

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

**MUNICIPIO DE GUAYAMA  
AUDITORÍA 2013-2014  
30 DE JUNIO DE 2014**

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**COMMONWEALTH OF PUERTO RICO**  
**AUTONOMOUS MUNICIPALITY OF GUAYAMA**

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**BASIC FINANCIAL STATEMENTS WITH  
ADDITIONAL REPORTS AND INFORMATION  
REQUIRED BY THE SINGLE AUDIT ACT**

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**YEAR ENDED JUNE 30, 2014**

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**HON. EDUARDO E. CINTRON SUAREZ**  
**MAYOR**

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**PEDRO C. ORTIZ LEDEE**  
CERTIFIED PUBLIC ACCOUNTANT

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**INDEPENDENT AUDITOR'S REPORT**

**To the Honorable Mayor and  
Members of the Municipal Legislature  
Municipality of Guayama, Puerto Rico**

**Report on the Financial Statements**

I have audited the accompanying financial statements of each major fund and the aggregate remaining fund information of the Municipality of Guayama, Puerto Rico (Municipality), as of and for the fiscal year ended June 30, 2014, and the related notes to the financial statements. I was engaged to audit the financial statements of the governmental activities. These financial statements 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**

My responsibility is to express opinions on these financial statements based on my audit. I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. Because of the matter described in the "Basis for Disclaimer of Opinion on Governmental Activities" paragraph, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the governmental activities.

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 risk 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, I 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.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinions.

## INDEPENDENT AUDITOR'S REPORT (CONTINUED)

### **Basis for Disclaimer of Opinion on Governmental Activities**

The Municipality did not maintain complete, updated and accurate accounting records that supports the amounts presented as capital assets and its related accumulated depreciation, in the governmental activities. I was unable to satisfy myself about such balances through alternate procedures. Therefore, I was unable to obtain sufficient and competent evidential matter related to the capital assets reported in the accompanying statement of net position for \$121,922,153 net of accumulated depreciation of \$26,015,602 and the amount of depreciation expense stated at \$1,123,748 reported in the accompanying statement of activities for the year then ended. In addition, the expenses and the net result of operations reported in the accompanying statement of activities are also misstated for amounts that could not be determined for the fiscal year ended June 30, 2014.

The Municipality did not comply with the requirements established by GASB No. 18, *Accounting for Municipal Solid Waste Landfill Closure and Post Closure Care Costs*, issued by the Governmental Accounting Standards Board and the regulations set forth by the U.S. Environment Protection Agency in its "Solid Waste Disposal Facility Criteria", issued on October 9, 1991. At June 30, 2014, the accompanying statement of net position include a liability of \$10,450,048 for closure and post closure care costs not based on a formal study of the actual landfill available and used capacity. Because, of the inadequacy of the accounting records, I was unable to form an opinion regarding the liability for closure and post closure costs of the landfill.

### **Disclaimer of Opinion**

Because of the significance of the matter described in the "Basis for Disclaimer of Opinion on Governmental Activities" paragraph, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the governmental activities of the Municipality as of June 30, 2014, or the changes in financial position, thereof for the year then ended. Accordingly, I do not express an opinion on the statement of net position and the statement of activities.

### **Basis for Qualified Opinion on the General Fund, Head Start Fund, Bond Issuances Fund and the aggregate remaining fund**

The Municipality did not maintain adequate accounting records of the interfund cash transactions and the corresponding due from and due to account balances. I was unable to obtain sufficient evidence to support and satisfy myself about the amounts recorded in the interfund balances in the amount of \$7,428,175 recorded in the General Fund, Head Start Fund, Bond Issuances Fund and the aggregate remaining fund in the balance sheet of the governmental funds at June 30, 2014.

### **Qualified Opinion**

In my opinion, except for the possible effects of the matters discussed in the "Basis for Qualified Opinion on the General Fund, Head Start Fund, Bond Issuances Fund and the aggregate remaining fund" paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the General Fund, Head Start Fund, Bond Issuances Fund and the aggregate remaining fund of the Municipality, as of June 30, 2014, and the respective changes in financial position thereof for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

## INDEPENDENT AUDITOR'S REPORT (CONTINUED)

### **Unmodified Opinions**

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Debt Service Fund as of June 30, 2014, and the respective changes in financial position thereof for the fiscal 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 comparison information on pages 5 through 15 and 67 through 68 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. I 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 my inquiries, the basic financial statements, and other knowledge I obtained during my audit of the basic financial statements. I do not express an opinion or provide any assurance on the information because the limited procedures do not provide me with sufficient evidence to express an opinion or provide any assurance.

#### **Other Information**

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial statements. The Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the financial statements. Because of the significance of the matter described in the "Basis for Disclaimer of Opinion on Governmental Activities" paragraph, it is inappropriate to and I do not express an opinion on the supplementary information referred to above.

#### **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, I have also issued my report dated May 10, 2015, on my consideration of the Municipality's internal control over financial reporting and on my 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 my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Municipality's internal control over financial reporting and compliance.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)



Pedro C. Ortiz Ledée, CPA  
License Number 5200

Guayama, Puerto Rico  
May 10, 2015



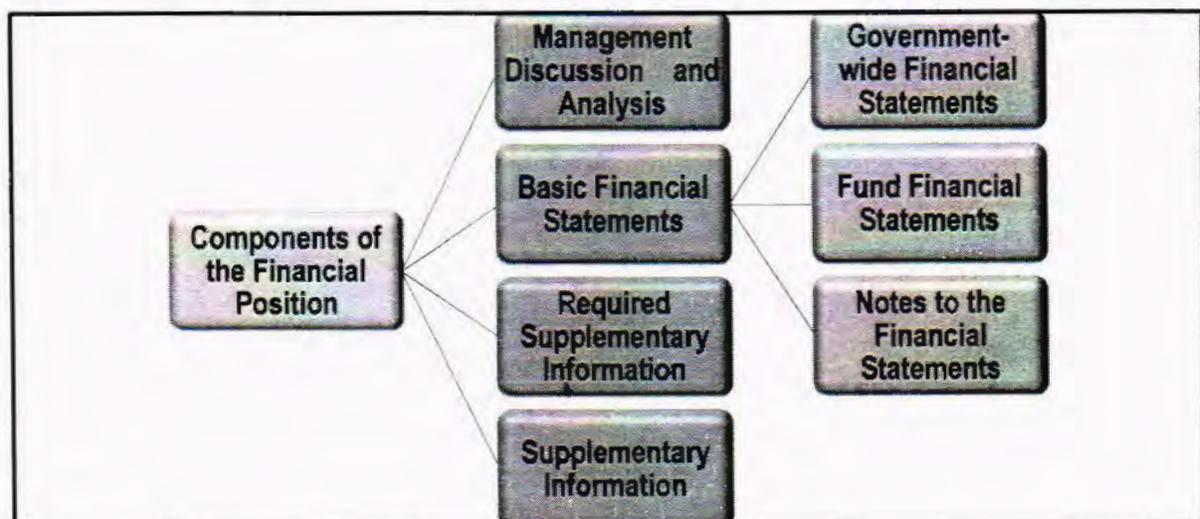
The discussion and analysis of the Municipality of Guayama's (Municipality) financial performance provides an overall review of the Municipality's financial activities for the year ended June 30, 2014. The intent of this discussion and analysis is to look at the Municipality's financial performance as a whole; this section should be read in conjunction with the basic financial statements to obtain a better understanding of the financial position and the results of operations of the Municipality. Our analysis follows this section.

### FINANCIAL HIGHLIGHTS

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2014 by \$95,775,924 (net position), an increase of 21% in comparison with 2013, as restated. Of this amount, the Municipality presented an unrestricted deficit of \$3,394,616.
- Revenues increased 33% and expenses decreased 19% when compared with fiscal year 2013, as restated. Net position increased \$16,573,315 in 2014.
- A negative net change in the fund balances of the Municipality's governmental funds of \$1,985,002 in the fiscal year 2014 resulted in reported ending fund balances of \$11,055,134.
- For the fiscal year 2014, the General Fund reported an excess of expenditures and other financing uses over revenues and other financing sources of \$1,217,764. The unassigned fund deficit amounts to \$4,768,426, for an increase of 36% when compared to the prior year, as restated.
- The investment in capital assets as of June 30, 2014 was \$121,922,153 (net of depreciation).
- Long-term debt (total primary government) decreased to \$57,649,110 or approximately 5% with respect to the prior year, as restated.
- On a budgetary basis, actual expenditures exceeded actual revenues by \$875,575.

### OVERVIEW OF THE FINANCIAL STATEMENTS

The Municipality's financial report comprises four components: (1) management's discussion and analysis (presented here), (2) basic financial statements, (3) required supplementary information and (4) other supplementary information.



The Municipality's basic financial statements consist of two kinds of statements, each with a different view of the Municipality's finances. The government-wide financial statements provide both long-term and short-term information about the Municipality's overall financial status. The fund financial statements focus on major aspects of the Municipality's operations, reporting those operations in more detail than the government-wide statements:

### **Basic Financial Statements**

- ***Government-Wide Financial Statements***

The government-wide statements report information about the Municipality as a whole using accounting methods similar to those used by private-sector businesses. They are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. The first government-wide statement, the *statement of net position*, presents all of the reporting entity's non-fiduciary assets, deferred outflows, liabilities and deferred inflows, with the difference reported as net position. Over time, increases or decreases in the Municipality's net position are an indicator of whether its financial health is improving or deteriorating. Other non-financial factors such as the condition of the Municipality's capital assets may need to be considered to assess the overall health of the Municipality. The second statement, the *statement of activities*, presents information showing how the net position changed during the year. All of the current year's revenues and expenses are taken into account in the statement of activities regardless of when cash is received or paid.

The government-wide statements report as governmental activities the Municipality's basic services such as public works and sanitation, public safety, culture and recreation, housing, welfare, community, urban and economic development, education and general administration. These activities are primarily financed through property taxes, other local taxes and intergovernmental revenues. Included in the governmental activities are the governmental funds.

- ***Fund Financial Statements***

The fund financial statements provide more detailed information about the Municipality's most significant funds. Funds are accounting devices that the Municipality uses to keep track of specific sources of funding and spending for particular purposes. Some funds are required by Federal and Commonwealth regulations, as well as by bond covenants.

The Municipality's basic services are included in governmental funds, which are used to account for essentially the same functions reported as governmental activities in the government-wide statements. However, unlike the government-wide statements, the governmental funds are prepared using the flow of current financial resources measurement focus and the modified-accrual basis of accounting. Under this approach, the financial statements focus on near-term inflows and outflows of external resources, as well as on balances of spendable resources available at year-end. Consequently, the governmental fund statements provide a detailed short-term view that helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, additional information is provided on a subsequent page that explains the relationship (or differences) between the government-wide and fund statements.

The governmental fund statements focus on major funds. The Municipality's major funds are the general fund (which accounts for the main operating activities of the Municipality) and funds that comply with a minimum criterion that is, a percentage of the assets and deferred outflows; liabilities and deferred inflows; revenues or expenditures or based on the Municipality's official's criteria if the fund is particularly important to financial statement users. Funds that do not comply with this criterion are grouped and presented in a single column as other governmental funds.

- ***Notes to financial statements***

The basic financial statements also include notes to explain information in the financial statements and provide more detailed data.

### **Required supplementary information**

The statements and notes are followed by the required supplementary information that contains the budgetary comparison schedule for the General Fund.

### **Supplementary information**

The supplementary information included is the Schedule of Expenditures of Federal Awards which presents the federal awards expended by the Municipality during the fiscal year 2013-2014.

## **FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE**

### **Net position**

The following table presents a summary of the Statements of Net Position as of June 30, 2014 and 2013:

**TABLE 1**  
**Summary Statement of Net Position**  
**As of June 30,**

	Governmental Activities	
	2014	2013, as restated
<b>Assets</b>		
Current and other assets	\$ 40,063,875	\$ 46,232,246
Capital assets	121,922,153	123,045,901
<b>Total assets</b>	<b>\$ 161,986,028</b>	<b>\$ 169,278,147</b>
<b>Liabilities</b>		
Current and other liabilities	8,560,994	29,563,665
Long-term liabilities	57,649,110	60,511,873
<b>Total liabilities</b>	<b>66,210,104</b>	<b>90,075,538</b>
<b>Net Position</b>		
Net investment in capital assets	85,270,448	90,966,664
Restricted	13,900,092	9,510,712
Unrestricted (deficit)	(3,394,616)	(21,274,767)
<b>Total net position</b>	<b>\$ 95,775,924</b>	<b>\$ 79,202,609</b>

Net position (difference of non-fiduciary assets, deferred outflows versus liabilities and deferred inflows) serve as a useful indicator of a government's financial position. Over time, increases or decreases in the Municipality's net position is one indicator of whether its financial health is improving or deteriorating. At June 30, 2014, assets exceeded its liabilities by \$95,775,924. Of this amount, \$3,394,616 represents unrestricted deficit. Generally, this component of net position reflects a deficit, primarily due to the effect of long-term obligations such as compensated absences, debts to CRIM, landfill, among other debts, for which the Municipality did not provide funding in previous budgets. Historically, such obligations have been budgeted on a "pay as you go" basis without providing funding for their future liquidation. In addition, operational loans and certain general obligation bonds do not have a related capital asset to be reported as net investment in capital assets. Therefore, they are reported as part of the unrestricted net position section. For the 2014, unrestricted deficit decreased significantly due to the collection of a municipal license tax deficiency claim against a mayor pharmaceutical taxpayer in the amount of \$17 million dollars and to a significant reduction in the expenses of the Municipality's operating fund. Restricted net position represents resources that are subject to external restrictions on how they may be used. Net position reported an increase of 21% with respect to fiscal period 2013.

The largest portion of the Municipality's net position reflects its investment in capital assets (land, buildings, equipment, and infrastructure) less accumulated depreciation and less any related outstanding debt used to acquire those assets. The Municipality uses these assets to provide services to its citizens and, consequently, these assets are not available for future spending. The resources needed to repay the debt related to these capital assets must be provided from other sources because capital assets are not generally liquidated for the purpose of retiring debt.

**Changes in net position**

The following table summarizes the changes in net position for the fiscal years ended 2014 and 2013:

**TABLE 2**  
**Summary of Changes in Net Position**  
**As of June 30,**

	Governmental Activities	
	2014	2013, as restated
<b>Program revenues:</b>		
Fees, fines and charges for services	\$ 3,531,057	\$ 3,768,893
Operating grants and contributions	13,459,274	16,040,817
Capital grants and contributions	1,047,889	972,604
<b>General revenues:</b>		
Property taxes	13,744,118	12,998,860
Municipal license taxes	26,341,325	7,304,313
Sales and use taxes	3,342,628	3,335,800
Grants and contributions not restricted to specific programs	1,510,053	1,351,537
Interest	459,192	1,054,558
Miscellaneous	490,769	154,799
<b>Total revenues</b>	<b>63,926,305</b>	<b>46,982,181</b>
<b>Expenses:</b>		
General government	10,858,815	15,864,864
Public safety	2,560,114	3,487,261
Public works and sanitation	13,852,833	12,833,332
Culture and recreation	2,163,493	2,979,345
Health, welfare and community development	5,242,501	7,020,557
Education	10,394,238	12,791,592
Interest on long-term debt	2,280,996	1,203,582
<b>Total expenses</b>	<b>47,352,990</b>	<b>56,180,533</b>
<b>Change in net position</b>	<b>16,573,315</b>	<b>(9,198,352)</b>
<b>Net position-beginning of year, as restated</b>	<b>79,202,609</b>	<b>88,400,961</b>
<b>Net position-end of year</b>	<b>\$ 95,775,924</b>	<b>\$ 79,202,609</b>

The three major sources of revenues of the Municipality in fiscal year 2014 are: municipal license taxes with 41% of total revenues, property taxes with 21%, and operating grants and contributions with 21%. Revenues increased 36% due mainly to an increase of 261% in municipal license taxes, which were offset by a decrease of 56% and 16% in interest revenue and operating grants and contributions, respectively. As indicated in the previous paragraph, the significant increase reported in municipal license tax is due to the settlement of a legal claim against a mayor pharmaceutical taxpayer for taxes owed for the fiscal years 2003-04 through 2013-14. The following chart illustrates the revenue comparison between 2014 and 2013:

Figure 1

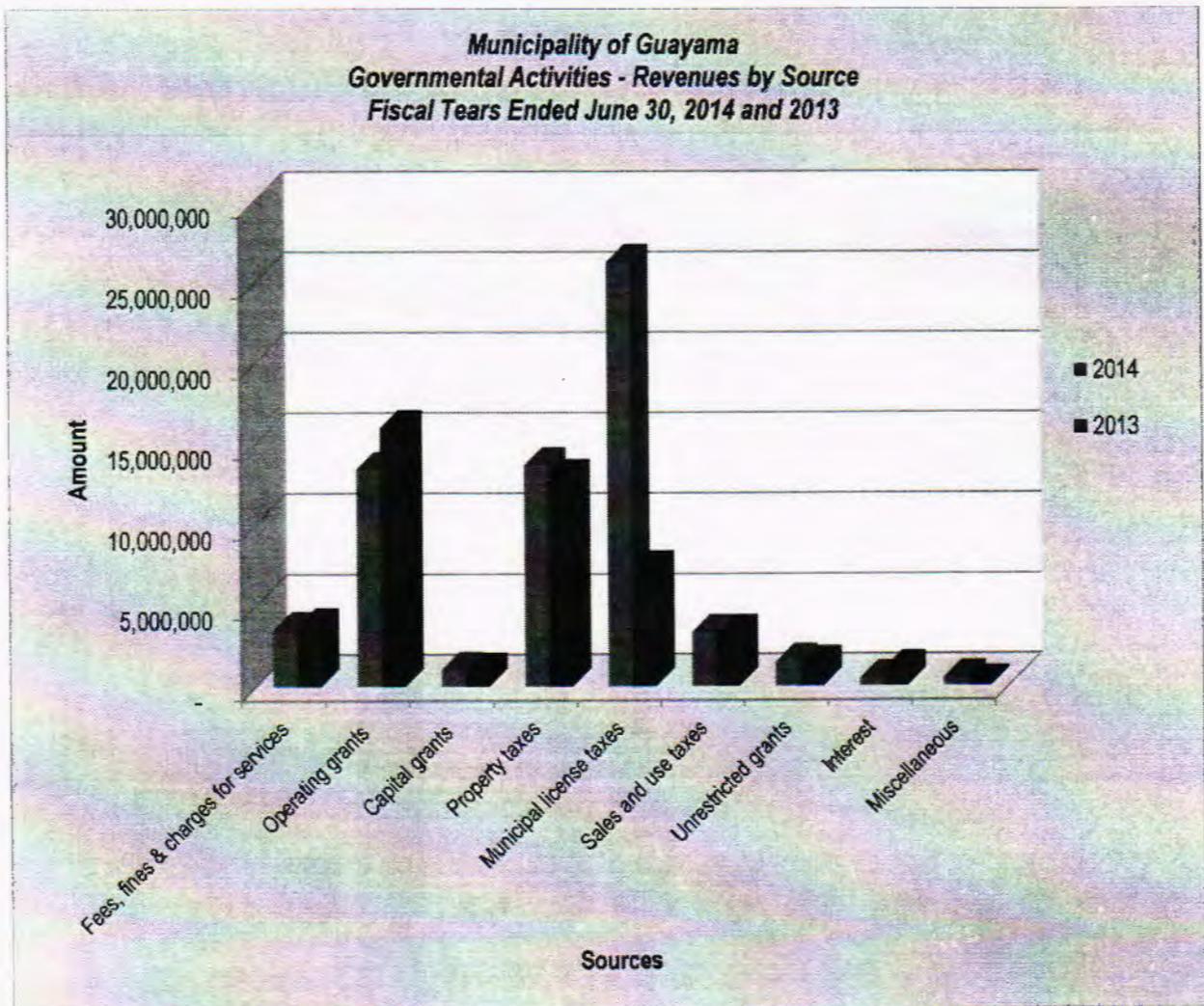
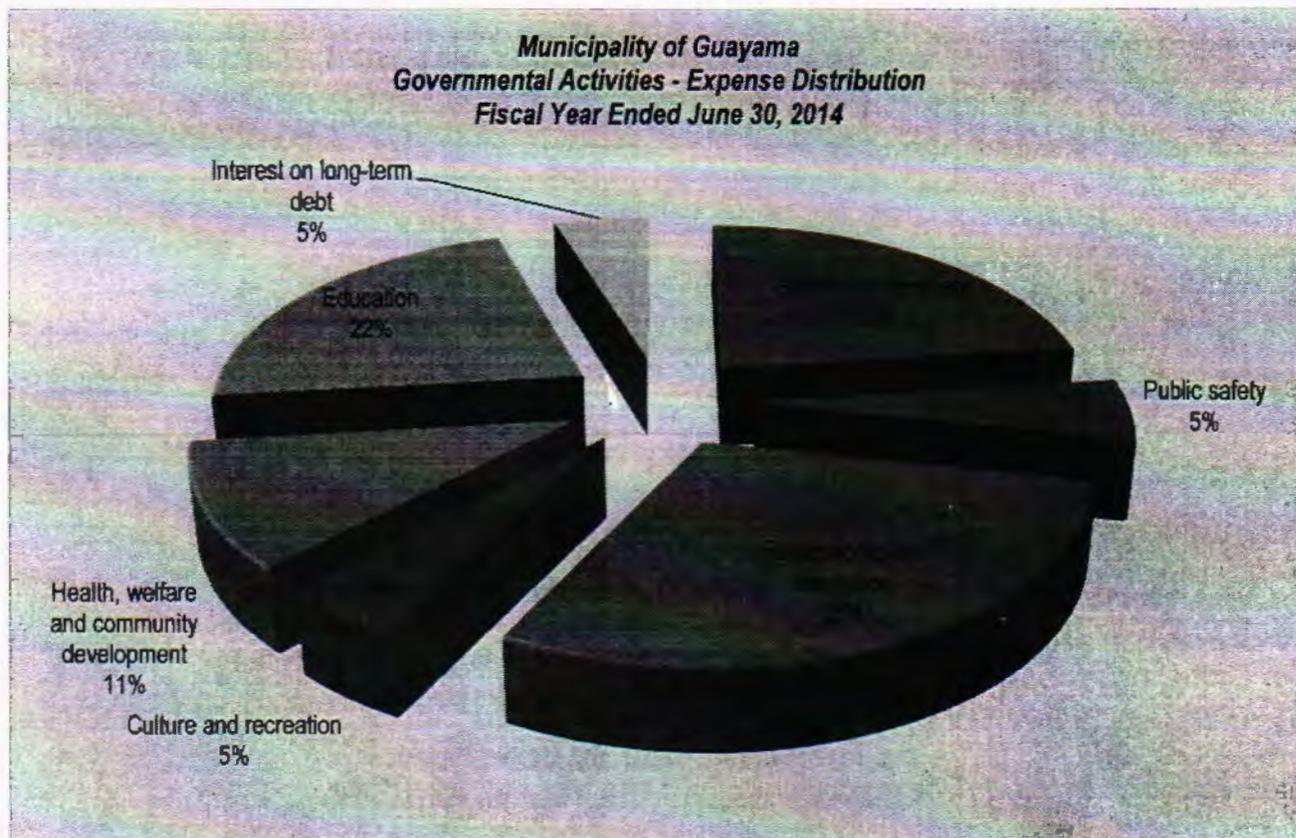


Figure 2



The Municipality's expenses cover a range of services. **Figure 2** illustrates the distribution of expenses in fiscal year 2014. As disclosed, the largest governmental activities expenses are general government with 23%, public works and sanitation with 29% and education with 22%. Total expenses decreased 16% when compared with fiscal year 2013.

