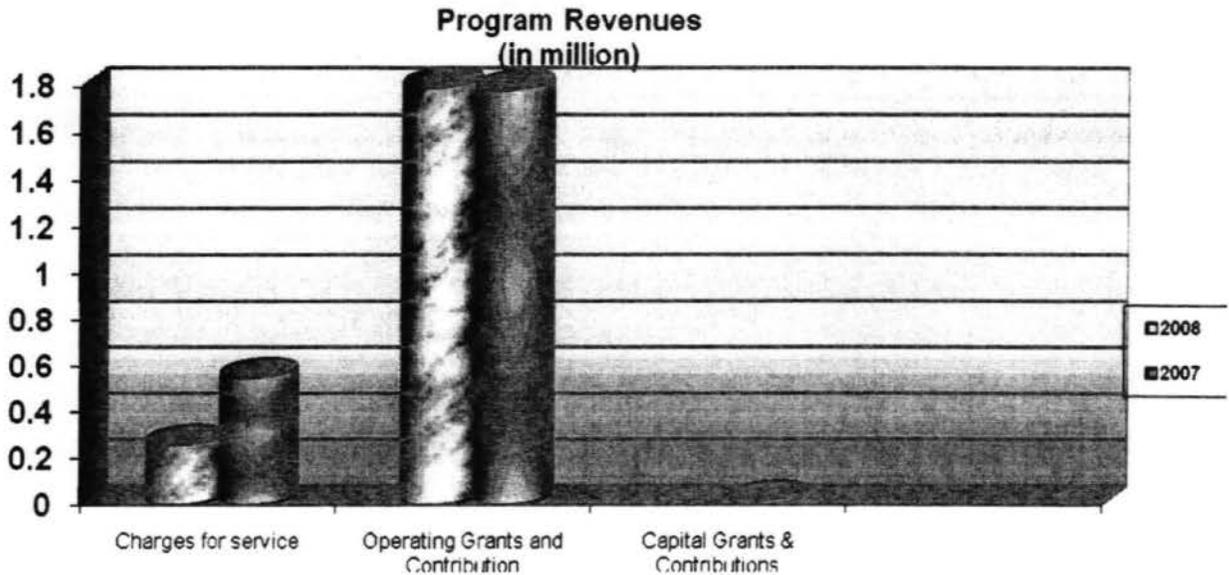
Table 3
Governmental Activities
(in Million)

	General Revenues By major sources	
	2007	2008
Property taxes	\$1.62	\$1.82
Municipal license taxes	.37	.36
Sale tax		.81
Grants and contributions	8.04	7.28
Totals	\$10.03	\$10.27

Table 4
Governmental Activities
(in Million)

	Program Revenues by major sources	
	2007	2008
Charges for service	\$.55	\$.26
Operating Grants and Contribution	1.79	1.80
Capital Grants and Contributions	.02	
Totals	\$2.36	\$2.06

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008



THE MUNICIPALITY'S FUND

As the Municipality completed the year, its governmental funds reported a combined fund balance of \$4.39 million, which is more than last year total of \$1.17 million.

General Fund Budgetary Highlights

Over the course of the year, the Municipal Assembly revised the Municipality of Guánica budget several times. These budget amendments fall into various categories. The first category includes amendments and supplemental appropriations that were approved shortly after the beginning of the year and reflect the actual beginning balances (versus the amounts we estimated in May 2007).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

CAPITAL ASSET AND DEBT ADMINISTRATION

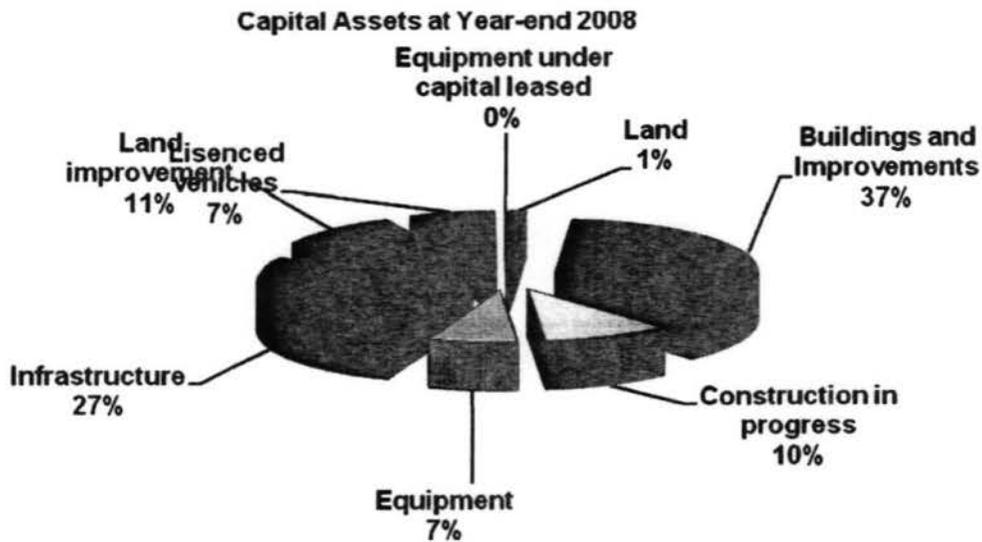
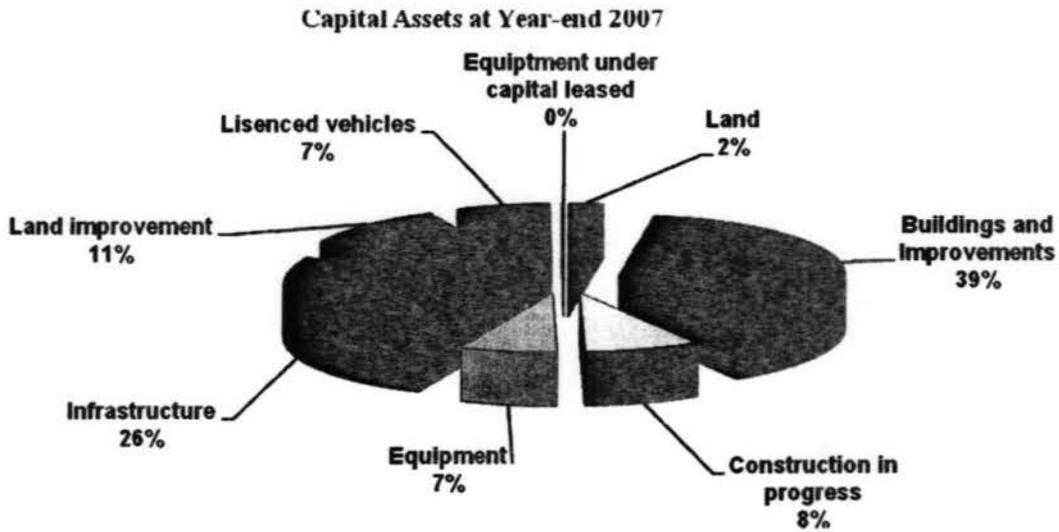
Capital Assets

As of June 30, 2008, the Municipality of Guánica had \$ 27.84 million invested in a broad range of capital assets, including buildings, parks, roads, bridges, and equipment. (See Table 5). This amount represents a net increase (including additions and deductions) of just over \$1.32 million, or 5 %, over last year. In this table you see few changes in amount compared to last year due to reclassifications of real property to proper division.

