

**MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO**

SINGLE AUDIT REPORT
For the Fiscal Year Ended June 30, 2012
(With Independent Auditor Report Thereon)

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

**MUNICIPIO DE GUAYANILLA
AUDITORÍA 2011-2012
30 DE JUNIO DE 2012**

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Basic Financial Statements and
Supplemental Schedule
Single Audit Report
Fiscal Year Ended June 30, 2012

	Page
Independent Auditor's Report.....	1-2
Required Supplementary Information:	
Management's Discussion and Analysis	3-16
Basic Financial Statements:	
Government-Wide Financial Statements:	
Statement of Net Assets	18
Statement of Activities	19
Governmental Fund Financial Statements:	
Balance Sheet – Governmental Funds.....	20
Statement of Revenues, Expenditures and Changes in Fund Balances (Deficits) – Governmental Funds	21
Reconciliation of the Balance Sheet – Governmental Funds and the Statement of Net Assets	22
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances (Deficits) – Governmental Funds and the Statement of Revenues, Expenses and Changes in Fund Net Assets	23
Notes to Basic Financial Statements.....	24-69
Required Supplementary Information:	
Budgetary Comparison Schedule - General Fund.....	70-71
Financial Data Schedule.....	72-73
Notes to the Financial Data Schedule	74
Schedule of Expenditures of Federal Awards	75-76
Notes to Schedule of Expenditures of Federal Awards.....	77
Internal Control and Compliance:	
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards.....	78-79
Independent Auditors' Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133	80-81
Audit Findings and Questioned Costs:	
Schedule of Findings and Questioned Costs:	
Section I: Summary of Auditors' Results.....	82
Section II: Financial Statements Findings and Questioned Costs.....	83-86
Section III: Federal Awards Findings and Questioned Costs.....	87-90
Schedule of Prior Year Findings and Questioned Costs	91



MENDOZA & RAMOS
Contadores Públicos Autorizados, C.S.P.

P.O. Box 35 • Guayama, Puerto Rico 00785

INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying financial statements of the governmental activities and each major fund of the Municipality of Guayanilla, Puerto Rico, as of and for the year ended June 30, 2012, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

The Municipality did not have a complete, updated and accurate accounting records of the capital assets in order to obtain sufficient and competent appropriate audit evidence related to the capital assets reported in the accompanying statement of net assets for \$55,188,570 (net of accumulated depreciation of \$27,474,896) as of June 30, 2012, and the amount of depreciation expense stated at \$2,533,165 for the year then ended. Therefore, we were unable to form an opinion regarding the capital assets and related depreciation expense as reported in the governmental activities of the Municipality.

Because of the significance of the matter discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial position of the governmental activities of the Municipality of Guayanilla as of June 30, 2012, and the changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In addition, in our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of each major fund of the Municipality of Guayanilla as of June 30, 2012 and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITORS' REPORT

Page 2

In accordance with Government Auditing Standards, we have also issued a report dated July 18, 2013, on our consideration of the Municipality's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 16 and 70 through 71 be presented to supplement basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standard Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economical or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management responses to our inquiries, the basic statements, and other knowledge we obtain during our audit to the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Guayanilla's basic financial statements as a whole. The accompanying Financial Data Schedule is presented for purpose of additional analysis as required by the U.S. Department of Housing and Urban Development. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the basic financial statements of the Municipality. The Financial Data Schedule and the Schedule of Expenditures of Federal Awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements taken as a whole.

Mendoza & Ramos CPA's

Mendoza & Ramos, C.S.P
Certified Public Accountants

Guayama, Puerto Rico
July 18, 2013

The stamp number 2573191
was affixed to the original of this report.



**Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012**

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

As management of the Municipality of Guayanilla (the Municipality), we offer readers the following discussion and analysis of the Municipality's financial activities reported in the accompanying basic financial statements as of and for the fiscal year ended June 30, 2012. We encourage readers to consider the information presented here in conjunction with additional information that is furnished in the accompanying financial statements, which follow this narrative.

