

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA, PUERTO RICO**



***BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY
INFORMATION AND INDEPENDENT
AUDITOR'S REPORT***

***AS OF AND FOR THE FISCAL YEAR ENDED
JUNE 30, 2013***



***Hon. Santos Seda Nazario
Mayor***

***Mr. Daniel Rodríguez
Finance Director***

29

TABLE OF CONTENTS

<u>FINANCIAL SECTION</u>	<u>PAGE</u>
Independent Auditor's Report	1-2
Management's Discussion and Analysis	3-8
Basic Financial Statements:	
Government-wide Financial Statements:	
Statement of Net Position	9
Statement of Activities	10
Governmental Funds' Financial Statements:	
Balance Sheet – Governmental Funds	11
Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds	12
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position	13
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balance of Governmental Funds to the Statement of Activities	14
Notes to Basic Financial Statements	15-43
Required Supplementary Information:	
Budgetary Comparison Schedule – General Fund	44
Note to Required Supplementary Information - Budgetary Comparison Schedule – General Fund	45

INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and Member of the
Municipal Assembly
Guánica, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Municipality of Guánica, Puerto Rico, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Basis for Adverse Opinion on Governmental Activities

Because of the inadequacy of accounting records for the year 2013, we were unable to obtain sufficient appropriate audit evidence regarding the amounts at which capital assets, accumulated depreciation, and net investment in capital assets, are recorded in the accompanying statement of net position at June 30, 2013 (stated at \$36,379,579, \$17,494,669, and \$13,893,810, respectively), the amount of depreciation expenses for the year then ended (stated at \$4,950,464).

Management has not capitalized certain acquisition of properties and equipment and the construction in progress in governmental activities and, accordingly, such disbursements are recognized as expenses in the statement of activities. Accounting principles generally accepted in the United States of America require that those assets be capitalized, which would increase the assets, net position and decrease the expenses of the governmental activities. The amount by which this departure would affect the assets, net position, and expenses of the governmental activities has not been determined.

Adverse Opinion

In our opinion, because of the significant effects of the matter discussed in the "Basis for Adverse Opinion" paragraph, the financial statements referred to above do not present fairly, in all material respects, the respective financial position of the governmental activities of Municipality of Guánica, Puerto Rico, as of June 30, 2013, and the changes in financial position thereof for the year then ended.

Unmodified 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, Puerto Rico, as of June 30, 2013, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

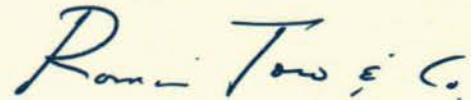
Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary information on pages 3 through 8 and 44 through 45 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 25, 2014, on our consideration of the Municipality of Guánica, Puerto Rico's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Municipality of Guánica, Puerto Rico's internal control over financial reporting and compliance.



ROMAN TORO & CO., CPA, C.S.P.
LICENSE # 35 - IN FORCE

Yauco, Puerto Rico
March 25, 2014

Stamp #E93383 was affixed to
the original report



Our discussion and analysis of the **Municipality of Guánica's** financial performance provides an overview of the Municipality's financial activities for the fiscal year ended June 30, 2013. 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.

The reporting model, required by Governmental Accounting Standards Board Statement No. 34, was implemented during the fiscal year 2003-2004. This MD&A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

- a broader basis in focusing important issues;
- acknowledgment of an overview of the Municipality's financial activities;
- provide for an evaluation of its financial condition as of the end of indicated fiscal year, compared with prior results;
- identification of users of funds in the financing of the Municipality's activities and;
- asset management's ability to handle budgetary functions.

FINANCIAL HIGHLIGHTS

Highlights for Government-wide Financial Statements

The government-wide financial statements use the economic resources measuring focus and the accrual basis of accounting to report information about the Municipality as a whole:

- Total assets of the Municipality, on a government-wide basis, exceed its liabilities at the close of fiscal year 2013 by \$ 3,050,694 (net position).
- Revenues increase 11% while expenses had change 53%, when compared with fiscal year 2012.
- Net change (deficit) in net position amounted to \$ (6,155,582), a decrease of approximately 1,405% with respect to the prior year's net change of \$(408,922).

Highlights for Fund Financial Statements

The fund financial statements provide detailed information about the Municipality's most significant funds. These financial statements use the current financial resources measurement focus and modified accrual basis of accounting.

- A net change in the fund balance of the Municipality's governmental funds in the amount of \$ 1,146,917 in the fiscal year 2013 resulted in reported ending fund deficit of \$ (1,411,519). This fund balance includes a net unassigned deficit in the amount of (\$ 5,171,113).
- For the year 2013 the General Fund reported an excess of revenues and other financial sources over expenditures and other financial uses of \$1,003,152 and an unassigned fund deficit of (\$5,171,113).

General Financial Highlights

- The investment in capital assets as of June 30, 2013 was \$13,184,910 (net of depreciation).
- Long-term debt increase of \$2,473,399 or approximately a 20% increase with respect to the prior year.

FINANCIAL HIGHLIGHTS (CONTINUED)

This annual report consists of a series of financial statements. The Statement of Net Position 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 Municipality's 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.

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 overview of the Municipality's operations and finances 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 position and the statement of activities.

The Statement of Net Position and the Statement of Activities

The Statement of Net Position 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 position* and changes in them. You can think of the Municipality's net position, 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 position 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 assess the *overall health* of the **Municipality of Guánica**.

In the Statement of Net Position and the Statement of Activities, we present the Municipality 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.

FINANCIAL HIGHLIGHTS (CONTINUED)

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.

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 Position 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 position decreased from a year ago, from \$9,206,278 million to \$ 3,050,694 million. Our analysis below focuses on the net position (Table 1) and changes in net position (Table 3) of the Municipality's governmental activities. This change is mainly due to the increase in the accumulated depreciation of the Capital Assets and the issuance of bonds and notes that amounted to \$3,995,000.

Table 1
NET POSITION
(in Million)

	Governmental Activities	
	2013	2012 As restated
Current and other assets	\$ 5,064,615	\$4,516,416
Capital assets	18,884,910	23,930,887
Total assets	23,949,525	28,447,303
Current liabilities	5,761,134	6,576,727
Long-term debt outstanding	15,137,697	12,664,298
Total liabilities	20,898,831	19,241,025
Net position:		
Net investment in capital assets,	13,184,910	19,324,639
Restricted for:		
Debt services	1,929,757	2,313,304
Special purposes	989,310	72,452
Capital project	840,527	447,894
Unrestricted (Deficit)	(13,893,810)	(12,952,011)
Net Position	\$3,050,694	\$9,206,278

THE MUNICIPALITY AS A WHOLE (CONTINUED)

Net Position of the Municipality's governmental activities decreased by \$6,155,582. *Unrestricted* net position, the part of net position that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements, changed by approximately \$ 5.9 million at June 30, 2013. 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:

	<u>2013</u>	<u>2012</u> <u>As restated</u>
Revenues:		
Program revenues:		
Operating grants and contributions	\$ 2,519,465	\$ 1,684,032
Capital grants and contributions	551,437	282,904
Charges for services	1,826,544	1,944,099
General revenues:		
Property taxes	1,850,167	1,793,542
Municipal license taxes	349,460	286,453
Sales tax	1,074,510	334,693
Grants and contributions not restricted to specific program	6,099,991	6,078,594
License and permits and other local taxes	252,258	552,964
Interests, fines and penalties	229,086	114,326
Miscellaneous	66,574	229,927
Total revenues	<u>14,819,492</u>	<u>13,301,534</u>
Expenses:		
General government	3,213,805	5,497,583
Public works	8,451,527	944,702
Public Safety	1,127,774	1,331,351
Culture and recreation	2,531,668	895,036
Health and sanitation	1,943,221	3,232,590
Human services and welfare	3,100,873	1,497,772
Urban and Economic Development	120,156	-
Interests	486,050	311,422
Total expenses	<u>20,975,075</u>	<u>13,710,456</u>
Net (decrease) increase in net position	(6,155,582)	(408,922)
Net position-at the beginning of the year, as restated	9,206,278	9,615,200
Net position- at end of the year	<u>\$ 3,050,694</u>	<u>\$ 9,206,278</u>

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 spend able resources. Such information is useful in assessing the Municipality's financial requirements. In particular, unreserved fund balance may serve as an useful measure of a government's net resources available for spending at the end of fiscal year.

Total revenues of Municipality's governmental activities increased by \$1,517,958; while total expenses increase by \$7,264,618. The **Municipality of Guánica** took the following major actions this year to improve the financial position:

- The Mayor of the **Municipality of Guánica** assigned personnel 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 with respect to 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.

THE MUNICIPALITY AS A WHOLE (CONTINUED)

Expenses during the fiscal year ended June 30, 2013 was substantially related to the following:

	Total expenses	
	2013	2012
General government	\$ 3.66	\$ 5.21
Public safety	.92	.84
Public works	6.13	1.04
Culture and recreation	.71	.70
Health and sanitation	1.97	3.21
Human service and welfare	3.07	1.48
Debt service	1.2	1.56
Capital outlays		.89
Totals	17.66	14.93

The cost of all governmental activities this year was \$ 17.66 millions compared to \$14.93 million last year.

Table 2 presents the cost of each of the Municipality of Guánica's largest programs.

	General Revenues by major sources	
	2013	2012
Property taxes	\$ 1.9	\$ 1.80
Municipal license taxes	.35	.29
Sale tax	1.07	.89
Grants and contributions	9.13	8.03
Totals	\$ 12.45	\$ 11.01

The major sources of general revenue are property taxes, municipal license taxes, sales tax and grant and contributions not restricted, which in total represent 12.45 (46%) of all revenues in 2013 and 10.07 (84%) 2012, respectively.

	Program Revenues by major sources	
	2013	2012
Charges for service	\$ 1.82	\$ 1.94
Operating Grants and Contribution	2.51	1.68
Totals	\$ 4.33	\$ 3.62

THE MUNICIPALITY AS A WHOLE (CONTINUED)

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.

Budget and actual comparison schedules are provided in the Basic Financial Statements for the General Fund. The Budgetary Comparison Schedule of the General Fund shows the original adopted budgets, the final revised budget, actual results, and variance between the final budget and actual result for the general and major special funds.

Capital Assets

As of June 30, 2013, the **Municipality of Guánica** had \$ 18.88 million invested in a broad range of capital assets, including buildings, parks, roads, bridges, and equipment. This amount represents a net decrease (including additions and deductions) of \$ 5,045,977, or .17%, under last year.

Long-term debt

The Municipality had a total of \$15,137,697 in general obligations and others outstanding debts. Of this amount, \$12,320,000 are bonds and notes and the remainder \$ 2,817,697 are other long term obligations.

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 other installment payment agreements with various governmental agencies.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's elected and appointed officials considered many factors when setting the fiscal-year 2013-2014 budget. 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 2014.

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.

	<u>Governmental Activities</u>
Assets	
Cash and cash equivalents	\$ 605,431
Cash with fiscal agent	4,003,516
Accounts receivable:	
Intergovernmental	455,668
Capital assets	
Land, improvements, and construction in progress	1,523,706
Other capital assets, net of depreciation	17,361,204
Total capital assets	<u>18,884,910</u>
Total assets	<u>23,949,525</u>
Liabilities	
Accounts payable and accrued liabilities	3,361,371
Due to other governmental entities	1,477,553
Deferred revenues:	
Municipal license tax	289,850
Federal grant revenues	35,691
Intergovernmental	339,839
Interest payable	256,830
Noncurrent liabilities:	
Due within one year	920,417
Due in more than one year	14,217,280
Total liabilities	<u>20,898,831</u>
Net Position	
Net investment in capital assets	13,184,910
Restricted for:	
Capital projects	840,527
Debt service	1,929,757
Other purposes	989,310
Unrestricted (deficit)	<u>(13,893,810)</u>
Total net position	<u>\$ 3,050,694</u>

The notes to the financial statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUANICA

Statement of Activities
For the Year Ended June 30, 2013

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and
		Charges for	Operating	Capital	Changes in Net Assets
		Services	Grants and	Grants and	Governmental
			Contributions	Contributions	Activities
General government	\$ 3,213,805	\$ 49,301	\$ 100,680	\$ -	\$ (3,063,824)
Public safety	1,127,774		56,172		(1,071,602)
Public works	8,451,527		145,633	551,437	(7,754,457)
Human services and welfare	3,100,874		2,027,449		(1,073,425)
Culture and recreation	2,531,668	10,557			(2,521,111)
Urban and economic development	120,156	1,766,686	189,531		1,836,061
Health and sanitation	1,943,221				(1,943,221)
Interest on long-term debt	486,050				(486,050)
Total governmental activities	\$ 20,975,075	\$ 1,826,544	\$ 2,519,465	\$ 551,437	(16,077,629)