Table 5
Capital Assets at Year-end
(At cost, in Thousands)

	<i>Governmental Activities</i>	
	2007	2008
Land	.66	.37
Land improvement	2.89	2.89
Buildings and Improvements	10.28	10.28
Construction in progress	2.22	2.87
Licensed vehicles	1.79	1.91
Equipment	1.86	2.01
Equipment under capital leases	.04	.04
Infrastructure	6.78	7.47
Totals	\$26.52	\$27.84

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008



More detailed information about the Municipality's capital assets is presented in Note 11 to the financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

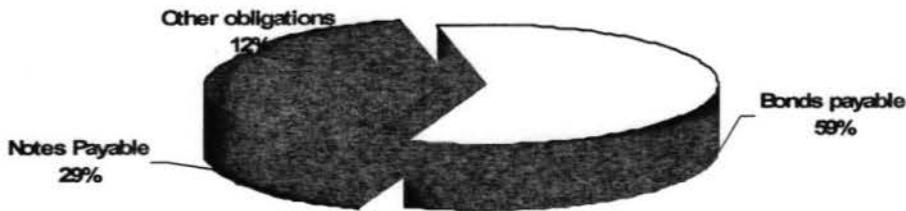
Debt

At year-end, the Municipality had \$ 14.33 million in bonds and notes outstanding versus \$ 10.79 million last year, an increase of 32.80 percent, as shown in Table 6.

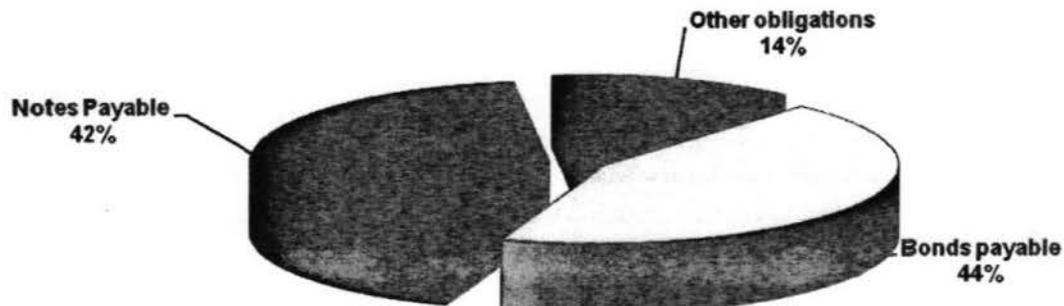
Table 6
Outstanding Debt, at Year-End
(in Thousands)

	Governmental Activities	
	2007	2008
Bonds payable	\$4.73	\$8.45
Notes Payable	4.59	4.23
Other obligations	1.47	1.66
Totals	\$10.79	\$14.33

Outstanding Debt, at Year-end 2008



Outstanding Debt, at Year-end 2007



COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
Management Discussion and Analysis
June 30, 2008

New bonds in the amount of \$3.995 million were issued. The Municipality is required to limit the amount of general obligation debt to 10% of the total assessment of property located within the Municipality, for bonds to be repaid with the proceeds of property taxes restricted for debt services. Other obligations include accrued vacation and sick leave, claims and judgments, and Christmas bonus.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's elected and appointed officials considered many factors when setting the fiscal-year 2008 budget. Unemployment in the Municipality now stands at 14.4 percent.

Budgeted expenditures are expected to rise accordingly to the increase in budgeted revenues.

If these estimates are realized, the Municipality's budgetary General Fund balance is expected to increase modestly by the close of 2009.

CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, and creditors with a general overview of the Municipality's finances and to show the accountability for the money it receives. If you have questions about this report or need additional financial information, contact us at Municipality of Guánica, PO Box 785, Guánica, Puerto Rico 00653.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
STATEMENT OF NET ASSETS
JUNE 30, 2008**

<u>Assets</u>	<u>Governmental Activities</u>
Cash (Notes 2 and 5)	\$ 760,184
Cash with fiscal agent (Notes 2 and 5)	5,574,624
Due from other agencies (Note 9)	1,656,781
Capital assets, net (Note 11)	<u>19,078,413</u>
 Total assets	 <u><u>\$ 27,070,002</u></u>
 <u>Liabilities and Net Assets</u>	
Liabilities	
Accounts payable and accrued liabilities	\$ 1,435,999
Due to other agencies (Note 12)	1,169,509
Deferred revenues (Note 13):	
Municipal license tax	227,325
Property tax	26,662
Federal government	252,631
Noncurrent liabilities (Note 15):	
Due within one year	1,060,038
Due in more than one year	13,285,892
Accrued interest	180,114
Total liabilities	<u>17,638,170</u>
Net Assets	
Investment in capital assets, net of related debt	10,633,413
Restricted for:	
Debt service	456,046
Capital projects	6,436,102
Federal programs	219,276
Unrestricted	<u>(8,313,005)</u>
Total net assets	<u>9,431,832</u>
 Total liabilities and net assets	 <u><u>\$ 27,070,002</u></u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenues</u>		<u>Net (Expense) Revenue and Changes in Net Assets</u>
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	
General government	\$ 6,596,168	\$ 264,165	\$ -	\$ (6,332,003)
Public safety	988,860			(988,860)
Culture and recreation	699,316			(699,316)
Public housing and welfare	1,623,330		552,906	(1,070,424)
Economic development	2,774,006		1,243,496	(1,530,510)
Interest on long-term debt	294,834			(294,834)
Total	<u>\$ 12,976,514</u>	<u>\$ 264,165</u>	<u>\$ 1,796,402</u>	<u>(10,915,947)</u>
General revenues:				
Property taxes (Note 6)				1,819,208
Municipal license tax (Note 7)				363,337
Sales and use tax (Note 8)				809,669
Grants and contributions not restricted to specific programs				7,277,283
Interest, fines and penalties				120,062
Miscellaneous				865,985
Total general revenues				<u>11,255,544</u>
Change in net assets				339,597
Net assets at beginning of year				<u>9,092,235</u>
Net assets at end of year				<u>\$ 9,431,832</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
BALANCE SHEET-GOVERNMENTAL FUNDS
JUNE 30, 2008**

<u>Assets</u>	<u>General</u>	<u>Commonwealth Legislature Resolutions</u>	<u>Debt Service</u>	<u>Section 8 Program</u>	<u>Capital Improvement Loan Bond</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Cash (Notes 2 and 5)	\$ 42,725	\$ 299,369	\$ -	\$ 225,500	\$ -	\$ 192,590	\$ 760,184
Cash with fiscal agent (Notes 2 and 5)			935,604		4,199,225	439,795	5,574,624
Due from other agencies (Note 9)	567,345	510,446	5,556	99	4,742	568,593	1,656,781
Due from other funds (Note 10)	980,884	2,095,116				154,680	3,230,680
Total assets	\$ 1,590,954	\$ 2,904,931	\$ 941,160	\$ 225,599	\$ 4,203,967	\$ 1,355,658	\$ 11,222,269

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
BALANCE SHEET-GOVERNMENTAL FUNDS
JUNE 30, 2008**

<u>Liabilities and Fund Balance (Deficit)</u>	<u>General</u>	<u>Commonwealth Legislature Resolutions</u>	<u>Debt Service</u>	<u>Section 8 Program</u>	<u>Capital Improvement Loan Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Liabilities							
Account payable and accrued liabilities	\$ 974,629	\$ 23,361	\$ -	\$ 1,966	\$ 60,731	\$ 375,312	\$ 1,435,999
Due to other agencies (Note 12)	1,169,509						1,169,509
Due to other funds (Note 10)	1,958,336	539,744		4,357	48,960	679,283	3,230,680
General obligations:							
Bonds			305,000				305,000
Interest			180,114				180,114
Deferred revenues: (Note 13)							
Municipal license tax	227,325						227,325
Property tax	26,662						26,662
Federal government						252,631	252,631
Total liabilities	<u>4,356,461</u>	<u>563,105</u>	<u>485,114</u>	<u>6,323</u>	<u>109,691</u>	<u>1,307,226</u>	<u>6,827,920</u>
Fund Balances (Deficit)							
Reserved for:							
Encumbrances	30,644						30,644
Federal programs				219,276			219,276
Debt service			456,046				456,046
Capital projects		2,341,826			4,094,276		6,436,102
Unreserved fund balance (deficit)	(2,796,151)					48,432	(2,747,719)
Total fund balance (deficit)	<u>(2,765,507)</u>	<u>2,341,826</u>	<u>456,046</u>	<u>219,276</u>	<u>4,094,276</u>	<u>48,432</u>	<u>4,394,349</u>
Total liabilities and fund balance (deficit)	<u>\$1,590,954</u>	<u>\$ 2,904,931</u>	<u>\$ 941,160</u>	<u>\$ 225,599</u>	<u>\$ 4,203,967</u>	<u>\$ 1,355,658</u>	<u>\$ 11,222,269</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO STATEMENT OF NET ASSETS
JUNE 30, 2008**