The Statement of Activities reports revenues and expenses in a format that focus on the net cost of each function of the Municipality. Both the gross and net cost of the function, which is otherwise being supported by the general government revenues, is compared to the revenues generated directly by the function. This Statement reduces gross direct expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. The following table discloses the 2014 expenses net of program revenue and the general revenues available to finance remaining costs:

TABLE 3

<b>Expenses Net of Program Revenues - Governmental Activities</b>	
<b>Fiscal Year ended June 30, 2014</b>	
<b>Net expenses</b>	<b>2014</b>
General government	\$ (7,549,762)
Public safety	(2,258,915)
Public works and sanitation	(12,740,214)
Culture and recreation	(1,965,544)
Health, welfare and community development	(2,332,577)
Education	(186,762)
Interest on long term debt	(2,280,996)
<b>Total expenses, net of program revenues</b>	<b>(29,314,770)</b>
<b>General revenues</b>	
Taxes	43,428,071
Grants and contributions not restricted to specific programs	1,510,053
Interest and other	949,961
<b>Total general revenues</b>	<b>45,888,085</b>
<b>Change in net position</b>	<b>\$ 16,573,315</b>

Expenses of governmental activities not covered by program revenues were finally covered by other general revenues.

## FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

### Governmental funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending. Such information is useful in assessing the Municipality's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a Municipality's net resources available at the end of a fiscal year as they represent the portion of fund balance which has not yet been limited to use for a particular purpose by either an external party.

For the fiscal year ended June 30, 2014, the governmental funds reported ending fund balances of \$11,055,134, a net decrease of \$1,985,002 or 15%, due to a decrease of 17% in the revenue received from federal grants. Even though there was a net decrease for the year, in overall, total revenues increased by \$68,316 and expenditures decreased by 28% due to a significant decrease of 79% in the capital outlays expenditure reported in the Bond Issuances Fund. \$2,984,921 and \$1,507,187 represent committed and assigned fund balances, respectively, leaving a remaining unassigned fund deficit of \$4,768,426. The remaining fund balance of \$11,331,452 is restricted to indicate that is not available for new spending.

The general fund is the operating fund of the Municipality. The fund deficit of the general fund represents approximately 42% of total ending fund balances. Also, this fund presented restricted fund balance of \$144,389 for public works. Unassigned fund deficit of \$4,768,426 increased 18% with respect to the prior year.

During the fiscal year, the fund deficit of the general fund increased by \$1,217,764. The main sources of revenues of the general fund in fiscal year 2014 are: taxes (property taxes, sales and use taxes and municipal license taxes) with 80%, and intergovernmental subsidies from the Commonwealth with 16%. Revenues increased 5% in comparison to 2013 due to increases in taxes and interests and miscellaneous revenues. The largest expenditures of the general fund are general government with 47% and public works and sanitation with 29%. Expenditures decreased 11%.

### **GENERAL FUND BUDGETARY HIGHLIGHTS**

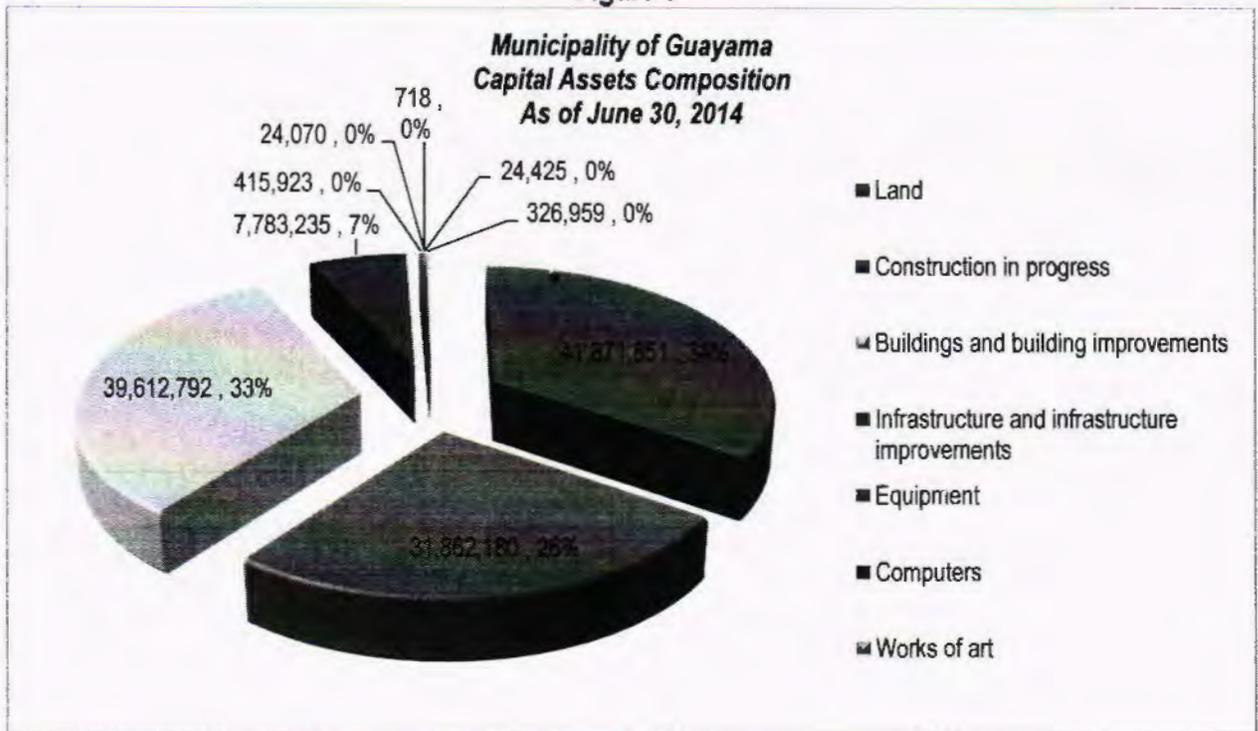
The general fund original budget for the fiscal year 2013-2014 presented a 28% decrease with respect to the prior year budget. Actual revenues were less than revised budgeted revenues by \$1,987,944 (net). However, the Municipality reported a positive variance of \$1,112,369 between revised budgeted appropriations and actual expenditures. Actual expenditures exceeded actual revenues by \$875,575.

### **CAPITAL ASSET AND DEBT ADMINISTRATION**

#### **Capital assets**

At the end of the fiscal year, the Municipality has invested \$121,922,153 (net of accumulated depreciation) in a broad range of capital assets, including buildings, parks, roads, bridges, land, furniture, works of art and equipment. The following graphic discloses the capital assets balances composition as of June 30, 2014:

Figure 3



**Long-term debt**

The following is a summary of the Municipality's outstanding debt as of June 30, 2014 and 2013:

TABLE 4

<b>Outstanding Long-term Debt Fiscal years ended June 30,</b>		
	<b>Governmental Activities</b>	
	<b>2014</b>	<b>2013, as restated</b>
General and special obligation bonds and notes	\$ 41,870,105	\$ 44,810,105
Notes payable to CRIM – Law 42	111,192	114,341
Payable to CRIM – Property tax advances	228,149	-
Compensated absences	3,315,378	2,842,081
Christmas bonus	658,192	482,875
Claims and judgments	1,016,046	1,812,423
Landfill obligation	10,450,048	10,450,048
<b>Total</b>	<b>\$ 57,649,110</b>	<b>\$ 60,511,873</b>

At year-end, the Municipality had outstanding \$41,870,105 in general and special bonds and notes, a decrease with respect to the prior year of \$2,940,000, mainly due to the absence of issuance of new bonds and notes during the year.

More detailed information about the Municipality's long-term liabilities is presented in Note 11 of the financial statements.

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGET**

The Municipality's officials considered certain factors when establishing the fiscal year's 2014-2015 budget. One of these factors is the economy. Among economic areas considered are the estimates for the growth or decline in population, personal income, housing statistics and unemployment rates. The Municipality's unemployment rate at June 2014 stands at 19.5%, and the Commonwealth rate stands at 13.1%.

For the fiscal year 2014-2015, the Municipality applied a conservative approach in the development of budget estimates. Amounts available for appropriations in the General Fund are \$24,797,214, almost the same amount as the prior year estimates. In addition to the general fund estimated budget, the Municipality plans to submit to the Federal and Commonwealth government fund proposals for welfare and community development as well as permanent capital improvements and public works.

### **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 demonstrate the Municipality's accountability for the money it receives. If you have any questions about this report or need any additional information contact the Finance Department at the Municipality of Guayama at P.O. Box 360, Guayama, Puerto Rico, 00785.

	<u>Governmental Activities</u>
<b>Assets</b>	
Cash and cash equivalents	\$ 10,922,492
Cash with fiscal agent	26,530,427
Receivables, net:	
Municipal license taxes	1,015,484
Sales and use taxes	333,513
Due from:	
Commonwealth Government	1,144,062
Federal Government	117,897
Capital assets	
Land and construction in progress	73,734,031
Other capital assets, net	48,188,122
Total capital assets	<u>121,922,153</u>
Total assets	<u>161,986,028</u>
<b>Liabilities</b>	
Accounts payable and accrued liabilities	1,357,871
Interest payable	1,125,648
Due to:	
Commonwealth Government	544,390
Unearned revenues:	
Municipal license taxes	4,924,527
Federal grants	608,558
Noncurrent liabilities:	
Due within one year	4,244,940
Due in more than one year	53,404,170
Total liabilities	<u>66,210,104</u>
<b>Net position</b>	
Net investment in capital assets	85,270,448
Restricted for:	
Debt service	7,769,512
Other purposes	6,130,580
Unrestricted	(3,394,616)
Total net position	<u>\$ 95,775,924</u>

Functions/Programs	Expenses	Program Revenues			Net (Expenses) Revenues and Change in Net Position
		Fees, Fines and Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
<b>Governmental Activities:</b>					
General government	\$ 10,858,815	\$ 3,121,313	\$ 187,740	\$ -	\$ (7,549,762)
Public safety	2,560,114	187,001	114,198	-	(2,258,915)
Public works and sanitation	13,852,833	24,794	39,936	1,047,889	(12,740,214)
Culture and recreation	2,163,493	197,949	-	-	(1,965,544)
Health, welfare and community development	5,242,501	-	2,909,924	-	(2,332,577)
Education	10,394,238	-	10,207,476	-	(186,762)
Interest on long-term debt	2,280,996	-	-	-	(2,280,996)
	<u>\$ 47,352,990</u>	<u>\$ 3,531,057</u>	<u>\$ 13,459,274</u>	<u>\$ 1,047,889</u>	<u>(29,314,770)</u>
<b>General revenues:</b>					
Taxes:					
Property taxes					13,744,118
Municipal license taxes					26,341,325
Sales and use taxes					3,342,628
Grants and contributions not restricted to specific programs					1,510,053
Interest					459,192
Miscellaneous					490,769
Total general revenues					<u>45,888,085</u>
Change in net position					16,573,315
Net position - beginning, as restated					79,202,609
Net position - ending					<u>\$ 95,775,924</u>

	General Fund	Debt Service Fund	Head Start Fund	Bond Issuances Fund	Other Governmental Funds	Total Governmental Funds
<b>ASSETS</b>						
Cash and cash equivalents	\$ 6,655,935	\$ -	\$ 13,858	\$ -	\$ 4,252,699	\$ 10,922,492
Cash with fiscal agent	9,500,000	8,741,408	-	7,771,918	517,101	26,530,427
Receivables, net:						
Municipal license taxes	1,015,484	-	-	-	-	1,015,484
Sales and use taxes	200,526	79,457	-	-	53,530	333,513
Due from:						
Commonwealth Government	183,426	74,295	737,020	-	149,321	1,144,062
Federal Government	-	-	-	-	117,897	117,897
Other funds	4,066,612	-	-	-	3,361,563	7,428,175
<b>Total assets</b>	<b>\$ 21,621,983</b>	<b>\$ 8,895,160</b>	<b>\$ 750,878</b>	<b>\$ 7,771,918</b>	<b>\$ 8,452,111</b>	<b>\$ 47,492,050</b>
<b>LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND FUND BALANCES</b>						
<b>Liabilities</b>						
Accounts payable and accrued liabilities	\$ 679,608	\$ -	\$ 186,945	\$ 118,483	\$ 372,835	\$ 1,357,871
Matured bonds and notes payable	-	3,115,000	-	-	-	3,115,000
Matured interest payable	-	1,125,648	-	-	-	1,125,648
Due to:						
Commonwealth Government	544,390	-	-	-	-	544,390
Other funds	2,914,069	-	563,933	2,610,035	1,340,138	7,428,175
Unearned revenues:						
Municipal license tax	4,924,527	-	-	-	-	4,924,527
Federal Government	-	-	-	-	608,558	608,558
<b>Total liabilities</b>	<b>9,062,594</b>	<b>4,240,648</b>	<b>750,878</b>	<b>2,728,518</b>	<b>2,321,531</b>	<b>19,104,169</b>
<b>Deferred inflows of resources</b>						
Unavailable revenues:						
Municipal license tax	17,000,000	-	-	-	-	17,000,000
Commonwealth Government	183,426	-	-	-	149,321	332,747
<b>Total deferred inflows of resources</b>	<b>17,183,426</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>149,321</b>	<b>17,332,747</b>
<b>Fund balances</b>						
Restricted	144,389	4,654,512	-	5,043,400	1,489,151	11,331,452
Committed	-	-	-	-	2,984,921	2,984,921
Assigned	-	-	-	-	1,507,187	1,507,187
Unassigned	(4,768,426)	-	-	-	-	(4,768,426)
<b>Total fund balances (deficit)</b>	<b>(4,624,037)</b>	<b>4,654,512</b>	<b>-</b>	<b>5,043,400</b>	<b>5,981,259</b>	<b>11,055,134</b>
<b>Total liabilities, deferred inflows of resources and fund balances</b>	<b>\$ 21,621,983</b>	<b>\$ 8,895,160</b>	<b>\$ 750,878</b>	<b>\$ 7,771,918</b>	<b>\$ 8,452,111</b>	<b>\$ 47,492,050</b>

	General Fund	Debt Service Fund	Head Start Fund	Bond Issuances Fund	Other Governmental Funds	Total Governmental Funds
<b>Revenues</b>						
Property taxes	\$ 8,956,858	\$ 5,376,959	\$ -	\$ -	\$ -	\$ 14,333,817
Municipal license taxes	9,341,325	-	-	-	-	9,341,325
Sales and use taxes	2,520,206	500,031	-	-	322,391	3,342,628
Fees, fines and charges for services	348,833	-	-	-	409,744	758,577
Intergovernmental:						
Commonwealth Government	4,232,002	-	-	-	1,260,893	5,492,895
Federal Government	-	-	10,168,494	-	3,162,455	13,330,949
Interest	458,299	644	-	-	249	459,192
Miscellaneous	320,524	-	-	-	170,245	490,769
Total revenues	<u>26,178,047</u>	<u>5,877,634</u>	<u>10,168,494</u>	<u>-</u>	<u>5,325,977</u>	<u>47,550,152</u>
<b>Expenditures</b>						
Current:						
General government	10,538,902	-	-	387	375,140	10,914,429
Public safety	2,476,519	-	-	4,289	42,920	2,523,728
Public works and sanitation	7,644,720	-	-	480,228	2,286,848	10,411,796
Culture and recreation	1,622,620	-	-	-	66,883	1,689,503
Health, welfare and community development	2,027,264	-	-	-	3,193,078	5,220,342
Education	155,969	-	10,168,494	-	16,354	10,340,817
Debt service:						
Principal	-	3,155,000	-	-	-	3,155,000
Interest and other charges	-	2,280,996	-	-	-	2,280,996
Capital outlays	-	-	-	2,681,068	317,475	2,998,543
Total expenditures	<u>24,465,994</u>	<u>5,435,996</u>	<u>10,168,494</u>	<u>3,165,972</u>	<u>6,298,698</u>	<u>49,535,154</u>
Excess (deficiency) of revenues over (under) expenditures	1,712,053	441,638	-	(3,165,972)	(972,721)	(1,985,002)
<b>Other financing sources (uses)</b>						
Transfers in	396,985	31,497	-	-	3,295,305	3,723,787
Transfers out	(3,326,802)	(396,985)	-	-	-	(3,723,787)
Total other financing sources (uses)	<u>(2,929,817)</u>	<u>(365,488)</u>	<u>-</u>	<u>-</u>	<u>3,295,305</u>	<u>-</u>
Net change in fund balances	(1,217,764)	76,150	-	(3,165,972)	2,322,584	(1,985,002)
Fund balance (deficit), beginning, as restated	(3,406,273)	4,578,362	-	8,209,372	3,658,675	13,040,136
Fund balance (deficit), ending	<u>\$ (4,624,037)</u>	<u>\$ 4,654,512</u>	<u>\$ -</u>	<u>\$ 5,043,400</u>	<u>\$ 5,981,259</u>	<u>\$ 11,055,134</u>

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

<b>Total governmental fund balances</b>		<b>\$ 11,055,134</b>
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		121,922,153
Other assets are not available to pay current-period expenditures and, therefore, are reported as deferred inflows of resources in the funds:		
Receivables:		
Municipal license taxes	\$ 17,000,000	
Due from Commonwealth Government:		
P.R. Department of Labor - Law Num. 52	149,321	
Christmas bonus reimbursement	<u>183,426</u>	17,332,747
Long-term liabilities, including bonds and notes payable, are not due and payable in the current period and, therefore, are not reported in the funds:		
General obligation bonds and notes	38,755,105	
Note payable to CRIM - Law No. 42	111,192	
Payable to CRIM - property tax advances	228,149	
Compensated absences	3,315,378	
Christmas bonus	658,192	
Claims and judgments	1,016,046	
Landfill obligation	<u>10,450,048</u>	<u>(54,534,110)</u>
<b>Net position of governmental activities</b>		<b><u>\$ 95,775,924</u></b>

**Net change in fund balances (deficit) - total governmental funds** **\$ (1,985,002)**

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

Governmental funds report capital assets outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense:

Expenditures for capital assets	\$ -	
Less: current-year depreciation	<u>(1,123,748)</u>	(1,123,748)

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds:

Municipal license taxes	17,000,000	
Christmas bonus reimbursement (current year)	183,426	
P.R. Department of Labor - Law Num. 52	<u>149,321</u>	17,332,747

Revenues reported in the funds that are not reported as revenues in the Statement of Activities:

Property taxes - General Fund (current year)	(228,149)	
Property taxes - General Fund (prior year)	(361,550)	
Christmas bonus reimbursement (prior year)	(132,895)	
Federal grants - C.D.B.G.	<u>(234,000)</u>	(956,594)

Expenditures reported in the funds which are not reported as expenses in the Statement of Activities:

Matured bonds and notes principal payments (net change)		215,000
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Repayment of long-term debt is an expenditure in the governmental funds, but reduces long-term liabilities in the Statement of Net Position:

General obligation bonds and notes	2,940,000	
Other long-term liabilities	<u>1,863,777</u>	4,803,777

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures:

Compensated absences	(989,673)	
Christmas bonus	(658,192)	
Claims and judgments	<u>(65,000)</u>	<u>(1,712,865)</u>

**Change in net position of governmental activities** **\$ 16,573,315**

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Guayama (the Municipality) is a local municipal government in the Commonwealth of Puerto Rico (the Commonwealth) founded in 1736. The Municipality has full legislative, fiscal and all other governmental powers and responsibilities expressly assigned by Public Act No. 81 of August 30, 1991, as amended, known as Autonomous Municipalities Act of the Commonwealth of Puerto Rico (Act No. 81). The Municipality is one of seventy-eight municipalities legally separated from the Commonwealth's government.

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

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

The basic financial statements of the Municipality have been prepared in conformity with Generally Accepted Accounting Principles as applied to local governmental units in the United States of America (US GAAP). The Governmental Accounting Standards Board (GASB) is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its governmental accounting and financial reporting standards which, along with subsequent GASB Statements and Interpretations, constitute GAAP for governmental entities.