Besides, this document includes comparative data with prior year as this information was available for the fiscal year ended on June 30, 2011. This MD & A is prepared in order to comply with the Governmental Accounting Standards Board (GASB) Statement No. 34, "*Basic Financial Statements – and Management's Discussion and Analysis-for State and Local Governments.*" and, among other purposes, to provide the financial statements users with the following major information:

- a broader basis in focusing important issues;
- acknowledgement of an overview of the Municipality's financial activities;
- provides for an evaluation of its financial condition as of the end of fiscal year 2011-2012 compared with prior year results;
- identification of uses of funds in the financing of the Municipality's variety of activities and;
- assess management's ability to handle budgetary functions.

FINANCIAL HIGHLIGHTS

Government-Wide Highlights:

- Total Net Assets of the Municipality Governmental Activities as of the end of the indicated fiscal year amounted to \$5,949,967 or eighteen percent (18%) of total assets.
- The Municipality's Governmental Activities total Net Assets increased by \$69,678 or one (1%) from the prior fiscal year-end balance.
- At the end of fiscal year 2012, total liabilities of the Municipality Governmental Activities amounted to \$27,158,586. Out of said amount, \$24,236,288 corresponded to long-term liabilities of which \$16,793,000 represented the outstanding balance of bonds issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues.

Governmental Funds' Highlights:

- As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$1,842,441 (\$3,944,548 in previous fiscal year 2010-2011).
- At the end of the current fiscal year, the fund deficit of the Municipality's General Fund amounted to \$2,256,129 or \$506,950 less than the previous fiscal year.
- The actual General Fund budgetary activities resulted in unfavorable balance of \$1,353,295.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The purpose of financial reporting is to provide external users of basic financial statements with information that will help them to make decisions or draw conclusions about the Municipality. There are many external parties that use the basic financial statements of the Municipality; however, these parties do not always have the same specific objectives. In order to address the needs of as many parties as reasonably possible, the Municipality, in accordance with required financial reporting standards, presents this Management's Discussion and Analysis (MD&A) as an introduction to the accompanying basic financial statements. This narrative represents an overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2012. Because this MD&A is designed to focus on the current year activities, resulting changes and currently known facts, we encourage readers to consider the information presented in this MD&A in conjunction with the additional information furnished in the accompanying basic financial statements.

The Municipality's basic financial statements include three components: (1) government-wide financial statements (GWFS), (2) fund financial statements (FFS), and (3) notes to the basic financial statements (NBFS). This report also contains additional required information in addition to the basic financial statements themselves. These components are described below.

The basic financial statements focus on: (1) the Municipality as a whole (government-wide financial reporting) and, (2) the Municipality's major individual governmental funds. Both perspectives allow the users to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability. The components of the basic financial statements are described below.

a) Government-Wide Financial Statements

The GWFS are composed of: (1) the statements of net assets (SNA) and (2) the statement of activities (SA). These financial statements can be found immediately following this MD&A. GWFS are designed to provide readers with a broad overview of the Municipality's operations as a whole in a manner similar to private-sector business. These statements provide short-term and long-term information about the Municipality's financial position, which assist the Municipality's management to determine the economic condition at June 30, 2012. The GWFS are prepared using methods that are similar to those used by most private businesses.

Both of the government-wide financial statements distinguish functions of the Municipality that are principally supported by taxes and intergovernmental activities (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*).

1. Statement of Net Assets

The purpose of SNA is to attempt to report all assets owned and all liabilities owed by the Municipality. The Municipality reports of all of its assets when it acquires ownership over the assets and reports all of its liabilities when they are incurred. For example, the Municipality reports buildings and infrastructure as assets, even though they are not available to pay the obligations incurred by the Municipality. On the other hand, the Municipality reports liabilities, such as claims and judgments, bonds and notes payable, obligations under capital leases,

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

compensated absences and certain accounts payable and accrued liabilities, even though these liabilities might not be paid until several fiscal years into the future.

The difference between the Municipality's total assets and total liabilities reported in SNA is presented as *net assets*, which is similar to the total owners' equity reported by a commercial enterprise in its financial statements. Although the purpose of the Municipality is not to accumulate net assets, as this amount increases or decreases over time, such amount represents a useful indicator of whether the financial position of the Municipality is either improving or deteriorating, respectively.