Total fund balances - governmental funds \$ 4,394,349

Amounts reported for governmental activities in the statement of net assets are different because:

- Capital assets, net used in governmental activities are not current financial resources and therefore are not reported in the governmental funds balance sheet 19,078,413

- Some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds. **(Note 4)** (14,040,930)

Net assets of governmental activities \$ 9,431,832

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUANICA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES-GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

	General	Commonwealth Legislature Resolutions	Debt Service	Section 8 Program	Capital Improvement Loan Fund	Other Governmental Funds	Total Governmental Funds
REVENUES							
Property taxes (Note 6)	\$ 1,551,457	\$ -	\$ 267,751	\$ -	\$ -	\$ -	\$ 1,819,208
Municipal license taxes (Note 7)	363,337						363,337
Sales and use taxes (Note 8)	537,837		271,832			-	809,669
Licenses and permits	226,729					6,800	233,529
Charges for service and rents	10,397					20,239	30,636
Intergovernmental revenues (Note 14):							
Federal grants and contributions		61,664		236,058		1,498,680	1,796,402
State contributions	5,040,010	950,783				1,286,490	7,277,283
Interest, fines, and penalties	106,085	422	11,252	102		2,201	120,062
Other revenues	837,977	3,683		23,171		1,154	865,985
Total revenues	<u>8,673,829</u>	<u>1,016,552</u>	<u>550,835</u>	<u>259,331</u>	<u>-</u>	<u>2,815,564</u>	<u>13,316,111</u>
EXPENDITURES							
Current:							
General government	4,505,393	404,468			33,972	1,294,701	6,238,534
Public safety	889,959					5,427	895,386
Culture and recreation	478,161					9,744	487,905
Public housing and welfare	1,259,856			212,191		326,544	1,798,591
Economic development	1,930,340	283,875				155,313	2,369,528
Capital outlays		475,530			547,578	592,444	1,615,552
Debt service:							
Principal retirement			679,640				679,640
Interest and other			294,834				294,834
Total expenditures	<u>9,063,709</u>	<u>1,163,873</u>	<u>974,474</u>	<u>212,191</u>	<u>581,550</u>	<u>2,384,173</u>	<u>14,379,970</u>
Excess (deficiency) of revenues under expenditures	<u>(389,880)</u>	<u>(147,321)</u>	<u>(423,639)</u>	<u>47,140</u>	<u>(581,550)</u>	<u>431,391</u>	<u>(1,063,859)</u>
OTHER FINANCING SOURCES (USES)							
Sales of assets	292,324						292,324
Loan proceeds					3,995,000		3,995,000
Transfers in	18,201		669,098			149,768	837,067
Transfers out	(818,866)		(18,201)				(837,067)
Total other financing sources (uses)	<u>(508,341)</u>	<u>-</u>	<u>650,897</u>	<u>-</u>	<u>3,995,000</u>	<u>149,768</u>	<u>4,287,324</u>
Excess (deficiency) of revenues and other sources over (under) expenditures and other uses	<u>(898,221)</u>	<u>(147,321)</u>	<u>227,258</u>	<u>47,140</u>	<u>3,413,450</u>	<u>581,159</u>	<u>3,223,465</u>
FUND BALANCE AT BEGINNING OF YEAR, AS RESTATED (Note 20)							
	<u>(1,867,286)</u>	<u>2,489,147</u>	<u>228,788</u>	<u>172,136</u>	<u>680,826</u>	<u>(532,727)</u>	<u>1,170,884</u>
FUND BALANCE (DEFICIT) AT END OF YEAR							
	<u>\$ (2,765,507)</u>	<u>\$ 2,341,826</u>	<u>\$ 456,046</u>	<u>\$ 219,276</u>	<u>\$ 4,094,276</u>	<u>\$ 48,432</u>	<u>\$ 4,394,349</u>

ADD 5/11/09

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF
ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Net change in fund balances - total governmental funds	\$ 3,223,465
Amounts reported for governmental activities in the statement of activities are different because:	
• Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.	1,615,552
• Governmental funds report issuance of long-term debt as other financial resources because provided current financial resources.	(3,995,000)
• Depreciation expense on capital assets is reported in the statement of activities, but do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditure in governmental funds.	(678,186)
• Governmental funds report principal payments on long-term obligations as expenditures, whereas the principal payments reduces the long-term obligations in the statement of activities.	679,640
• Sales of assets is reported in the statement of activities, but do not require the use of current financial resources	(292,324)
• Some expenses reported in the statement of activities do not require the use of current financial resources; therefore, are not reported as expenditures in governmental funds.	<u>(213,550)</u>
Changes in net assets of governmental activities	<u>\$ 339,597</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUANICA
STATEMENT OF REVENUES AND EXPENDITURES - BUDGET AND ACTUAL-GENERAL AND DEBT SERVICE FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

	General Fund				Debt Service Fund			
	Budgeted Amounts		Actual	Variance with Final Budget- Positive (Negative)	Budgeted Amounts		Actual	Variance with Final Budget- Positive (Negative)
	Original	Final			Original	Final		
REVENUES								
Property taxes	\$ 1,215,038	\$ 1,215,038	\$ 1,551,457	\$ 336,419	\$ 353,916	\$ 353,916	\$ 267,751	\$ (86,165)
Municipal license taxes	365,000	365,000	363,337	(1,663)				
Sales and used tax	310,000	310,000	537,837	227,837			271,832	\$ 271,832
Licenses and permits	950,507	950,507	221,083	(729,424)				
Charges for services and rent	39,300	39,300	16,042	(23,258)				
Intergovernmental revenues:								
State contributions	5,466,336	5,466,336	5,040,010	(426,326)				
Interest, fines, and penalties	47,000	47,000	106,085	59,085				
Other revenues	648,007	648,007	837,977	189,970			11,252	11,252
Total revenues	<u>9,041,188</u>	<u>9,041,188</u>	<u>8,673,828</u>	<u>(367,360)</u>	<u>353,916</u>	<u>353,916</u>	<u>550,835</u>	<u>196,919</u>
EXPENDITURES								
Current:								
General government	5,303,294	5,453,388	5,211,017	242,371				
Public safety	989,817	937,385	891,757	45,628				
Public housing and welfare	655,475	663,930	595,454	68,476				
Culture and education	446,387	486,773	480,982	5,791				
Economic development	1,646,215	1,499,712	1,937,508	(437,796)				
Debt service:								
Principal					198,788	198,788	679,640	480,852
Interest					155,128	155,128	294,834	139,706
Total expenditures	<u>9,041,188</u>	<u>9,041,188</u>	<u>9,116,718</u>	<u>(75,530)</u>	<u>353,916</u>	<u>353,916</u>	<u>974,474</u>	<u>620,558</u>
Excess (deficiency) of revenues over (under) expenditures	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (442,890)</u>	<u>\$ (442,890)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (423,639)</u>	<u>\$ (423,639)</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

1. ORGANIZATION

The Municipality of Guánica, Puerto Rico (Municipality) was founded in 1914. The Municipality is a political legal entity with full legislative and administrative faculties in every affair of municipal character, with perpetual succession existence and legal identity, separate and independent from the central government of the Commonwealth of Puerto Rico. The Municipality provides a full range of services including: public safety, public works, culture, recreation, health and welfare, education and other miscellaneous services.