General revenues:

Property taxes	1,850,167
Municipal sales and use tax	1,074,511
Municipal license tax	349,460
Other local taxes	252,258
Grants and contributions not restricted to specific programs	6,099,991
Interest and investment earnings	229,086
Miscellaneous	66,574
Total general revenues	9,922,047
Change in net position	(6,155,582)
Net position - beginning, as restated	9,206,276
Net position - ending	\$ 3,050,694

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUANICA

Balance Sheet-Governmental Funds
June 30, 2013

	General Fund	Commonwealth Legislature Resolutions	Debt Service Fund	Loans Fund	Community Development Block Grant	Other Governmental Funds	Total Governmental Funds
Assets							
Cash and cash equivalents	\$ -	\$ 8,611	\$ -	\$ -	\$ 4,928	\$ 591,892	\$ 605,431
Cash with fiscal agent			2,892,384	1,091,768		19,364	4,003,516
Accounts receivable:							-
Intergovernmental	30,373		9,202			12,784	52,359
Federal grants					188,918	214,391	403,309
Due from other funds	905,899	1,347,434				389,025	2,642,358
Total assets	\$ 936,272	\$ 1,356,045	\$ 2,901,586	\$ 1,091,768	\$ 193,846	\$ 1,227,456	\$ 7,706,973
Liabilities and Fund Balances							
Liabilities :							
Accounts payable and accrued liabilities	\$ 2,896,382	\$ -	\$ -	\$ 166,231	\$ 175,813	\$ 122,945	\$ 3,361,371
Due to other governmental entities	1,418,330			59,223			1,477,553
Due to other funds	1,502,823	589,791		180,215	18,033	351,496	2,642,358
Bonds and Notes Payable			715,000				715,000
Accrued interest			256,830				256,830
Unearned revenues:							
Municipal license tax	289,850						289,850
Intergovernmental						339,839	339,839
Federal grant revenues						35,691	35,691
Total liabilities	6,107,385	589,791	971,830	405,669	193,846	849,971	9,118,492
Fund balances:							
Restricted		766,254	1,929,756	686,099		74,746	3,456,855
Committed						302,739	302,739
Unassigned	(5,171,113)						(5,171,113)
Total fund balances	(5,171,113)	766,254	1,929,756	686,099	-	377,485	(1,411,519)
Total liabilities and fund balances	\$ 936,272	\$ 1,356,045	\$ 2,901,586	\$ 1,091,768	\$ 193,846	\$ 1,227,456	\$ 7,706,973

The notes to the financial statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUANICA

Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2013

	General Fund	Commonwealth Legislature Resolutions	Debt Service Fund	Loans Fund	Community Development Block Grant	Other Governmental Funds	Total Governmental Funds
Revenues							
Property taxes	\$ 1,384,271	\$ -	\$ 465,896	\$ -	\$ -	\$ -	\$ 1,850,167
Municipal license taxes	349,460						349,460
Municipal sales and use tax	325,550		748,959				1,074,509
Licenses, permits and other local taxes	252,258						252,258
Charges for services	1,781,019					45,525	1,826,544
Intergovernmental	6,099,991	51,024				657,264	6,808,279
Interest, fines and penalties	228,960					126	229,086
Federal grants					1,522,501	811,369	2,333,870
Miscellaneous	66,574					28,744	95,318
Total revenues	10,488,083	51,024	1,214,855	-	1,522,501	1,543,028	14,819,491
Expenditures							
Current							
General government	3,105,366			452,603		105,323	3,663,292
Public safety	843,540					77,400	920,940
Public works	5,619,042	78,426		960		432,800	6,131,228
Human services and welfare	760,676				1,522,501	783,151	3,066,328
Culture and recreation	711,915						711,915
Health and sanitation	1,972,821						1,972,821
Debt service:							
Principal			715,000				715,000
Interest			486,050				486,050
Total expenditures	13,013,360	78,426	1,201,050	453,563	1,522,501	1,398,674	17,667,574
Excess (deficiency) of revenues over (under) expenditures	(2,525,277)	(27,402)	13,805	(453,563)	-	144,354	(2,848,083)
Other financing sources (uses)							
Transfers in	3,621,076		92,647				3,713,723
Transfers out	(92,647)			(3,621,076)			(3,713,723)
Long-term debt issued				3,995,000			3,995,000
Total other financing sources (uses)	3,528,429	-	92,647	373,924	-	-	3,995,000
Net change in fund balances	1,003,152	(27,402)	106,452	(79,639)	-	144,354	1,146,917
Fund balance, beginning as restated	(6,174,265)	793,656	1,823,304	765,738	-	233,131	(2,558,436)
Fund balance, ending	\$ (5,171,113)	\$ 766,254	\$ 1,929,756	\$ 686,099	\$ -	\$ 377,485	\$ (1,411,519)

Handwritten notes:
 1/27/14
 O'Neil
 a lot of work
 (854,881)

The notes to the financial statements are an integral part of this statement.

Total Fund Balances - Governmental Funds **\$ (1,411,519)**

Amounts reported for Governmental Activities in the Statement of Net Position are different because:

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

Non Depreciable Capital Assets	\$1,523,706	
Depreciable Capital Assets, net of depreciation	<u>17,361,204</u>	
Total Capital Assets		18,884,910

Bonds and notes matured recognized on Fund Financial Statements 715,000

Some liabilities are not due and payable in the current period and therefore, are not reported in the funds. Those liabilities consist of:

General bonds and notes payable	12,320,000	
Revenue Department -loan for payment of legal settlement	524,892	
Property tax debt-Law No. 42	879,296	
Compensated absences	1,388,909	
Claims and judgments	<u>24,600</u>	
Total Long-Term Liabilities		<u>(15,137,697)</u>

Total Net Position of Governmental Activities **\$ 3,050,694**

The notes to the financial statements are an integral part of this statement.

Net Change in Fund Balances - Total Governmental Funds	\$ 1,146,917
Amounts reported for governmental activities in the Statement of Activities are different because:	
Bonds and notes mature are recognized in the Governmental Fund Financial Statements, but they do not require the use of current financial resources. The following amount represents the change in long-term bonds and notes mature from prior year.	225,000
Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Position, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period.	375,819
Depreciation expense on capital assets is reported in the Government-Wide Statements of Activities and Change in Net Position, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds.	(5,326,283)
Governmental Funds report capital assets sold as revenues. However, in the Government-Wide Statement of Activities and Changes in Net Position, Disposal of capital assets require removal of cost of the capital assets from the capital asset account on the Government-Wide Statement of Net Position.	(95,513)
Bonds and notes proceeds provide current financial resources to Governmental Funds, but issuing debt increase long-term liabilities in the Government-Wide statement of Net Position. Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long-term liabilities in the Government-Wide Statement of Net Position. This is the amount by which the debt service principal payments exceed debt proceeds.	(3,505,000)
Property tax debt related to Law No. 42 repayment plan, was reported in the Government-Wide Statement of Activities and Change in Net Position. Repayment of long term property tax advance debt is an expenditure in Governmental Funds, but the repayment reduces long-term property tax advance debt in the Government-Wide Statement of Net Position. The following represented the change in property tax debt.	22,785
Repayment of long term Puerto Rico Treasury Department is an expenditure in Governmental Funds, but the repayment reduces long term debt in the Government-Wide Statement of Net Position. The following amount represent the change in long term debt from prior year.	674,775
Puerto Rico Treasury Department payment plan, was reported in the Government-Wide Statement of Activities and Change in Net Position, Repayment of long term payment plan debt is an expenditure in Governmental Funds, but the repayment reduces long-term payment plan in the Government-Wide Statement of Net Position. The following represented the change in PR Treasury Department debt.	46,200
Puerto Rico Labor Department payment plan, was reported in the Government-Wide Statement of Activities and Change in Net Position. Repayment of long term payment plan debt is an expenditure in Governmental Funds, but the repayment reduces long-term payment plan in the Government-Wide Statement of Net Position. The following represented the change in the PR Labor Department debt.	91,950
Puerto Rico Treasury Department payment plan, was reported in the Government-Wide Statement of Activities and Change in Net Position. Repayment of long term payment plan debt is an expenditure in Governmental Funds, but the repayment reduces long-term payment plan in the Government-Wide Statement of Net Position. The following represented the change in the PR Treasury Department debt.	60,000
Long-term compensated absences are reported in the Government-Wide Statement of Activities and Changes in Net Position, but they do not require the use of current financial resources. Therefore, long-term compensated absences were not reported as expenditures in Governmental Funds. The following amount represents the change in long-term compensated absences from prior year.	40,492
Amortization of bond issuance cost was reported in the Government-Wide Statement of activities and Change in Net Position. The following represented the change in the amortization of bond issuance cost.	(8,124)
Long-term claims and judgments and other notes payables are reported in the Governmental-Wide Statement of Activities and Changes in Net Position, but they do not require the use of current financial resources. Therefore, claims and judgments are not reported as expenditures in Government Funds. The following amount represents the change in long-term claims and judgments from prior year.	95,400
Change in Net Position of Governmental Activities	\$ (6,155,582)

The notes to the financial statements are an integral part of this statement.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Guánica** of the Commonwealth of Puerto Rico (the "Municipality") was founded in 1771. The Municipality is a local government with full legislative, fiscal and administrative powers to operate as a government under Law No. 81 of August 30, 1991, as amended, known as the *Autonomous Municipalities Act of the Commonwealth of Puerto Rico (Law No. 81)*.

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

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

The accounting policies of the Municipality conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The following is a summary of the more significant policies.

The accompanying basic financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB). The GASB is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards which, along with subsequent GASB pronouncements (Statements and Interpretations) constitutes GAAP for governmental units.

In June 1999, GASB issued Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments (GASB No. 34). This statement established new financial reporting requirements for state and local governments. On July 1, 2003, the Municipality adopted the provisions of GASB No. 34 as well as other statements referred to below.

The accompanying basic financial statements present the financial position and the results of operations of the Municipality and its various funds and fund types. The basic financial statements are presented as of June 30, 2011, and for the fiscal year then ended. The more significant of these accounting policies are described below and, where appropriate, subsequent pronouncements will be referenced.

According to the financial reporting model established by GASB No. 34, the minimum required financial statement presentation applicable to the Municipality is composed of the following elements: (1) government-wide financial statements (GWFS), (2) governmental fund financial statements (GFFS), (3) notes to basic financial statements, and (4) required supplementary information (RSI).

The required supplementary information, which consists of a management discussion and analysis (MD&A), is information presented along with, but separate from, the Municipality's basic financial statements. The MD&A is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the year ended June 30, 2013, based on the Municipality's knowledge of the transactions, events and conditions reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

As previously mentioned, on July 1, 2003, other statements and interpretations were also adopted in conjunction and simultaneously with GASB No. 34. Those statements and interpretations are: (1) GASB Statement No. 33 – Accounting and Financial Reporting for Nonexchange Transactions, (2) GASB Statement No. 37 – *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, (3) GASB Statement No. 38 – *Certain Financial Statement Note Disclosures* and (4) GASB Interpretation No. 6 – *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

GASB No. 34 also required that the accounting for all governmental activities reported in the GWFS be based on applicable pronouncements issued by the Financial Accounting Standards Board (FASB) and its predecessor bodies, such as the Accounting Principles Board (APB), issued on or before November 30, 1989, provided those pronouncements do not conflict with or contradict GASB pronouncements. Accordingly, in conjunction and simultaneously with the adoption of GASB No. 34, the Municipality also adopted the following pronouncements: (1) APB Opinion No. 20 – *Accounting Changes*, (2) APB Opinion No. 21 – *Interest on Receivables and Payables*, (3) FASB Statement No. 5 - *Accounting for Contingencies* and (4) FASB Statement No. 16 – *Prior Period Adjustments*. The Municipality has elected to not apply all statements and interpretations issued by FASB after November 30, 1989.

The provisions of the GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*, an amendment of Statements No. 14 and 34, were considered in the evaluation of the potential component units. This statement modifies certain requirements for inclusion of component units in the financial reporting entity and amends the criteria for reporting component units as if they were part of the primary government under certain circumstances.

The GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements (GASB 62)*, incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance included in FASB pronouncements, which does not conflict with or contradict GASB pronouncements, and eliminates the criteria to apply post-November 30, 1989 FASB pronouncements that do not conflict with or contradict GASB pronouncements.

In current year, the Municipality adopted the provisions of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* establishing a new statement of net position format that reports separately all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (which is the net residual amount of the other elements). The Statement requires deferred outflows of resources and deferred inflows of resources to be reported separately from assets and liabilities. The financial reporting impact resulting from the implementation of GASB 63 in the Municipality's financial statements was the renaming of "Net Assets" to "Net Position", including changing the name of the financial statement from "Statement of Net Assets" to "Statement of Net Position"

A. COMPONENT UNITS

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 GASB Statement No. 14, as amended. The basic, but not the only criterion for including a potential component unit within the reporting entity is if a primary government is financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: 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. Based on the above criteria, the Municipality does not have component units to include within its reporting entity.