### A. Financial reporting entity

The financial reporting entity included in this report consists of the financial statements of the Municipality (primary government) and organizations for which the primary government is financially accountable. In addition, the primary government may determine, through exercise of management's professional judgment, that the inclusion of an organization that does not meet the financial accountability criteria is necessary in order to prevent the reporting entity's financial statements from being misleading. Other entities should be evaluated as potential component units if they are closely related to, or financially integrated with, the primary government. It is a matter of professional judgment to determine whether the nature and the significance of a potential component unit's relationship with the primary government warrant inclusion in the reporting entity. An entity should be considered a component unit if meets any of the following three conditions:

1. The primary government appoints a voting majority of the entity's governing body, and either:
  - A financial benefit/ burden exist between the primary government and the entity or
  - The primary government can impose its will on the entity.

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

2. The entity is fiscally dependent on the primary government and there is a financial benefit/burden between the primary government and the entity.
3. It would be necessary to include the entity as a component unit since the primary government's financial statements would be misleading without it.

In addition, "special criteria" applies when evaluating a legally separate, tax-exempt organization as potential component unit. Specifically, such entities must be treated as component units if they meet all of the following criteria:

1. The economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents.
2. The primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization.
3. The economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

Legally separate, tax-exempt organizations that do not meet the above special criteria should still be included as a component unit if the financial statements of the primary government would be misleading without them.

There are two methods of presentation of the component unit in the financial statements: (a) *blending* the financial data of the component units' balances and transactions and (b) *discrete* presentation of the component unit's financial data. When a component unit functions as an integral part of the primary government, its data is *blended* with those of the primary government ("*blended component units*"). That is, the component unit's funds are treated just as though they were funds of the primary government with one exception: the general fund. Component units should be reported as blended if meets any of the following criteria:

1. The component unit's governing body is substantively the same as the governing body of the primary government and there is either:
  - A financial benefit/ burden exist between the primary government and the entity or
  - Management of the primary government has operational responsibility for the primary government.
2. The component unit provides services entirely, or almost entirely, to the primary government or otherwise exclusively, or almost exclusively, benefits the primary government.
3. The component unit's debt is expected to be paid by the primary government.

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Otherwise, the component unit should be presented as discrete. Those component units do not function as an integral part of the primary government and its data is presented discretely (separately) from the data of the primary government (“*discretely component units*”). Legally separate, tax-exempt organizations that meet the special criteria should be included as *discretely component units*.

Based on the above criteria, there are no potential component units which should be included as part of the financial statements as of and for the fiscal year ended June 30, 2014.

### B. Financial statement presentation, measurement focus and basis of accounting

The financial report of the Municipality consists of the Management’s Discussion and Analysis (MD&A), basic financial statements and required supplementary information other than the MD&A. Following is a summary presentation of each, including the measurement focus and basis of accounting. Measurement focus is a term used to describe *which* transactions are recorded within the various financial statements. Basis of accounting refers to *when* transactions are recorded regardless of the measurement focus:

#### Management’s Discussion and Analysis

It provides a narrative introduction and analytical overview of the Municipality’s financial activities.

#### Basic financial statements

The basic financial statements include both the government-wide and fund financial statements. Both sets of statements categorize primary activities as governmental type, which are primarily supported by taxes and intergovernmental revenues.

#### Government-wide Financial Statements (GWFS)

The government-wide financial statements consist of a Statement of Net Position and a Statement of Activities. These statements are prepared using the *economic resources* measurement focus, which refers to the reporting of all of the net position available to the governmental unit for the purpose of providing goods and services to the public. The statements are reported on the *accrual basis of accounting*. Revenues are recognized in the period earned and expenses in the period in which the associated liability is incurred, regardless of the timing of related cash flows. Fiduciary activities, if any, whose resources are not available to finance government programs, are excluded from the government-wide statements. The effect of inter-fund activities is eliminated.

The Statement of Net Position presents all of the reporting entity’s non-fiduciary assets, deferred outflows, liabilities and deferred inflows, with the difference reported as net position. The Statement of Activities reports revenues and expenses in a format that focus on the net cost of each function of the Municipality. Both the gross and net cost of the function, which is otherwise being supported by.

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

the general government revenues, is compared to the revenues generated directly by the function. This Statement reduces gross direct expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. Direct expenses are those that are clearly identifiable with a specific function. As a policy, indirect expenses are not allocated in the Statement of Activities. Program revenues must be directly associated with the function.

The types of transactions included as program revenues are: charges for services, fees, rent, licenses and permits; operating grants which include operating-specific and discretionary (either operating or capital) grants; and capital grants which are capital-specific grants. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes. Property taxes (imposed non-exchange transactions) are recognized as revenues in the year for which they are levied and municipal license taxes and sales and use taxes (derived tax revenues) when the underlying exchange has occurred and time requirements are met. Revenues on both operating and capital grants are recognized when all eligibility requirements (including time requirements) imposed by the provider have been met. For certain expenditure-driven grants, revenue is recognized after allowable expenditures are incurred.

The Municipality reports unearned revenues in the government-wide statements. Unearned revenues arise when resources are received before the Municipality has a legal claim to them (such as advances of derived tax revenues) or before applicable eligibility requirements are met (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the Municipality has a legal claim to the resources, the liability for unearned revenues is removed from the statement of net position and the revenue is recognized.

**Fund Financial Statements (FFS)**

The financial transactions of the Municipality are recorded in individual funds, each of which are considered an independent fiscal entity. Each fund is accounted for by providing a separate set of self-balancing accounts that comprise its assets, deferred outflows, liabilities, deferred inflows, fund equity, revenues and expenditures. Funds are segregated according to their intended purpose which helps management in demonstrating compliance with legal, financial and contractual provisions. Governmental Funds are those through which most governmental functions of the Municipality are financed. The governmental fund statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances with one column for the general fund, one for each major fund and one column combining all non-major governmental funds. Major funds are determined based on a minimum criteria, that is, a percentage of the assets and deferred outflows; liabilities and deferred inflows; revenues or expenditures or based on the Municipality's official's criteria if the fund is particularly important to financial statement users.

The Municipality reports the following major governmental funds:

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**General Fund** – This is the general operating fund of the Municipality. It is used to account for and report all financial resources not accounted for and reported in another fund.

**Debt Service Fund** – This fund is used to account for and report financial resources that are restricted for expenditure for the payment of principal and interest of general obligation bonds and notes issued by the Municipality. This fund accounts for the resources of three individual funds: 1) "CAE Fund," the sinking fund which accounts for the 2% of property taxes collected by the Municipal Revenue Collection Center (CRIM); 2) "Municipal Redemption Fund," the sinking fund that accounts for the 0.2% of the 0.5% collected from the sales and use tax that is, by law, deposited in the Governmental Development Bank (GDB) for the financing of loans to Municipalities; and 3) operational loans that are paid from the general fund's operating revenues.

**Head Start Fund** – This fund is used to account for and report revenues sources received from the U.S. Department of Health and Human Services that are restricted for expenditure for the activities performed under the Head Start program. These activities consist of providing services to pregnant women and children (birth to 5 years-old) and their families that are under the poverty line or are eligible for public assistance.

**Bond Issuances Fund** – This fund is used to account fund and report the financial resources received from the issuance of general obligations bonds and notes for capital outlays, including the acquisition, development and improvement of capital assets.

The FFS are accounted for using the *current financial resources* measurement focus and the *modified-accrual basis of accounting*. Under this method of accounting, revenues are recognized when they are susceptible to accrual (i.e. both *measurable* and *available*). Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Municipality considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

Revenues susceptible to accrual include property taxes, recognized as revenue in the year for which they are levied; municipal license taxes and sales and use taxes, recognized when the underlying exchange has occurred and time requirements are met; and interest. In applying the susceptible to accrual concept to intergovernmental revenues, revenues are recognized when all eligibility requirements (including time requirements) imposed by the provider have been met and revenue becomes available. There are, however, essentially two types of these revenues. In the first case, on expenditure-driven grants, monies must be expended on the specific project or purpose (eligibility requirement), before any amounts are paid to the Municipality. Revenue is, therefore, recognized as expenditures are incurred to the extent available. In the other cases, monies are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. In these cases, revenues are recognized at the time of receipt or earlier, if the susceptible-to-accrual criterion is met. Licenses and permits, charges for services, rent, fines and miscellaneous revenues are generally recorded as revenues when received or are recognized earlier if the susceptible-to-accrual criterion is met.

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

The Municipality reports unearned revenues in the governmental funds statements. Unearned revenues arise when resources are received before the Municipality has a legal claim to them (such as advances of derived tax revenues) or before applicable eligibility requirements are met (in case of certain federal expenditure-driven grants, if resources are received before allowable expenditures are incurred). In subsequent periods, when the Municipality has a legal claim to the resources, the liability for unearned revenues is removed from the balance sheet and the revenue is recognized.

Expenditures are generally recognized when the related liability is incurred as under accrual basis of accounting. Certain exceptions to this fundamental concept include the following: (1) payments of principal and interest on general long-term debt, which are recorded as expenditures when due, except for principal and interest due on July 1 (in this case, amounts are recorded as liabilities and expenditures on June 30 since amounts have been accumulated or transferred to the debt service fund before July 1 payments are made) and (2) vested compensated absences, claims and judgments and special termination benefits, which are recorded as expenditures only to the extent that they are expected to be liquidated with expendable financial resources (in the GWFS, the expense and related accrual liability for long-term portions of debt must be included).

Long-term assets and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying Balance Sheet – Governmental Funds of the FFS. Likewise, long-term liabilities (generally, those un-matured that will not require the use of current financial resources to pay them) are also not accounted for in the FFS.

Since the FFS are presented on a different measurement focus and basis of accounting than the GWFS, reconciliation is necessary to explain the adjustments needed to transform the FFS into the GWFS. This reconciliation is part of the financial statements.

**Notes to financial statements**

The notes to financial statements provide information that is essential to a user's understanding of the basic financial statements.

**Required Supplementary Information (RSI)**

The Required Supplementary Information consists of the Budgetary Comparison Schedule – General Fund as required by GASB.

**C. Financial reporting presentation**

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

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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

**Special Revenue Fund** – Is a governmental fund used to account for and report the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments or for major capital projects) that are legally restricted or committed to expenditure for specified purposes other than debt service or capital projects. Resources restricted or committed to expenditure for purposes normally financed from the general fund are generally accounted for in the general fund provided that all applicable legal requirements can be appropriately satisfied and the use of special revenue funds is not required unless they are legally mandated.

**Capital Projects Fund** – is a governmental fund used to account for and report financial resources that are restricted or committed to expenditure for capital outlays, including the acquisition or construction of major capital facilities, including those outlays financed by the general obligation bond proceeds (other than those financed by proprietary funds or in trust funds for individuals, private organizations, or other governments).

The use of the capital projects funds has been limited to only for major capital acquisitions, construction or improvement activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalizable assets (such as furniture, office equipment, vehicles and other minor capital assets or improvements) have been reported in the governmental fund from which financial resources were used for the payment.

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

**D. Deposits and investments**

The Municipality's cash and cash equivalents consist of cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. Nonnegotiable certificates of deposits with original maturity of more than three months are considered time deposits as required by current standards. The Municipality follows the practice of pooling cash of all funds except for certain Commonwealth's grants, restricted funds generally held by outside custodians and federal grants. Available pooled cash balance beyond immediate needs is invested in certificates of deposits. Cash and cash equivalents related to Commonwealth and Federal grants (including Commonwealth Legislature Resolutions) are restricted since their use is limited by applicable agreements or required by law.

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

The laws and regulations of the Commonwealth of Puerto Rico authorize the Municipality to invest 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 the GDB.

**E. Restricted assets**

Restricted assets are liquid assets which have third-party limitations on their use. Cash and cash equivalents related to Commonwealth and Federal grants (including Commonwealth Legislature Resolutions) are restricted since their use is limited by applicable agreements or required by law.

Restricted cash with fiscal agent in the debt service fund consists of the undisbursed balance of property and sales tax collections retained by the Commonwealth of Puerto Rico, which are restricted for the repayment of the Municipality's general and special obligation bonds and notes as established by law. Restricted cash with fiscal agent of the other governmental funds represents the undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the GDB or a federal government agency.

**F. Receivables and due from governmental entities**

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions. Amounts due from Commonwealth government in the general and debt service funds represent property tax revenues of the current fiscal year collected by the CRIM on the subsequent fiscal year. Amounts due from Commonwealth and federal governments reported in the special revenue or capital project funds represent amounts owed to the Municipality for the reimbursement of expenditures incurred pursuant to federally funded or state funded programs.

**G. Inter-fund receivables and payables**

Activities among funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due from/to other funds" (i.e., the current portion of inter-fund loans) or "advances to/from other funds" (i.e., the non-current portion of inter-fund loans). All other outstanding balances among funds are reported as "due from/to other funds".

Advances between funds, as reported in the fund financial statements, if any, are reported as "nonspendable" in the fund balance section of the Balance Sheet to indicate that they are not available for appropriation and are not expendable available financial resources.

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**H. Inventories**

The Municipality purchases gasoline, oil and other expendable supplies held for consumption. The cost of those purchases is recorded as expenditure when incurred in the appropriate fund but the year-end inventory is not recorded in the Statement of Net Position, as management believes is not significant.

**I. Capital assets**

Capital assets reported in the governmental activities in the Statement of Net Position include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items). The Municipality defines capital assets (except infrastructure assets) as assets with an individual cost of more than \$500 and an estimated useful life in excess of one year. Infrastructure assets are capitalized based on a percentage of the estimated useful life. The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets are capitalized at historical cost or estimated historical cost if historical cost is not available. Donated assets are recorded as capital assets at their estimated fair market value at the date of donation. All capital assets, other than land and construction in progress, are depreciated using the straight-line method over the following useful lives:

<u>Description</u>	<u>Useful Life</u>
Buildings and site improvements	40 years
Infrastructure	40 years
Infrastructure improvements	15 years
Equipment	5 years
Computers	3 years
Works of art	10 years
Furniture and fixtures	5 years
Vehicles	5 years

In accordance with current accounting standards, capital assets are reviewed for impairment. Impairment occurs when there is a significant decline in asset service utility due to the occurrence of a prominent event or change in circumstances affecting the asset. Current standards provide guidance for accounting and reporting for impairment and for insurance recoveries.

**J. Deferred outflows/inflows of resources**

In addition to assets, the Statement of Net Position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/ expenditure) until then.

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

In addition to liabilities, the Statement of Financial Position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The government has two items that qualify for reporting in this category:

1. **Government-mandated or voluntary non-exchange transactions received before the time requirements have been met** – Federal and state grants received before the beginning of the fiscal year to which they pertain are recognized as deferred inflows of resources on both the Balance Sheet of the governmental funds and in the government-wide Statement of Net Position. The amounts deferred would be recognized as an inflow of resources (revenue) in the period in which the time requirements are fulfilled.
2. **Unavailable revenue reported under the modified-basis of accounting** – Amounts collected or to be collected after the availability period are recognized as *unavailable revenue* in the governmental funds Balance Sheet. The amounts are deferred and recognized as an inflow of resources (revenue) in the period that the amounts become available. Since this deferred inflow of resources is the result of the modified-accrual basis of accounting, it is only reported in the governmental fund financial statements.

**K. Long-term obligations**

Long-term debt and other long-term obligations, which are reported as liabilities in the governmental activities column in the Statement of Net Position, include general and special obligation bonds and notes, liabilities for compensated absences, claims and judgments, landfill closure and post-closure costs and long-term liabilities to other governmental entities.

Related bond issuance costs, whenever rise, are reported as current outflows of resources in the Statement of Activities, as required by current standards. Governmental fund types recognize bond issuance costs as expenditures during the current period. Those issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the appropriate fund.

**L. Compensated absences**

The Municipality's employees accumulate vacation, sick leave and compensatory time based on continuous service. Compensated absences are recorded as a liability if (1) are earned on the basis of services already performed by employees, (2) it is probable that will be paid (in the form of paid time off, cash payments at termination or retirement, or some other means) and (3) are not contingent on a specific event (such as illness). The compensated absences are accumulated on the basis of 2½ days per month of vacation and 1½ days per month of sick pay and compensatory time up to a maximum of 60 days of vacations and 90 days of sick leave. Upon separation from employment, the accumulated vacations are liquidated up to the maximum number of days. Accumulated sick leave, which is accrued

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

based on all vesting amounts for which payment is probable, is liquidated to employees with 10 years or more service up to the maximum number of days.

The accrual of compensated absences includes estimated payments that are related to payroll. The entire compensated absence liability is reported on the government-wide financial statements. For governmental fund financial statements, the current portion of unpaid compensated absences is the amount that is normally expected to be paid using expendable available financial resources. The non-current portion of the liability is not reported.

Pursuant to Law No. 152 of August 20, 1996, effective July 1, 1997, the Municipality is required to pay any excess of vacations and sick leave accumulated over 90 days as of December 31 of each year. Payments should be made on or before March 31 of the following year.

### M. Claims and judgments

The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund when they matured (generally, when payment is due). The accompanying government-wide financial statements include an amount estimated as a contingent liability for liabilities as incurred.

### N. Net position

In the government-wide statements, assets plus deferred outflows of resources less liabilities and deferred inflows of resources equal net position, and should be displayed in three components: net investment in capital assets, restricted, and unrestricted, as follows:

**Net investment in capital assets:** Consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of bonds, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. The portion of the debt or deferred inflows of resources attributable to the unspent debt proceeds is not included in the calculation of net investment in capital assets. Instead, the portion of the debt or deferred inflows of resources is included in the same net position component (restricted or unrestricted) as the unspent amount.

**Restricted net position:** The restricted component of net position consists of restricted assets (subject to restrictions beyond the Municipality's control) reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported. Restrictions are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or imposed by the law through constitutional provisions or enabling legislation.

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

**Unrestricted net position:** Unrestricted net position is the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position. Unrestricted net position is 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.

### O. Net position flow assumption

Sometimes, the government will fund outlays for a particular purpose from both restricted (restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

### P. Fund balances

The GASB Statement No. 54 *Fund Balance Reporting and Governmental Fund Type Definitions* ("GASB No. 54") establishes accounting and reporting standards for all governments that report governmental funds. It also establishes criteria for classifying fund balances into specifically defined classifications and clarifies definitions for governmental fund types. These classifications comprise a hierarchy based primarily on the extent to which the Municipality is bound to observe constraints upon the use of the resources reported. The classifications are as follows:

**Nonspendable:** Amounts that cannot be spent because are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

**Restricted:** Amounts constrained by external parties (creditors, grantors, contributors, or laws and regulations of other governments), imposed by law through constitutional provisions or by enabling legislation. Enabling legislation authorizes the Municipality to assess, levy, charge or otherwise mandate payment or resources (from external resource providers) and includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation. Legally enforceability means that the Municipality can be compelled by an external party such as citizens, public interest groups, or the judiciary to use resources created by enabling legislation only for the purposes specified by the legislation.

**Committed:** Amounts that can be used only for the specific purposes pursuant to constraints imposed through formal action (ordinance or resolution) by consent of the government's highest level of decision-making authority, which in the case of the Municipality is the Mayor and the Municipal Legislature. Those committed amounts cannot be used for any other purposes unless the Mayor and the Municipal Legislature removes or changes the specified use by taking the same type of action (ordinance or resolution) it employed to commit those amounts. Formal action to commits fund balance to a specific purpose should occur prior to the end of the fiscal year, but the amount, if any, which will be subject to the constraint, may be determined in the subsequent period.

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

**Assigned:** Amounts that are constrained by the Municipality's intent to be used for specific purposes, but are neither restricted nor committed. In distinction to committed balances, the authority for making an assignment is not required to be the government's highest level of decision-making authority. (both the Mayor and the Municipal Legislature). It is the Municipality's policy that intent can be expressed by the Mayor, the Finance Director (the official to which the Mayor has also delegated the authority to assign amounts) or by any other official or body to which the Mayor delegates. Furthermore, the nature of the actions necessary to remove or modify an assignment is not as prescriptive as it is with committed fund balances. With the exception of the general fund, this is the residual fund balance of the classification of all governmental funds with positive fund balances. Action taken to assign fund balance may be made after year-end.

**Unassigned:** Is the residual classification for the general fund and includes all spendable amounts not restricted, committed or assigned. The general fund is the only fund that reports a positive unassigned fund balance amount. For all other governmental funds the unassigned classification is used only to report a deficit balance resulting for the 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, 2014.

### Q. Fund balance flow assumptions

Sometimes, the government will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

### R. Accounting for pension costs

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

## NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

For the purpose of applying the requirements of GASBS No. 27, the 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), a multi-employer hybrid defined contribution plan in which the employees of the Municipality participate. The Municipality is considered a participant, and not a sponsor, of this retirement system since the majority of the participants in the aforementioned pension trust fund are employees of the Commonwealth of Puerto Rico and the basic financial statements of such retirement system are part of the Commonwealth's financial reporting entity.

### S. Inter-fund and intra-entity transactions

The Municipality has the following types of transactions among funds:

1. **Operating transfers** - Legally required transfers that are reported when incurred as "Transfers-in" by the recipient fund and as "Transfers-out" by the disbursing fund.
2. **Intra-entity transactions** - Transfers between the funds of the primary government are reported as inter-fund transfers with receivables and payables presented as amounts due to and due from other funds.

### T. Risk financing

The Municipality carries commercial insurance that consists of professional, public responsibility, property and theft, auto and fidelity bond coverage. Under Law Num. 63 of June 21, 2010, the Legislature of the Commonwealth of Puerto Rico authorized the municipalities to procure and manage, at their own discretion, all insurance policies, including those related to the health plans provided to the municipal employees. The Municipality's commercial insurance and health plan coverages are procured and negotiated through a single insurance broker. The broker obtains quotes from the different insurance companies and the Municipality's management makes the selection based on coverage and price. The total cost of the annual premiums is financed through a payment plan made with an insurance financing company, and the monthly payments are deducted from the advances of property tax and amounts of the municipal equalization fund sent to the Municipality by the CRIM.