The Municipal Government comprises the executive and legislative branches. The executive power is exercised by the Mayor and the legislative by the Municipal Assembly, which has 14 members. The members of these branches are elected every four years in the Puerto Rico general elections.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The financial information of the Municipality is presented in this report as follows:

- Management's Discussion and Analysis - Introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.
- Government - Wide Financial Statements - This reporting model includes financial statements prepared using full accrual of accounting for all of the government's activities. This approach includes not just current assets and liabilities, but also capital assets and long-term liabilities (such as buildings and infrastructure, including bridges and roads, and general obligation debt).
- Statement of Net Assets - The statement of net assets is designed to display the financial position of the Municipality, including capital assets and infrastructure.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

The net assets of the Municipality will be broken down into three categories; invested in capital assets, net of related debt; restricted; and unrestricted.

- **Statement of Program Activities** - The government - wide statement of activities report expenses and revenues in a format that focuses on the cost of each of the government's functions. The expense of individual functions is compared to the revenues generated directly by the function.
- **Budgetary comparison schedules** - Demonstrating compliance with the adopted budget is an important component of a government's accountability to the public. Under the new reporting model, the Municipality will continue to provide budgetary comparison information in their financial statements. An important change, however, is a requirement to add the government's original budget to the current comparison of final budget and actual results.

The following is a summary of the more significant policies.

a. Reporting Entity

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, as amended by Statement No. 39, "Determining whether Certain Organizations are Component Units" - an amendment of GASB Statement No. 14, "The Financial Reporting Entity," of the GASB. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government appoint a voting majority of the entity's governing body, and if either one of the following conditions exists: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete.

GASB Statement No. 39 provided additional guidance to determine whether certain organization for which the primary government is not financially

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

accountable should be reported as components units, A legally separate, tax-exempt organization should be discretely presented as a component unit if all of the following criteria are met: (a) the economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents; (b) the primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and; (c) the economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

GAAP details two methods of presentation: blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component units' financial data in columns separate from the Municipality's balances and transactions. Based on the aforementioned criteria, the Municipality has no component units.

b. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all the activities of the Municipality. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities are supported mainly by taxes and intergovernmental revenues.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

The fund financial statements segregate transactions related to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

c. Measurement Focus, Basis of Accounting and Financial Statement Presentation

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

Governmental fund financial statements are reported using the *current financial resources measurement focus and the modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within the current period or soon enough thereafter. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

The Municipality reports the following major governmental funds:

- General Fund

This is the operating fund of the Municipality and accounts for all financial resources, except those required to be accounted for in another fund.

- Section 8 Program

This fund account for revenue sources for the decent housing, suitable living environment, rental assistance to help very low-income families afford decent, safe and sanitary housing by encouraging property owners to rehabilitate substandard housing and lease the units with rental subsidies to low-income family.

- Debt Service Fund

This fund is used to account for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

- Commonwealth Legislature Resolutions Fund

This fund is used to account for revenue sources to be used for the construction and improvement of capital facilities and for welfare purposes.

- Capital Improvement Loan Fund

This fund is used to account for capital projects such as community facilities repairs, improvements of certain sport courts, and improvements to municipality roads.

Private-section standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements.

Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, licenses, permits, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

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

d. Cash and Cash with Fiscal Agent

The Municipality's Finance Director is responsible for investing available resources. The Municipality is restricted by law to invest only in savings accounts and certificates of deposits with banks qualified as a depository of public funds by the Puerto Rico Treasury Department (PRTD) or in instruments of the Government Development Bank for Puerto Rico (GDB).

Cash with fiscal agent in the capital project's fund consists of unused proceeds from appropriations from the Legislature of Puerto Rico, for the payment of current liabilities, and bonds and notes issued for the acquisition and construction of major capital improvements. 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.

e. Interfund Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year is 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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

f. Capital Assets

Capital assets purchased or acquired are carried at historical cost or estimated historical cost. Contributed assets are recorded at fair market value as of the date donated. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation in capital assets is calculated on the straight-line basis over the following estimated useful lives:

	<u>Useful Life</u>
Infrastructure	20-50 years
Buildings and building improvements	30-50 years
Furniture and fixtures	5-20 years
Vehicles	8 years
Machinery and equipment, excluding those under capital leases	5-20 years

g. Reservation of Fund Balance

Reservations of fund balance represent portions of fund balances that are legally segregated for a specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:

- Encumbrances

Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.

- Debt Service

Represents net assets available to finance future debt service payments.

- Capital Projects Fund

Represents the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. The committed

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

amounts generally will become liabilities in future periods as the projects are completed.

h. Risk Financing

The Municipality carries 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 Municipal Revenue Collection Center (the "CRIM") for the year ended June 30, 2008 amounted to approximately \$214,000. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$143,000 for workers compensation insurance covering all municipal employees.

i. Compensated Absences

Employees are entitled to 30 days vacations leave and 18 days sick leave per year. Sick leave is recorded as an expenditure in the year paid. Employees are entitled to payment of unused sick leave upon retirement if have been employed for at least 10 years in the municipal government. On July 1997, state Law 152 supra amended the Article 12.016, Section b (2) of the Municipal Law, authorizing the Municipality to pay any excess of vacations and sick leave accumulated over the maximum previously permitted by law. Calculations must be made until December 31 of every year. Excess of sick leave must be paid until March 31 next every natural year. Excess of vacations can be paid after July 1 of every fiscal year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

j. Future Adoption of Accounting Pronouncements

The Governmental Accounting Standards Board has issued the following statements that the Municipality has not yet adopted:

<u>Statement Number</u>	<u>Statement Name</u>	<u>Adoption Required in Fiscal Year</u>
51	Accounting and Financial Reporting for Intangible Assets	2009-10
52	Land and Other Real Estate Held as Investments by Endocuments	2008-09
53	Accounting and Financial Reporting for Derivative Instruments	2009-10

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

k. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. The most significant estimates consist of the contribution received from the Puerto Rico Electric Power Authority and the Municipal Revenue Collection Center caused by the delay of the notification of the actual revenues and expenditures to the presented in the financial statements of the agencies mentioned above.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

3. 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 GAAP, 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 and the debt service funds.

Revenues and Expenditures - Budget and Actual (Budgetary Basis), accordingly, includes only the operations of the general and the debt service funds. The amounts budgeted under the Special Revenue Fund were excluded since they are received and expended over a period of time which generally exceeds the current year.

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP 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.

b. Budget/GAAP Reconciliation

The following schedule presents comparisons of the legally adopted budget with actual data on a budget basis. Because accounting principles applied for

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of entity and timing differences in the excess of revenues over expenditures for the year ended June 30, 2008 is presented below for the general fund and debt service funds:

	<u>General Fund</u>	<u>Debt Service Fund</u>
Excess of revenues over (under) expenditures - budgetary basis	(\$442,890)	(\$423,639)
Entity differences:		
Non-budgeted transfer in	18,201	669,098
Non-budgeted transfer out	(818,866)	(18,201)
Non-budgeted revenue	690,537	
Timing differences:		
Prior year encumbrances recorded as current year expenditures for GAAP basis	(314,559)	\$ -
Current year encumbrances recorded as expenditure for budgetary basis	(<u>30,644</u>)	<u>-</u>
Excess (deficiency) of revenues over (under) expenditures - GAAP basis	(\$ <u>898,221</u>)	\$ <u>227,258</u>

c. Legal Compliance

The legal level of budgetary control is at the individual department level for general fund expenditures, and principal and interest due for the debt service fund.

4. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

The governmental fund balance sheet includes a reconciliation between fund balance-governmental funds and net assets of governmental activities as reported in the government-wide statement of net assets. One element of that reconciliation

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explains that some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds. The details of the approximately \$14.0 million difference are as follows:

Bonds payable	\$ 8,140,000
PR Treasury Department	1,873,940
Compensated absences	1,409,895
Due to Puerto Rico Labor Department	357,257
Due to Puerto Rico Land Authority	118,064
Due to CRIM	1,119,782
Due to FEMA	750,467
Claims and judgements	64,524
Christmas bonus	187,001
Puerto Rico Water and Sewer Authority	<u>20,000</u>
Net adjustment to reduce fund balance governmental funds to arrive at net assets of governmental activities	<u>\$ 14,040,930</u>

5. DEPOSITS - CUSTODIAL CREDIT RISK

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. Under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. 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).

The Municipality's bank balances in commercial banks of approximately \$850,000 in the governmental activities were fully collateralized at June 30, 2008. The deposits at GDB of approximately \$5 million that are restricted principally for capital projects, and the \$480,000 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

The Municipality maintains its deposits in one bank located at Puerto Rico. All kind of deposit is guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000.

The excess is covered by collateral provided by banks and held by the Treasury Department of the Commonwealth of Puerto Rico pursuant to applicable laws and regulations.

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6. PROPERTY TAXES

The Municipal Revenues Collection Center (CRIM) of the Commonwealth of Puerto Rico is responsible by law for the assessment, levy and collection of all real and personal property taxes. The tax on personal property is self assessed by the taxpayer. The assessment is made in a return which must be filed with the CRIM by May 15 of each year. The tax on real property is assessed by the CRIM. The assessment is made as of January 1 of each year and is based on estimated current values of the property as of year 1957. The tax on personal property must be paid in full together with the return on or before May 15. The tax on real property is due in two equal installments in July 1 and January 1, following the assessment date.

The rates are 8.58% for real property and 6.58% for personal property. The composition is as follows:

	<u>Real</u>	<u>Personal</u>
Basic property	6.50%	4.50%
Additional special property - state	1.03%	1.03%
Additional special property - municipal	1.25%	1.25%
Discounts made by state to tax payer	< .20% >	< .20% >
	<u>8.58%</u>	<u>6.58%</u>

The Municipality's basic property tax rate represents the portion which is appropriated for general purposes and accounted for in the general fund.

The "Additional special property tax - municipal" is restricted for debt service and retained by GDB for such purposes and it is recorded as revenue in the Debt Service Fund when collected by the CRIM and reported to the Municipality.

The "Additional special property tax - state" is collected by the CRIM for the payment of principal and interest of general obligation bonds and certain other obligations issued by the state government.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempted

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amounts, the Department of Treasury assumes payment of the basic tax to the Municipality, except for property assessed at less than \$3,500, for which no payment is made. Revenue related to the basic tax on exempt property is recorded in the General Fund when payments are received from the CRIM.

Complete exemption from personal property taxes up to an assessment of \$50,000 is granted to merchants with an annual volume of net sales less than \$150,000.

Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement 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 settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year ends. 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.

Currently, the Municipality has received the preliminary settlement from CRIM related to fiscal year 2007-08, but not the final settlement as the six months period after fiscal year ends, provided by law to CRIM to issue this, has not yet expired. Management believes, based in part on the experience from prior years, that when received, the final settlement from CRIM will not show a significant difference from the preliminary settlement and that such difference, if any, will not have a material effect on the financial condition of the Municipality.

Based on the preliminary settlement already received, for the year ended June 30, 2008, the amount received by CRIM, less than the amount collected from taxpayers and charges by CRIM received by the Municipality for the same period by approximately \$53,307. Such amount is presented as due from other governmental agencies in the general fund in the basic financial statements. (See Note 9).

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7. MUNICIPAL LICENSE TAX

Municipal License Tax is recorded in the fiscal year in which payment is due and, accordingly, represent taxes which are due and uncollected at June 30, 2008. The annual Municipal License Tax is determined based on the gross income of all commerce and industrial organizations who have operations in the Municipality of Guánica, and are not totally or partially exempt under the Industrial Incentive Law of Puerto Rico.

An annual return of business volume should be filed on or before April 15 of each year and payable in two equal installments due on July 1 and January 1. A discount of 5% is allowed when full payment is made on or before April 15. The rates of municipal license in the Municipality of Guánica, are as follows:

Savings and loans associations	= 1.50%
Financial institutions	= 1.50%
Other organizations:	= .50%

The amounts collected in advance are recorded as deferred revenues in the General Fund. The Municipality invoiced and collected in advance during the current year approximately \$228,000, corresponding to the next fiscal year municipal license.

8. SALES AND USE TAXES

On July 29, 2007 the Commonwealth Legislature approved Act No. 80 ("Act 80") which imposed to all the Municipalities of Puerto Rico a uniform municipal sales and use tax of 1.5%. Effective August 1, 2007 1% of the 1.5% will be collected by the Municipalities and the remaining .5% of the 1.5% will be collected by the Puerto Rico Department of Treasury.

Act 80 also provides for restrictions on the use of the resources (including the .5 of 1.5% collected by the Commonwealth Government) to be invested in solid waste and recycling programs, capital improvements and health and public safety costs. Amount collected by the Commonwealth Government will be deposited in accounts or special

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funds in the Governmental Development Bank of Puerto Rico ("GDB"), subject to restrictions imposed and distributed as follows:

- a. .2% of the .5% will be deposited in a "Municipal Development Fund" to finance costs as restricted by the Act,
- b. .2% of the .5% will be deposited in a "Municipal Redemption Fund" to finance loans to municipalities subject to restrictions imposed by the Act and,
- c. .1% of the .5% will be deposited in a "Municipal Improvement Fund" to finance capital improvement projects; these funds will be distributed based on legislation from the Commonwealth's Legislature.

9. DUE FROM OTHER AGENCIES

Represents grants and contributions due from local and federal agencies:

Municipal Revenues Collection Center (General Fund)	\$ 336,419
Puerto Rico Electric Power of Authority	230,926
Municipal Revenues Collection Center (Debt Service Fund)	5,556
Puerto Rico Labor Department	44,869
Department of Housing and Urban Development (Section 8)	99
Department of Housing and Urban Development (CDBG)	522,725
Governmental Development Bank of Puerto Rico	4,742
Commonwealth Legislative	510,446
Puerto Rico Department of Justice	999
	<hr/>
Total	<u>\$ 1,656,781</u>

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10. INTERFUND TRANSACTIONS

a. Due From/To Other Funds:

The due from and due to other fund balances as of June 30, 2008 are as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General Fund	Commonwealth Legislature Resolutions	\$ 314,627
General Fund	Section 8 Program	4,357
General Fund	Capital Improvement Loan Fund	28,187
General Fund	Other Governmental Fund	633,713
Commonwealth Legislature Resolutions	General Fund	1,805,282
Other Governmental Funds	General Fund	153,054
Other Governmental Funds	Other Governmental Funds	1,626
Other Governmental Funds	Commonwealth Legislature Resolutions	43,944
Capital Loan Improvement	Commonwealth Legislature Resolutions	20,773
Commonwealth Legislature Resolutions	Commonwealth Legislature Resolutions	<u>225,117</u>
		<u>\$3,230,680</u>

b. Interfund Transfers:

Interfund transfers for the year ended June 30, 2008 consisted of the following:

<u>Transfer In</u>	<u>Transfer Out</u>	<u>Amount</u>
General	Debt Services	\$ 18,201
Debt Services	General	669,098
Other Governmental Funds	General	<u>149,768</u>
Total		<u>\$837,067</u>

The transfer from the general fund to the debt service fund of \$669,098 represents monies transferred to cover debt service payments as become due.