The Municipality's management has concluded that based on the aforementioned criteria, there are no legally separate entities or organizations that should be reported as component units of the Municipality for the fiscal year ended June 30, 2013. Accordingly, these basic financial statements present only the Municipality as the reporting entity.

These financial statements present the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2013, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

B. MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements (the Statement of Net Position and the Statement of Activities) are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grant and similar items are recognized as revenue as soon as all eligibility requirements have been met.

GOVERNMENTAL FUND FINANCIAL STATEMENTS

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recorded when susceptible to accrual; as soon as it is both measurable and available. "Available" means collectible within the current period or soon enough thereafter, normally within sixty (60) days, to be used to pay liabilities of the current period. Expenditures are generally recognized when the related liability is incurred.

The exception to this general rule is the principal and interest on general obligation long-term debt and compensated absences, if any, are recognized when due.

In applying the "susceptible to accrual" concept to intergovernmental revenues (federal grants) pursuant to GASBS No. 33, Accounting and Financial Reporting for Non-exchange Transactions (the Municipality may act as either provider or recipient), the provider should recognize liabilities and expenses and the recipient should recognize receivables and revenue when the applicable eligibility requirements including time requirements, are met. Resources transmitted before the eligibility requirements are met should, under most circumstances, be reported as advances by the provider and deferred revenue by the recipient.

There are essentially two types of revenue. For some grants, funds must be expended by the Municipality on the specific purpose or project before any amounts will be reimbursed. Revenue is, therefore, recognized as expenditures are incurred to the extent available. For the other revenue, moneys are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenue at the time of receipt or earlier if the susceptible to accrual criteria is met.

Expenditures are generally recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include the following:

- ❖ Employee's vested annual vacation and sick leave is recorded as expenditure when utilized. The amount of accumulated annual vacation and sick leave unpaid at June 30, 2013, has been reported only in the government-wide financial statements.

C. FINANCIAL STATEMENT PRESENTATION

The basic financial statements include both government-wide (based on the Municipality as a whole) and fund financial statements. While the previous financial reporting model emphasized fund types (the total of all funds of a particular type), in the new financial model the focus is on either the Municipality as a whole, or major individual funds (within the basic financial statements). Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as either governmental or business type.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements (the Statement of Net Position and the Statement of Activities) report information of all the activities of the Municipality. For most part, the effect of interfund activity has been removed from these government-wide financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The focus of the Statement of Net Position is designed to be similar to bottom line results for the Municipality and its governmental activities. This statement, for the first time, combines and consolidates governmental fund's current financial resources (short-term expendable resources) with capital assets and long-term obligations.

The Statement of Net Position presents the reporting entities' assets and liabilities, with the difference reported as net position. Net position is reported in three categories:

- ❖ **Net investment in capital assets** – These consists of capital assets, net of accumulated depreciation and amortization, and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
- ❖ **Restricted Net Position** – These results when constraints are placed on net position use, which can be either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- ❖ **Unrestricted Net Position** – These consists of net position which do not meet the definition of the two preceding categories. Unrestricted net position often is designated, to indicate that management does not consider them to be available for general operations. Unrestricted net position often has constraints on resources that are imposed by management, but can be removed or modified.

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

The Statement of Activities is focused on both the gross and net costs per functional category, and reflects the direct expenses of each functional category or identifiable activity, which are supported by program revenues. Direct expenses are those that are clearly identifiable with a specific function or activity, and the Municipality generally does not allocate indirect expenses. Program revenues include (a) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function.

Activity and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or activity. Taxes and other items not included in program revenues are reported instead as general revenues.

GOVERNMENTAL FUND FINANCIAL STATEMENTS

The fund financial statements (the Balance Sheet and the Statement of Revenues, Expenditures, and Changes in Fund Balances) are, in substance, very similar to the financial statements presented in the previous financial reporting model. Emphasis here is on the major funds in the governmental category. Non-major funds are summarized into a single column.

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is on Major Funds, rather than the previous financial model's fund types. The Governmental Major Fund Statements are presented on current financial resources and modified accrual basis of accounting.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

This is the manner in which these funds are normally budgeted. This presentation deemed most appropriate to (a) demonstrate legal and covenant compliance, (b) demonstrate the source and use of liquid resources, and (c) demonstrate how the Municipality's actual experience conforms to the budgeted fiscal plan.

Since the governmental fund statements are presented in a different measurement focus and basis of accounting than the government-wide statements, reconciliation is presented and a separate explanation for each differences.

The Municipality reports its financial position (Balance Sheet) and results of operations (Statement of Revenues, Expenditures and Changes in Fund Balance) in funds, which are considered separate accounting entities. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions.

The new model as defined in GASBS No. 34 established criteria (percentage of the assets, liabilities, revenues, or expenditures/expenses of either fund category in the governmental fund) for the determination of major funds. The non-major funds are combined in a single column in the fund financial statements. The Municipality reports the following major funds:

General Fund – This is the general operating fund of the Municipality. It is used to account for all financial resources, except those required to be accounted for in another fund.

Commonwealth Legislature Resolutions – This is the fund used to account for all the transactions of the State Assignments by Legislature Resolutions. The primarily objectives of this assignment is the development of construction projects on communities.

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

Loans Fund – This is the fund used to account for all financial resources and transactions related to the loans for construction purposes and capital outlays of the Municipality, which is financed by loans from the Government Development Bank of Puerto Rico.

Community Development Block Grant – This fund accounts for revenues related to federal program HUD-Community Development Block Grant. The purpose of the program is to provide community development and public services.

GASBS No. 34 eliminates the presentation of Account Groups, but provides for these records to be maintained and incorporates the information into the Governmental column in the Government-Wide Statement of Net Position.

D. FINANCIAL REPORTING PRESENTATION

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

General Fund – Is the general operating fund of the Municipality. It is used to account for all governmental activity, except those required to be accounted for in another fund.

Special Revenue Fund– This is the fund used to account for revenues derived from local funds, state grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or state statutes.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

Capital Projects Fund – This is the fund used to account for financial resources used for the acquisition or construction of major capital facilities. The uses and limitations of each capital projects fund are specified by Municipality ordinances or state statutes.

E. FUND BALANCES

In the current year, the Municipality adopted the provisions of GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions (GASB 54), which enhanced the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied. This statement establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which the Authority is bound to observe constraints imposed upon the use of resources reported in governmental funds.

Pursuant to the provisions of GASB 54, the fund balances amounts can be reported as non-spendable, restricted, committed, assigned and unassigned, based on the relative strength of the constraints that control how specific amounts can be spent, as described as follows:

- ❖ **Non-spendable** – Represent resources that cannot be spent readily with cash or are legally or contractually required not to be spent, including but not limited to inventories, prepaid items, long-term balances of loans and notes receivable.
- ❖ **Restricted** – Represent resources that can be spent only for the specific purposes stipulated by constitutional provisions, external resource providers (externally imposed by creditors or grantors), or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
- ❖ **Committed** – Represent resources used for specific purposes, imposed by formal action of the entity's highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by similar law, ordinance or resolution, no later than the end of the fiscal year.
- ❖ **Assigned** – Represent resources intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed (generally executive orders approved by the Mayor). Intent can be expressed by the Municipal Legislature, the Mayor or by an official or body to which the Municipal Legislature delegates authority in conformity with Autonomous Municipalities Act of Puerto Rico, as amended. In governmental funds other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed.
- ❖ **Unassigned** – Represent the residual classification for the Municipality's general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely. However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balances amounts as of for the fiscal year ended June 30, 2013.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

F. Net Position

Net Position has been reported pursuant to the provisions of GASB Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position. Net Position represents the difference between all assets plus deferred outflows of resources and all liabilities plus deferred inflows of resources. The Net Position consists of net resources restricted by external parties (such as debt covenants, creditors, grantors, contributions, laws or regulations of other governments, etc.), or net position for which constraints are imposed by the constitutional provisions or enabling legislation.

Enabling legislation consists of legislation that authorizes the Municipality to assess, levy, charge or otherwise mandate payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

A legally enforceable enabling legislation restriction is one that a party external to the Municipality (such as citizens, public interest groups, or the judiciary) can compel the Municipality to honor. The Municipality periodically reevaluates the legal enforceability of an enabling legislation to determine if any of the resources raised by the enabling legislation are used for a purpose not specified by the enabling legislation or if the Municipality has other cause for consideration.

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

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

In the government-wide statements, net position is segregated into three categories:

- A. Net Investment in capital assets:** Represent the component of the net position that consist of capital asset balances net of accumulated depreciation and amortization reduced by the outstanding balances of any bonds, notes and other borrowings that are attributable to the acquisition, construction, or improvement of those assets. This category should not include cash that is restricted to capital assets acquisition or construction (unspent bond proceeds) and any unamortized debt issue costs.
- B. Restricted net position:** Represents the component of the net position that is subject to restrictions beyond the Municipal's control. These include restrictions that are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or restrictions imposed by the law through constitutional provisions or enabling legislation (including enabling legislation passed by the government itself).
- C. Unrestricted net position:** Represents the component of the net position that do not meet the definition of net position invested in capital assets, net of related debt or restricted. Unrestricted assets are often designated to indicate that management does not consider them to be available for general operations. These types of constraints are internal and management can remove or modify them. Designations are not reported on the face of the Statement of Net Position.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

G. BUDGETARY DATA

The Municipality annually adopts the Budget Resolution for all operating funds of the Municipality except for certain restricted accounts of Proprietary Funds and Special Revenue Funds. Budgetary control is legally maintained at the fund level. The budget is prepared using the modified accrual basis of accounting with encumbrance included as budgetary basis expenditures. The Municipality's Budget Resolution provides transfer authority (1) to the Mayor and the Management and Budget Director, within and between departments and funds, as long as the total budget of the Municipality (net of interfund transfers) is not increased; (2) to the Management and Budget Director to implement grant budgets as the grant applications are accepted by the Municipality; and (3) to the Management and Budget Director to amend (re-appropriate) each new year's budget, to the extent of outstanding encumbrances, and/or unexpended project/grant appropriations at year end. Municipality's Legislature action is required for (1) use of the budgeted Legislature contingency, and (2) the approval of supplemental appropriations. During the year, several supplemental appropriations were necessary.

The budget columns (original and final budgets) of the Budgetary Comparison – General Fund reflect the original budget and the amended budget (which have been adjusted for legally authorized revisions of the annual budgets during the year). Appropriations, except remaining project appropriations, encumbrances, and unexpended grant appropriations, lapse at the end of each fiscal year.

Amendments to the budget, including transfers, require the approval of the Municipal Legislature. Unencumbered appropriations lapse at the end of the next fiscal year. The Municipality follows these procedures, in accordance with law, in order to establish the budgetary data reflected in the basic financial statements:

1. Prior of May 31 of each fiscal year, the Mayor submits to the Municipal Legislature a proposed budget for the fiscal year commencing the following July 1 in addition of a budget message;
2. The budget document is available for public inspection prior to its approval by the Municipal Legislature;
3. The Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law;
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance;
5. If a budget is not adopted prior to the end of the end of the fiscal year, the annual budget for the preceding fiscal year, as approved by the Municipal Legislature and the Mayor, is automatically renewed for the ensuing fiscal year until a new budget is approved. This permits the Municipality to continue making payments for its operating and other expenses until the new budget is approved;
6. Subsequent to the enactment of the annual appropriation ordinance, the Municipal Legislature has the authority to make necessary amendments made during the fiscal year and are reflected in the budget information included in the Budgetary Comparison Schedule – General Fund;
7. Budgetary data for the Special Revenue Fund has not been presented in the accompanying basic financial statements as such funds are budgeted over the life of the respective grant or project and not on an annual basis.

Since the budgetary basis differs from accounting principles generally accepted in the United States of America (GAAP), actual amounts for the General Fund in the accompanying Budgetary Comparison Schedule, is presented on the budgetary basis to enhance comparability.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The principal differences between the budgetary and GAAP bases are the following:

1. Encumbrances are recorded as expenditures under the budgetary basis and as a reserve of fund balances under GAAP.
2. The non-exonerated portion of the property tax advances are presented as revenue in the budgetary basis and as other financing sources under GAAP.
3. Interfund transactions of the General and Special Revenue Funds are not included in the budgetary basis.
4. Certain accrued liabilities and other debts are not included in the budgetary basis.
5. Certain revenues susceptible to accrual, i.e., both measurable and available, are not included in the budgetary data.