The Municipality obtains workers' compensation insurance through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth of Puerto Rico. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. The annual premium is also deducted from the monthly advances issued by the CRIM.

#### NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

#### U. Use of estimates

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

#### V. Future adoption of accounting pronouncements

The GASB has issued the following statements, which the Municipality has not yet adopted:

1. **GASB Statement No. 68 "Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27."** The provisions of this Statement are effective for fiscal years beginning after June 15, 2014 (fiscal year ended June 30, 2015).
2. **GASB Statement No. 69 "Government Combinations and Disposals of Government Operations."** The provisions 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 (fiscal year ended June 30, 2015).
3. **GASB Statement No. 71 "Pension Transition for Contributions Made Subsequent to the Measurement Date."** The provisions of this Statement should be applied simultaneously with the provisions of Statement 68 (fiscal year ended June 30, 2015).

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

## NOTE 2 – CASH AND CASH EQUIVALENTS

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

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

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

Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2014.

**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, 2014, 2) limiting the weighted average maturity of its investments to three months or less, and 3) keeping most of its bank deposits in interest-bearing accounts generating interests at prevailing market rates. At June 30, 2014, the Municipality's investments in certificates of deposits are recorded at cost, which approximates their fair value.

Therefore, the Municipality's management has concluded that, at June 30, 2014, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

**Custodial credit risk** – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. The Municipality maintains cash deposits in commercial and governmental banks located in Puerto Rico. Under Commonwealth of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral by the Municipality are held by the Secretary of Treasury of Puerto Rico in the Municipality's name. Deposits with the GDB are uninsured and uncollateralized. However, no losses related to defaults by the GDB on deposit transactions have been incurred by the Municipality through June 30, 2014.

Therefore, the Municipality's management has concluded that, at June 30, 2014, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

## NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

**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, 2014.

**Deposits** – At year-end, the Municipality's bank balance of deposits in commercial banks amounting to \$10,922,492 was covered by federal depository insurance or by collateral held by the Secretary of Treasury of Puerto Rico in the Municipality's name. Deposits in governmental banks (all of which are uninsured and uncollateralized), amounts to \$26,530,427 as of June 30, 2014.

## NOTE 3 – RECEIVABLES

### A. Municipal license taxes

Municipal License taxes are assessed annually by the Municipality to all organizations or entities subject to the tax doing business in the Municipality's location except for entities totally or partially exempt pursuant to certain Commonwealth's statutes. This tax is based generally on volume of business or gross sales as shown in a tax return that should be submitted on or before April 15.

During the fiscal year ended June 30, 2014, the tax rates were as follows:

- Financial business – 1.50% of gross revenues
- Other organizations - .50% of gross revenues

The tax is due in two equal installments on July 1 and January 1 of each fiscal year. Tax revenue is recognized at that moment by the Municipality. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year in the amount of \$4,924,527 is recorded as unearned revenues.

On March 18, 2015 the Municipality of Guayama signed a legal transactional agreement with Pfizer Pharmaceuticals, LLC ("Pfizer") in the amount of \$17,000,000 for the final settlement of municipal license tax deficiencies, claimed by the Municipality for the fiscal years 2003-04 through 2013-14. Of this amount, \$15,984,516 was already paid by Pfizer to the Municipality in March 2011 as part of the bond requirement established in the legal proceedings. This amount was recognized as a contingency in the prior years' financial statements pending the resolution of the legal claim. The remaining balance due of \$1,015,484 was recognized as a receivable as of June 30, 2014 and was subsequently collected in April 2015. Since both amounts were not available for the payment of current liabilities, the entire \$17,000,000 was recognized as deferred inflows of resources in the fund financial statements.

### NOTE 3 – RECEIVABLES (CONTINUED)

#### B. Sales and use taxes

On July 4, 2006, the Commonwealth Legislature approved Act No. 117 ("Act 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 117 also authorizes each municipal government to impose a municipal sale 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.

On July 29, 2007, the Commonwealth Legislature approved Act No. 80 (Act 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).

The amount collected by the PRDT, (.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 be distributed among all the municipalities in accordance with a formula created by the Act,
- .2% of the .5% will be deposited in a Municipal Redemption Fund to finance loans to Municipalities 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

The Municipal Legislature approved a municipal ordinance to conform to dispositions of Act 80. Effective January 1, 2011, the Commonwealth of Puerto Rico adopted a new Internal Revenue Code (2011 PR Code). Subtitle D (Sections 4010 to 4070) of the 2011 PR Code incorporates the dispositions applicable to the sales and use tax. As stated by Section 4050, the Municipalities may use the sales and use tax proceeds to finance solid waste, recycling, capital projects, health and public safety programs as well as any other activity that promotes sound public administration.

Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the PRDT. The tax is due the 10th day of each month based on tax collected in the preceding month. The Municipality recorded as revenue \$2,520,206 in the general fund corresponding to the 1% imposition; \$500,031 in the debt service fund corresponding to the Municipal Redemption Fund; and \$322,391 in the other governmental funds corresponding to the Municipal Development Fund.

Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the Municipality. The tax is due the 20th day of each month based on tax collected in the preceding month. Municipal sales and use tax receivable of \$200,526 in the general fund, represents the tax collected on

**NOTE 3 – RECEIVABLES (CONTINUED)**

June by individuals, organizations and entities but reported and paid to the Municipality on or before July 20, net of uncollectible accounts; \$79,457 in the debt service fund and \$53,530 in the other governmental fund, respectively, represent amounts of Municipal Redemption Fund and the Municipal Development Fund, respectively, collected on June from individuals, organizations and entities but paid by the PRDT subsequent to June 30, which are reported as receivable in the other governmental and debt service funds.

On June 30, 2013, the Commonwealth approved Act No. 40 which, among other things, reduces the municipal sales and use tax from 1.5% to 1% and increasing the Commonwealth sales and use tax from 5.5% to 6% effective December 1, 2013. This Act was subsequently amended to change this effective date from December 1, 2013 to February 1, 2014.

In order to address the fiscal and credit crisis of the Commonwealth of Puerto Rico, the GDB liquidity and the difficult fiscal situation of the municipalities of Puerto Rico, on January 24, 2014, Commonwealth approved Act No. 18 and 19. Those Acts provide for the restructuring and creation of financing structures from sales and use tax sources to guarantee and pay municipal long-term debt issuances. As a result of this legislation, the municipalities of Puerto Rico may improve their credit capacity along with maintaining sufficient resources for operations.

**Act No. 18 of January 24, 2014**

The purpose of this Act is to create a special fund called Municipal Administration Fund (FAM) under custody of the Government Development Bank of Puerto Rico (GDB) that permits the Municipalities to guarantee and pay long term debt and provide funds for its general operations. In addition, this Act improves the financing capacity of the Puerto Rico Sales Tax Financing Corporation (COFINA), a Commonwealth fund administered by GDB and the P.R. Secretary of Treasury. The Act includes provisions for municipalities that do not want to be covered by the Act. Special rules apply for those municipalities. The Act is effective on February 1, 2014.

The 6% corresponding to the Commonwealth's sales and use tax will be deposited in COFINA. From these funds, during a transitory period from February 1, 2014 to June 30, 2014, the Commonwealth will deposit \$43,440,184 in the FAM to be distributed to the Municipalities as follows:

- .2% will be deposited in a Municipal Development Fund to be distributed to the municipalities,
- .2% will be deposited in a Municipal Redemption Fund to guarantee and repay the municipalities long term debt and,
- .1% 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.

After July 1, 2014 the 6% corresponding to the Commonwealth's sales and use tax will be deposited in COFINA. From these funds, the Commonwealth will deposit .5% in the FAM. Distribution to municipalities will depend on whether the municipalities signed an agreement to be covered or not covered by the Act's provisions. The Municipality of Guayama signed the agreement to be covered.

### NOTE 3 – RECEIVABLES (CONTINUED)

For municipalities covered by the agreement, the .5% will be distributed as follows:

- .2% will be deposited in the Municipal Development Fund to be distributed to the municipalities,
- .2% will be deposited in a Municipal Redemption Fund to then be deposited in the municipalities general fund (the municipalities have the option to maintain funds in the Municipal Redemption Fund or to transfer funds from the Municipal Development Fund to increase its debt margin and issue loans to be obtained from financial institutions)
- .1% 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.

For municipalities not covered by the agreement the .5% will be distributed as follows:

- .2% will be deposited in the Municipal Development Fund. Section 4 of the Act requires amounts deposited in the Municipal Development Fund of municipalities not covered by the Act to be redistributed to the municipalities covered by the Act,
- .2% will be deposited in a Municipal Redemption Fund to guarantee and repay long-term debt through any financial institution (each semester the municipalities may transfer to their general fund the funds in excess of debt service requirements),
- .1% 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.

#### **Act No. 19 of January 24, 2014**

The purpose of this Act is to create the Municipal Finance Corporation (COFIM), a public corporation and a component unit of the Governmental Development Bank of Puerto Rico (GDB) which may issue, pay or refinance long-term debt of municipalities. Principal and interest of these bonds and loans will be guaranteed with the municipal sales and use tax (1%). The Act includes provisions for municipalities that do not want to be covered by the Act. Special rules apply for those municipalities. The Act is effective on February 1, 2014.

After July 1, 2014, the 1% corresponding to the municipalities' sales and use tax will be deposited in COFIM. From these funds COFIM will deposit to the COFIM's sinking fund the greater of: .3% of the 1% municipal sales and use tax or an Annual Rental Fee (RFA). The RFA for fiscal year 2014-2015 will be \$65,541,281 and thereafter will be 1.5% of the RFA of the preceding fiscal period. The excess of the required deposit to the COFIM's sinking fund (.7% of the 1% of the municipal sales and use tax) will be transferred to the general fund of municipalities covered by the agreement or to the Municipal Redemption Fund as decided by the municipality. Before the transfer of the .7% to the municipalities covered by the Act, COFIM will transfer the 1% municipal sales and use tax to the municipalities not covered by the Act. These municipalities cannot obtain loans guaranteed by COFIM's sinking fund.

If at any moment the required deposits to the COFIM's sinking fund were not sufficient to pay the principal and interest of any outstanding obligation, the deficiency will be covered by appropriations of the Commonwealth's general fund budget.

**NOTE 4 – DUE FROM (TO) GOVERNMENTAL ENTITIES**

**A. Amounts due from governmental entities as of June 30, 2014 are as follows:**

	<u>Commonwealth Government</u>	<u>Federal Government</u>
<b><u>Major fund – General fund:</u></b>		
P.R. Department of Treasury – Christmas bonus reimbursement	\$ 183,426	-
<b><u>Major fund – Debt service fund:</u></b>		
Municipal Revenue Collection Center (CRIM) – property taxes	74,295	-
<b><u>Major fund – Head Start:</u></b>		
P.R. Department of Family - Administration for the Care and Integral Development of Children	737,020	-
<b><u>Other Governmental Funds:</u></b>		
P.R. Department of Labor and Human Resources – Law No. 52	149,321	-
U.S. Department of Housing and Urban Development – C.D.B.G. Entitlement	-	117,897
	<u>\$ 1,144,062</u>	<u>\$ 117,897</u>

Certain amounts are recorded as deferred inflows of resources in the governmental funds statements since they are not available as required by current standards. See related note 8.

**B. Amounts due to governmental entities as of June 30, 2014 are as follows:**

<u>Description</u>	<u>Commonwealth Government</u>
<b><u>Major fund – General fund:</u></b>	
P.R. Employees Retirement System (FRS)	\$ 150,041
P.R. Department of Treasury	31,149
P.R. Department of Labor	11,726
P.R. Aqueduct and Sewer Authority (PRASA)	169,067
P.R. General Services Administration	78,716
Association of Employees of the Commonwealth of Puerto Rico	77,571
Others	26,120
	<u>\$ 544,390</u>

**NOTE 5 – INTERFUND TRANSACTIONS**

**A. Due from/to other funds**

Amounts due from/to other funds in the general fund represent advances to other funds to finance payroll, payroll taxes and other expenditures as follows:

Receivable Fund	Payable Funds	Amount
<b>General Fund</b>	<b><u>Major Funds:</u></b>	
	Head Start	\$ 563,933
	Bond Issuances	2,162,541
	<b><u>Other Governmental Funds:</u></b>	
	Special Revenue State & Local – Law No. 52	149,321
	Special Revenue State & Local – Committed Funds	1,021,579
	Special Revenue Federal – Section 8 HCVP	18,525
	Special Revenue Federal – C.D.B.G. Entitlement	54,626
	Special Revenue Federal – Homeland Security	50,396
	Special Revenue Federal - Emergency Solutions Grants Program	15,000
	Capital Project State & Local – P.R. Department of Transportation	30,691
		<u>\$ 4,066,612</u>
<b>Other Governmental Funds</b>	<b><u>Major Funds:</u></b>	
	General Fund	\$ 2,914,069
	Bond Issuances Fund	447,494
		<u>3,361,563</u>
	<b>Total</b>	<b><u>\$ 7,428,175</u></b>

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**NOTE 5 – INTERFUND TRANSACTIONS (CONTINUED)**

**B. Transfers-in (out)**

Transfers among individual funds were made for operational purposes as follows:

<u>Originating Fund</u>	<u>Receiving Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Other Governmental Funds	Creation of assigned and committed funds	\$ 2,731,295
General Fund	Other Governmental Funds	Reimbursement of expenditures	564,010
General Fund	Debt Service Fund	Principal and interest payment of operational loans	31,497
Debt Service Fund	General Fund	Transfer of excess funds available in sinking fund for use in operating activities	396,985
<b>Total</b>			<b><u>\$ 3,723,787</u></b>

**NOTE 6 – ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

Accounts payable and accrued liabilities as of June 30, 2014 are detailed as follows:

	<u>General Fund</u>	<u>Head Start Fund</u>	<u>Bond Issuances Fund</u>	<u>Other Governmental funds</u>	<u>Total</u>
Accounts payable - vendors	\$ 618,404	\$ 186,945	\$ 118,483	\$ 372,835	\$ 1,296,667
Accrued liabilities – payroll withholdings	61,204	-	-	-	61,204
<b>Total</b>	<b><u>\$ 679,608</u></b>	<b><u>\$ 186,945</u></b>	<b><u>\$ 118,483</u></b>	<b><u>\$ 372,835</u></b>	<b><u>\$ 1,357,871</u></b>

**NOTE 7 – UNEARNED REVENUES**

The amounts reported as unearned revenues as of June 30, 2014 are detailed as follows:

	<u>Amount</u>
<b><u>Major fund – General fund:</u></b>	
Municipal license taxes collected in the fiscal year 2013-2014 that correspond to the 2014-2015 fiscal year budget	<u>\$ 4,924,527</u>
<b><u>Other Governmental Funds:</u></b>	
Federal grants received for which qualifying expenditures have not been incurred:	
Rural Development Grants	\$ 338,690
Child and Adult Care Food Program	104,316
U.S. Department of Homeland Security Grants	43,591
Emergency Solutions Grants Program	12,582
Housing Preservation Grants Program	23,637
Others	85,742
	<u>\$ 608,558</u>

**NOTE 8 – DEFERRED INFLOWS OF RESOURCES – GOVERNMENTAL FUNDS**

As required by current standards, revenues and other governmental fund financial resources should be recognized in the accounting period in which they become both measurable and available. When an asset is recorded in governmental fund's financial statements but the revenue is not available, the Municipality should report a deferred inflow of resources until such time as the revenue becomes available. A detail of these balances follows:

	<u>Municipal License Taxes</u>	<u>Commonwealth Government</u>
<b><u>Major fund - General fund:</u></b>		
Settlement of municipal license tax deficiency claims against Pfizer Pharmaceuticals, LLC	\$ 17,000,000	\$ -
P.R. Department of Treasury – Christmas bonus reimbursement	-	183,426
<b><u>Other governmental funds:</u></b>		
P.R. Department of Labor – Law No. 52	-	149,321
	<u>\$ 17,000,000</u>	<u>\$ 332,747</u>

**NOTE 9 – FUND BALANCE**

**A. Fund balance classifications**

The governmental fund balance classifications and amounts at June 30, 2014 are shown in the following table:

	General Fund	Debt Service Fund	Head Start Fund	Bond Issuances Fund	Other Governmental Funds	Total Governmental Funds
Restricted:						
Public works and sanitation	\$ 144,389	\$ -	\$ -	\$ -	\$ 838,677	\$ 983,066
Public safety	-	-	-	-	415,841	415,841
Health, welfare and community development	-	-	-	-	127,779	127,779
Education	-	-	-	-	35,206	35,206
Debt service	-	4,654,512	-	-	-	4,654,512
Capital outlays	-	-	-	5,043,400	-	5,043,400
General government and other purposes	-	-	-	-	71,648	71,648
	<u>144,389</u>	<u>4,654,512</u>	<u>-</u>	<u>5,043,400</u>	<u>1,489,151</u>	<u>11,331,452</u>
Committed:						
Public works and sanitation	-	-	-	-	2,548,352	2,548,352
Public safety	-	-	-	-	166,783	166,783
Culture and recreation	-	-	-	-	100,610	100,610
Capital outlays	-	-	-	-	37,560	37,560
General government and other purposes	-	-	-	-	131,616	131,616
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,984,921</u>	<u>2,984,921</u>
Assigned:						
Public works and sanitation	-	-	-	-	734,129	734,129
Culture and recreation	-	-	-	-	67,968	67,968
Health, welfare and community development	-	-	-	-	23,393	23,393
General government and other purposes	-	-	-	-	681,697	681,697
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,507,187</u>	<u>1,507,187</u>
Unassigned	(4,768,426)	-	-	-	-	(4,768,426)
<b>Total Fund Balance</b>	<b><u>\$(4,624,037)</u></b>	<b><u>\$ 4,654,512</u></b>	<b><u>\$ -</u></b>	<b><u>\$ 5,043,400</u></b>	<b><u>\$ 5,981,259</u></b>	<b><u>\$ 11,055,134</u></b>

**NOTE 9 – FUND BALANCE (CONTINUED)**

**NOTE 10 – CAPITAL ASSETS**

Capital assets and depreciation activity as of and for the year ended June 30, 2014 is as follows:

	Balance July 1, 2013, as restated	Additions	Retirements	Balance June 30, 2014
<b>Governmental Activities:</b>				
Capital asset, not being depreciated:				
Land	\$ 41,871,851	\$ -	\$ -	\$ 41,871,851
Construction in progress	31,862,180	-	-	31,862,180
<b>Total capital assets not being depreciated</b>	<b>73,734,031</b>	<b>-</b>	<b>-</b>	<b>73,734,031</b>
Capital assets, being depreciated:				
Buildings and building improvements	50,406,646	-	-	50,406,646
Infrastructure and infrastructure improvements	17,448,981	-	-	17,448,981
Equipment	2,441,577	-	-	2,441,577
Computers	448,207	-	-	448,207
Works of art	7,400	-	-	7,400
Furniture and fixtures	963,041	-	-	963,041
Vehicles	2,487,872	-	-	2,487,872
<b>Total capital assets being depreciated</b>	<b>74,203,724</b>	<b>-</b>	<b>-</b>	<b>74,203,724</b>
<b>Less accumulated depreciation for:</b>				
Buildings and building improvements	(10,163,843)	(630,011)	-	(10,793,854)
Infrastructure and infrastructure improvements	(9,393,163)	(272,583)	-	(9,665,746)
Equipment	(1,926,449)	(99,205)	-	(2,025,654)
Computers	(411,756)	(12,381)	-	(424,137)
Works of art	(6,312)	(370)	-	(6,682)
Furniture and fixtures	(934,200)	(4,416)	-	(938,616)
Vehicles	(2,056,131)	(104,782)	-	(2,160,913)
<b>Total accumulated depreciation</b>	<b>(24,891,854)</b>	<b>(1,123,748)</b>	<b>-</b>	<b>(26,015,602)</b>
<b>Total capital assets being depreciated, net</b>	<b>49,311,870</b>	<b>(1,123,748)</b>	<b>-</b>	<b>48,188,122</b>
<b>Governmental activities capital assets, net</b>	<b>\$ 123,045,901</b>	<b>\$ (1,123,748)</b>	<b>\$ -</b>	<b>\$ 121,922,153</b>

**NOTE 10 – CAPITAL ASSETS (CONTINUED)**

Depreciation expense was charged to governmental functions/programs as follows:

<u>Governmental activities</u>	<u>Amount</u>
General government	\$ 95,298
Public safety	36,386
Public works and sanitation	442,494
Culture and recreation	473,990
Health, welfare and community development	22,159
Education	53,421
<b>Total depreciation expense</b>	<b><u>\$ 1,123,748</u></b>

**NOTE 11 - LONG-TERM LIABILITIES**

**A. Summary of long-term debt activity**

Long-term liability activity for the year ended June 30, 2014, was as follows:

<u>Description</u>	<u>Beginning Balance, as restated</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
General and special obligation bonds and notes payable	\$ 44,810,105	\$ -	\$ (2,940,000)	\$ 41,870,105	\$ 3,156,000
Notes payable to CRIM – property tax advances (Law No. 42)	114,341	-	(3,149)	111,192	3,345
Payable to CRIM- property tax advances	-	228,149	-	228,149	-
Compensated absences	2,842,081	989,673	(516,376)	3,315,378	427,403
Christmas bonus	482,875	658,192	(482,875)	658,192	658,192
Claims and judgments	1,812,423	65,000	(861,377)	1,016,046	-
Landfill obligation	10,450,048	-	-	10,450,048	-
<b>Total</b>	<b><u>\$ 60,511,873</u></b>	<b><u>\$ 1,941,014</u></b>	<b><u>\$ (4,803,777)</u></b>	<b><u>\$ 57,649,110</u></b>	<b><u>\$ 4,244,940</u></b>

**NOTE 11 – LONG-TERM LIABILITIES (CONTINUED)**

**B. Legal debt margin**

For general obligation debt, the Municipality is subject to a legal debt margin requirement of 10% of the total assessment value of the property located within the Municipality. For special obligation debt, this debt margin cannot exceed 10% of the average recurring operating revenues generated by the Municipality within the last two preceding fiscal years. For obligations to be financed through the "Municipal Redemption Fund IVU," the debt margin is determined based on the repayment capacity of each Municipality. Long-term debt, except for general and special obligation bonds and notes, is paid with unrestricted funds.