2. Statement of Activities

The SA presents information showing how the Municipality's net assets changed during the fiscal year ended June 30, 2012, by presenting all of the Municipality's revenues and expenses. As previously discussed, the items reported in SA are measured in a manner similar to the approach used by a commercial enterprise in that revenues are recognized when earned or established criteria are satisfied, and expenses are recorded when incurred by the Municipality. Consequently, revenues are reported even when they may not be collected for several months after the end of the fiscal year and expenses are recorded even though they may not have used cash during the current year.

Although SA looks different from a commercial enterprise's income statement, the difference is only in format, not substance. Whereas the bottom line in a commercial enterprise represents its net income, the Municipality reports an amount described as *net change in net assets*, which is essentially the same concept.

The focus of SA is on the *net cost* of various activities provided by the Municipality. The statement begins with a column that identifies the cost of each of the Municipality's major functions. Another column identifies the revenues that are specifically related to the classified governmental functions. The difference between the expenses and revenues related to specific functions/programs identifies the extent to which each function of the Municipality draws from general revenues or is self-financing through fees, intergovernmental aid, and other sources of resources.

This statement also presents a comparison between direct expenses and program revenues for each function of the Municipality.

GWFS and FFS present all of the Municipality's governmental activities, which are supported mostly by taxes, intergovernmental revenues (such as federal and state grants and contributions), and charge for services. All services normally associated with the Municipality fall into this category, including culture, recreation and education; general government; health and sanitation; public safety; public housing and welfare; and economic and urban development.

b) Fund Financial Statements

The Municipality's FFS consist of: (1) the balance sheet – governmental funds, and (2) the statement of revenues, expenditures and changes in fund balances – governmental funds. These financial

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

statements report the financial position, the results of operations of the Municipality's governmental, with an emphasis on the Municipality's major governmental funds.

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Municipality, like most other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. Each fund is considered an independent fiscal entity accounted for within a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenue, and expenditures. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial and contractual provisions. All of the funds of the Municipality can be divided into two categories: governmental funds and proprietary funds.

1. Governmental funds

Governmental funds are used to account for most of the services provided by the Municipality. These funds are used to account for essentially the same functions reported as governmental activities in the GWFS. Unlike GWFS, the focus of governmental funds in the FFS is directed to specific activities of the Municipality rather than the Municipality as a whole; therefore, governmental funds in FFS report the Municipality's operations in more detail than the GWFS.

Governmental funds in FFS provide a detailed short-term view of the Municipality's finances that assist in determining whether there will be adequate financial resources available to meet the current needs of the Municipality, which is, evaluating the Municipality's near-term financing requirements. For financial reporting purposes, the Municipality classifies its governmental funds within the following types: (1) general fund, (2) debt service fund, (3) special revenue funds, (4) capital projects funds and (5) permanent funds.

Governmental funds FFS are prepared on an accounting basis that is significantly different from that used to prepare GWFS. In general, governmental funds FFS focus on near-term inflows and outflows of expendable financial resources, consequently, they measure and account for cash and other assets that can easily be converted to cash. For example, amounts reported on the balance sheet include capital assets within a very short period of time, but do not include capital assets such as land and buildings. Governmental fund liabilities generally include amounts that normally are going to be paid within a short period after the end of the fiscal year. The difference between a fund's total assets and total liabilities is reported as the fund balance or deficit, and generally indicates the amount that can be used to finance the next fiscal year's activities. Likewise, the operating statement for governmental funds reports only those revenues and expenditures that were collected in cash or paid with cash, respectively, during the current fiscal year or very shortly after the end of the fiscal year.

Because the focus of governmental funds FFS is narrower than that of the GWFS, it is useful to compare the fund information presented for governmental funds with similar information presented for governmental activities in the GWFS. By doing so, readers may better understand the long-term impact of the Municipality's near-term financial decisions. Both the governmental funds' balance sheet and the governmental funds' statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate the comparison between governmental funds and the governmental activities reported in the government-wide financial statements.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

The Municipality has four major governmental funds. Each major fund is presented in a separate column in the balance sheet – governmental funds and the statement of revenues, expenditures and changes in fund balances – governmental funds. The five major governmental funds are: (1) general fund, (2) special revenue fund – federal grants, (3) special revenue fund – state and local grants, (4) capital project fund – state and local grants, and (5) debt service fund.

c) Notes to Basic Financial Statements

The NBFS provide additional information that is essential for a full understanding of the data provided in the GWFS and FFS. The NBFS can be found immediately following the basic financial statements.

d) Other Supplementary Information

The basic financial statements are followed by a section of other supplementary information consisting of budgetary comparison schedule – general fund.