All encumbrance appropriations in the operating budget lapse at the end of the fiscal year. Property taxes collected during the current year by the Municipal Revenue Collection Center (Fiscal Agent) are presented as revenues in the accounting basis but are not considered in the budgetary schedule.

The special funds of the Special Revenue Fund have not been included in the budgetary comparison because balances are not budgeted. Also, the budget prepared for the Federal Finance Awards Programs included in the Major and Non Major Funds is based on a program period which is not necessarily a year. Accordingly, it's not practical to present an annual comparison of budget for such programs.

H. CASH, CASH EQUIVALENT AND INVESTMENT

The Finance Director of the Municipality is responsible for investing the available resources in certificates of deposit and other short-term investments. Investments are made from the available combined funds of the Municipality and, accordingly, it is not practical to disclose certificates of deposit and other short-term investments individually by fund in the combined financial statements. Interest earned on certificates of deposit and other short-term investments are recognized as revenue in the General Fund. Cash in the Special Revenue, Debt Service and Capital Project Funds are restricted; accordingly, resources available were not used for pool investments.

Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the federal depository insurance generally provided by the Federal Deposit Insurance Corporation (FDIC). All securities pledged as collateral are held by agents designated by the Commonwealth's Secretary of the Treasury, but not in the Municipality's name.

Cash with fiscal agent represents property tax collections retained by the Municipal Revenues Collection Center and undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the Government Development Bank of the Commonwealth of Puerto Rico.

Cash balance recognized in the Debt Service Fund is restricted for the payment of the Municipality's obligations, and others are restricted for specific projects, such as the acquisition or construction of permanent improvements. The sinking fund is maintained by the Governmental Development Bank of Puerto Rico, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

I. RECEIVABLES

Receivable are stated net of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions. Receivable from Federal Government represents amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

J. INVENTORIES

The General, Special Revenue and Capital Project Funds, purchases office and printing supplies, gasoline, oil and other expendable supplies held for consumption. The cost of purchases is recorded as expenditure in the appropriate fund and the inventory is not recorded in the basic financial statements.

K. CAPITAL ASSETS

Property, plant and equipment purchased or acquired is carried at historical cost or estimated historical cost. Contributed assets are recorded at fair market value as of the date received. Other costs incurred for repairs and maintenance is expensed as incurred.

Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

Capital Assets	Years
Buildings and building improvements	20-50
Land improvement	20
Infrastructure	25-50
Vehicles	5-15
Machinery and equipment	5-20

L. LONG-TERM OBLIGATIONS

The liabilities reported in the government-wide financial statements included general and special obligation bonds and notes, and other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities.

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

M. COMPENSATED ABSENCES

The Municipality accrues accumulated unpaid vacation and sick leave and associated employee-related costs when earned (or estimated to be earned) by the employee. The Municipality's employees are granted 30 days of vacations and 18 days of sick leave annually. Vacations may be accumulated up to a maximum of sixty (60) days and sick leave up to a maximum of ninety (90) days. In the event of employee resignation, the employee is paid for accumulated vacation days up to the maximum allowed. Separation from employment prior to use of all or part of the sick leave terminates all rights for compensation, except for employees with ten years of service who are entitled to sick leave pay up to the maximum allowed. The Municipality accrued a liability for compensated absences, which meet the following criteria:

1. The Municipality's obligation relating to employee's rights to receive compensation for future absences is attributable to employee's services already rendered.
2. The obligation relates to rights that vest or accumulate.
3. Payment of the compensation is probable.
4. The amount can be reasonably estimated.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

M. COMPENSATED ABSENCES (CONTINUED)

In accordance with the above criteria and requirements as established by GASBS No. 16; the Municipality has accrued a liability for compensated absences, which has been earned but not taken by Municipality's employees. For the government-wide statements, the current portion is the amount estimated to be used in the following year. For the governmental funds statements, all of the compensated absences are considered long-term and therefore, are not a fund liability and represents a reconciling item between the fund level and government-wide presentations.

The following is a summary of changes in the balance of Compensated Absences for the fiscal year ended June 30, 2013.

<u>BALANCE</u> <u>JULY 1, 2011</u>	<u>NEW ISSUES</u>	<u>RETIREMENTS</u>	<u>BALANCE</u> <u>JUNE 30, 2013</u>
<u>\$1,429,401</u>	<u>\$ -</u>	<u>\$46,492</u>	<u>1,388,909</u>

N. INSURANCE

The Municipality has insurance coverage for its public facilities, primarily to provide protection from catastrophic losses. Also, principal officials of the Municipality are covered under various surety bonds. The Secretary of the Treasury Department of the Commonwealth of Puerto Rico is the agent commissioned to place all of the Municipality's insurance coverage. Corresponding premiums payable are withheld by the Municipal Revenue Collection Center from quarterly advances of annual property tax and subsidy send to the Municipality.

O. INTERFUND TRANSACTIONS

Interfund transactions are reflected as loans, reimbursements or transfers. Loans are reported as receivables and payables as appropriate and are subject to elimination upon consolidation. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers between governmental or proprietary funds are netted as part of the reconciliation to the government-wide columnar presentation. The Municipality has the following types of reciprocal and nonreciprocal interfund activities:

- ❖ **Interfund loans** – Represent amounts provided with a requirement for repayment, which are recorded as “due from” in the lender governmental fund and “due to” in the borrower governmental fund. Interfund receivables, which are not considered currently available financial resources, are reported as advances. For amounts not expected to be collected within a reasonable period, interfund receivables/payables are reduced to the estimated realizable value and the amount that is not expected to be repaid is reported as a transfer from the governmental fund that made the loan.
- ❖ **Interfund transfers** – Represent flows of assets (permanent reallocation of financial resources among governmental funds) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported as other financing uses in the governmental fund making transfers and as other financing sources in the governmental fund receiving transfers.
- ❖ **Interfund reimbursements** – Represent repayments from the governmental fund responsible for particular expenditures or expenses to the governmental fund that initially paid for them.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

P. CLAIMS AND JUDGMENTS

The estimated amount of the liability for claims and judgments, if any, which is due on demand, such as from adjudicated or settled claims, is recorded in the General Fund. The Long-Term Liabilities includes an amount estimated by the external counselors of the Municipality as a contingent liability or liabilities with a fixed or expected due date, which will require future available financial resources for its payment.

Q. USE OF ESTIMATES

The preparation of the basic 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 disclosures of contingent assets and liabilities at the date of the basic financial statements and the reported revenue and expenses during the reporting period. Actual result could differ from those estimates.

R. ACCOUNTING FOR PENSION COSTS

For the purpose of applying the requirements of GASB Statement No. 27, Accounting for Pensions by State and Local Government Employers (GASB No. 27), amended by GASB Statement No. 50, Pension Disclosures. The Municipality accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions. The state government of the Commonwealth of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multi-employer cost-sharing defined benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate. The Municipality is considered a participant and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Commonwealth of Puerto Rico and the basic financial statements of such retirement systems are part of the financial reporting entity of the Commonwealth of Puerto Rico. Accordingly, no portion of the net pension obligation (NPO) related to ERS has been allocated to the Municipality in the accompanying basic financial statements. The basic financial statements of the Commonwealth of Puerto Rico report the total amount of the net pension obligation of ERS, including any amount that may correspond to the Municipality.

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

S. RISK FINANCING

The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico.

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2013 amounted to \$7,709. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$190,303 for workers compensation insurance covering all municipal employees.

T. FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

The GASB has issued the following statements that have effective dates after June 30, 2013:

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- a) GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. The requirements of this statement are effective for periods beginning after December 15, 2012.
- b) GASB Statement No. 66, *Technical corrections-2013* – an amendment of GASB Statements No. 10 and No.62. The requirements of this statement are effective for periods beginning after December 15, 2012.
- c) GASB Statement No. 67, *Financial Reporting for Pension Plans-an amendment of GASB Statement No. 25*. The requirements of this statement are effective for periods beginning after June 15, 2012.
- d) GASB Statement No. 68 *Accounting and Financial Reporting for Pensions-an amendment of GASB Statement No. 27*. The requirements of this statement are effective for periods beginning after June 15, 2014.
- e) GASB Statement No. 69 *Government Combinations and Disposals of Government Operations*. The requirements of this statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis.
- f) GASB Statement No. 70 *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. This statement is effective for periods beginning after June 15, 2013.
- g) GASB Statement No. 71 *Pension Transition for Contributions made Subsequent to the Measurement Date- an amendment of GASB 68*. This statement is effective for periods beginning after June 15, 2014.

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

2. NEW ACCOUNTING STANDARDS

The provisions of the following Governmental Accounting Standards Board (GASB) Statement have been implemented for the year ended June 30, 2013:

GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements:

1. Financial Accounting Standards Board (FASB) Statements and Interpretations
2. Accounting Principles Board Opinions
3. Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure

GASB 62 does not have any impact on the Municipality's financial statements.

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources.

2. NEW ACCOUNTING STANDARDS (CONTINUED)

GASB Statement No. 64 ("GASB 64") Derivative Instruments: Application of Hedge Accounting Termination Provisions – an amendment of GASB Statement No. 53 was issued in June 2011. The objective of this Statement is to clarify whether an effective hedging relationship continues after the replacement of a swap counterparty or a swap counterparty's credit support provider. This statement sets forth criteria that establish when the effective hedging relationship continues and hedge accounting should continue to be applied. The requirements of Statement No. 64 are effective for financial statements for periods beginning after June 15, 2011 and were adopted the Municipality effective July 1, 2012 with no significant impact on the financial statements.

GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as revenues and expenses. The adoption of this statement require that debt issuance costs be recognized as an expenses in the period incurred.

GASB Statement No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, and No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements. GASB 66 does not have any impact on the Municipality's financial statements.

3. CASH AND CASH EQUIVALENTS

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

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

Credit risk – This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as it's custodial and credit risk policy, the Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico. Accordingly the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2013.

Interest rate risk – This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investment portfolio at June 30, 2013, (2) limiting the weighted average maturity of its investments to three months or less, and (3) keeping most of its bank deposits in interests bearing accounts generating interests at prevailing market rates. Therefore, the Municipality's management has concluded that at June 30, 2013, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

3. CASH AND CASH EQUIVALENTS (CONTINUED)

Custodial credit risk – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$250,000 per depositor. In addition, public funds deposited in commercial banks by the Municipality are fully securities pledged as collateral are held, in the Municipality's name, by the agents of the Commonwealth's Secretary of Treasury. Deposits with GDB are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2013. Therefore, the Municipality's management has concluded that at June 30, 2013 the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

Foreign exchange risk – The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, the Municipality is prevented from investing in foreign securities or any other types of investments in which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2013.

The Municipality's bank balances in commercial banks of \$8,611 in Commonwealth Legislature Resolutions, \$4,928 in Community Development Block Grant, and \$591,892 in other governmental funds, were fully collateralized at June 30, 2013. The deposits at GDB of \$1,091,768 in Loans Fund, \$2,892,384 in the Debt Service Fund, \$19,364 in other governmental funds, are unsecure and uncollateralized, as no collateral is required to be carried by governmental banks.

4. RECEIVABLES

Amounts due from governmental entities as of June 30, 2013 follows:

	<u>Commonwealth Government</u>	<u>Federal Grants</u>
Municipal Revenue Collection Center (CRIM) – property taxes (debt service fund)	\$39,575	\$ -
Other governmental entities	12,784	-
Office of Commissioner of Municipal Affairs – CDBG	-	188,918
Special Programs for Aging – Title III, Part B – Grant for Supportive Services and Senior Center.	-	141,645
Child Care – Commonwealth of Puerto Rico, Administration for Children and Families	-	59,922
Emergency Shelter Grants Programs - Department of Housing and Urban Development	-	12,824
Total	<u>\$52,359</u>	<u>\$403,309</u>

5. INTERFUND TRANSACTIONS

a. **Due from/to other funds-** Amounts due from/to other funds represent temporary advances to other funds for payroll and payroll taxes expenditures and to record the overdrawn of pool cash by the general fund to other special funds as follows:

Receivable Fund	Payable Fund	Amount
Other governmental fund	General fund	\$183,199
Commonwealth Legislative Resolutions	General fund	1,319,624
General fund	Commonwealth Legislative fund	385,791
Other governmental funds	Other governmental fund	1,826
General fund	Loans fund	180,215
General fund	Other governmental fund	321,860
Other governmental funds	Commonwealth Legislative fund	204,000
Commonwealth Legislative Resolutions	Other governmental fund	27,810
General fund	Community Development Block Grant	<u>18,033</u>
Total		<u>\$2,642,358</u>

Operating transfers- Transfers between individual funds were made for operational purposes. Transfers includes: interest earned on restricted cash with fiscal agents in the debt service fund and operating and capital improvement loans in other governmental funds which is transferred to the general fund; principal and interest payments of general long term debt transferred from the general fund to the debt service fund; and transfers of funds from general fund to other special funds for matching purposes or to finance unreimbursable funds from governmental agencies.