**B. General and special obligation bonds and notes**

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2014 amount to \$41,870,105. All these bonds and notes are serviced by the Governmental Development Bank of Puerto Rico (GDB) maturing at various dates. As required by law, the Commonwealth Government is obligated to collect property taxes for payment of principal and interest on bonds and notes. The Municipality levies an annual additional special ad valorem tax of three and a quarter percent (3.25%) of the assessed value of personal and real property. In addition, .2% of the .5% municipal sales and use tax collected by the P.R. Department of Treasury is deposited in a "Municipal Redemption Fund" at the GDB to finance loans to Municipalities subject to restrictions imposed by law. The proceeds of the additional special ad valorem tax and of 0.2% sales and use tax are deposited in sinking funds established at GDB to redeem the bonds and notes payable of the Municipality in minimum annual or semiannual principal and interest payments, whereby sufficient funds are set aside in order to cover the projected debt service requirements, before any new bonds are issued.

Principal and interest payments on long-term debt are made through the CAE sinking fund except the special obligation bond \$3,475,000, whose payments are made through the "Municipal Redemption Fund (IVU);" and the special obligation bond \$400,000, for which the debt service requirements are made through withholdings from the monthly property tax advances sent to the Municipality by CRIM (operational loans). During the year, the \$3,475,000 special obligation note was converted to a special obligation bond with a maturity period of 25 years from its original issuance date with the Municipal Legislature Ordinance Number 23, Series 2013-14.

These bonds and notes are mainly issued to provide funds for the acquisition of equipment, construction of major capital facilities and for road paving.

A detail of the general and special obligation bonds and notes outstanding as of June 30, 2014 follows:

**NOTE 11 – LONG-TERM LIABILITIES (CONTINUED)**

Description	Outstanding Balance
1995 series, \$27,000 bond for public improvements, payable in annual installments of \$1,000 to \$2,000 through January 1, 2020; bearing interest at a fixed rate of 4.50%	\$ 10,000
1995 series, \$550,000 bond for public improvements, payable in annual installments of \$3,896 to \$55,105 through January 1, 2020; bearing interest at a fixed rate of 4.50%	232,105
1996 series, \$5,105,000 bond for capital improvements, payable in annual installments of \$70,000 to \$450,000 through July 1, 2020; bearing interest at rates ranging from 4.70% to 6.63% (6.58% at June 30, 2014)	2,525,000
1996 series, \$400,000 bond for capital improvements, payable in annual installments of \$10,000 to \$40,000 through July 1, 2016; bearing interest at rates ranging from 1.48% to 8.00% (1.48% at June 30, 2014)	100,000
1999 series, \$4,590,000 bond for capital improvements, payable in annual installments of \$65,000 to \$385,000 through July 1, 2024; bearing interest at rates ranging from 2.70% to 7.81% (4.73% at June 30, 2014)	3,010,000
1999 series, \$3,840,000 bond for capital improvements, payable in annual installments of \$110,000 to \$370,000 through July 1, 2017; bearing interest at rates ranging from 2.70% to 7.81% (4.73% at June 30, 2014)	1,325,000
2003 series, \$705,000 bond for capital improvements, payable in annual installments of \$10,000 to \$60,000 through July 1, 2027; bearing interest at rates ranging from 4.17% to 5.31% (4.45% at June 30, 2014)	525,000
2003 series, \$2,450,000 bond for capital improvements, payable in annual installments of \$40,000 to \$190,000 through July 1, 2027; bearing interest at rates ranging from 4.17% to 5.31% (4.45% at June 30, 2014)	1,810,000
2004 series, \$1,810,000 bond for capital improvements, payable in annual installments of \$45,000 to \$150,000 through July 1, 2023; bearing interest at rates ranging from 2.36% to 5.25% (4.45% at June 30, 2014)	1,165,000
2004 series, \$1,810,000 bond for capital improvements, payable in annual installments of \$85,000 to \$170,000 through July 1, 2019; bearing interest at rates ranging from 3.28% to 4.80% (4.45% at June 30, 2014)	890,000

**NOTE 11 – LONG-TERM LIABILITIES (CONTINUED)**

Description	Outstanding Balance
2005 series, \$4,745,000 bond for capital improvements, payable in annual installments of \$100,000 to \$325,000 through July 1, 2029; bearing interest at rates ranging from 4.17% to 5.31% (4.45% at June 30, 2014)	3,650,000
2008 series, \$3,475,000 bond for capital improvements, payable in annual installments of \$185,000 to \$420,000 through July 1, 2020; bearing interest at rates ranging from 1.48% to 7.50% (1.48% at June 30, 2014)	2,380,000
2009 series, \$400,000 note for capital improvements, payable in annual installments of \$45,000 to \$70,000 through July 1, 2016; bearing interest at rates ranging from 5.00% to 7.50% (5.00% at June 30, 2014)	195,000
2010 series, \$355,000 note for the payment of operating expenses, payable in annual installments of \$40,000 to \$60,000 through July 1, 2016; bearing interest at rates ranging from 5.00% to 7.50% (5.00% at June 30, 2014)	175,000
2010 series, \$585,000 note for capital improvements, payable in annual installments of \$65,000 to \$105,000 through July 1, 2017; bearing interest at rates ranging from 6.00% to 7.50% (6.00% at June 30, 2014)	375,000
2011 series, \$43,000 bond for capital improvements, payable in annual installments of \$1,000 to \$4,000 through January 1, 2036; bearing interest at a fixed rate of 4.50%	40,000
2011 series, \$12,035,000 bond for capital improvements, payable in annual installments of \$375,000 to \$1,185,000 through July 1, 2028; bearing interest at rates ranging from 6.00% to 7.50% (6.00% at June 30, 2014)	11,260,000
2011 series, \$284,000 bond for capital improvements, payable in annual installments of \$7,000 to \$19,000 through January 1, 2036; bearing interest at a fixed rate of 4.25%	263,000
2012 series, \$2,665,000 bond for capital improvements, payable in annual installments of \$90,000 to \$275,000 through July 1, 2027; bearing interest at rates ranging from 6.00% to 7.50% (6.00% at June 30, 2014)	2,475,000
2012 series, \$2,015,000 note for capital improvements, payable in annual installments of \$345,000 to \$465,000 through July 1, 2016; bearing interest at rates ranging from 6.00% to 7.50% (6.00% at June 30, 2014)	1,295,000

**NOTE 11 – LONG-TERM LIABILITIES (CONTINUED)**

Description	Outstanding Balance
2012 series, \$7,610,000 bond for capital improvements, payable in annual installments of \$290,000 to \$800,000 through July 1, 2027; bearing interest at rates ranging from 6.00% to 7.50% (6.00% at June 30, 2014)	7,320,000
2012 series, \$960,000 note for capital improvements, payable in annual installments of \$110,000 to \$175,000 through July 1, 2019; bearing interest at rates ranging from 6.00% to 7.50% (6.00% at June 30, 2014)	850,000
<b>Total</b>	<b>\$ 41,870,105</b>

The annual debt service requirements to maturity for bonds payable as of June 30, 2014 are as follows:

June 30,	Principal	Interest
2015	\$ 3,156,000	\$ 2,459,657
2016	3,379,000	2,266,817
2017	3,626,000	2,102,500
2018	3,208,000	1,863,829
2019	2,926,000	1,726,314
2020-2024	13,359,105	5,850,525
2025-2029	11,761,000	1,550,920
2030-2034	412,000	16,978
2035-2039	43,000	988
<b>Total</b>	<b>\$ 41,870,105</b>	<b>\$ 17,838,528</b>

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**NOTE 11 – LONG-TERM LIABILITIES (CONTINUED)**

**D. Other long-term liabilities**

**Outstanding  
Amount**

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**Note payable to CRIM (Law No. 42)** – Law No. 42 of January 26, 2000 (as amended by Law No. 146 of October 11, 2001 and Law No. 172 of August 11, 2002) was enacted to authorize the CRIM to obtain a special loan in the form of a line of credit from the Governmental Development Bank of Puerto Rico (GDB) to finance a debt the municipalities of Puerto Rico owe to CRIM for excess property tax advances as of June 30, 2000. Principal and interest payments are financed through .48% of the net increase of subsidy provided by the Commonwealth of Puerto Rico's general fund. Amounts are retained from advances of property tax and amounts of municipal equalization fund sent to the Municipality by the CRIM. Law No.42 was amended by Law no. 146 to extend from 10 to 30 years the financing period and by Law No. 172 to extend the debt period to June 30, 2001. On July 1, 2002 the Municipality entered into the financing agreement with the CRIM for a total amount of \$138,029, bearing interest at 6.19% and due on July 1, 2032. Debt service requirements in future years are as follows:

**\$ 111,192**

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June 30,	Principal	Interest
2015	\$ 3,345	\$ 6,829
2016	3,557	6,619
2017	3,781	6,395
2018	4,018	6,158
2019	4,271	5,905
2020-2024	25,733	25,147
2025-2029	34,898	15,982
2030-2032	31,589	4,028
<b>Total</b>	<b>\$ 111,192</b>	<b>\$ 77,063</b>

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**NOTE 11 – LONG-TERM LIABILITIES (CONTINUED)**

	<u>Outstanding Amount</u>
<p><b>Payable to CRIM – property tax advances</b> - 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. 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. If actual collections exceed the advances, a receivable from CRIM is recorded. However, if advances exceed actual collections, a payable to CRIM is recorded. The final settlement made by CRIM for the fiscal year 2013-2014 reported an excess of advances over actual collections. The resulting payable will be amortized in the 2015-2016 fiscal year through withholdings from the monthly advances to be received by the Municipality in that fiscal year.</p>	<p><u>\$ 228,149</u></p>
<p><b>Compensated absences</b> - 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. Amount is paid with unrestricted funds.</p>	<p><u>\$ 3,315,378</u></p>
<p><b>Christmas bonus</b> - represents the accrued portion corresponding to the fiscal year 2014 of the Christmas bonus to be paid in December 2014.</p>	<p><u>\$ 658,192</u></p>
<p><b>Claims and judgments</b> - represents the estimated loss of legal cases to be paid subsequent to June 30, 2014. The awarded amount, if any, will be paid with unrestricted funds.</p>	<p><u>\$ 1,016,046</u></p>
<p><b>Landfill Obligation</b> – represents the Municipality's estimate for the closure and post closure costs related to the closing of its landfill (see note 12).</p>	<p><u>\$ 10,450,048</u></p>

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**NOTE 12 – LANDFILL CLOSURE AND POST CLOSURE CARE COST OBLIGATION**

The Municipality owns a municipal solid waste landfill which requires the application of the provisions set forth in Statement No. 18, "*Accounting for Municipal Solid Waste Landfill Closure and Post Closure Care Costs*", issued by the Governmental Accounting Standards Board (GASB No. 18) and the regulations set forth by the U.S. Environmental Protection Agency (EPA) in its "Solid Waste Disposal Facility Criteria", issued on October 9, 1991. State and federal laws and regulations require the Municipality to place a final cover on its landfill site, when it stops accepting waste, and perform certain maintenance and monitoring functions at the site for 30 years after closure. In accordance with GASB Statement No. 18, "*Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Costs*", the Municipality is required to perform a study of the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. Although closure and post closure care costs will be paid only near or after the date that the landfill stops accepting waste, the Municipality reports a portion of these closure and post-closure care costs as an operating expense in each period until the landfill ceases its operations based on the updated estimates provided by the study.

However, the Municipality has not performed such study and, as of June 30, 2014, has reported a liability for closure and post closure care costs in the amount of \$10,450,048 based on the percentage used of the estimated capacity of the landfill. The estimated life of the landfill according to the engineers of the Municipality is approximately twenty five (25) years. Actual costs may be higher due to inflation, changes in technology, or changes in regulations.

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**NOTE 13 – 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 1<sup>st</sup> and January 1<sup>st</sup>. Total tax rates in force as of June 30, 2014 are 8.28% for personal property and 10.28% for real property. The distribution of these rates follows:

Description	Personal Property	Real Property
Basic property tax rate, which is appropriated for general purposes and accounted in the Municipality's general fund:	4.00%	6.00%
Percent that belongs to the Commonwealth's debt service fund:	1.03%	1.03%
Percent that belongs to the Municipality's debt service fund:	3.25%	3.25%
Total tax rate:	8.28%	10.28%
 Discount granted by law to the taxpayers but reimbursed to the Municipality by the P.R. Treasury Department:	 (.20%)	 (.20%)
 <b>Total percent to be paid by taxpayers:</b>	 <b>8.08%</b>	 <b>10.08%</b>

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. This amount is recorded as long-term debt. The Municipality has a net payable of \$228,149 resulting from the final settlement of fiscal year 2014 recorded as other long-term debt in the Statement of Net Position.

**NOTE 13 – PROPERTY TAXES**

On December 9, 2013, Law No. 145 "Getting Caught Up with Past Due CRIM Taxes – Incentive Plan for the Payment of Due Taxes" was approved granting an amnesty from the payment of interest, surcharges and penalties on real and personal property taxes owed from the fiscal years prior to 2013-2014. This amnesty/incentive plan was available from December 18, 2013 to March 27, 2014. This plan also awarded CRIM the faculty to grant payment plans to taxpayers up to a maximum of four years. During the fiscal year 2013-14, the Municipality received revenues from this property tax amnesty in the amount of \$484,576.

**NOTE 14 – INTERGOVERNMENTAL REVENUES AND FEES, FINES AND CHARGES FOR SERVICES - GENERAL FUND**

**A. Intergovernmental revenues in the general fund are comprised of the following:**

	<u>Amount</u>
Amount of municipal equalization fund sent by CRIM	\$ 1,231,702
Reimbursement from P.R. Department of Treasury - Christmas Bonus reimbursement	227,820
Compensation in lieu of tax from the Puerto Rico Electric Power Authority (PREPA)	2,767,215
9-1-1 service grants	<u>5,265</u>
	<b><u>\$ 4,232,002</u></b>

**B. Fees, fines and charges for services revenues reported in the general fund are comprised of the following:**

	<u>Amount</u>
Construction permits	\$ 286,159
Medical emergency services	23,045
Licenses and permits	23,596
Waste removal and disposal services	<u>16,033</u>
	<b><u>\$ 348,833</u></b>

## NOTE 15 – PENSION PLAN

### A. Act No. 447 and System 2000 (until June 30, 2013)

As of June 30, 2014 regular employees of the Municipality contribute to a cost-sharing multiple employer defined benefit retirement plan administered by the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). ERS covers all regular full-time public employees working for the central government, the municipalities of Puerto Rico and certain public corporations not having their own retirement systems. The system provides retirement pensions, death, and disability benefits. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

The System operates under *Act 447, approved on May 15, 1951* effective on January 1, 1952 and *Act 1 of February 16, 1990* for employees that entered as participants of the Plan starting April 1, 1990 and ending December 31, 1999. Under this Act, retirement benefits were determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation was computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member was eligible, was limited to a minimum of \$200 per month and a maximum of 75% of the average compensation. ERS issues a publicly financial report that includes financial statements and required supplementary information of the Plan, which may be obtained from the ERS.

*Act No. 305 of September 24, 1999* amended *Act No. 447 of 1951* and *Act 1 of February 16, 1990* to establish a new pension program (System 2000). The new pension program became effective on January 1, 2000. Employees participating in the Act 447 system as of December 31, 1999 had the choice to either stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000 were only allowed to become members of the new program. System 2000 was a hybrid defined contribution plan, also known as a cash balance plan. There would be a pool of pension assets, which would be invested by the System, together with those of the current defined benefit plan. Benefits at retirement age would not be guaranteed by the State government and would be subjected to the total accumulated balance of the savings account. The annuity would be based on a formula, which assumed that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) would be invested in an account which would either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. If the savings accounts balance was \$10,000 or less at time of retirement, the balance would be distributed by the System to the participant as a lump sum. Participants received periodic account statements similar to those of defined contribution plans showing their accrued balances. The employer contributions (11.275% of the employee's salary) would be used to fund the plan. Under System 2000 the retirement age was reduced from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

The Act 447, as amended, was the authority under which obligations to contribute to the Plan by the Plan members, employers and other contributing entities were established or amended. Plan members were required to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess

**NOTE 15 – PENSION PLAN (CONTINUED)**

of \$6,600 except for the Mayor or employee under a supplementation plan, which contributed 8.275% of gross salary. In order to address the unfunded actuarial accrued liability of the System, on July 6, 2011 (effective July 1, 2011) the Commonwealth Legislature approved Act No. 116 increasing the employers' contributions rate from 9.275% to 10.275% of employee compensation for fiscal year 2012, an additional 1% annually for each of the next four years, and 1.25% annually for each of the five years thereafter, reaching an aggregate contribution rate of 20.525% effective July 1, 2020. The purpose of this Act was to provide cash flow and strength the System to adequately cover administrative expenses and payment of benefits. The Municipality was required to contribute 11.275% of gross salary until the fiscal year ended on June 30, 2013. As stated in the Act, percent increases applicable to municipalities for fiscal years 2011-2012, 2012-2013 y 2013-2014 would be financed through the Commonwealth's budget approved by the Commonwealth's Legislature.

**B. Act No. 3 of 2013 (beginning July 1, 2013)**

In order to address its unfunded liability and rescue the System from insolvency, on April 4, 2013 the Commonwealth of Puerto Rico enacted Act No. 3 of 2013, representing 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:

- All participants (employees) under the defined benefit pension plans (Act 447 and Act 1) and the defined contribution plan (System 2000) were moved to a new hybrid plan ("New Plan").
- 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 were frozen. Thereafter, all future benefits will accrue under the New Plan. Participants will receive a pension at retirement age equivalent to what they had accrued under Act 447 and Act 1 up to June 30, 2013, and a supplemental annuity corresponding to contributions made after July 1, 2013.
- Participants under System 2000 will no longer receive a lump-sum payment upon retirement, but rather a lifetime annuity calculated at retirement based on a factor that will incorporate the individual's life expectancy and a rate of return.
- New participants under the New Plan will receive a lifetime annuity based on the accumulated balance of their individual accounts (employees' contributions plus a return on investment)
- Eliminated the possibility of accruing a merit pension (payable once the participant had achieved 30 years of creditable service) after June 30, 2013.
- Increased employee contributions from 8.275% to a minimum of 10.000%.

**NOTE 15 – PENSION PLAN (CONTINUED)**

- After July 1, 2013 all employers must contribute 12.275% of employee contribution with an additional 1% annually up to June 30, 2016; after July 1, 2016 an additional 1.25% annually for each of the five years thereafter, reaching an aggregate contribution rate of 20.525% effective July 1, 2020. These contributions will be used to increase the System's assets, reduce the actuarial deficit and enable the System to comply with future obligations.
- Retirement age was modified as follows:
  - ✓ Act 447 regular employees: age 58 to 61,
  - ✓ Act 447 high risk employees (state and municipal police, firefighters and custody officials): from age 50 to 55 years,
  - ✓ Act 305 (System 2000) regular employees: age 60 to 65; high risk employees remains the same (55 years).

Act 1 employees remained the same (65 years for regular employees and 55 for high risk employees. For new employees under the New Plan will retire after 67 years (retirement age will be 67 for regular employees and 58 for high risk employees).

- Due to changes to Special Laws (see note 15), the minimum monthly pension for current retirees was increased from \$400 to \$500.
- Disability benefits were eliminated and substituted for a mandatory disability insurance policy. Beginning July 1, 2013, each employee must contribute to this insurance plan .25% of his or her monthly salary, up to a monthly maximum of \$5,000. Therefore, the maximum monthly employee contribution will be \$12.50 (\$5,000 x .25%).
- Survivor benefits were modified.

The Municipality's actual contribution for the current and the previous three fiscal years, which is equal to the required contribution, follows:

<u>Fiscal year ended:</u>	<u>Law No. 447 &amp; System 2000</u>	<u>Law No. 3</u>
2014	\$ -	\$ 655,327
2013	\$ 696,550	\$ -
2012	\$ 734,000	\$ -

**NOTE 15 – PENSION PLAN (CONTINUED)**

**C. Act 32 of 2013 (beginning July 1, 2013)**

On June 25, 2013, Act 32 was approved in order to amend Act 447 of 1957 by creating a new Article 5-117 *Additional Uniform Contribution (AUC)*, with the purpose of solving the cash flow deficit of the System. For each fiscal year, beginning on July 1, 2013, the ERS will: 1) determine the portion of the AUC attributable to each participating employer based on the percentage each employer's contributions represent of the total employer contributions established for that fiscal year; and 2) send to the director of the P.R. Office of Management and Budget (OMB) and to each public corporation and municipality whose employees are covered by this Act, a certification of the AUC owed by each employer.

Act 32 defines the concept of the AUC as follows:

- For the fiscal year 2013-2014, the AUC will be one hundred and forty million dollars (\$140,000,000)
- For each subsequent fiscal year, beginning with the 2014-2015 fiscal year until 2032-2033, the AUC will be the contribution certified by the external actuary of the System, at least 120 days prior to the beginning of each fiscal year, deemed necessary to prevent that the value of the System's projected gross assets, during any subsequent fiscal year, be lower than one thousand million dollars (\$1,000,000,000). If, for any fiscal, the certified AUD is not available within the 120-day period prior to the beginning of the said fiscal year or within a shorter term with the consent of the OMB, the AUC will be equal to the contribution certified for the immediate preceding fiscal year.