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11. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2008 was as follows:

	Balance July 1, 2007	Increases	Decreases	Balance June 30, 2008
Capital assets, not being depreciated:				
Land	\$ 665,008	\$ -	\$ 292,324	\$ 372,684
Construction in progress	2,220,253	654,680	-	2,874,933
Total capital assets, not being depreciated	<u>2,885,261</u>	<u>654,680</u>	<u>292,324</u>	<u>3,247,617</u>
Capital assets, being depreciated:				
Buildings and building improvements	10,281,994			10,281,994
Infrastructure	6,780,118	688,035		7,468,153
Land improvements	2,892,996			2,892,996
Vehicles	1,791,242	116,968		1,908,210
Machinery and equipment	1,856,311	155,869		2,012,180
Equipment under capital leases	43,571			43,571
Total capital assets, being depreciated	<u>23,646,232</u>	<u>960,872</u>	<u>-</u>	<u>24,607,104</u>
Less accumulated depreciation for:				
Buildings and building improvements	2,717,852	207,395		2,925,247
Infrastructure	1,379,218	148,654		1,527,872
Land improvements	2,079,257	85,382		2,164,639
Vehicles	1,088,210	121,715		1,209,925
Machinery and equipment	795,515	115,040		910,555
Equipment under capital leases	38,070	-		38,070
Total accumulated depreciation	<u>8,098,122</u>	<u>678,186</u>	<u>-</u>	<u>8,776,308</u>
Total capital assets, being depreciated, net	<u>15,548,110</u>	<u>282,686</u>	<u>-</u>	<u>15,830,796</u>
Governmental activities capital assets, net	<u>\$ 18,433,371</u>	<u>\$ 937,366</u>	<u>\$ 292,324</u>	<u>\$ 19,078,413</u>

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

General government	\$ 144,084
Public safety	93,474
Public works	147,509
Culture and recreation	211,411
Public Housing and welfare	36,930
Economic development	<u>44,778</u>
Total	<u>\$ 678,186</u>

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12. DUE TO OTHER AGENCIES

Due to other agencies at June 30, 2008 are as follows:

Puerto Rico Electric Power of Authority	\$ 230,926
Puerto Rico General Services Administration	297,155
Puerto Rico Water and Sewer Authority	59,454
Puerto Rico Treasury Department	248,735
Retirement System Administration	303,005
State Insurance Fund Corporation	<u>30,234</u>
 Total	 <u><u>\$ 1,169,509</u></u>

13. DEFERRED REVENUES

a. Municipal License Tax

The deferred revenues of approximately \$227,325 in the general fund related to municipal license tax collected in fiscal year 2007-08 that will be earned in fiscal year 2008-09.

b. Federal Government

The deferred revenues presented as federal government represents the portion of federal grants received for which qualifying expenditures have not been incurred. The amounts were determined taking into consideration the specific years of the grant. These were related to the following federal programs/grants:

Program/Grant Description

Other governmental funds	<u><u>\$252,631</u></u>
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14. INTERGOVERNMENTAL REVENUES

Intergovernmental revenues in the general and capital projects funds consist mainly of collections from the Commonwealth of Puerto Rico and the CRIM, and payments in lieu of taxes from the Puerto Rico Electric Power Authority.

15. LONG-TERM DEBTS

Bonds and notes payable and other debt outstanding at June 30, 2008 are as follows:

Bonds

\$375,000 series of 1992, payable in annual installments of \$25,000 to \$50,000 until July 1, 2009, interest from 5% to 7.81%.	\$ 95,000
\$530,000 series of 2002, payable in annual installments of \$10,000 to \$40,000 until July 1, 2026, interest from 2.7% to 5.6%.	460,000
\$1,310,000 series of 2005, payable in annual installments of \$35,000 to \$105,000 until July 1, 2025, interest from 4.23% to 5.33%.	1,240,000
\$335,000 series of 2007, payable in annual installments of \$60,000 to \$80,000 until July 1, 2011, interest from 6.6% to 7.5%.	275,000
\$710,000 series of 2008, payable in annual installments of \$10,000 to \$60,000 until July 1, 2032, interest from 7% to 7.5%.	710,000
\$1,125,000 series of 1995, payable in annual installments of \$20,000 to \$110,000 until July 1, 2016, interest from 4.7% to 6.63%.	715,000
\$135,000 series of 2000, payable in annual installments of \$10,000 to \$20,000 until July 1, 2009, interest from 5% to 7.81%.	35,000
\$1,740,000 series of 2002, payable in annual installments of	

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\$10,000 to \$130,000 until July 1, 2026, interest from 5% to 6%.	\$1,525,000
\$1,270,000 series of 2008, payable in annual installments of \$15,000 to \$110,000 until July 1, 2032, interest from 7% to 7.5%.	1,270,000
\$805,000 series of 2008, payable in annual installments of \$10,000 to \$70,000 until July 1, 2032, interest from 7% to 7.5%.	805,000
\$1,210,000 series of 2008, payable in annual installments of \$85,000 to \$210,000 until July 1, 2017, interest from 7% to 7.5%.	1,210,000
\$145,000 series of 2005, payable in annual installments of \$10,000 to \$20,000 until July 1, 2014, interest from 5% to 8%.	<u>110,000</u>
Total bonds payable	<u>8,445,000</u>

Loan for payment of legal settlement - On December 1, 2003, the Municipality obtained a loan from the Puerto Rico Treasury Department to pay a legal settlement related to the Federal Civil Case No. 01-2692 (JP). The face amount of the loan was \$2,000,000 at no interest. This note has an imputed interest rate of 3.00% and was originally recorded at its present value of \$1,635,177, net of an unamortized discount of \$364,823, at inception.

1,424,775

Financing of the excess of property tax advances over collections - On November 4, 1999 the Municipality entered into a financing agreement with the Puerto Rico Treasury Department to pay a debt related to the excess of property tax advances over collections made by the Puerto Rico Treasury Department prior to the creation of CRIM in 1993.

449,165

The Municipality entered into a financing agreement with the Puerto Rico Department of Labor for a total amount of \$657,139 for unemployment benefits paid by the Commonwealth of

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Puerto Rico in behalf of the Municipality. The agreement is payable in monthly installments of \$15,059, including interest of 11.08% and due on October 5, 2010.	\$ 357,502
The Municipality entered into a financing agreement with the Puerto Rico Water and Sewer Authority for a total amount of \$60,000. The agreement is payable in monthly installments of \$5,000, due on October 1, 2009.	20,000
On October 22, 2003, the Municipality acquired a parcel of land from the Puerto Rico Land Authority in the amount of \$250,000 for which the Municipality issue a note payable. The note bears no interest and has an imputed interest rate of 6.00. The note was originally recorded at its present value of \$135,020, net of an unamortized discount of \$114,980, at inception.	118,064
\$1,061,453 note payable that represents a repayment agreement with GDB and CRIM to repay the excess of property taxes advances from fiscal years up to 2001. The repayment agreement is payable in annual aggregate principal installments of \$77,700 approximately, plus interest rate of 6.25% until July 1, 2032.	980,524
Note payable of \$178,730 represents a financing agreement with CRIM to the repayment of catastral digitalization. The agreement is due in semester payment of \$17,805 until November 28, 2011 at interest rate 6%.	55,731
Note payable of \$251,724 represents a financing agreement with CRIM to the repayment of bonds issued for the sale of delinquent accounts.	<u>83,527</u>
Total notes payable	<u>1,615,103</u>

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Other Long-Term Debts

Note payable to FEMA - This amount represent final disallowed costs as determined by an audit performed by the Governor's Authorized Representative (GAR) of FEMA funds related to Hurricane Georges. As of June 30, 2008, the outstanding balance amounts to \$750,467. The Municipality intends to pay the amount through a payment plan with FEMA which will be financed with unrestricted funds.