6. CAPITAL ASSETS

Capital assets and depreciation as of and for the year ended June 30, 2013 is as follows:

Governmental Activities	Balance July 1, 2012	Additions	Retirements	Balance June 30, 2013
Capital Assets not being depreciated:				
Land	\$ 741,684	\$ -	\$ -	\$ 741,684
Construction in progress	782,022			782,022
Total Capital Assets not being depreciated:	<u>1,523,706</u>			<u>1,523,706</u>
Capital Assets being depreciated:				
Building, structures and building improvements	17,719,421			17,719,421
Infrastructure	9,250,131			9,250,131
Land improvements	2,892,996			2,892,996
Licensed vehicles	2,233,782	210,764		2,444,546
Machinery and equipment	2,346,134	165,055	5,981	2,505,208
Equipment under capital leases	43,571			43,571
Total Capital Assets being depreciated:	<u>34,486,035</u>	<u>375,819</u>	<u>5,981</u>	<u>34,855,873</u>
Less accumulated depreciation for:				
Building, structures and building improvements	3,853,080	1,275,634	428,585	4,700,129
Infrastructure	2,600,924	3,255,468	(881,742)	6,738,134
Land improvements	2,512,480	204,011	173,920	2,542,571
Licensed vehicles	1,724,172	277,732	237,683	1,764,221
Machinery and equipment	1,350,128	313,438	(47,978)	1,711,544
Equipment under capital leases	38,070			38,070
Total accumulated depreciation	<u>12,078,854</u>	<u>5,326,283</u>	<u>(89,532)</u>	<u>17,494,669</u>
Total capital assets, being, depreciated, net	<u>22,407,181</u>	<u>(4,950,464)</u>	<u>95,513</u>	<u>17,361,204</u>
Governmental activities capital assets, net	<u>\$ 23,930,887</u>	<u>\$ (4,950,464)</u>	<u>\$ 95,513</u>	<u>\$ 18,884,910</u>

6. CAPITAL ASSETS(CONTINUED)

Depreciation and amortization of capital assets was charge to functions/activities in the accompanying government-wide statement of activities as follows:

Governmental activities:	Amount
General government	\$617,576
Public safety	237,649
Public works	2,326,701
Human services and welfare	79,244
Culture and education	1,832,927
Health and sanitation	112,064
Urban and economic development	120,122
Total depreciation expense-governmental activities	<u>\$5,326,283</u>

7. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2013 are summarized as follows:

Description	General Fund	Community Legislature Resolutions	Debt Service Fund	Loans Fund	Community Development Block Grant	Other Governmental Funds	Total Governmental Funds
Accounts payable	\$ 2,669,579	\$ -	\$ -	\$ 166,231	\$ 175,813	\$ 122,945	\$ 3,134,568
Bank overdraft	33,348						33,348
Accrued liabilities	<u>193,455</u>	-	-	-	-	-	<u>193,455</u>
Total	<u>\$ 2,896,382</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 166,231</u>	<u>\$ 175,813</u>	<u>\$ 122,945</u>	<u>\$ 3,361,371</u>

8. LIABILITIES

Due to governmental units

Amounts due to other agencies as of June 30, 2013 follows:

	Commonwealth Entities
Puerto Rico – Water and Sewer Authority	\$ 59,885
Puerto Rico – Land Authority	158,450
Puerto Rico Telephone Company	13,480
Puerto Rico Employee Retirement System Administration	61,052
Puerto Rico Industrial Development Corporation (PRIDCO)	264,367
FEMA	858,203
Other entities	62,116
	<u>\$ 1,477,553</u>

8. LIABILITIES(CONTINUED)

Deferred revenues

The Municipality reports deferred revenues on its GFFS and GWFS as follows:

	<u>Revenues not available</u>	<u>Revenues received before allowable cost are incurred</u>
Unearned volume of municipal license taxes	\$ 289,850	\$ -
Energy Efficiency and Conservation Block Grant Program	-	11,274
Rural Development Corporation	-	339,839
Child and Adult Care Food Program	-	15,543
Solid Waste Authority Fund	-	4,067
Others	-	4,807
	<u>\$289,850</u>	<u>\$375,530</u>

Long-term liabilities- Long-term liabilities activity for the year ended June 30, 2013 was as follows:

Description	<u>Balance July 1, 2012</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance June 30, 2013</u>	<u>Due within one year</u>
Bonds payable	\$ 7,100,000	\$2,675,000	\$ 410,000	\$ 9,365,000	\$ 480,000
Notes payable	1,715,000	1,320,000	80,000	2,955,000	235,000
Puerto Rico Treasury Department	674,775		674,775	-	
Excess of property tax	571,092		46,200	524,892	46,200
Puerto Rico Labor Department	91,950		91,950	-	
CRIM	902,081		22,785	879,296	24,217
Puerto Rico Water and Sewer Authority	60,000		60,000	-	
Compensated absences	1,429,401		40,492	1,388,909	135,000
Claims and judgments	120,000	24,600	120,000	24,600	
Total	<u>\$12,664,299</u>	<u>\$4,019,600</u>	<u>\$ 1,546,202</u>	<u>\$15,137,697</u>	<u>\$ 920,417</u>

The Municipality's Legislature is legally authorized to determine the contracting of debts of the Municipality. Nevertheless, the laws and regulations of the Commonwealth also provide that:

- Direct obligations of the Municipality (evidenced principally by bonds and notes) are backed by the full faith, credit and taxing power of the Municipality; and
- Direct obligations are not to be issued if the amount of the principal of, and interest on, such bonds and notes (and on all such bonds and notes issued thereafter) which are payable in any fiscal year, together with any amount paid by the Municipality in the preceding fiscal year on account of bonds or notes guaranteed by the Municipality, exceed 10 percent of the total assessed value of the property located within the Municipality plus the balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service.

8. LIABILITIES(CONTINUED)

In addition, before any new bonds or notes are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. At June 30, 2013, the Municipality is in compliance with the debt limitation requirements.

Bonds and notes outstanding at June 30, 2013 are as follows:

<u>Bonds Descriptions</u>	<u>Balance as of June 30, 2013</u>
\$530,000 series of 2002, general obligation bonds payable in annual installments \$10,000 to \$40,000 until July 1, 2026, interest from 2.7% to 5.6%	\$ 380,000
\$1,310,000 series of 2005, general obligation bond payable in annual installments of \$35,000 to \$105,000 until July 1, 2025, interest from 4.23% to 5.33%	1,010,000
\$710,000 series of 2008, general obligation bond payable in annual installments of \$10,000 to \$60,000 until July 1, 2032, interest from 7% to 7.5%	650,000
\$1,125,000 series of 1995, general obligation bond payable in annual installments of \$20,000 to \$110,000 until July 1, 2016 interest from 4.7% to 6.63%	385,000
\$1,740,000 series of 2002, operational obligation bond payable in annual installments of \$10,000 to \$130,000 until July 1, 2026, interest from 5% to 6%	1,265,000
\$2,675,000 series of 2012, general obligation bond payable in annual installments of \$60,000 to \$130,000 until July 1, 2027 interest from 1.28% to 7.50%	2,675,000
\$805,000 series of 2008, special obligation bond payable in annual installments of \$10,000 to \$70,000 until July 1, 2032, interest from 7% to 7.5%	750,000
\$1,210,000 series of 2008, special obligation bond payable in annual installments of \$85,000 to \$210,000 until July 1, 2017, interest from 7% to 7.5%	830,000
\$145,000 series of 2005, operational purpose bond payable in annual installments of \$10,000 to \$20,000 until July 1, 2014, interest from 5% to 8%	35,000
\$1,440,000 series of 2012, special obligation bond payable in annual installments of \$55,000 to \$150,000 until July 1, 2026 interest from 6% to 7.5%	<u>1,385,000</u>
Total bonds payable	<u>\$ 9,365,000</u>

8. LIABILITIES (CONTINUED)

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

Year ending June 30,	Principal	Interest
2014	\$ 480,000	\$ 406,361
2015	520,000	612,909
2016	580,000	554,887
2017	630,000	532,833
2018	560,000	491,215
2019-2023	2,075,000	2,023,143
2024-2028	2,310,000	1,197,747
2029-2033	1,235,000	611,062
2034-2038	975,000	194,063
Total	\$ 9,365,000	\$ 6,624,220

Notes Descriptions	Balance as of June 30, 2013
\$1,270,000 series of 2008, special obligation bond payable in annual installments of \$15,000 to \$110,000 until July 1, 2032, interest from 7% to 7.5%	\$ 1,190,000
\$95,000 series of 2012, general obligation bond payable in annual installments of \$95,000 to \$20,000 until July 1, 2018, interest from 6% to 7.5%	85,000
\$80,000 series of 2012, special obligation bond payable in annual installments of \$80,000 to \$15,000 until July 1, 2018 interest from 6.0% to 7.5%	70,000
\$325,000 series of 2013, general obligation bond payable in annual installments of \$35,000 to \$55,000 until July 1, 2018, interest from 6% to 7.5%	290,000
\$60,000 series of 2013, general obligation bond payable in annual installments of \$5,000 to \$10,000 until July 1, 2019, interest from 6% to 7.5%	60,000
\$140,000 series of 2013, general obligation bond payable in annual installments of \$15,000 to \$25,000 until July 1, 2019, interest from 6% to 7.5%	140,000
\$350,000 series of 2012, special obligation bond payable in annual installments of \$40,000 to \$60,000 until July 1, 2019, interest from 6% to 7.5%	350,000
\$770,000 series of 2013, special obligation bond payable in annual installments of \$90,000 to \$135,000 until July 1, 2019, interest from 6% to 7.5%	<u>770,000</u>
Total notes payable	<u>\$ 2,955,000</u>

8. LIABILITIES (CONTINUED)

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

Year ending June 30,	Principal	Interest
2014	\$ 235,000	\$ 126,326
2015	250,000	194,625
2016	280,000	174,750
2017	300,000	153,000
2018	325,000	129,563
2019-2023	715,000	321,437
2024-2028	305,000	264,563
2029-2033	435,000	128,062
2034-2038	110,000	4,125
TOTAL	\$ 2,955,000	\$ 1,496,451

These bonds and notes are payable from the special and valorem property tax of 1.25% which is restricted for debt service and retained by the Municipality and the municipal sales and use tax imposed by the Municipality and collected by the Commonwealth of Puerto Rico Treasury Department.

Other long-term liabilities:

Description	Balance as of June 30, 2013
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.	\$ 524,892
The Municipality entered into a financing agreement with the Puerto Rico Department of Labor for a total amount of \$429,377 for unemployment benefits paid by the Commonwealth of Puerto Rico in behalf of the Municipality. The agreement paid in monthly installments of \$14,637, including interest, was due on July 2012.	-
\$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 \$18,979 approximately, plus interest rate of 6.25% until July 1, 2032.	879,296
On May 25, 2011 the Municipality entered into a financing with the Puerto Rico Water and Sewer Agency for the amount of \$216,000 paid in monthly installments of \$12,000, as of November 15, 2012.	-
<u>Compensated absences</u> – 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, 2013, the outstanding balance amounts to \$1,388,909. This amount will be repaid with unrestricted funds	1,388,909

8. LIABILITIES (CONTINUED)

Other claims and judgments – Represent the final costs of legal cases paid subsequent to June 30, 2013 and other claims outstanding as of that date. The awarded amounts will be paid with unrestricted funds. As of June 30, 2013, the outstanding balance amounts to \$24,600.

24,600

9. REVENUES**Property taxes**

The Municipal Revenue Collection Center (CRIM) of the Commonwealth of Puerto Rico is responsible for the assessment, collection and distribution of real and personal property taxes. The tax on personal property is self-assessed by the taxpayer. The assessment is made on a return, which must be filed with the CRIM by May 15 of each year and is based on the current value at the date of the assessment. Real property is assessed by the CRIM. The tax is general assessed on January 1 on all taxable property located within the Municipality and is based on the current value existing in the year 1957.

For personal property the tax is due with the return filed on or before May 15. Taxes on real property may be paid on two equal installments, July 1st and January 1st, following the assessment date.

The tax rates in force as of June 30, 2013 are 8.78% for real property (of which 8.58% is paid by the taxpayer and .20% is reimbursed by the Puerto Rico Treasury Department) and 6.58% for personal property (of which 6.38% is paid by the taxpayer and .20% is reimbursed by the Puerto Rico Treasury Department). For both tax rates 1.03% belongs to the Commonwealth and 7.75% and 5.75%, respectively, belongs to the Municipality. Of the portion belonging to the Municipality, 6% on real property and 4% on personal property represents the Municipality's portion which is appropriated for general purposes and accounted in the general fund. The remaining portion of 1.75% on both tax rates belonging to the Municipality is restricted for debt service and accounted in the debt service fund.