Each public corporation and municipality covered by this Act is directly responsible for the payment of their corresponding certified AUC. However, for any fiscal year, the OMB will consign in the Commonwealth's General Budget enough resources to subsidy totally or partially the AUC certified to any public corporation, municipality or governmental entity, including the Judiciary Branch, whose operating expenditures are not fully or partially covered by the General Budget and for which the OMB, has subsequently determined it does not have the financial capacity to assume such obligation during the fiscal year.

For the fiscal year 2013-2014, \$41.142 million dollars were assigned to OMB through Commonwealth Legislative Resolution of Special Assignments No. 17 (RC 17-2013) for the total or partial subsidy of the AUC of any public corporation or municipality that the agency determined did not have the financial capacity to assume this obligation. The OMB's evaluation of a municipality's financial capacity was based on two parameters: financial indicators and population. The financial indicators to be evaluated were: profitability index (net income as a percentage of revenues); capital ratio (the proportion between the net position of the entity and the AUC) and debt margin ratio (the proportion between the AUC and the municipality's special ad valorem tax debt margin (CAE)).

#### **NOTE 16 – POSTEMPLOYMENT BENEFITS**

In addition to the pension benefits described in note 15, the Municipality is required to cover annually the 3% increase in the retirement plan of its retired employees, as required by Commonwealth's laws. Also, the Municipality is required to finance costs related to the application of certain "Special Laws" issued by the Commonwealth Government. Those Special Laws granted increases in pensions and other benefits to retired employees of the Municipality such as medicines bonus, Christmas and summer bonuses and death benefits. However, beginning July 1, 2013, Act 3 of 2013 modified these Special Laws benefits as follows:

- Reduction in the Christmas bonus from \$600 to \$200 (current retirees),
- Elimination of summer bonus of \$100 (current retirees),
- No change in medical plan contribution of up to \$1,200 and medicine bonus of \$100 (current retirees)
- Eliminated all Special Law benefits to future retirees.

Act 3 also established that employers will contribute \$2,000 per for each retiree that began working for the government on or before December 31, 1999. This contribution was established based on the assumption that the System will benefit from the savings generated between this employer contribution and the Special Law benefits paid out to retirees. The total costs related to these post-employment benefits for the fiscal year ended June 30, 2014 amounted to \$106,712. These benefits are recorded as expenditures in the general fund.

#### **NOTE 17 - COMMITMENTS**

##### **A. Operating leases**

The Municipality leases office space and office equipment under operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same terms. Rental expenses amounted to \$263,124. Management believes that the summary of the future minimum rental commitments under non-cancelable equipment leases with terms exceeding one year is not significant.

##### **B. Encumbrances**

As of June 30, 2014 the Municipality has encumbrances outstanding totaling \$578,281, which represent the estimated amount of expenditures required to complete contracts, purchase orders and other commitments in process of completion at fiscal year-end. As required by current standards, outstanding encumbrances as of June 30, 2014 are reported as unassigned amounts in the general fund. Purpose classification follows:

**NOTE 17 – COMMITMENTS (CONTINUED)**

<u>Purpose</u>	<u>General Fund- unassigned fund balance</u>
Public works and sanitation	\$ 329,888
Culture and recreation	27,660
Public Safety	305
Health, welfare and community development	82,654
Education	5,240
General government and other purposes	132,534
	<u>\$ 578,281</u>

Fund balance of major and other governmental funds (special revenue, capital project and debt service funds) is classified as restricted, some or all of which may be encumbered. Encumbrances of restricted fund balance are not reported separately from this classification because the encumbrance does not further restrict the purpose for which the resources may be used.

**NOTE 18 – CONTINGENCIES**

**A. Federal and State grants**

Projects financed by Federal and State Grants are subject to audits by grantors and other governmental agencies in order to determine that the expenditures to comply with the conditions of such grants. It is the Municipality's opinion that no additional material unrecorded liabilities will arise from audits previously performed or to be performed.

**B. Litigations**

The Municipality is, at present, a defendant in a number of legal matters that arise in the ordinary course of the Municipality's activities. There are cases whereby the Municipality is a defendant or codefendant that will be covered by insurance, certain cases whereby the legal counsel has not determined an outcome and other cases that will not be covered by insurance. As a result of various legal cases as of June 30, 2014 and not to be covered by insurance, the Municipality accrued an estimated loss of \$1,016,046 in the government-wide statements. However, it is the opinion of the Municipality and the legal counsels that based on their experience, such actions and the potential liabilities will not impair the Municipality financial position.

**NOTE 19 – RESTATEMENT OF FUND BALANCE AND NET POSITION**

The following table disclosed the net change in fund balances and net position at beginning of year as previously reported in the financial statements. The beginning balances have been restated as follows:

Description	Fund Balance		Net Position
	General Fund	Other Governmental Funds	Government-Wide Statements
<b>Fund balance / net position, at beginning of year, as previously reported</b>	<b>\$ (2,767,617)</b>	<b>\$ 4,209,498</b>	<b>\$ 81,513,700</b>
<u>Correction of errors:</u>			
Overstatement of due from Commonwealth Government	-	(549,490)	(549,490)
Overstatement of due from Federal Government	-	(10,623)	(10,623)
Understatement of unearned revenues – Federal Government	-	(3,382)	(3,382)
Understatement of cash and cash equivalents, net	-	12,672	12,672
Overstatement of due from other funds, net	(638,656)	-	(638,656)
Understatement of accumulated depreciation – capital assets	-	-	(1,121,612)
<b>Fund balance / net position, at end of year, as restated</b>	<b>\$ (3,406,273)</b>	<b>\$ 3,658,675</b>	<b>\$ 79,202,609</b>

## NOTE 20 – SUBSEQUENT EVENTS

### A. Implementation of Acts No. 18 and 19 of 2014

The dispositions established by Acts 18 and 19 of 2014 related to the municipal sales and use tax became effective on July 1, 2014 (see note 3). The most significant changes are the creation of the Municipal Finance Corporation (COFIM) and, for the municipalities covered by these Acts, the new collection method of the 1% municipal sales and use tax and the establishment of a monthly advances system for the transfers of the .2% destined for the Municipal Development Fund (FDM) and of the .2% related to the Municipal Redemption Fund (FRM).

For those municipalities that signed the agreement to be covered by these Acts (including the Municipality), the transfers to be made by the Governmental Development Bank (GDB) of the .2% destined for the FDM and of the .2% related to the FRM will be based on a system of monthly advances: each month the GDB will make the FDM and FRM transfers based on the amounts collected that same month in the preceding fiscal year (2013-2014). At the end of the year, a settlement will be made comparing the actual collections of the FDM and FRM with the monthly advances made to each municipality. If actual collections exceed the total advances received, an account receivable from GDB will be recognized; if actual collections are less than the total advances, a payable to the GDB will be recognized and amortized through withholdings from future advances. For municipalities not covered by these Acts, the monthly transfers will be made based on actual collections.

As stated in Act 19, the 1% corresponding to the municipalities' sales and use tax will be deposited in COFIM. From these funds COFIM will deposit to the COFIM's sinking fund the greater of: .3% of the 1% municipal sales and use tax or an Annual Rental Fee (RFA). The RFA for fiscal year 2014-2015 will be \$65,541,281 and, thereafter, 1.5% of the RFA of the preceding fiscal period. The excess of the required deposit to the COFIM's sinking fund (.7% of the 1% of the municipal sales and use tax) will be transferred to the general fund of municipalities covered by the agreement or to the FRM as decided by the municipality. Before the transfer of the .7% to the municipalities covered by the Act, COFIM will transfer the 1% municipal sales and use tax to the municipalities not covered by the Act.

On September 1, 2014, the sixteen municipalities that collect their sales and use tax through the P.R. Department of Treasury (Aguadilla, Aibonito, Arroyo, Barranquitas, Ciales, Culebra, Hatillo, Juncos, Lajas, Lares, Maricao, Maunabo, Naguabo, Patillas, Peñuelas and Rincon) began participating on a pilot program for the collection of the 1% municipal sales and use tax through COFIM. In this program, a standard monthly sales and use tax return was created to be used by the retailers of these municipalities. The monthly returns were filed in the bank branches of the financial institution designated by COFIM to be its intermediary, the Popular Bank of Puerto Rico (BPPR). BPPR would electronically process the returns and submit their data to COFIM. However, beginning November 1, 2014, the retailers also had the option of using COFIM's internet portal to electronically file and pay the return.

On the other hand, the Governing Board of COFIM has not established an implementation date for the remaining 62 municipalities. However, for those municipalities that voluntarily decided to use COFIM's internet portal or collection process through the BPPR, their implementation date was December 1, 2014. For those municipalities that want to be certified as collection agents for COFIM, the

**NOTE 20 – SUBSEQUENT EVENTS (CONTINUED)**

implementation date was January 1, 2015. As collection agents for COFIM, the retailers of these municipalities have the option of filing and paying the monthly sales and use tax in the municipality's Collection Office. The Collection Office's personnel have the responsibility to deposit the daily sales and use tax collections in the bank account designated by COFIM, and also submit electronically the returns' data to the agency for processing in COFIM's data base. The Municipality of Guayama has been certified by COFIM as a collection agent and the implementation of the new collection system began on February 1, 2015.

**B. Issuance of general obligation debt**

On October 15, 2014, the Municipality issued a general obligation bond in the amount of \$1,265,000 for the construction and improvement of various recreational facilities. This bond has a maturity period of seventeen (17) years and will be paid through the "CAE" debt service fund in annual installments ranging from \$35,000 to \$135,000.

In addition, on November 24, 2014 the Municipality issued a general obligation bond in the amount of \$3,020,000 for the construction of a soccer stadium. This bond has a maturity period of twenty-five (25) years and will be paid through the "CAE" debt service fund in annual installments ranging from \$40,000 to \$260,000.

Management has evaluated subsequent events through May 10, 2015, the date the financial statements were available to be issued and determined that no additional subsequent events require disclosure as of June 30, 2014.

	Budgeted Amounts		Actual Amounts (Budgetary Basis)	Variance with Final Budget
	Original	Final		Positive (Negative)
<b>Revenues</b>				
Property taxes	\$ 8,110,732	\$ 8,110,732	\$ 8,110,732	\$ -
Municipal license taxes	10,200,000	10,200,000	9,350,335	(849,665)
Fees, fines and charges for services	1,491,500	1,491,500	343,759	(1,147,741)
Intergovernmental:				
Commonwealth Government	3,695,386	3,695,386	4,226,736	531,350
Interest	550,000	550,000	457,588	(92,412)
Miscellaneous	750,000	750,000	320,524	(429,476)
<b>Total revenues</b>	<b>24,797,618</b>	<b>24,797,618</b>	<b>22,809,674</b>	<b>(1,987,944)</b>
<b>Expenditures</b>				
Current:				
General government	10,167,477	11,091,753	11,265,462	(173,709)
Public safety	2,827,793	2,793,870	2,476,823	317,047
Public works and sanitation	7,213,539	6,569,882	6,021,557	548,325
Culture and recreation	2,032,220	1,897,694	1,650,280	247,414
Health, welfare and community development	2,377,411	2,278,081	2,109,918	168,163
Education	179,178	166,338	161,209	5,129
<b>Total expenditures</b>	<b>24,797,618</b>	<b>24,797,618</b>	<b>23,685,249</b>	<b>1,112,369</b>
<b>Deficiency of revenues under expenditures</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (875,575)</b>	<b>\$ (875,575)</b>

**EXPLANATION OF DIFFERENCE BETWEEN BUDGETARY INFLOWS AND  
OUTFLOWS AND GAAP REVENUES AND EXPENSES**

**Sources/inflows of resources:**

Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule	\$ 22,809,674
Non-budgeted funds recorded as revenues for financial reporting purposes	3,377,382
Differences-budget to GAAP	(9,009)
<b>Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances</b>	<b>\$ 26,178,047</b>

**Uses/outflows of resources:**

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule	\$ 23,685,249
Differences-budget to GAAP:	
Non-budgeted funds recorded as expenditures for financial reporting	1,995,704
Prior year expenditure are not outflows of budgetary resources, but are expenditure for financial purposes	44,675
Encumbrances for supplies and equipment ordered, but not received, are reported in the year the order is placed for budgetary reporting purposes	(578,281)
Differences-budget to GAAP	(681,353)
<b>Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances</b>	<b>\$ 24,465,994</b>

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

**NOTE 1 – BUDGET PROCESS AND BUDGETARY BASIS OF ACCOUNTING**

The Municipal budget is prepared for the General Fund following the requirements of the Autonomous Municipal Law of 1991, as amended. It is developed utilizing elements of performance-based program budgeting and zero-based budgeting and includes estimates of revenues and other sources for ensuing fiscal year under laws existing at the time the budget is prepared.

Budget amendments are approved by the Municipal Legislature. Certain budget transfers within the limitations and restrictions of the Municipal Law can be approved by the Mayor or by the Municipal Legislature. The budget comparison schedule provides information about the original budget, the amended budget and the actual results, under the budgetary basis of accounting.

The budgetary basis of accounting is different from GAAP. Revenues are generally recorded when cash is received and expenditures are generally recorded when the related expenditure is incurred or encumbered. The encumbrances (that is, purchase orders, contracts) are considered expenditures when a commitment is made. On a GAAP basis encumbrances outstanding at year-end are reported in the governmental funds statements as assigned fund balance since they do not constitute expenditures or liabilities while on a budgetary basis encumbrances are recorded as expenditures of the current year. Encumbrance appropriations lapse one year after the end of the fiscal year. Unencumbered appropriations are lapsed at year-end. The legal level of budgetary control (the level at which expenditures may not legally exceed appropriations) is at the function level.

The presentation of the budgetary data excludes other appropriations such as capital projects, debt service and special revenue funds because projects are funded on a multi-year nature, generally requiring several years to complete or effective budgetary control is alternatively achieved through general obligation bond indentures and legal and contractual grant agreement provisions.

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Federal Expenditures
<b>U.S. DEPARTMENT OF AGRICULTURE</b>			
Pass-through programs from:			
<u>P.R. Department of Education</u>			
Child and Adult Care Food Program	10.558	CC-248	\$ 926,677
<b>Subtotal U.S. Department of Agriculture</b>			<b>926,677</b>
<b>U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>			
Direct Program:			
Community Development Block Grants/Entitlement Grants	14.218		1,043,663
Section 8 Housing Choice Vouchers	14.871		1,153,703
Pass-through programs from:			
<u>P.R. Department of Family</u>			
Emergency Solutions Grants Program	14.231	N/AV	7,270
<b>Subtotal U.S. Department of Housing and Urban Development</b>			<b>2,204,636</b>
<b>U.S. DEPARTMENT OF TRANSPORTATION</b>			
Pass-through programs from:			
<u>P.R. Traffic Safety Commission</u>			
State and Community Highway Safety	20.600	N/AV	3,320
<b>Subtotal U.S. Department of Transportation</b>			<b>3,320</b>
<b>U.S. DEPARTMENT OF HOMELAND SECURITY</b>			
Pass-through programs from:			
P.R. Governor's Office - Governor's Authorized Representative (GAR)			
Disaster Grants - Public Assistance (Presidentially-Declared Disasters)	97.036	N/AV	74,771
Homeland Security Program (NIMS)	97.067	N/AV	325
<b>Subtotal U.S. Department of Homeland Security</b>			<b>75,096</b>
<b>U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES</b>			
Pass-through programs from:			
<u>P.R. Department of Family - Administration for the Care and Integral     Development of Children</u>			
Head Start	93.600	241-2014-000147	10,168,494
<b>Subtotal U.S. Department of Health and Human Services</b>			<b>10,168,494</b>
<b>Total Expenditures of Federal Awards</b>			<b>\$ 13,378,223</b>

**NOTE 1 – BASIS OF PRESENTATION**

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Guayama (Municipality) under programs of the federal government for the year ended June 30, 2014. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments and Nonprofit Organizations*. Therefore, some amounts presented in this schedule may differ from the amounts presented in, or used in the preparation of, the basic financial statements. Because the schedule presents only a selected portion of the operations of the Municipality, it is not intended to and does not present the financial position or the result of operations of the Municipality.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Expenditures reported on the Schedule are reported on the modified accrual basis of accounting, except for Section 8 Housing Choice Voucher Program (HCV). Expenditures are recognized when the related liability is incurred following the cost principles contained in OMB Circular A-87 *Cost Principles for State, Local and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Expenditures for HCV Program are reported on a statutory basis as required by the U.S. Department of Housing and Urban Development. Such expenditures should equal the net ACC subsidy for the PHA's fiscal period.

The Catalog of Federal Domestic Assistance (CFDA) Number is a program identification number. The first two digits identify the federal department or agency that administers the program and the last three numbers are assigned by numerical sequence. State or local government redistributions of federal awards to the Municipality, known as "pass-through awards", should be treated by the Municipality as though they were received directly from the federal government. OMB Circular A-133 requires the schedule to include the name of the pass-through entity and the identifying number assigned by the pass-through entity for the federal awards received as a sub recipient. Numbers identified as N/AV are not available.

**NOTE 3 – SUBRECIPIENT AWARDS**

Of the federal expenditures of the Community Development Block Grants/ Entitlement Grants presented in the Schedule of Expenditures of Federal Awards, \$25,000 of federal awards were provided to a subrecipient.

**NOTE 4 – RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE BASIC FINANCIAL STATEMENTS**

Description	Head Start	Other Governmental Funds	Total
Total federal expenditures per Schedule of Expenditures of Federal Awards	\$ 10,168,494	\$ 3,209,729	\$ 13,378,223
Difference between total grant awarded and the amount recorded as expenditures under modified-accrual basis for Section 8 HCV Program	-	(9,709)	(9,709)
Non-federal awards expenditures	-	3,098,678	3,098,678
Total expenditures, fund statements	<u>\$ 10,168,494</u>	<u>\$ 6,298,698</u>	<u>\$ 16,467,192</u>

**PEDRO C. ORTIZ LEDEE**  
CERTIFIED PUBLIC ACCOUNTANT

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**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**

**To the Honorable Mayor and  
Members of the Municipal Legislature  
Municipality of Guayama, Puerto Rico**

I 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 each major fund, and the aggregate remaining fund information of Municipality of Guayama, Puerto Rico (Municipality), as of and for the fiscal year ended June 30, 2014, and the related notes to the financial statements. I was engaged to audit the financial statements of the governmental activities. These financial statements collectively comprise the Municipality's basic financial statements and have issued my report thereon dated May 10, 2015. The report on the governmental fund financial statements was qualified for the interfund balances and I did not express an opinion on the governmental activities because I was unable to obtain sufficient and competent evidential matter related to the capital assets and the landfill closure and post-closure care cost liability.

**Internal Control over Financial Reporting**

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

My consideration of internal control was for the limited purpose described in the preceding paragraph and was not design 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, I identified certain deficiencies in internal control that I 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 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. I consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses. Findings 2014-002, 2014-003, 2014-004 and 2014-006.

**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 (CONTINUED)**

A *significant deficiency* is a deficiency, or 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. I consider the deficiencies described in the accompany Schedule of Findings and Questioned Costs to be significant deficiencies. Finding 2014-001 and 2014-005.

**Compliance and Other Matters**

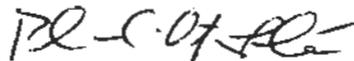
As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Questioned Costs as items 2014-002, 2014-003, 2014-004 and 2014-006.

**Municipality's Response to Findings**

Municipality's response to the findings identified in my audit are described in the accompanying Schedule of Findings and Questioned Costs. Municipality's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly I express no opinion on it.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of my 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.



Pedro C. Ortiz Ledée, CPA  
License Number 5200

Guayama, Puerto Rico  
May 10, 2015



**PEDRO C. ORTIZ LEDEE**  
CERTIFIED PUBLIC ACCOUNTANT

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

**To the Honorable Mayor and  
Member of the Municipal Legislature  
Municipality of Guayama, Puerto Rico**

**Report on Compliance for Each Major Federal Program**

I have audited Municipality of Guayama, Puerto Rico (Municipality) 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 Municipality's major federal programs for the fiscal year ended June 30, 2014. The Municipality'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**

My responsibility is to express an opinion on compliance for each of the Municipality's major federal programs based on my audit of the types of compliance requirements referred to above. I conducted my audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *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 I plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Municipality's compliance with those requirements and performing such other procedures as I considered necessary in the circumstances.

I believe that my audit provides a reasonable basis for my opinion on compliance for each major federal program. However, my audit does not provide a legal determination of Municipality's compliance

**Basis for Qualified Opinion on Major Federal Programs**

As identified in the findings numbers listed in the table below and described in the accompanying Schedule of Findings and Questioned Costs, the Municipality, did not comply with requirements regarding the following:

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

**Basis for Qualified Opinion on Major Federal Programs (continued)**

<b>Awarding Agency</b>	<b>Federal Program</b>	<b>Compliance Requirement</b>	<b>Finding Number</b>
Department of Health and Human Services	93.600- Head Start	Matching, Level of Effort, Earmarking	2014-008
Department of Health and Human Services	93.600- Head Start	Reporting	2014-009
Department of Housing and Urban Development	14.218- CDBG- Entitlement	Cash Management	2014-010
Department of Housing and Urban Development	14.218- CDBG- Entitlement	Matching, Level of Effort, Earmarking	2014-011
Department of Housing and Urban Development	14.218- CDBG- Entitlement	Program Income	2014-013
Department of Housing and Urban Development	14.218- CDBG- Entitlement	Reporting	2014-014
Department of Housing and Urban Development	14.218- CDBG- Entitlement	Special Test- Environmental Reviews	2014-015
Department of Housing and Urban Development	14.218- CDBG- Entitlement	Subrecipient Monitoring	2014-016
Department of Agriculture	10.558- Child and Adult Care Food Program	Period of Availability	2014-019
Department of Agriculture	10.558- Child and Adult Care Food Program	Reporting	2014-020

Compliance with such requirements is necessary, my opinion, for the Municipality to comply with the requirements applicable to the programs.