This Space Has Been Intentionally Left Blank

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

FINANCIAL ANALYSIS OF GOVERNMENT-WIDE FINANCIAL STATEMENTS

The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Guayanilla, governmental activities assets exceeded total liabilities by \$5,949,967 at the end of 2012, as compared with \$5,880,289 at the end of the previous year. The following condensed Statement of Net Assets of the Primary Government shows on a comparative basis the most important components of the \$69,678 increase reflected in the governmental activities Net Assets figure.

	Governmental activities	
	June 30, 2012	June 30, 2011 (as restated)
<i>Assets:</i>		
Current assets	\$ 5,394,879	\$ 7,750,451
Non-current assets:		
Capital assets, net	27,713,674	26,786,517
Total assets	33,108,553	34,536,968
<i>Liabilities:</i>		
Current liabilities, excluding long-term obligations	2,922,298	3,170,903
Long-term obligations:		
Due within one year	1,046,485	1,331,697
Due after one year	23,189,803	24,154,079
Total liabilities	27,158,586	28,656,679
<i>Net assets (deficit):</i>		
Invested in capital assets, net of related debt	16,375,674	14,920,517
Restricted	4,665,309	7,388,399
Unrestricted	(15,091,016)	(16,428,627)
Total net assets	\$ 5,949,967	\$ 5,880,289

The Statement of Activities reflects that for fiscal year 2012, the net effect of total expenses over the revenues derived from several programs plus current operating revenues, amounted to an increase of \$69,678 in governmental activities. Approximately thirty four percent (34%) of the Municipality's governmental activities total revenue came from taxes, while fifty three percent (53%) resulted from grants and contributions, including federal aid. The Municipality's governmental activities expenses included items such as general government, urban and economic development, health and welfare, public safety, public works, culture, recreation and education, community development and interest on long term obligations.

This Space Has Been Intentionally Left Blank

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

Approximately nineteen percent (19%) of total expenses resulted from general government, six percent (6%) of total expenses resulted from community development, twenty three percent (23%) of total expenses resulted from health and welfare, seven percent (7%) of total expenses resulted from public safety, thirty three percent (33%) of total expenses resulted from public works, eight percent (8%) of total expenses resulted from culture, recreation and education, while four percent (4%) of total expenses resulted from interest on long term obligations. The following is a condensed presentation of the Municipality's results of operations as reported in the statement of activities for the fiscal years ended June 30, 2012 and 2011:

	Governmental activities	
	June 30, 2012	June 30, 2011 (as restated)
Program revenues:		
Program-specific operating grants and contributions	\$ 3,381,095	\$ 3,408,037
Program-specific capital grants and contributions	1,571,765	958,611
Charges for services	1,760,445	1,336,867
Total program revenues	<u>6,713,305</u>	<u>5,703,515</u>
General revenues:		
Property taxes	1,900,517	2,662,144
Municipal license taxes	2,580,888	1,446,099
Sales and use taxes	948,363	841,235
Construction excise taxes	302,776	1,016,941
Unrestricted grants and contributions	3,952,398	3,694,087
Other general revenues (various sources)	452,208	584,462
Total general revenues	<u>10,137,690</u>	<u>10,244,968</u>
Total revenues	<u>16,850,995</u>	<u>15,948,483</u>
Program expenses:		
General government	3,145,874	4,391,176
Health and welfare	3,811,724	3,877,414
Public works	5,575,965	5,902,827
Public safety	1,173,014	965,166
Culture, recreation and education	1,364,383	838,011
Community development	1,086,066	1,216,063
Interest on long-term obligations	624,291	613,113
Total expenses	<u>16,781,317</u>	<u>17,803,770</u>
Net increase (decrease) in net assets	69,678	(1,855,287)
Net assets, at beginning of fiscal year, as restated	<u>5,880,289</u>	<u>7,735,576</u>
Net assets, at end of fiscal year	<u>\$ 5,949,967</u>	<u>\$ 5,880,289</u>