Residential real property occupied by its owner is exempt by law from property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the Puerto Rico Department of Treasury assumes payment of the basic tax to the Municipality, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. Revenue related to exempt property is recorded in the General Fund. The Municipality grants a complete exemption from personal property taxes up to an assessment value of \$50,000 to retailers with annual net sales of less than \$150,000.

The CRIM advances funds to the Municipality based on an estimate of special governmental subsidies and the property taxes to be levied and which are collected in subsequent periods. This distribution includes advances of property tax and amounts of municipal equalization fund from the Commonwealth government. 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. The CRIM prepares a preliminary settlement not later than three months after fiscal year-end and a final settlement not later than six months after fiscal year-end. If actual collections exceed the advances a receivable from CRIM is recorded. However, if advances exceed actual collections, a payable to CRIM is recorded.

Sales and use tax

On July 4, 2006 the Commonwealth Legislature approved Act No. 117 which amends the Puerto Rico Internal Revenue Code of 1994 to provide, among other things, for a sale and use tax of 5.5% to be imposed by the Commonwealth Government. Act No. 117 also authorizes each municipal government to impose a municipal sales and use tax of 1.5%. This municipal sales and use tax has in general the same tax base and limitations (except for unprocessed foods) as those provided by the Commonwealth's sales and use tax.

9. REVENUES (CONTINUED)

Section 6189 of the Puerto Rico Internal Revenue Code of 1994, as amended, authorizes the Municipalities in Puerto Rico to impose a sales and use tax to consumers. This tax must be imposed in conformity with the base, exemptions and limitations contained in Subtitle BB of the Code. The municipal sales and use tax is specifically imposed overall sales transactions of taxable items and combined transactions (as defined by the municipal internal regulation) taken place within municipal limits. The municipal sales and use tax is also specifically imposed over the purchase price for the use, storage or consumption of taxable transactions (as defined by the municipal internal regulation) taken place within Municipal limits.

On July 29, 2007 the Commonwealth Legislature approved Act No. 80 which amends Act No. 117 of July 4, 2006 to impose 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% is collected by the Municipalities and the remaining .5% of the 1.5% is collected by the Puerto Rico Department of Treasury (PRDT). Act No. 80 also provides for restrictions on the use of the sales tax, which is required be invested in solid waste and recycling programs, capital improvements and health and public safety costs.

Amount collected by the PRDT (the remaining .5% of the 1.5%) is deposited in accounts or special funds in the Governmental Development Bank of Puerto Rico ("GDB"), subject to restrictions imposed and distributed as follows:

- .2% of the .5% will be deposited in a "Municipal Development Fund" to finance costs as restricted by the Act,
- .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,
- .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

As a subsequent event new laws were established with a direct change in the collections and distributions of the sales and use tax (See Subsequent Events Note for more explanations)

Municipal license taxes

The Municipality is authorized by Law No. 81 to impose and collect municipal license taxes on all trade or business activities operated by any natural or legal person within the territorial area of Guánica. This is a self-assessed tax generally based on the business volume measured by gross sales. The Municipality establishes the applicable tax rates. At June 30, 2005, the municipal tax rates imposed by the Municipality were 1.50% for financing institutions and 0.50% for other types of taxpayers. Any taxpayers that have been granted with partial tax exemptions under any of the incentive tax laws of the Commonwealth ultimately pay municipal license taxes at reduced tax rates, generally between 60% and 90% under standard rates.

Each taxpayer must assess his/her corresponding municipal license tax by declaring his/her volume of business through a tax return to be filed every April 15 based on the actual volume of business generated in the preceding calendar year. Taxpayers with a sales volume of \$3millions or more must include audited financial statements with their tax returns. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration. The first installment of the tax covers the six-month period ended December 31, subsequent to the filing date of the declaration, while the second installment of the tax covers the six-month period ended June 30 of the subsequent calendar year. If a taxpayer elects to pay the tax in full on the filing date of the declaration (generally April 15), a 5% discount is granted automatically on the total tax amount due.

Any municipal license taxes collected in advance (that is, pertaining to a future period) are recorded as deferred revenues. Deferred municipal license tax revenues recorded in the accompanying GWFS and GFFS amounted to \$289,850 at June 30, 2013, which represents municipal licenses collected in advance for the taxable year 2013-2014.

9. REVENUES (CONTINUED)

Intergovernmental Revenues

Intergovernmental revenues in the General Fund are comprised of the following:

General Fund	Amount
Amount of municipal equalization fund and subsidy send by CRIM	\$4,508,740
Compensation in lieu of tax from the Puerto Rico Electric Power Authority (PREPA)	1,464,933
Reimbursement from Commonwealth Government - Christmas Bonus Expenditures	<u>126,318</u>
Total general fund	6,099,991
Commonwealth Legislative Resolutions	51,024
Other Governmental Fund	<u>657,264</u>
Total	<u>\$ 6,808,279</u>

10. EMPLOYEES RETIREMENT SYSTEM

Description of the Plan

Employees of the Municipality participate in the Employee's Retirement System of the Government of Puerto Rico and its instrumentalities (ERS). The ERS is cost-sharing multiple-employer defined benefit pension plan sponsored by the Government under the Act No. 447, approved on May 15, 1951, as amended. ERS covers all regular employees of the Government and its instrumentalities and of certain municipalities and components units not covered by their own retirement systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Head of Agencies and Public Instrumentalities, Assistants to the Governor, the Comptroller of the Puerto Rico, Gubernatorial Board and Committee appointees and Experimental Service Station employees. 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 at least 55 years of age and have completed at least 25 years of creditable service or members who have attained at least 58 years of age and have completed at least 10 years of creditable service are entitled to an annual benefit, payable monthly for life. The amount of the annuity shall be 1.5% of the average salary, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average salary, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive up to a maximum of 65% of the average salary, as defined, or if they have attained 55 years of age will receive up to a maximum of 75% of the average salary, as defined. Disability retirement benefits are available to members for occupational disability up to a maximum benefit of 50% of the average salary, as defined. However, for non-occupational disability, a member must have at least 10 years of creditable services.

10. EMPLOYEES RETIREMENT SYSTEM (CONTINUED)

The contribution requirements for both employees and employers are established by law and are not actuarially determined. Employees are required to contribute 5.775% for the first \$550 of monthly salary plus 8.275% for the excess of this amount, or on the alternative, 8.275% of their monthly gross salary. The Municipality is required by Act No. 447 to contribute 9.275% of its employees' gross salaries.

Act No. 1 of 1990 made certain amendments applicable to new participants joining the ERS effective April 1, 1990. These changes consist principally of the establishment of contributions at 8.275% of their monthly gross salary, an increase in the retirement age to 65, a decrease in the annuity benefit to 1.5% of the average salary, as defined, for all years of creditable services, a decrease in the maximum disability, and death benefits annuities from 50% to 40% of average salary, as defined, and the elimination of the Merit Annuity for participants who have completed 30 years of creditable services.

Law Number 305 was enacted on September 24, 1999, amended the Act Number 447 for the purpose of establishing a new program (System 2000). System 2000 became effective on January 1, 2000. Employees participating in the current system (ERS) as of December 31, 1999, may elect either to stay in the defined-benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000, will only be allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan there will be a pool of pension assets, which will be invested by the System, together with those of the current defined-benefit plan. Benefits at retirement age will not be guaranteed by the Government. The annuity will be based on a formula which assumes that each year the employees' contribution (with a minimum of 8.275% up to a maximum of 10%) of their monthly salary, and will be invested in an account which will either: (a) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (b) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (c) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The employers' contributions (9.275% of the employees' salary) will be used to fund the current plan.

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

Funding Policy

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

Contribution requirements are established by law and are as follows:

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

10. EMPLOYEES RETIREMENT SYSTEM (CONTINUED)***Annual Contribution***

The Municipality's actual contribution for the current fiscal year, which is equal to the required contribution follows:

<u>Fiscal year ended</u>	<u>Law No. 447</u>	<u>System 2000</u>
2013	<u>\$65,081</u>	<u>\$269,048</u>
2012	<u>\$59,029</u>	<u>\$182,709</u>
2011	<u>\$60,134</u>	<u>\$168,959</u>

These amounts represented the 100% of the required contribution for year 2011-2012. Additionally, changes made in the types and amounts of benefits offered by special laws and costs of living adjustments, led to a one-time recommended contribution to fund the retroactive adjustment related to the changes.

The Employee's Retirement System of the Government of Puerto Rico provides additional information of the ERS and System 2000. They issue a publicly available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Government. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, PR 00940-2003.

As a subsequent event new laws were established with a direct change in the Employees Retirement System (See Subsequent Events Note for more explanations)

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

12. CONTINGENCIES

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.

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. With respect to pending litigation, the Municipality has reported liabilities of \$24,600 in the government-wide statement of net position.

13. COMMITMENTS

The **Municipality of Guánica** had several outstanding or planned construction projects as of June 30, 2013. These projects are evidenced by contractual commitments with contractors. The construction projects are commitments of the Capital Projects' funds that amounted to approximately \$287,528.

14. FUND BALANCES (DEFICITS)

As of June 30, 2013, fund balances are compromised as follows:

	General Fund	Commonwealth Legislature Resolutions	Debt Service Fund	Loans Fund	Other Governmental Funds	Total Governmental Funds
Fund balances (deficits):						
Restricted for:						
General government	\$ -	\$ -	\$ -	\$ 613,941	\$ -	\$ 613,941
Public works		766,254		72,158		838,412
Human services and welfare					44,318	44,318
Culture and recreation					19,738	19,738
Health and sanitation					10,690	10,690
Debt service			1,929,756			1,929,756
Committed for:						
Public works					49,534	49,534
Culture and recreation					213,254	213,254
Health and sanitation					39,951	39,951
Unassigned	<u>(5,171,113)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(5,171,113)</u>
Total fund balances (deficits)	<u>\$ (5,171,113)</u>	<u>\$ 766,254</u>	<u>\$ 1,929,756</u>	<u>\$ 686,099</u>	<u>\$ 377,485</u>	<u>\$ (1,411,519)</u>

The budget project does not address the cumulative general fund deficit. The non-major governmental fund deficits result from the accrual of expenditures without accruing intergovernmental revenues for reimbursement of expenditures. As requires by current standards, the Municipality recorded intergovernmental revenues for reimbursement-based (expenditure-driven) grants on fund statements when all applicable eligibility requirements have been met and the resources are available. These deficits will be covered with future budgetary appropriations of the general fund, if necessary.

15. PRIOR PERIOD ADJUSTMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

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

Description	General Fund	Section 8 Voucher Program	Commonwealth Legislature Resolutions	Debt Service Funds	Loans Funds	Community Development Block Grant	Other Governmental Funds	Total Governmental Funds
Fund Balance, beginning	\$ (5,319,384)	\$ 132,989	\$ 601,231	\$ 1,881,060	\$ 767,461	\$ -	\$ (661,451)	\$ (2,598,094)
Adjustments to:								
Reclassification of fund due to major fund determination		(132,989)					132,989	-
To correct cash beginning balance	(871)		37,204	(57,756)	(1,723)		(123)	(23,269)
To correct Deferred Revenues							45,814	45,814
To correct the Intergovernmental receivables							157,624	157,624
To correct Due to other governmental entities	(165,069)		155,221				558,278	548,430
To correct Due from other funds	(481,856)							(481,856)
To correct Due to other funds	(207,085)							(207,085)
Fund Balance, beginning as restated	<u>\$ (6,174,265)</u>	<u>\$ -</u>	<u>\$ 793,656</u>	<u>\$ 1,823,304</u>	<u>\$ 765,738</u>	<u>\$ -</u>	<u>\$ 233,131</u>	<u>\$ (2,558,436)</u>

854,881

15. PRIOR PERIOD ADJUSTMENTS (CONTINUED)

B. GOVERNMENTAL WIDE FINANCIAL STATEMENTS

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

<u>Description</u>	<u>Governmental Activities</u>
Net assets, beginning	\$ 9,111,618
Adjustments to:	
To correct cash beginning balance according to Mod 4A	(23,269)
To correct cash beginning balance	45,814
To correct Deferred Revenues	157,624
To correct the Intergovernmental receivables	548,430
To correct Due to other governmental entities	(481,856)
To correct Due from other funds	(207,085)
Difference between reduction of Bonds and Notes and the matured amount recognized in prior year	55,000
Net assets, beginning as restated	<u>\$ 9,206,276</u>

16. SUBSEQUENT EVENTS

Act. No 3 of April 4, 2013

On April 4, 2013, the Governor of Puerto Rico signed into law Act No. 3 of 2013, which represents a comprehensive reform of the ERS. Act No. 3 became effective on July 1, 2013 and amends the provisions of the different benefits structures under the ERS, including, but not limited, to the following:

- For active participants of the contributory defined benefit programs under Act No. 447 of 1951 and Act No. 1 of 1990, all retirement benefits accrued through June 30, 2013 will be frozen, and thereafter, all future benefits will accrue under the defined contribution formula used for System 2000 participants, and will be paid at retirement through a lifetime annuity.
- Increases the minimum pension for current retirees from \$400 to \$500 per month.
- The retirement age for Act No. 447 participants will be gradually increased from age 58 to age 61.
- The retirement age for current System 2000 participants is increased gradually from age 60 to age 65.
- Eliminates the "merit annuity" available to participants who joined the ERS prior to April 1, 1990.
- The retirement age for new employees is increased to age 67, except for new state and municipal police officers, firefighters, and custody officers, which will be age 58.
- The employee contribution rate will increase from 8.275% to 10%.
- For System 2000 participants, the retirement benefits will no longer be paid as a lump sum distribution, instead, they will be paid through a lifetime annuity.