**Qualified Opinion on Major Federal Programs**

In my opinion, except for the noncompliance described in the "Basis for Qualified Opinion on Major Federal Programs" paragraph, the Municipality, 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 the major federal programs listed in the "Basis for Qualified Opinion on Major Federal Programs" paragraph for the year ended June 30, 2014.

**Unmodified Opinion on Each of the Other Major Federal Programs**

In my opinion, the Municipality 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 other major federal programs (Section 8 Housing Choice Vouchers) identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs for the year ended June 30, 2014.

**Other Matters**

The results of my 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 2014-007, 2014-012, 2014-017 and 2014-018. My opinion on each major federal program is not modified with respect to these matters.

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

Municipality's response to the noncompliance findings identified in my audit are described in the accompanying Schedule of Findings and Questioned Costs. Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly I express no opinion on the response.

### Report on Internal Control over Compliance

Management of the Municipality is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing my audit of compliance, I considered Municipality'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, I do not express an opinion on the effectiveness of the Municipality's internal control over compliance.

My 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, I identified certain deficiencies in internal control over compliance that I 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. I consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item 2014-008, 2014-009, 2014-010, 2014-011, 2014-013, 2014-014, 2014-015, 2014-16, 2014-019 and 2014-020 to be material weaknesses.

*A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. I consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned costs as items 2014-007, 2014-012, 2014-017 and 2014-018 to be significant deficiencies.

Municipality's response to the internal control over compliance findings identified in my audit are described in the accompanying Schedule of Findings and Questioned Costs. Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly I express no opinion on the response.

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

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



Pedro C. Ortiz Ledée, CPA  
License Number 5200

Guayama, Puerto Rico  
May 10, 2015



**SECTION I – SUMMARY OF AUDITOR’S RESULTS**

**Financial Statements**

Type of auditor’s report issued on the basic financial statements:

**Opinion Units**

**Type of Opinions**

Governmental activities	Disclaimer
General Fund	Qualified
Head Start Fund	Qualified
Bond Issuances Fund	Qualified
Debt Service Fund	Unmodified
Aggregate remaining fund	Qualified

Internal Control over financial reporting:

Material weakness identified?	Yes	X	
Significant deficiencies identified?	Yes	X	None reported
Noncompliance material to financial statements noted?	Yes	X	No

**Federal Awards**

Internal Control over major programs:

Material weakness identified?	Yes	X	No
Significant deficiencies identified?	Yes	X	None reported

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

**Qualified opinion on Child and Adult Care Food Program, Community Development Block Grants/ Entitlement Grants and Head Start**

**Unmodified opinion on Section 8 Housing Choice Voucher**

Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?

Yes	X	No
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**Identification of major programs**

CFDA Number	Name of Federal Program or Cluster
10.558	Child and Adult Care Food Program
14.218	Community Development Block Grants/ Entitlement Grants
14.871	Section 8 Housing Choice Voucher
93.600	Head Start

Dollar threshold used to distinguish between Type A and Type B programs

\$401,347

Auditee qualified as low-risk auditee?

Yes	No	X
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**SECTION II – FINANCIAL STATEMENTS FINDINGS**

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<b>FINDING NUMBER</b>	<b>2014-001</b>
<b>REQUIREMENT</b>	<b>ACCOUNTING RECORDS AND REPORTING SYSTEM</b>
<b>CONDITION</b>	The Municipality did not maintain complete accounting records.
<b>CONTEXT</b>	During the examination of the accounting records, I noted that the Municipality does not summarize the transactions in a formal accounting system in order to properly record and account for the transactions of the general fund and special revenue funds. The accounting records of the Municipality are maintained simultaneously, through a manual and a computerized accounting system for which no reconciliation procedures are made among them.
<b>CRITERIA</b>	Chapter VIII, Article 8.010 (b) of State Act Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico</i> of August 30, 1991, states that the Municipality must maintain its fund accounting in accordance with GAAP. In addition, Article 8.010 (c) states that uniform accounting system used by the Municipality must produce reliable reports and financial statements provide complete information about the results of the Municipality's operations and include the necessary internal controls to account for all funds, capital assets and other assets.
<b>CAUSE</b>	The Municipality has not established effective internal control procedures over the accounting system.
<b>EFFECT</b>	The Municipality is not in compliance with Chapter VIII, Articles 8.010 (b) and (c) of the State Law Number 81 of August 30, 1991.
<b>RECOMMENDATION</b>	I recommend management to establish the necessary internal controls and procedures in order to maintain a complete accounting system which adequately summarizes the accounting information of all the financial transactions related to assets, liabilities, revenues and expenditures of the Municipality's funds. Also, the accounting records of the Municipality should be precisely enough, to support the amounts presented in the financial statements.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

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**FINDING NUMBER**                      **2014-001**

**REQUIREMENT**                      **ACCOUNTING RECORDS AND REPORTING SYSTEM**

**MANAGEMENT RESPONSE**                      On January 1, 2015, the Municipality implemented a new computerized accounting system provided by company Rock Solid Technologies, Inc. This new system permits the integration of all of the main accounting modules (collections, purchasing, disbursements, payroll and budget) providing a complete trial balance that includes all the Balance Sheet and Income Statement accounts needed to correctly report the financial transactions of the Municipality in accordance with GAAP. The consolidation of all accounting transactions in one integrated system will facilitate the monthly review and reconciliation processes and will improve the detection of accounting errors.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

<b>FINDING NUMBER</b>	<b>2014-002</b>
<b>REQUIREMENT</b>	<b>ACCOUNTING RECORDS- CAPITAL ASSETS</b>
<b>CONDITION</b>	The Municipality does not have an effective system to account for capital assets, including the infrastructure assets.
<b>CONTEXT</b>	During the examination of the accounting records, I noted that the Municipality does not maintain an adequate capital assets subsidiary records. In addition, did not maintain adequate internal controls and procedures to ensure that all capitalizable expenditures and dispositions are recorded. Also, the Municipality did not maintain adequate supporting documentation of the cost of the capital assets, including the infrastructure, reported in the statement of net position at June 30, 2014.
<b>CRITERIA</b>	GASB 34 requires that all capital assets, including infrastructure, must be presented in the statement of net position and that there must be depreciated during its useful life. Chapter VIII, Article 8.010 (c) (3) of the State Law Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociados de Puerto Rico de 1991</i> of August 30, 1991, states that Municipality should maintain updated property accounting records.
<b>CAUSE</b>	The lack of an adequate capital assets register did not permit the proper accounting over the capital assets, the accumulated depreciation and the depreciation expense presented in the financial statements of the Municipality.
<b>EFFECT</b>	The Municipality's government wide financial statements do not present fairly, the financial position of the governmental activities, and the change in net position.
<b>RECOMMENDATION</b>	I recommend management and the Property Division of the Municipality to make an inventory of the capital assets, support it with adequate documentation and reconcile it with the capital assets subsidiary ledger. Also, the accounting staff should determine if the accumulated depreciation and depreciation expense are properly calculated.
<b>MANAGEMENT RESPONSE</b>	The Finance Department will assign personnel to perform a physical inventory of the Municipality's capital assets in order to adjust the property, plant and equipment subsidiary. Once the balances are adjusted to their correct values, the revised amounts will be recorded in the fixed assets module of the new accounting system (see response in Finding 2014-001).

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

<b>FINDING NUMBER</b>	<b>2014-003</b>
<b>REQUIREMENT</b>	<b>ACCOUNTING RECORDS- INTERFUND TRANSACTIONS</b>
<b>CONDITION</b>	The Municipality does not maintain an accurate record over the interfund transactions.
<b>CONTEXT</b>	<p>During the examination of the accounting records, I noted that the Municipality does not maintain complete and adequate subsidiary records to accurately account for the interfund transactions, presented in the Balance Sheet, for the fiscal year 2013-2014.</p> <p>In addition, I noted that the Municipality did not maintained adequate accounting over the interfund transactions of a bank account were the Municipality pooled the cash balances of various non federal special revenue funds.</p>
<b>CRITERIA</b>	Article 8.004 (c) of the State Law Number 81 - <i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico de 1991</i> - August 30, 1991, states that the restricted funds received by the Municipality should be only used for the purposes established by these resources. In addition, Article 8.010 (C) (2) and (3) of State Act Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico</i> of August 30, 1991, states that Municipalities should maintain accurate accounting records and funds controls.
<b>CAUSE</b>	The accounting staff did not maintain adequate subsidiary ledgers over the interfund transactions and the due from and due to account balances.
<b>EFFECT</b>	The Municipality is not in compliance with Chapter VIII, Article 8.004 (c) and Article 8.010 (c) (2) (3) of the State Act No. 81.
<b>RECOMMENDATION</b>	I recommend management to implement procedures in order to obtain and maintain accurate subsidiary records that supports the interfund transactions. These records should include the purpose of the transfers, the name of the funds that received the loans and the balance of the interfund, by each fund.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

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**FINDING NUMBER**

**2014-003**

**REQUIREMENT**

**ACCOUNTING RECORDS- INTERFUND TRANSACTIONS**

**MANAGEMENT RESPONSE**

The Municipality's accounting personnel has begun a comprehensive analysis of the beginning balances of the due to/ from accounts in order to determine the correct amounts owed between funds. Also, the new accounting system implemented on January 1, 2015 recognizes all interfund transactions related to payroll expenditures in the corresponding due to/ from accounts, which will facilitate the reconciliation and reimbursement process.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

<b>FINDING NUMBER</b>	<b>2014-004</b>
<b>REQUIREMENT</b>	<b>ACCOUNTING RECORDS- MUNICIPAL SOLID WASTE LANDFILL CLOSURE AND POSTCLOSURE CARE AND MAINTENANCE COSTS</b>
<b>CONDITION</b>	The Municipality did not adjust in its government wide financial statements, the required liability for closure and post closure care costs based on a study of the activities of the solid waste landfill.
<b>CONTEXT</b>	At June 30, 2014 the accompanying statement of net position presents a liability for closure and post-closure care cost of the Municipality solid waste landfill of \$10,450,048. However, this liability has not been updated based on a study, in conformity with the regulatory requirements established by the U.S. Environmental Protection Agency (EPA) and GASB 18.
<b>CRITERIA</b>	Regulations set forth by the U.S. Environmental Protection Agency (EPA) in its "Solid Waste Disposal Facility Criteria"; the Municipality is required to place a final cover on the Municipality's solid waste landfill site when it stops accepting waste, and to perform certain maintenance and monitoring functions at the site for 30 years after closure. GASB 18 requires the Municipality to perform a study of the activities that need to be implemented at the Municipality's solid waste landfill facilities to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. Based on this study, the Municipality must adjust the liability recorded in its statement of net position at June 30, 2014.
<b>CAUSE</b>	The Municipality failed to perform a study of the operation of the waste landfill, in accordance with the requirements of the EPA, in order to update the closure and post-closure liability.
<b>EFFECT</b>	The Municipality's government wide financial statements do not present fairly, the financial position of the governmental activities, and the change in net position. Also, the Municipality is not in compliance with GASB 18 and the "Solid Waste Disposal Facility Criteria" issued by the U.S. Environmental Protection Agency.
<b>RECOMMENDATION</b>	I recommend management to perform the study of the activities that need to be implemented at the Municipality's solid waste landfill facilities and determine the amount of the liability that should be reported in the governmental activities.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

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<b>FINDING NUMBER</b>	<b>2014-004 (CONTINUED)</b>
<b>REQUIREMENT</b>	<b>ACCOUNTING RECORDS- MUNICIPAL SOLID WASTE LANDFILL CLOSURE AND POSTCLOSURE CARE AND MAINTENANCE COSTS</b>
<b>MANAGEMENT RESPONSE</b>	The Municipality's management will perform the required study in order to record a reasonable estimate of the closure and post-closure costs of its landfill, so that the corresponding liability can be correctly reported in the June 30, 2015 government-wide financial statements.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

<b>FINDING NUMBER</b>	<b>2014-005</b>
<b>REQUIREMENT</b>	<b>ACCOUNTING RECORDS- BANK RECONCILIATIONS</b>
<b>CONDITION</b>	The Municipality does not maintain effective internal control procedures to ensure that the bank reconciliations of several bank accounts were prepared accurately, in a timely manner and reconciled with the accounting records.
<b>CONTEXT</b>	<p>During the examination of the bank reconciliations, I noted that the Municipality has not prepared the bank reconciliations for the months of May and June 2014 of several bank accounts. Also, I noted that the bank reconciliation process consists only of including the ending bank balance, less the outstanding checks of the month. In addition, the payroll bank reconciliation was not prepared for the month of June 2014.</p> <p>In addition, there was not a reconciliation process between the bank reconciliations and the accounting records, because the accounting personnel does not maintained an updated Model 4a (the manual accounting system that summarized the cash transactions of the Municipality), for the monthly cash transactions of the General Fund and the special revenue funds.</p>
<b>CRITERIA</b>	Chapter IV, Section 12 of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affair (OCAM), establishes that the accounting system of the municipalities shall provide for the timely and accurate preparation of bank reconciliations. In addition, the Municipality shall prepare a monthly report of revenues and disbursements, which has to be reconciled with the bank reconciliations.
<b>CAUSE</b>	The Municipality's internal control procedures failed to assure that the bank reconciliations were prepared in a complete manner and reconciled with the accounting records.
<b>EFFECT</b>	The Municipality is not in compliance with Chapter IV, Section 12 of the Municipal Administration Regulatory Manual of the OCAM.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

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<b>FINDING NUMBER</b>	<b>2014-005 (CONTINUED)</b>
<b>REQUIREMENT</b>	<b>ACCOUNTING RECORDS- BANK RECONCILIATIONS</b>
<b>RECOMMENDATION</b>	I recommend management to establish internal control procedures over the preparation of the bank reconciliations and assure that the accounting records are reconciled with the bank reconciliations within a reasonable amount of time in order to maintain proper control over cash.
<b>MANAGEMENT RESPONSE</b>	The Municipality's new accounting system implemented on January 1, 2015 includes a bank reconciliation module that will facilitate the monthly reconciliation process. Also, since all the cash collection and disbursement information is compiled in one place, it will facilitate the preparation of the monthly "Modelo 4a" report on a timely manner.

**SECTION II – FINANCIAL STATEMENTS FINDINGS**

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<b>FINDING NUMBER</b>	<b>2014-006</b>
<b>REQUIREMENT</b>	<b>SINGLE AUDIT SUBMISSION</b>
<b>CONDITION</b>	The Municipality did not comply with the required due date for the submission of the Single Audit Report.
<b>CONTEXT</b>	The Municipality did not submit, in a timely manner, the Single Audit Reporting package for the fiscal year ending on June 30, 2014. The due date for this report was no later than March 31, 2014.
<b>CRITERIA</b>	OMB Circular A-133, Subpart C, Section 320 (a) states that all audits shall be completed and submitted to the Federal Audit Clearinghouse and the cognizant agency within the earlier of 30 days after receipt of the auditor's report or nine (9) months after the end of the audit report.
<b>CAUSE</b>	Due to the lack of adequate accounting records, the Municipality did not comply with the requirements established in OMB Circular A-133.
<b>EFFECT</b>	The Municipality is not in compliance with OMB Circular A-133, Subpart C, Section 320 (a). Also, the Municipality could be sanctioned by the Federal Government for the noncompliance of this requirement.
<b>RECOMMENDATION</b>	I recommend management to maintain adequate accounting records that allow for the timely completion of the financial statements and performance of the Single Audit.
<b>MANAGEMENT RESPONSE</b>	With the implementation of the new accounting system, the accounting records will be reconciled in a timely manner, which will facilitate the preparation of the financial statements with sufficient time in order to comply with the March 31 deadline.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-007</b>
<b>FEDERAL PROGRAM</b>	<b>HEAD START (CFDA NO. 93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES; PASS THROUGH COMMONWEALTH OF PUERTO RICO- ADMINISTRATION FOR CARE AND INTEGRAL DEVELOPMENT OF CHILDHOOD (ACUDEN)</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>CASH MANAGEMENT</b>
<b>CONDITION</b>	The Program did not minimize the time between the receiving of the request of funds from the pass-through entity and the disbursement of funds.
<b>CONTEXT</b>	During the cash management test, I noted that the Head Start Program maintained an average cash balance, during the fiscal year 2013-2014, of approximately \$270,722 in bank reconciliations.
<b>CRITERIA</b>	Code of Federal Regulation 45, Subpart C, Section 92.21 (b) states that methods and procedures for payment shall minimize the time elapsing between the transfer of funds and disbursement by the grantee or subgrantee, in accordance with Treasury regulations at 31 CFR Part 205.
<b>CAUSE</b>	The Program did not maintain appropriate cash management procedures in order to disburse the funds requested to the pass-through entity in a timely manner.
<b>EFFECT</b>	The Program is not in compliance with Code of Federal Regulation 45, Subpart C, Section 92.21 (b).
<b>RECOMMENDATION</b>	I recommended management to continue strengthening its disbursement procedures to minimize the time between the transfer of funds by the pass through entity and the disbursements made by the Program.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	This situation is caused by the short time between the date that the pass-through entity transfer the funds to the Municipality and the closing of the accounting cycle of the Program. However, the Program has adopted mechanisms, directed to minimize the time between the receipt of funds and the payment of the obligations.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-008</b>
<b>FEDERAL PROGRAM</b>	<b>HEAD START (CFDA NO. 93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES; PASS THROUGH COMMONWEALTH OF PUERTO RICO- ADMINISTRATION FOR CARE AND INTEGRAL DEVELOPMENT OF CHILDHOOD (ACUDEN)</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>MATCHING, LEVEL OF EFFORT, EARMARKING</b>
<b>CONDITION</b>	The Program does not maintained an effective accounting system to account for the matching contribution and the 15% of administrative earmark.
<b>CONTEXT</b>	<p>During the matching test, I examined two (2) months (October 2013 and February 2014) of the in kind contributions of the Program and noted that the accounting records related to the matching contributions are composed of electronic worksheets that are not integrated to a formal accounting system. Also, I noted that during fiscal year 2013-2014, the Program reports monthly in-kind rent contributions, which were based on estimates made by the Program management and were not made by an independent appraisal.</p> <p>In addition, the Program did not maintain a complete accounting system which adequately separates the administrative and programmatic costs of the Program.</p>
<b>CRITERIA</b>	45 CFR Subpart C, Section 92.24 (b) (6) states that costs and third party in kind contributions counting towards satisfying a cost sharing or matching requirement must be verifiable from the records of grantees and subgrantee or cost- type contractors. Also, 45 CFR, Section 92.20 (b) (2) states that the grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially-assisted activities.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-008 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>HEAD START (CFDA NO. 93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES; PASS THROUGH COMMONWEALTH OF PUERTO RICO- ADMINISTRATION FOR CARE AND INTEGRAL DEVELOPMENT OF CHILDHOOD (ACUDEN)</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>MATCHING, LEVEL OF EFFORT, EARMARKING</b>
	<p>These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures and income. Also, CFR 92.24 (g) states that in some cases under paragraphs (d), (e) and (f) of this section, it will be necessary to establish the market value of land or a building or the fair rental rate of land or of space in a building. In these cases, the Federal agency may require the market value or fair rental value be set by an independent appraiser, and that the value or rate be certified by the grantee. This requirement will also be imposed by the grantee on subgrantees.</p>
<b>CAUSE</b>	The Program accounting staff is not maintaining adequate accounting records regarding the matching contributions transactions and the administrative earmarking.
<b>EFFECT</b>	The Municipality is not in compliance with 45 CFR, Subpart C, Sections 92.20 (b) (2) and 92.24 (b) (6) and (g).
<b>RECOMMENDATION</b>	I recommend management to continue strengthening the internal controls and procedures in order to assure that adequate accounting records are maintained for the in-kind contributions and the administrative earmarking.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	Management gave specific instructions and has adopted the necessary internal controls in order to improve the accounting of the in-kind contributions made by the Municipality to the Program.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-009</b>
<b>FEDERAL PROGRAM</b>	<b>HEAD START (CFDA NO. 93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES; PASS THROUGH COMMONWEALTH OF PUERTO RICO- ADMINISTRATION FOR CARE AND INTEGRAL DEVELOPMENT OF CHILDHOOD (ACUDEN)</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>REPORTING</b>
<b>CONDITION</b>	The Municipality did not maintain adequate internal controls over the accounting transactions of the Program.
<b>CONTEXT</b>	During the reporting test, I noted that the Program did not maintain an adequate set of accounting records in order to fairly present the financial position of the Program and the results of its operations. Also, I noted that the accounting system provided by the pass-through entity was not updated at June 30, 2014.
<b>CRITERIA</b>	Code of Federal Regulation 45, 92.20 (b) (1) states that the grantees and subgrantees financial management system must assure accurate, current, and complete disclosure of the financial results of the financially assisted activities in accordance with the financial reporting requirements of the grant or subgrant. In addition, Section 92.20 (b) (2) states that the grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially-assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures and income. Also, Clause Eight, Section (10) of the grant agreement with the pass-through entity, states that is requirement the use of the official accounting system provided by the pass-through entity. It will not be recognized other accounting system, as the official system of the program for the effects of an external audit, state or federal audit. The recording of all the accounting transactions of the program will be compulsory, through the official accounting system. It will be an obligation of the program maintaining updated accounting information in the system, to reflect the financial position of the program.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-009 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>HEAD START (CFDA NO. 93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES; PASS THROUGH COMMONWEALTH OF PUERTO RICO- ADMINISTRATION FOR CARE AND INTEGRAL DEVELOPMENT OF CHILDHOOD (ACUDEN)</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>REPORTING</b>
<b>CAUSE</b>	The accounting staff failed to maintain proper accounting records that supports adequately, the financial reports submitted to the pass-through entity. Also, the accounting staff of the Program is not following, adequately, the accounting guidance provided by the pass-through entity.
<b>EFFECT</b>	The program did not maintain its financial management system updated to assure compliance with the financial reports requirements of the pass through entity and Federal regulation.
<b>RECOMMENDATION</b>	The Program should continue strengthening its procedures and controls to ensure that the accounting system information is updated and assure that the financial information submitted to the pass through entity, is supported with complete and accurate accounting records.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	The Program has adopted and improved the internal controls through the acquisition of a new accounting system that will permit that the financial information will be completed and updated.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-010</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>CASH MANAGEMENT</b>
<b>CONDITION</b>	During the fiscal year 2013-2014, the Program maintain excess of cash in the bank account reconciliations.
<b>CONTEXT</b>	During the cash management test, I noted that in fiscal year 2013-2014, the Program maintained an average cash balance, in the bank reconciliations, of approximately \$33,550. Also, I noted that the bank reconciliation for the month of June 2014 was not prepared.
<b>CRITERIA</b>	Code of Federal Regulations 24, 85.20 (b) (7) states, that procedures for minimizing the time elapsing between the transfer of funds from the U.S Treasury and disbursement by grantees and sub grantees must be whenever advance payment procedures used.
<b>CAUSE</b>	The Program and the Finance Department of the Municipality did not maintain appropriate cash management procedures in order to drawdown funds only for immediate needs.
<b>EFFECT</b>	The Program is not in compliance with Code of Federal Regulations 24, 85.20 (b) (7).
<b>RECOMMENDATION</b>	I recommend management to make an analysis of the excess of cash maintain in bank to determine from which activities and program year correspond in order to determine the purpose of such drawdowns. Also, the accounting staff should make drawdowns only for immediate needs.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	The Program made administrative changes directed to improve the accounting and the management of the assigned funds. Management gave instructions to make drawdowns only when is necessary.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-011</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>MATCHING, LEVEL OF EFFORT, EARMARKING</b>
<b>CONDITION</b>	The Program did not comply with the administrative earmarking during the fiscal year 2013-2014.
<b>CONTEXT</b>	<p>For fiscal year 2013-2014, the Municipality received an entitlement grant of \$796,200. The Program administrative cap for the program year was \$159,240. During the examination, I noted that during fiscal year 2013-2014, the Program make drawdowns amounting to \$245,915 for planning and administrative costs, which included \$198,155 for the payment of the current year administrative obligations and \$47,760 for the payment of prior year unliquidated obligations. The drawdowns amounting to \$198,155, used to pay the current year administrative obligations exceeded the administrative cap for fiscal year 2013-2014.</p> <p>Also, I noted that in the PR26- CDBG Financial Summary Report, the Program included, in line 43 as current year program income, the amount of \$387,629, to determine the administrative cap. During my examination I found that during the fiscal year 2013-2014 the Program did not received program income.</p>
<b>CRITERIA</b>	Code of Federal Regulations 24, 570.200 (g) states that no more than 20 percent of the sum of any grant, plus program income, shall be expended for planning and program administrative costs, as defined in 570.205 and 507.206, respectively. Recipients of entitlement grants under subpart D of this part shall conform with this requirement by limiting the amount of CDBG funds obligated for planning plus administration during each program year to an amount no greater than 20 percent of the sum of its entitlement grant made for that program year (if any) plus the program income received by the recipient and its subrecipients (if any) during that program year.
<b>CAUSE</b>	The Program did not monitored adequately, the administrative earmarking, during the fiscal year 2013-2014, to assure that only obligated funds for planning and administrative costs up to a 20% of the program year grant.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING</b>	<b>2014-011 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>MATCHING, LEVEL OF EFFORT, EARMARKING</b>
<b>EFFECT</b>	The Program is not complying with Code of Federal Regulation 24, 570.200 (g).
<b>RECOMMENDATION</b>	I recommend management to continue improving the internal controls and procedures over the administrative earmarking, to assure that not more than 20% of the total grant received during the program year is obligated for planning and administrative cost.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	The Program is very cautious with the obligation of the administrative costs. Management has implemented the necessary internal controls to assure that the Program does not exceed the assigned limit for administrative costs. This situation respond to the reimbursements of administrative costs of prior years that were disbursed in the current year, but charged to prior years.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-012</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>PROCUREMENT AND SUSPENSION AND DEBARMENT</b>
<b>CONDITION</b>	The Program did not included in the contracts, all the required clauses.
<b>CONTEXT</b>	<p>During the contract provisions test, I examined two (2) construction contracts to verify the completeness of its clauses and noted the following:</p> <ul style="list-style-type: none"><li>❖ Two (2) construction contracts did not include a provision for the compliance with executive order 11246;</li><li>❖ Two (2) construction contracts did not include a provision for compliance with Sections 103 and 107 "Contract Work Hours &amp; Safety Standards Act;</li><li>❖ Two (2) construction contracts did not include a provision for compliance with the Energy Policy and Conservation Act (Pub L. 94-163, 89 Stat 871);</li><li>❖ Two (2) construction contracts did not include a provision for compliance with the Copeland "Anti-kickback";</li><li>❖ Two (2) contracts did not include a provision for retention of all required records for three (3) years.</li></ul>
<b>CRITERIA</b>	Code of Federal Regulations 24, Subpart C, Section 85.36 (i) (1-13) establishes all the required clauses that contracts should include.
<b>CAUSE</b>	The Contract Division of the Municipality failed to assure that the contracts included all the required clauses.
<b>EFFECT</b>	The Program is not in compliance with Code of Federal Regulations 24, Subpart C, Section 85.36 (i) (1-13).
<b>RECOMMENDATION</b>	I recommend management to update the Municipality's contract model according with the Federal requirements.
<b>QUESTIONED COSTS</b>	None