Compensated absences - Includes accrued vacations, sick leave benefits and other benefits with similar characteristics such as compensatory time, represents the Municipality's commitment to fund such costs from future operations. As of June 30, 2008, the outstanding balance amounts to \$1,409,895. This amount will be repaid with unrestricted funds.

Other claims and judgments - Represent the final costs of legal cases paid subsequent to June 30, 2008 and other claims outstanding as of that date. The awarded amounts will be paid with unrestricted funds. As of June 30, 2008, the outstanding balance amounts to \$64,524.

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As described in Note 6, the Municipality levies an annual special tax of 1.25% of the assessed value of real property. The proceeds of this tax are required to be credited to the Debt Service Fund for payment of general obligation bonds and notes of the Municipality. The property taxes are collected and retained by the CRIM.

<u>Primary Government</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Payments</u>	<u>Ending Balance</u>	<u>Due within One Year</u>
Governmental Activities:					
Bonds payable	\$ 4,735,000	\$ 3,995,000	\$ 285,000	\$ 8,445,000	\$ 415,000
Total long-term debt	4,735,000	3,995,000	285,000	8,445,000	415,000
Other Long-Term Liabilities:					
Treasury Department:					
Loan for payment of legal settlement	1,530,309		105,534	1,424,775	159,437
Excess of property taxes	463,026		13,861	449,165	14,876
PR Labor Department	572,502		215,245	357,257	147,614
PR Land Authority	118,064			118,064	
CRIM-Law 42	997,324		16,800	980,524	17,856
CRIM-LIMS	69,663		13,932	55,731	14,774
CRIM-Delinquent accounts	87,007		3,480	83,527	3,480
CRIM-Excess of property tax advances	-			-	
PR Water and Sewer Authority		60,000	40,000	20,000	20,000
Payable to FEMA	750,467			750,467	
Compensated absences	1,206,095	203,800		1,409,895	80,000
Claims and judgments	64,524			64,524	
Obligation under capital leases	-			-	
Christmas bonus	198,039		11,038	187,001	187,001
Total other liabilities	6,057,020	263,800	419,890	5,900,930	645,038
Total noncurrent liabilities	<u>\$ 10,792,020</u>	<u>\$ 4,258,800</u>	<u>\$ 704,890</u>	<u>\$ 14,345,930</u>	<u>\$ 1,060,038</u>

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The annual requirements for the amortization of bonds payable at June 30, 2008, are as follows:

	<i><u>Bonds Payable</u></i>	
	<u>Principal</u>	<u>Interest</u>
2009	\$ 415,000	\$ 338,745
2010	455,000	528,168
2011	405,000	517,343
2012	445,000	489,458
2013	385,000	461,232
2014-2018	1,670,000	1,854,853
2019-2023	2,105,000	1,203,404
2024-2028	1,665,000	633,804
2029-2033	900,000	205,500
	<u>\$ 8,445,000</u>	<u>\$ 6,232,507</u>

16. RETIREMENT PLAN

a. Plan Description

The Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) is the administrator of a cost-sharing multiple-employer retirement system established by the Commonwealth of Puerto Rico. The System was created under the Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952.

ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentalities and of certain municipalities and components units not covered by their own retirements systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Heads for Agencies and Public Instrumentalities, Assistants to the Governor, the Comptroller of Puerto Rico, Gubernatorial Board and Committee appointees and Experimental Service Station employees.

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ERS provides retirement, death and disability benefits. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

Members who have attained an age of at least fifty-five (55) years and have completed at least twenty-five (25) years of creditable service or members who have attained an age of at least fifty-eight (58) years and have completed at least fifty-eight (58) years and have completed at least ten (10) years of creditable service, are entitled to an annual benefit, payable monthly for life.

The amounts of the annuity will be one and one-half percent of the average compensation multiplied by the number of years of creditable service up to twenty years, plus 2% of the average compensation multiplied by the number of years of creditable service in excess of twenty years. In no case the annuity will be less than \$200 per month.

Participants who have completed at least thirty (30) years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained fifty-five (55) years of age will receive 65% of the average compensation or if they have attained fifty-five (55) years of age will receive 75% of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten (10) years of service.

No benefit is payable if the participant receives a refund of his accumulated contributions.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created ERS, was enacted with the purpose of establishing a new pension program (System 2000). Employees participating in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Municipality on or after January 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.

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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. Benefits at retirement age will not be guaranteed by the Commonwealth of Puerto Rico. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary upon 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 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.

b. Contribution Requirements

Commonwealth legislation requires employees to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600. The Municipality's contributions are 9.275% of gross salary. Contributions' requirements are established by law. The actuarially determined contribution requirement and contributions actually made for the year ended June 30, 2008 was approximately \$232,932. The Municipality's payroll for employees covered by ERS was approximately \$2.5 million. The Municipality total payroll for all employees was approximately \$4.2 million.

Additional information on the ERS is provided in its financial statements for the year ended June 30, 2008, a copy of which can be obtained from the ERS, Minillas Station, PO Box 42003, San Juan, PR 00940.

17. RISK MANAGEMENT

The Risk Management Division of the Municipality's Legal Department is responsible of assuring that the Municipality's property is properly insured. Annually, the Risk Management Division compiles the information of all property owned and its respective market value. After evaluating this information, the Risk Management 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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

who is responsible for purchasing all property and casualty insurance policies of all municipalities.

18. CONTINGENCIES

- a. The Municipality receives Federal Grants for specific purposes that are subject to review and audit by the grantor agencies. Although such audits could generate expenditure disallowances under the terms of the grants, management believes that any required reimbursements would not be material.
- b. The Municipality is a defendant and/or co-defendant in various lawsuits which claims for actual damages. Some of these lawsuits are covered by insurance. The Municipality's management and outside counsels believe that is probable that any potential liability that might exist, if any, in excess of the insurance, will not affect significantly the financial position of the Municipality.

19. COMMITMENTS

The Municipality of Guánica had several outstanding or planned construction projects as of June 30, 2008. These projects are evidenced by contractual commitments with contractors. The construction projects are commitments of the Capital Projects' funds that amounted to approximately \$2.1 million.

20. RESTATEMENTS

Fund Balances

The beginning fund balance of the general fund and other governmental fund were restated to reclassify fund balance.

	General Fund	Other Governmental Fund
Beginning fund balance, as previously reported	\$(1,938,708)	\$ (461,305)
Reclassification of funds balances	71,422	(71,422)
Beginning fund balance, as restated	\$(1,867,286)	\$ (532,727)

PART II - SINGLE AUDIT SECTION

-52-

ORTIZ, RIVERA, RIVERA & CO.

CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal Disbursements/ Expenditures</u>
U.S. Department of Housing and Urban Development (HUD)		
Pass-through State -Commissioner Office of Municipal Affairs - Community Development State Block Grant Program - SBGP	14.228	\$ 1,170,334
Section 8 Housing Choice Vouchers	14.871	212,191
Subtotal U.S. Department of HUD		<u>1,382,525</u>
U.S. Department of Commerce		
Grant for Public Works and Economic Development	11.300	11,525
Subtotal U.S. Department of Commerce		<u>11,525</u>
U.S. Department of Agriculture		
Passed through the Puerto Rico Department of Education:		
Child and Adult Care Food Program	10.558	9,466
Subtotal U.S. Department of Agriculture		<u>9,466</u>
U.S. Department of Health and Human Services (HHS)		
Pass-through de Puerto Rico Department of Family - Families and Children Administration:		
Child Care and Development Block Grant	93.575	95,831
Subtotal U.S. Department of HHS		<u>95,831</u>
U.S. Department of Homeland Security-Federal Emergency Management Agency (FEMA)		
Pass-through de Puerto Rico Governor's Office (Governor's Authorized Representative - GAR):		
Hazard Mitigation Grant Program		
Subtotal U.S. Department of FEMA	97.039	51,401
TOTAL		<u>\$ 1,550,748</u>

See notes to schedule of expenditures of federal awards.