16. SUBSEQUENT EVENTS (CONTINUED)

- Eliminates or reduces various retirement benefits previously granted by special laws, including Christmas and summer bonuses. The Christmas bonus payable to current retirees is reduced from \$600 to \$200 and is eliminated for future retirees. The summer bonus will be eliminated.
- Disability benefits will be eliminated and substituted for a mandatory disability insurance policy.
- Survivor benefits will be modified.

In addition, the Commonwealth has proposed incremental annual contributions from the General Fund of \$140 million per year, for the next 20 years, to increase the liquidity and solvency of the ERS. An appropriation for such annual contribution has been included in the Commonwealth's proposed budget for the fiscal year 2014.

Based on current census data, expectations of market conditions and other actuarial information provided by consulting actuaries, the changes instituted by Act No. 3, along with the additional annual contributions of \$140 million to be received from the Commonwealth during the next 20 years, will be sufficient to cover the System's current and future obligations.

The successful implementation of these measures cannot be assured, as it is dependent upon future events and circumstances whose outcome cannot be anticipated.

Act. No. 18 of 2014

On January 24, 2014, was signed the Act No. 18 of 2014, to create the "Law of Municipal Administration Fund", to establish a special fund called the Municipal Administration, authorize municipalities to pledge the funds deposited in the Local Government Fund to which they are to secure the repayment of any loan, bond, note or other evidence of debt, whose repayment source are the funds deposited in the Special Fund and to meet any expenditure budget of the municipality and the municipality any activity or project, authorize the Government Development Bank for Puerto Rico to make disbursements for the purposes set out in this Act, amend paragraph (b) of Section 4020.01, amend paragraph (b) of Section 4020.02, and amend paragraph (a) and to repeal paragraph (e) of Section 6080.14 of the Act No. 1-2011, as amend, known as the "Internal Revenue Code for a New Puerto Rico", in order to restructure the sales and use tax so that the tax rate is six (6) percent state level and one (1) percent at the municipal level.

Act. No 19 of 2014

On January, 24, 2014, the Commonwealth of Puerto Rico enacted Act No. 19 (also known as the Municipal Financing Corporation Act), to authorize the creation of a public corporation and instrumentality of the Commonwealth of Puerto Rico, attached to the Government Development Bank for Puerto Rico, known as "Municipal Financing Corporation" (COFIM, by its acronyms in Spanish), with the power to issue and/or use other mechanisms to pay or refinance the debt incurred by the municipalities, whose payment of principal and interest is supported by municipal sales and use taxes; establish that the first collections of municipal sales and use tax of one percent (1%) will be collected by municipalities and deposited directly to the Redemption Fund of the Municipal Financing Corporation; establish that bonds and obligations issued by the "Municipal Financing Corporation" will be payable and secured by the pledge of the greater of (i) a fixed amount of the municipal sales and municipal tax or (ii) the amount of the municipal sales and use tax fixed at zero point three percent (0.3%) collected during the previous fiscal year; and amend the paragraph (c) of section 4050.06, amend paragraph (a) of section 4050.07, amend paragraph (a) and (b) of section 4050.08, amend paragraph (a) of section 4050.09, and amend paragraphs (b), (c) and (d), repeal paragraph (e) and renumber paragraph (f) as (e) of section 6080.14 of the Act 1-2011, as amended, known as the "Internal Revenue Code for a new Puerto Rico".

On January 23, 2014 the Municipality's Executive Branch approved Ordinance Number 82 (2013-2014), authorizing to issue a general obligation bond in the amount of \$175,000.

	Budgeted Amounts		Actual Amounts (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 1,165,715	\$1,165,715	\$ 1,384,271	\$ 218,556
Municipal license taxes	380,000	380,000	349,460	(30,540)
Municipal sales and use tax	407,000	407,000	325,550	(81,450)
Licenses, permits and other local taxes	300,000	300,000	252,258	(47,742)
Charges for services	2,516,800	2,516,800	1,761,310	(755,490)
Intergovernmental	6,183,112	6,183,112	6,099,991	(83,121)
Interest, fines and penalties	90,000	90,000	228,960	138,960
Miscellaneous	808,364	808,364	148,729	(659,635)
Total revenues	11,850,991	11,850,991	10,550,529	(1,300,462)
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
General government	2,112,189	2,210,242	2,188,940	21,302
Public safety	908,219	887,446	843,540	43,906
Public works	5,608,989	5,342,587	5,619,042	(276,455)
Human services and welfare	797,974	810,710	760,676	50,034
Culture and recreation	666,227	665,481	711,915	(46,434)
Health and sanitation	1,584,893	1,762,025	1,972,821	(210,796)
Transfer out	172,500	172,500	92,647	79,853
Total expenditures, encumbrances and other financing uses	11,850,991	11,850,991	12,189,581	(338,590)
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)	\$ -	\$ -	\$ (1,639,052)	\$ (1,639,052)
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 10,550,529
Differences-budget to GAAP:				
Non budgeted transfer in				3,621,076
GAAP adjustments to revenues				(62,446)
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances				\$ 14,109,159
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 12,189,581
Differences-budget to GAAP:				
Non-budgeted expenditures				916,426
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				\$ 13,106,007

The accompanying notes are an integral part of this required supplementary information

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

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.

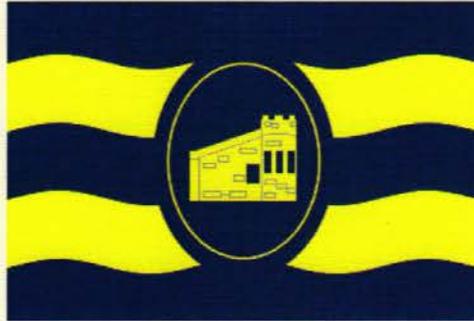
The Municipality prepares its annual budget including the operations of the general fund.

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.

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2013 representing the original budget. There were no supplemental appropriations for the year ended June 30,2013.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA, PUERTO RICO



SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2013



Hon. Santos Seda Nazario
Mayor

Mr. Daniel Rodríguez
Finance Director

**MUNICIPALITY OF GUÁNICA, PUERTO RICO
SINGLE AUDIT REPORT
FISCAL YEAR ENDED JUNE 30, 2013**

CONTENTS

	PAGE
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	1-2
Independent Auditor's Report on Compliance for Each Major Program and On Internal Control over Compliance Required by OMB Circular A-133	3-5
Schedule of Expenditures of Federal Awards	6-7
Notes to Schedule of Expenditures of Federal Awards	8
Schedule of Findings and Questioned Costs	9-15
Summary Schedule of Prior Audit Findings	16-17

**INDEPENDENT AUDITOR'S 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**

Honorable Mayor and Members of the
Municipal Assembly
Guánica, Puerto Rico

We have audited, in accordance with the 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, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Municipality of Guánica, Puerto Rico as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise Municipality of Guánica, Puerto Rico's basic financial statements, and have issued our report thereon dated March 25, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Municipality of Guánica, Puerto Rico's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Municipality of Guánica, Puerto Rico's internal control. Accordingly, we do not express an opinion on the effectiveness of Municipality of Guánica, Puerto Rico's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and questioned costs as item 2013-001 to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompany schedule of findings and questioned costs as item 2013-002 to be significant deficiencies.

Compliance and Other Matters

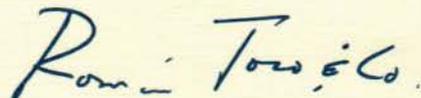
As part of obtaining reasonable assurance about whether Municipality of Guánica's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items 2013-003 through 2013-004.

Municipality of Guánica's Response to Findings

Municipality of Guánica's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Municipality of Guánica's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



ROMAN TORO & CO., CPA, C.S.P.
LICENSE # 35 - IN FORCE

Yauco, Puerto Rico
March 25, 2014

Stamp #E93384 was affixed to
the original report



**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133**

Honorable Mayor and Members of the
Municipal Assembly
Guánica, Puerto Rico

Report on Compliance for Each Major Federal Program

We have audited Municipality of Guánica, Puerto Rico's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Municipality of Guánica, Puerto Rico's major federal programs for the year ended June 30, 2013. Municipality of Guánica, Puerto Rico's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Municipality of Guánica, Puerto Rico's major federal programs based on our audit of the types of compliance requirements referred to above. 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, Puerto Rico'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 on compliance for each major federal program. However, our audit does not provide a legal determination of Municipality of Guánica, Puerto Rico's compliance.

Opinion on Each Major Federal Program

In our opinion, Municipality of Guánica, Puerto Rico, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2013.

Other Matters

The results of our auditing procedures disclosed other instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2013-003 and 2013-004. Our opinion on each major federal program is not modified with respect to these matters.

Municipality of Guánica, Puerto Rico's response to the noncompliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Municipality of Guánica, Puerto Rico's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of Municipality of Guánica, Puerto Rico, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Municipality of Guánica, Puerto Rico's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality of Guánica, Puerto Rico's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2013-003 and 2013-004 to be material weaknesses.

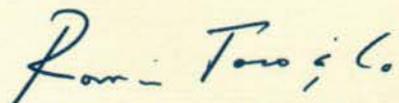
Municipality of Guánica, Puerto Rico's response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Guánica's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Municipality of Guánica, Puerto Rico, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise Municipality of Guánica, Puerto Rico's basic financial statements. We issued our report thereon dated March 25, 2014, which contained unmodified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Purpose of this Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.



ROMAN TORO & CO., CPA, C.S.P.
LICENSE # 35 - IN FORCE

Yauco, Puerto Rico
March 25, 2014

Stamp #E93385 was affixed to
the original report



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF AGRICULTURE			
Pass-through the Commonwealth of Puerto Rico Department of Education			
Child and Adult Care Food Program	10.558	Not Available	\$ 24,539
Total U.S. Department of Agriculture			24,539
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT			
Direct Program:			
Emergency Shelter Grants Program	14.231		18,962
Direct Program:			
Section 8 Housing Choice Voucher	14.871		227,626
Pass-through the Commonwealth of Puerto Rico – Office of the Commissioner for Municipal Affairs:			
Community Development Block Grant	14.228		1,522,501
Neighborhood Stabilization Program (HERA) (NSP1)	14.228		202,420
Total U.S. Department of Housing and Urban Development			1,971,509
U.S. DEPARTMENT OF ENERGY			
Direct Program:			
Energy Efficiency and Conservation Block Grant Program (Recovery Act Funded)	81.128	Not Available	124,699
Total U.S. Department of Energy			124,699

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (Continued)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico – Governor’s Office (Elderly Office):			
Special Program for Aging – Title III, Part B – Grants for Supportive Services and Senior Centers	93.044	Not Available	189,531
Pass-through the Commonwealth of Puerto Rico – Family Department:			
Child Care and Development Block Grant	93.575	Not Available	<u>2,658</u>
Total U.S. Department of Health and Human Services			<u>192,189</u>
U.S. DEPARTMENT OF HOMELAND SECURITY			
Pass-through the Commonwealth of Puerto Rico – Governor Authorized Representative (GAR):			
Hazard Mitigation Grant	97.039		<u>20,934</u>
Total U.S. Department of Homeland Security			<u>20,934</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u><u>\$2,333,870</u></u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

1. BASIS OF PRESENTATION:

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

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Special Revenue – Section 8 Voucher Program Fund, Community Development Block Grant, and in the Other Governmental Funds in the Municipality's fund financial statements. The reconciliation between the expenditures in the funds financial statements and expenditures in the Schedule of Expenditures of Federal Awards is as follows:

<u>Description</u>	<u>Community Development Block Grant</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Per Schedule of Expenditures of Federal Awards	\$ 1,522,501	\$ 811,369	\$ 2,333,870
Non federal programs expenditures and other adjustments	-	587,305	587,305
Total expenditures in the fund financial statements	<u>\$ 1,522,501</u>	<u>\$ 1,398,674</u>	<u>\$ 2,921,175</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION I – SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditor's report issued: Unqualified on Fund Financial Statement Opinion Qualified Opinion
 Adverse on Government-Wide Financial Statement Opinion Disclaimer Opinion

Internal control over financial reporting:

- Significant deficiency identified? Yes None reported
- Material weakness (es) identified? Yes No

Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major programs:

- Significant deficiency identified? Yes None reported
- Material weakness (es) identified? Yes No

Type of auditor's report issued on compliance for Major Programs: Unqualified Opinion Qualified Opinion
 Adverse Opinion Disclaimer Opinion

Any audit finding disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133? Yes No

Identification of Major Programs:

CFDA Number	Name of Federal Program or Cluster
14.228	Community Development Block Grant – State Grant
14.871	Section 8 – Rental Housing Choice Vouchers

Dollar threshold used to distinguish between Type A and Type B Programs: \$300,000

Auditee qualified as low-risk auditee? Yes No

END OF SECTION

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – FINANCIAL STATEMENTS FINDINGS

2013-001

Type of finding: Financial statement.