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-012 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>PROCUREMENT AND SUSPENSION AND DEBARMENT</b>
<b>MANAGEMENT RESPONSE</b>	Management gave the instructions to work on the update of a contract model which includes all the required clauses.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-013</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>PROGRAM INCOME</b>
<b>CONDITION</b>	The Program did not comply with the program income requirement.
<b>CONTEXT</b>	During the examination, I found that the transactions related with the program income were not accurately recorded in the accounting records of the Program. Also, I noted that the Program did not maintain an adequate inventory of the sales of the housing units that generated the program income.
<b>CRITERIA</b>	Code of Federal Regulations 24, Section 570.504 (a), states that the receipts and expenditures of program income shall be recorded as part of the financial transactions of the grant program.
<b>CAUSE</b>	The accounting staff does not maintained appropriate and complete accounting records over the program income transactions.
<b>EFFECT</b>	The Program is not in compliance with Code of Federal Regulations 24, Section 570.504 (a).
<b>RECOMMENDATION</b>	The Program's accounting staff should include in the accounting records of the Program, all the transactions of the program income, related to revenues and expenditures. Also, the Program should maintain an adequate inventory and records regarding the available housing units, proceed and use of the sale of the housing units.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	This situation was corrected. Management gave instructions directed to account adequately the transactions related to program income and to maintain an adequate inventory of the available units.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-014</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>REPORTING</b>
<b>CONDITION</b>	The Program accounting records were not updated as of June 30, 2014.
<b>CONTEXT</b>	During the reporting test, I noted that the SF-425, Federal Financial Report, applicable to fiscal year 2013-2014, were not available for examination. Also, I noted that the Program did not maintained an accurate, complete and updated accounting system in which the financial transactions of the Program are properly recorded.
<b>CRITERIA</b>	CFR 24, Section 85.20 (b) (1) and (2) <i>Financial reporting</i> , states that accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or subgrant. <i>Accounting records</i> , states that grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.
<b>CAUSE</b>	The accounting staff is not maintaining adequate accounting records regarding the financial transactions of the Program.
<b>EFFECT</b>	The Program did not maintain its financial management system updated to assure compliance with the financial reports requirements established in the Federal regulation.
<b>RECOMMENDATION</b>	The Program should improve its internal control over the recording of the financial transactions of the Program in order to assure that the information submitted to HUD is adequately supported and recorded in complete accounting registers.
<b>QUESTIONED COSTS</b>	None

**SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-014 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>REPORTING</b>
<b>MANAGEMENT RESPONSE</b>	The Program has made administrative changes in order to improve the internal controls. Also, the Program has adopted procedures directed to improve the accounting and the presentation of the financial reports of the Program.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-015</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>SPECIAL TEST- ENVIRONMENTAL REVIEWS</b>
<b>CONDITION</b>	The Program did not provide sufficient evidence about the environmental reviews for improvement projects.
<b>CONTEXT</b>	During the disbursement test, I selected the projects "Pavement of roads and streets", "Construction of wall in Comm. Caimital", and the Historic Preservation Program" and I did not found that the Program performed a written determination stating that the environmental reviews were not required for these activities. In addition, the only environmental reviews provided by the Program was the one related with the State Historic Preservation Office.
<b>CRITERIA</b>	As stated in 24 CFR 58.22 (a) neither a recipient nor any participant in the development process, including public or private nonprofit or for profit entities, or any of their contractors, may commit HUD assistance under a program listed in 58.1 (b) on an activity or project until HUD or the State has approved the recipient's RROF and the related certification from the responsible entity. In addition, until the RROF and the related certification have been approved neither a recipient nor any participant in the development process may commit non HUD funds on or undertake an activity or project under a program listed in 58.1 (b) if the activity or project would have an adverse environmental impact or limit the choice of reasonable alternatives. Also, 24 CFR 58.22 (b) states that if a project or activity is exempt under 58.34, or is categorically excluded (except in extraordinary circumstances) under 58.35(b), no RROF is required and the recipient may undertake the activity immediately after the responsible entity has documented its determination as required in 58.34(b) and 58.35(d), but the recipient must comply with applicable requirements under 58.6.
<b>CAUSE</b>	The Program incurred in such disbursements without the necessary environmental reviews or without documenting adequately, that a review was not required.
<b>EFFECT</b>	The Program is not in compliance with 24 CFR 58.22 (a) and (b).

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-015 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>SPECIAL TEST- ENVIRONMENTAL REVIEWS</b>
<b>QUESTIONED COSTS</b>	None
<b>RECOMMENDATION</b>	Management should not encumber or expend CDBG funds on an activity or project until the environmental reviews are obtain or a written determination is made stating that the review is not necessary.
<b>MANAGEMENT RESPONSE</b>	Management gave instructions that no matter the projects did not require environmental reviews, the personnel in charge has to document the projects that are considered categorical exclusions. The projects mentioned in this finding were categorically excluded.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-016</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>SUBRECIPIENT MONITORING</b>
<b>CONDITION</b>	The Program did not maintain adequate procedures to monitor the subrecipient's use of Federal awards.
<b>CONTEXT</b>	During fiscal year 2013-2014, the Program disbursed funds, amounting to \$25,000, to one (1) not for profit subrecipient. During the examination, I noted that the Program did not have adequate monitoring procedures to verify the use of the Federal funds sub-granted to the subrecipient. There was no evidence that, during fiscal year 2013-2014, the Program monitored the subrecipient through reporting, site visits or regular contact to provide reasonable assurance that the use of funds are in compliance with the contract formalized.
<b>CRITERIA</b>	Code of Federal Regulations 84.51 (a) states that recipients are responsible for managing and monitoring each project, program, subaward, function or activity supported by the award. Recipients shall monitor subawards to ensure sub-recipients have met the audit requirements as delineated in § 84.26.
<b>CAUSE</b>	The Program failed to establish adequate internal controls over the monitoring process of the subrecipients use of Federal funds.
<b>EFFECT</b>	The Program is not in compliance with CFR 84.51 (a).
<b>RECOMMENDATION</b>	I recommend management to established adequate internal controls over the subrecipient monitoring, which include visits, limited scope audits and reporting requirements.
<b>QUESTIONED COSTS</b>	None

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-016 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>COMMUNITY DEVELOPMENT BLOCK GRANTS/ ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>SUBRECIPIENT MONITORING</b>
<b>MANAGEMENT RESPONSE</b>	The Program has adopted controls and mechanisms directed to strengthen the monitoring of the funds granted to the subrecipient. This situation was referred to the office of the internal auditor of the Municipality, for the required monitoring procedures.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-017</b>
<b>FEDERAL PROGRAM</b>	<b>SECTION 8 HOUSING CHOICE VOUCHERS (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>SPECIAL TEST- REASONABLE RENT</b>
<b>CONDITION</b>	The determination of the reasonable rent to owners was not properly documented by the Program.
<b>CONTEXT</b>	<p>During the eligibility test, I examined a sample of twenty-five (25) participant's file and found the following conditions related to the compliance with the reasonable rent special test:</p> <ul style="list-style-type: none"><li>• In one (1) participant's file, I did not found the reasonable rent study for a change of unit made during the fiscal year 2013-2014;</li><li>• In three (3) participants' files, the reasonable rent studies were not certified by the responsible employee;</li><li>• In addition, I noted that the data base used by the Program for the reasonable rent studies were not updated in the last four years.</li></ul>
<b>CRITERIA</b>	Code of Federal Regulation 24, 982.507 (a) (1) (2) and (b) states that the PHA may not approve a lease until the PHA determines that the initial rent to owner is a reasonable rent; (2) the PHA must re-determine the reasonable rent: (a) before any increase in the rent to owner; (b) if there is a five percent decrease in the published FMR in effect 60 days before the contract anniversary as compared with the FMR in effect one year before the contract anniversary; and (c) if directed by HUD. (b) <i>Comparability</i> , states that the PHA must determine whether the rent to owner is a reasonable rent in comparison to rent for other comparable unassisted units. To make this determination, the PHA must consider: (1) The location, quality, size, unit type, and age of the contract unit; and (2) Any amenities, housing services, maintenance and utilities to be pro-vided by the owner in accordance with the lease.
<b>CAUSE</b>	The Program did not maintain adequate documentation in the participants' files to support the basis for the determination that the rent paid to the owners are reasonable.
<b>EFFECT</b>	The Program is not in compliance with Code of Federal Regulation 24, Section 982.507 (a) (1), (2) and (b).

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-017 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>SECTION 8 HOUSING CHOICE VOUCHERS (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>SPECIAL TEST- REASONABLE RENT</b>
<b>RECOMMENDATION</b>	I recommend management to continue strengthening the internal control procedures to assure that the rents paid to the owners are reasonable. Also, I recommend that adequate, proper and updated documentation about the reasonable rent determination is maintained in the participants' files.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	Management gave instructions in order to update the reasonable rents. This situation will be corrected immediately.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-018</b>
<b>FEDERAL PROGRAM</b>	<b>CHILD AND ADULT CARE FOOD PROGRAM (CFDA NO. 10.558) U.S. DEPARTMENT OF AGRICULTURE; PASS THROUGH COMMONWEALTH OF PUERTO RICO- DEPARTMENT OF EDUCATION</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>CASH MANAGEMENT</b>
<b>CONDITION</b>	The Program maintain high average balances in the monthly bank reconciliations.
<b>CONTEXT</b>	During the cash management test, I noted that during the fiscal year 2013-2014, the Program maintained an average monthly cash balance of approximately \$188,502 in books.
<b>CRITERIA</b>	Code of Federal Regulations 7, Section 3016.21 (b) <i>Basic standard</i> , states that methods and procedures for payment shall minimize the time elapsing between the transfer of funds and disbursement by the grantee or subgrantee, in accordance with Treasury regulations at 31 CFR part 205.
<b>CAUSE</b>	The Program and Finance Department of the Municipality did not maintain appropriate cash management procedures.
<b>EFFECT</b>	The Program is not in compliance with Code of Federal Regulations 7, Section 3016.21 (b).
<b>RECOMMENDATION</b>	I recommend management to make an analysis of the cash balance and verify if there are cash carryovers and determine if those carryovers have to be reimburse to the pass-through entity.
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	Management gave instructions to make an analysis of the balances maintained by the Program and to implement the necessary internal controls in order to maintain the minimum required balances.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

<b>FINDING NUMBER</b>	<b>2014-019</b>
<b>FEDERAL PROGRAM</b>	<b>CHILD AND ADULT CARE FOOD PROGRAM (CFDA NO. 10.558) U.S. DEPARTMENT OF AGRICULTURE; PASS THROUGH COMMONWEALTH OF PUERTO RICO- DEPARTMENT OF EDUCATION</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>PERIOD OF AVAILABILITY</b>
<b>CONDITION</b>	The Program disbursed funds for goods after the period of availability.
<b>CONTEXT</b>	During the grant disbursement test, I examined fourteen (14) disbursement vouchers, for the purchase of food and I noted that two (2) invoices amounting to \$136,755 were paid, after of the period of availability. The purchase orders related to this invoices were from the budget obligations of program year 2012-2013 and 2011-2012.
<b>CRITERIA</b>	Code of Federal Regulation 7, Section 3016.23 (b) states that a grantee must liquidate all obligations incurred under the award not later than 90 days after the end of the funding period (or as specified in a program regulation) to coincide with the submission of the annual Financial Status Report (SF-269). The Federal agency may extend this deadline at the request of the grantee.
<b>CAUSE</b>	The Program does not maintained adequate internal controls to monitor the outstanding obligations which are scheduled to be paid during the period of availability.
<b>EFFECT</b>	The Program is not in compliance with Code of Federal Regulation 7, Subpart C, Section 3016.23 (b).
<b>RECOMMENDATION</b>	I recommend management to establish adequate internal controls, to assure that the purchases orders are prepared in a timely basis and that are liquidated during the period of availability.
<b>QUESTIONED COSTS</b>	None

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-019 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>CHILD AND ADULT CARE FOOD PROGRAM (CFDA NO. 10.558) U.S. DEPARTMENT OF AGRICULTURE; PASS THROUGH COMMONWEALTH OF PUERTO RICO- DEPARTMENT OF EDUCATION</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>PERIOD OF AVAILABILITY</b>
<b>MANAGEMENT RESPONSE</b>	Management has strengthen the internal controls in order to adjust the purchases and the time in which the obligations are paid.

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-020</b>
<b>FEDERAL PROGRAM</b>	<b>CHILD AND ADULT CARE FOOD PROGRAM (CFDA NO. 10.558) U.S. DEPARTMENT OF AGRICULTURE; PASS THROUGH COMMONWEALTH OF PUERTO RICO- DEPARTMENT OF EDUCATION</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>REPORTING</b>
<b>CONDITION</b>	The Municipality did not maintain adequate internal controls of the accounting transactions of the Program.
<b>CONTEXT</b>	During the reporting test, I noted that the Program did not maintain an adequate set of accounting records. I found that the amounts reported in the accumulated expenditures report submitted to the pass-through entity was not traceable to adequate accounting records
<b>CRITERIA</b>	Code of Federal Regulation 7, Section 3016.20 (b) (1) and (2) states that the financial management systems of other grantees and subgrantees must meet the following standards: (1) <i>Financial reporting</i> . Accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or subgrant. (2) <i>Accounting records</i> . Grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.
<b>CAUSE</b>	The Program's internal controls failed to maintain proper accounting records that supports adequately, the financial reports submitted to the pass-through entity.
<b>EFFECT</b>	The program did not maintain its financial management system updated to assure compliance with the financial reports requirements of the pass through entity.
<b>RECOMMENDATION</b>	The Program should continue strengthening its procedures and controls to ensure that the financial information submitted to the pass through entity, is supported with complete and accurate accounting records

**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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<b>FINDING NUMBER</b>	<b>2014-020 (CONTINUED)</b>
<b>FEDERAL PROGRAM</b>	<b>CHILD AND ADULT CARE FOOD PROGRAM (CFDA NO. 10.558) U.S. DEPARTMENT OF AGRICULTURE; PASS THROUGH COMMONWEALTH OF PUERTO RICO- DEPARTMENT OF EDUCATION</b>
<b>REQUIREMENT</b>	<b>COMPLIANCE AND INTERNAL CONTROL</b>
<b>NONCOMPLIANCE</b>	<b>REPORTING</b>
<b>QUESTIONED COSTS</b>	None
<b>MANAGEMENT RESPONSE</b>	The Program has adopted and improved the internal controls through the acquisition of a new accounting system that will permit that the financial information will be completed and updated.

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
13-III-04	Cash Management	93.600	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-007
13-III-05	Matching, Level of Effort, Earmarking	93.600	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-008
13-III-06	Reporting	93.600	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-009
13-III-07	Allowable Cost	14.218	None	No corrective action has been taken. During fiscal year 2013-2014, the Program did not have the activity "Financial Assistance to Small Businesses".
13-III-08	Cash Management	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-010
13-III-09	Procurement and Suspension and Debarment-Excluded Party List	14.218	None	Full corrective action was taken.

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
13-III-10	Program Income	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-013
13-III-11	Reporting	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-014
13-III-12	Special Test- Environmental Reviews	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-015
13-III-13	Special Test- Rehabilitation	14.218	None	Full corrective action was taken.
13-III-14	Cash Management	10.558	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-018
12-III-07	Cash Management	93.600	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-007

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
12-III-09	Reporting	93.600	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-009
12-III-10	Allowable Cost	14.218	None	Partial corrective action has been taken.  During fiscal year 2013-2014, the Program did not have the activity "Financial Assistance to Small Businesses".
12-III-11	Cash Management	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-010
12-III-12	Procurement and Suspension and Debarment	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-012
12-III-13	Program Income	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-013
12-III-14	Reporting	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-014

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
12-III-15	Special Test- Environmental Reviews	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-015
12-III-16	Special Test- Rehabilitation	14.218	None	Full corrective action was taken.
12-III-18	Cash Management	10.558	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-018
11-III-09	Reporting	93.600 93.708	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-009
11-III-10	Cash Management	14.218 14.253	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-010
11-III-11	Procurement and Suspension and Debarment	14.218	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-012

<b>FINDING NUMBER</b>	<b>COMPLIANCE</b>	<b>CFDA NUMBER</b>	<b>QUESTIONED COSTS</b>	<b>AUDITEE COMMENTS</b>
11-III-13	Cash Management	10.558	None	No corrective action has been taken.  The auditor reissued the finding for the current year. Finding reference 2014-018