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Management Consulting
Services Division

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Honorable Mayor
and Municipal Legislature
Municipality of Guánica
Guánica, Puerto Rico

We have audited the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Guánica as of and for the year ended June 30, 2008, which collectively comprise the Municipality of Guánica's basic financial statements, and have issued our report thereon dated December 23, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

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

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control

deficiency, or combination of control deficiencies, that adversely affects the Municipality's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Municipality's financial statements that is more than inconsequential will not be prevented or detected by the Municipality's internal control. We consider the deficiencies described in the accompanying schedule of findings and responses to be significant deficiencies in internal control over financial reporting and include as items 07-A and 07-B.

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.

Our consideration of 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 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, we consider items 07-A and 07-B to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality of Guánica's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect of the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our test disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Municipality's response to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit Municipality's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the management, Commissioner Office of Municipal Affairs, and the federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

San Juan, Puerto Rico
December 23, 2008

The stamp 2386836 was affixed
to the original of this report.



Ortiz, Rivera, Rivera & Co.

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**INDEPENDENT AUDITOR'S 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 Municipal Legislature
Municipality of Guánica
Guánica, Puerto Rico

Compliance

We have audited the compliance of Municipality of Guánica 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, 2008. Municipality of Guánica's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Municipality of Guánica's management. Our responsibility is to express an opinion on Municipality of Guánica's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Municipality of Guánica's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Municipality of Guánica's compliance with those requirements.

In our opinion, the Municipality of Guánica, in all material respects, with the requirements referred to above that are applicable to the major federal program for the year ended June 30, 2008.

Internal Control over Compliance

The management of Municipality of Guánica is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Municipality of Guánica's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control over compliance.

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.

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.

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

This report is intended solely for the information of the audit committee, Commissioner Office of Municipal Affairs, management and the federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ortiz, Rivera, Rivera & Co.

San Juan, Puerto Rico
December 23, 2008

The stamp 2386837 was affixed
to the original of this report



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

1. SUMMARY OF AUDIT RESULTS

- a. The auditors' report expresses an unqualified opinion on the basic financial statements of the Municipality of Guánica.
- b. There were no significant deficiencies on internal controls.
- c. Instances of noncompliance material to the financial statements of Municipality of Guánica were disclosed during the audit.
- d. There were no significant deficiencies on internal controls over major programs.
- e. The auditor's report on compliance for the major federal award programs for Municipality of Guánica express an unqualified opinion.
- f. Audit findings relation to the major federal award programs for Municipality of Guánica are reported in number 3 of this schedule.
- g. The programs tested as major programs are:
 - SBGP - CFDA No. 14.228
- h. The threshold for distinguishing types A and B programs was \$300,000.
- i. Municipality of Guánica was determined to be a high-risk auditee.

2. FINDINGS - FINANCIAL STATEMENTS AUDIT

08-A: General Fund Deficit

Condition

As of June 30, 2008, the Municipality closed the general fund with an accumulated deficit of \$2.7 million. For the fiscal year ended, the Municipality reported a net change in general fund balance of (\$898,221).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

1. SIGNIFICANT ACCOUNTING POLICIES

The accompanying Schedule of Expenditures of Federal Awards is a summary of the activity of the Municipality of Guánica's federal award programs presented on the modified accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

2. BASIS OF PRESENTATION

The expenditures of the schedule are included in the Municipality's basic financial statements in the accompanying Statement of Revenues, Expenditures and Changes in Fund Balances-Governmental Funds. The reconciliation of expenditures in the basic financial statements to the Schedule of Expenditures of Federal Awards is as follows:

Expenditures as per basic financial statements:	
Included within other governmental funds	\$1,338,557
Section 8 Program	<u>212,191</u>
Total federal expenditures per schedule	<u>\$1,550,748</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Cause

The deficit is caused by the overestimation of budgeted revenues and by the incurrence of obligations without the proper consideration of current and future available resources. The mayor and the Finance Director did not follow adequate budgeting procedures.

Criteria

Article 7.011(a) of Autonomous Municipal Act (Law 81 of August 30, 1991), as amended, establishes that municipalities with deficits at their closing dates must provide for sufficient resources during the next fiscal year period in order to cover such deficit.

Section 3 of the Revised Regulation over Basic Standards for Municipalities of Puerto Rico (The Regulation) states that special care must be provided for the estimation of future revenues in order to avoid budget appropriations in excess of available resources.

Recommendation

The continuing deficit reported by the Municipality of Guánica may harm the basic governmental services provided to its citizens. We strongly recommend that the necessary measures are taken in order to stop this trend. The Municipality must work on increasing actual revenues and/or substantially reducing expenditures.

07-B: Estimated Revenue Shortfall

Condition

As of June 30, 2008, the Municipality did not meet certain projected revenues by significant amounts, causing an increase in its General Fund deficit (see Finding 07-A). The following deficiencies were noted based on our comparison of budgeted revenues versus final operating results:

- a. For charges for services and rent, the Municipality failed to meet its expectations by \$23,257.
- b. For state contributions, the Municipality failed to meet its expectations \$426,362.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

- c. For licenses and permits, the Municipality failed to meet its expectations by \$729,424.
- d. For economic development, the Municipality excise their expectation by \$437,796.

Criteria

Section 3 of the Revised Regulation over Basic Standards for Municipalities of Puerto Rico (The Regulation) states that special care must be provided for the estimation of future revenues in order to avoid budget appropriations in excess of available resources.

Cause

The Mayor and the Finance Director did not follow adequate budgeting procedures for establishing reasonable estimates.

Recommendation

The Municipality should revise and amend the budget as current information related to collections of budgeted revenues became available.

**3. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAM
AUDIT**

None

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF STATUS OF PRIOR YEAR
AUDIT FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

During the current examination, follow-up was given to the findings informed to the Municipality in prior years. It was noted that corrective action has been taken, except for certain conditions that still exist and require further action. These are included in the accompanying Schedule of Prior Year Audits Findings and Questioned Costs.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF STATUS OF PRIOR YEAR
AUDIT FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

<u>Program</u>	<u>Finding/Noncompliance</u>	<u>Status</u>
SBGP CFDA No. 14.228	Condition 07-1 The Municipality has excess cash in bank for an unreasonable period on time after transfer of funds by the pass-through entity. The Municipality maintained an average monthly excess of cash of \$45,444 during the fiscal year 2006-2007.	Condition was corrected.
Section 8 Voucher CFDA No. 14.871	Condition 07-2 The program did not comply with the procedures require for minimizing the time elapsing between the transfer of federal funds and the disbursement by grantees. In addition, the program maintains a high balance in bank.	Condition was observed.



ESTADO LIBRE ASOCIADO DE PUERTO RICO
MUNICIPIO DE GUANICA
OFICINA DE AUDITORIA INTERNA

Sra. Iris N. Quiñones González
Auditora Interna Interina

March 31, 2009

OCAM
PO Box 70167
San Juan, PR 00936-8167

RECIBIDO
UNIDAD DE CORREO
9 MAR 31 AM 11:27
Café-1100

To whom it may concern:

Accompanied herewith please find (1) copy of our Financial Statements and Report of Independent Certified Public Accountants with Additional Reports required under the OMB Circular A-133 for Municipality of Guánica for the year ended June 30, 2008.

Should you have question regarding to the above mentioned, please let us know.

Cordially yours,


Iris N. Quiñones González
Interim Internal Auditor

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DIVISION REGULATORIA
E INTERVENCION

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