Situation: Material weakness over financial reporting; Compliance of local regulations

Prior-Year(s) Audit Finding(s): 2011-II-4, 2012-II-4.

Questioned Costs: Not applicable.

Condition:

The Municipality does not maintain proper recordkeeping of documentation in relation to its capital assets and its related debt as required by local regulations.

Context:

During our substantive audit tests and tests of internal controls over the Municipality's capital assets, we found that the Municipality does not maintain a centralized archive of all property records, including vendor invoices, purchase orders, receiving reports and payment analysis for the acquisition of property and construction in progress, requiring extensive work in order to substantiate the items within the property subsidiary ledgers and its balances. Among the issues found:

1. Capital assets inventoried as required by federal, state, and local regulations are not regularly reconciled with the subsidiary ledgers which support the balances in the financial statements.
2. Missing dates of acquisition, property numbers, and other information of certain items.
3. Construction in progress expenditures not accounted for during the year as addition in capital assets.

The Municipality also does not maintain documentation of the debt used to acquire or construct municipal property, the property acquired with such loans, and the available balance of such loans, if any. This does not allow a simple tracing of capital assets to their debt and determine their net investment to report as required by GAAP, requiring significant work to trace such debt.

Criteria:

Chapter VII, Section 15(1) of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affairs (OCAM) requires that all records concerning municipal property be under the custody of the person in-charge of property, under supervision of the Finance Director.

Cause:

The Municipality's personnel in charge of property management has not maintained copies of all property transactions documentation in a centralized archive.

Effect:

The Municipality's financial statement preparation process requires significant work in order to assure of all property transactions and balances are accounted for.

Auditor's Recommendation:

The Municipality should maintain a centralized archive of all property documentation required for the management of property, and instruct its employees to facilitate all documents regarding the acquisition, transfer, disposal, and any other transaction involving municipal property to the person in-charge of property.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – FINANCIAL STATEMENTS FINDINGS

2013-001, continued

Views of responsible officials and corrective actions:

Instructions were given to the person in charge of property record keeping to inventory, reconcile, classify and record transactions related to the acquisition of capital assets following the instructions of the “Manual del Módulo de Propiedad” made by OCAM. The Municipality will hire a consulting firm in order to update all acquisitions of capital assets as of June 30, 2014.

Audit finding status:

Unresolved.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
FOR THE YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS, continued

2013-002

Type of finding: Financial statement.

Situation: Significant deficiency over financial reporting; Compliance of local regulations

Prior-Year(s) Audit Finding(s): 2011-II-2, 2012-II-2

Questioned Costs: Not applicable.

Condition:

The Municipality's General Fund has used restricted resources from other funds in order to fund its operations.

Context:

The Municipality's General Fund has used cash resources from the Municipality's State Legislative Joint Resolutions Fund for its own operations, which has created, as of June 30, 2013, an outstanding liability totaling \$1,319,624. The State Legislative Joint Resolutions Fund consists of grants and contributions from the State Legislature which are restricted by Joint Resolutions of both the State House of Representatives and Senate.

Criteria:

Local laws and regulations prohibit Municipalities from the use of restricted funds to cover the costs of unauthorized activities. Additionally, each State Legislative Joint Resolutions grants and contribution is individually restricted to their use by the Resolution passed by the State Legislature, and any other use not previously included in the Resolution requires strict and expressive consent by the State Legislature. This is specifically mentioned in the Municipal Administration Manual in Chapter III, Section 2, as issued by the Puerto Rico Commissioner's Office for Municipal Affairs.

Cause:

The Municipality's General Fund cash resources have been decreasing significantly over the course of several years due to excess expenditures over revenues, and the Municipality's management decided to use restricted resources of other funds in order to avoid decreases in the General Fund's activities and expenditures.

Effect:

The Municipality's State Legislative Joint Resolutions Fund was left without sufficient resources to comply with the activities intended by the State Legislature for which such appropriations were restricted.

Auditor's Recommendation:

The Municipality's General Fund should reimburse all funds obtained from the State Legislative Joint Resolutions Fund as immediate as resources become available. The Municipality should revise its controls to assure that General Fund's operations do not infringe on the resources and appropriations of other funds whose use are restricted.

Views of responsible officials and corrective actions:

We concur with the finding. During the fiscal year 2012-2013 this condition did not happen. The increase of \$248,766 in the liability, from fiscal year 2011-2012 to 2012-2013, was due to the restatement of the beginning balances as of June 30, 2012.

Audit finding status:

Unresolved.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
FOR THE YEAR ENDED JUNE 30, 2012**

SECTION III – FEDERAL AWARD FINDINGS

2013-003

Type of finding: Federal award finding.

Situation: Material Weakness; Compliance of federal regulations

Federal Program: All Federal programs in the Schedule of Expenditures of Federal Awards

Compliance Requirements: Reporting.

Prior-Year(s) Audit Finding(s): None.

Questioned Costs: None.

Condition:

The Municipality submitted late its Single Audit Reporting Package for the fiscal year ended June 30, 2012 to the Federal Audit Clearinghouse (FAC) because of deficiencies in its financial reporting process which produces the required financial statements, an important element of the package.

Context:

As reported in the prior year audit finding 2012-II-1, the Municipality submitted their unaudited trial balance schedules and worksheets of funds on February 20, 2013 to the auditor, more than eight months after the fiscal year closing date at June 30, 2012, and 40 days before the Single Audit report due date, which consisted of various spreadsheets used to compile the financial statements. This documentation and supporting evidence were found to have various material misstatements which were reported for correction and adjustment. This situation caused for the audit of the financial statements to be delayed culminating on the auditors issuing their report on April 3, 2013, and the Reporting Package being submitted to and received by the FAC on April 12, 2013.

Criteria:

OMB Circular A-133 section 320(a) requires that recipients of federal awards who expend \$500,000 or more of federal awards in a single year (12-month period) must submit its Single Audit Reporting Package within the earlier of 30 days after receipt of the auditor's report, or nine months after the end of the audit period.

Cause:

The computer accounting system's self-balancing set of accounts and ledgers are not fully utilized by the Municipality's accounting staff to account for all assets, liabilities, and residual balances and changes there in, required to provide a comprehensive picture of the financial operations, positions, and results of the Municipality's funds. Automatic year-end closing procedures in this system are currently limited to three basic areas: cash, revenues and expenditures. They are not performed to account for all potential transactions in modified-accrual basis accounting for all funds or full accrual basis for government-wide reporting. Meanwhile, the manual accounting system does not provide for a self-balancing set of accounts for each fund, but does provide more detail to assist in preparing budget to actual results reports, and account for receipts, encumbrances, and disbursements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
FOR THE YEAR ENDED JUNE 30, 2012**

SECTION III – FEDERAL AWARD FINDINGS (continued)

2013-003, continued

Cause, continued:

Both systems are dependent on each other to provide a comprehensive accounting of the Municipality financial operations, but a compilation of all this information has to be done manually to report complete financial information. This process is not done continually by the accounting staff, but at year end by an external CPA contractor. This contractor must correct all errors or omissions which are not detected during the year have to before the audit starts, and failure to do so will compromise information in the financial statements.

Effect:

The Municipality submitted late its FY2011-2012 Single Audit Reporting Package to the FAC.

Auditor's Recommendation:

The Municipality financial reporting system must be modified or changed significantly in order to avoid this situation from worsening and to improve the timing of the availability of information for the compilation and auditing of the financial statements. The Municipality should consider which resources can be obtained to improve this situation, including changing the OCAM system to an improved and centralized accounting system to incorporate both the automated accounting and the manual accounting in one system, or an accounting system that can at least produce financial statements on their own in a reasonable timeframe, even if they would still require the review of a third-party contractor for technical issues, complicated matters, and final compilation.

Views of responsible officials and corrective actions:

We concur with the finding. However, this finding will be eliminated this year since we will comply with the March 31, 2014 deadline as required by regulation.

Audit finding status:

Unresolved.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
FOR THE YEAR ENDED JUNE 30, 2012

SECTION III- FEDERAL AWARD FINDINGS, Continued

2013-004

Type of finding: Financial statement.

Situation: Significant deficiency; Compliance of local regulations

Federal Program: Community Development Block Grant - State's Program (CFDA 14.228)

Compliance Requirements: Equipment and Real Property Management (E).

Prior-Year(s) Audit Finding(s): 2011-III-2.

Questioned Costs: None.

Condition:

As discussed in finding 2013-01, the Municipality has certain deficiencies in the recordkeeping of capital assets, which also includes acquired federal property under the CDBG program.

Context:

As discussed more fully in finding 2013-01, the Municipality does not maintain a proper archive of equipment and real property records for its items. While federal programs coordinators maintain a record of program income and other federally-funded properties, local laws and regulations require that all properties' records be safeguarded and maintained by personnel in-charge of property, because such records are used for financial reporting, inventorying, and insurance purposes.

Criteria:

Chapter VII, Section 15(1) of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affairs (OCAM) requires that all records concerning municipal property be under the custody of the person in-charge of property, under supervision of the Finance Director. Additionally, OMB Circular A-110, section 34(f) states that equipment records shall be maintained accurately and include information detailed in the Circular.

Cause:

The Municipality's personnel in charge of property management has not maintained copies of all property transactions documentation in a centralized archive.

Effect:

The Municipality's financial statement preparation process requires additional work in order to assure of all property transactions and balances are accounted for.

Auditor's recommendation:

The Municipality should maintain a centralized archive of all property documentation required for the management of property, and instruct its employees to facilitate all documents regarding the acquisition, transfer, disposal, and any other transaction involving municipal property to the person in-charge of property.

Views of responsible officials and corrective actions:

Instructions were given to the person in charge of property record keeping to inventory, reconcile, classify and record transactions related to the acquisition of capital assets following the instructions of the "Manual del Módulo de Propiedad" made by OCAM. The Municipality will hire a consulting firm in order to update all acquisitions of capital assets as of June 30, 2014.

Audit finding status:

Unresolved.

END OF SECTION

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2013**

Year	Finding Number	Finding	CFDA Number	Questioned Cost(s)	Comments
(1) Prior Audit Findings, fully corrected or not noted during our audit:					
2012	2012-II-1	The Municipality's financial system does not provide sufficient resources to produce GAAP oriented governmental financial statements free of material misstatements.	N/A	None.	Situation was mitigated in current year.
2012	2012-II-3	The Municipality did not classify General Fund's balances as required by GASB.	N/A	None.	Situation corrected.
2012	2012-III-1	The IRS levied taxes allegedly owed by the Municipality and the same were not returned to the program as of June 30, 2012.	N/A	None.	The Municipality returned the amount owed to the federal program.
(2) Prior Audit Findings, not corrected or partially corrected:					
2012	2012-II-2	The Municipality's general fund has used restricted resources from other funds in order to fund its operation.	N/A	None.	Situation not corrected.
2012	2012-II-4	The Municipality does not maintain proper record keeping of its capital assets.	N/A	None.	Situation not corrected.
2012	2012-III-2	The Municipality has certain deficiencies in record keeping of capital assets, which also includes acquired federal property under CDBG program.	14.228	None.	Situation not corrected.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUÁNICA
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (Continued)
FOR THE YEAR ENDED JUNE 30, 2013**

Year	Finding Number	Finding	CFDA Number	Questioned Cost(s)	Comments
-------------	---------------------------	----------------	------------------------	-------------------------------	-----------------

(3) Corrective action taken is significantly different from corrective action previously reported:

None.

(4) Prior Audit Findings, are no longer valid:

None.

END OF SCHEDULE