This Space Has Been Intentionally Left Blank

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

FINANCIAL ANALYSIS OF GOVERNMENTAL ACTIVITIES

Analysis of Financial Position of Governmental Funds

As discussed earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of expendable resources. Such information is useful in assessing the Municipality's compliance with finance-related legal requirements. Specifically, unreserved fund balance may serve as a useful measure of the Municipality's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances amounting to \$1,842,441, which represents a decrease of \$2,102,107 when compared with the prior year. Out of the indicated balance, \$4,125,309 were restricted for the following purposes: 1) to liquidate accounts payable with suppliers (\$26,739); 2) to pay for capital projects (\$2,671,170); 3) for debt service payments (\$710,285); 4) to finance federal programs (\$212,256), and 5) to finance state and local grants (\$504,859). As of June 30, 2012, the General Fund, which is the main operating fund of the Municipality, reflected an unassigned fund deficit of \$2,282,868.

The following table presents the condensed financial position of governmental funds at June 30, 2012 and 2011:

	2012	2011 (as restated)
Assets:		
Total assets - major governmental funds	\$ 7,047,548	\$ 9,825,573
Combined total assets	7,047,548	9,825,573
Liabilities:		
Total liabilities - major governmental funds	5,205,107	5,881,025
Combined total liabilities	5,205,107	5,881,025
Fund balances (deficits):		
Restricted - major governmental funds	4,125,309	6,773,705
Committed - major governmental funds	-	36,607
Unassigned - major governmental funds	(2,282,868)	(2,865,764)
Combined total fund balances	1,842,441	3,944,548
Total liabilities and fund balances	\$ 7,047,548	\$ 9,825,573

This Space Has Been Intentionally Left Blank

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

Major Governmental Funds

General fund (GF) – The GF is the principal operating fund of the Municipality. The GF's total assets amounted to \$483,928 at June 30, 2012. Such assets consist principally of: restricted cash in fiscal agent (\$26,739), municipal license tax receivables (\$3,276), sales and use tax receivables (\$31,105), construction excise taxes (\$34,440), interest receivable (\$9,337), short-term amounts due from other funds (\$363,325) and other account receivables (\$15,706).

The GF's total liabilities amounted to \$2,740,057 at June 30, 2012. Such liabilities are composed mainly of: deferred revenues (\$825,300), amounts due to other governmental funds (\$1,050,545), and accounts payable and accrued liabilities, including amounts due to other governments (\$864,212).

At the end of the current fiscal year, restricted fund balance reached \$26,739, and unassigned fund deficit of the GF amounted to \$2,282,868, while total fund deficit reached \$2,256,129.

Special revenue fund – federal grants (SRF-FG)- The SRF-FG's total assets amounted to \$1,143,479 at June 30, 2012, which consist mainly of cash in commercial banks (\$527,193), receivables from intergovernmental grants and contributions (\$613,019) and other account receivables (\$3,267). The SRF-FG's total liabilities amounted to \$931,223 at June 30, 2012, which are composed mainly of accounts payable and accrued liabilities (\$491,468), short-term amounts due to other funds (\$278,884), and deferred revenue (\$160,871). At the end of the current fiscal year, restricted and total fund balance reached \$212,256.

Special revenue fund – state and local grants (SRF-S&LG)- The SRF-S&LG's total assets amounted to \$984,221 at June 30, 2012, which consist of cash in commercial banks (\$142,762), other accounts receivable for charge for services (\$262,131), amounts due from other funds (\$579,309), and due from governmental entities (\$19). The SRF-S&LG's total liabilities amounted to \$479,362 at June 30, 2012, which are composed mainly of accounts payable and accrued liabilities (\$84,198), and short-term amounts due to other funds (\$395,164). At the end of the current fiscal year, restricted and total fund balance reached \$504,859.

Capital project fund – state and local grants (CPF-S&LG)- The CPF-S&LG's total assets amounted to \$2,929,447 at June 30, 2012, which consist of cash in commercial banks (\$1,540), cash with fiscal agent (\$2,127,732), and due from other governmental funds (\$800,175). The CPF-S&LG's total liabilities amounted to \$258,277 at June 30, 2012, which are composed mainly of accounts payable and accrued liabilities (\$240,061), and short-term amounts due to other funds (\$18,216). At the end of the current fiscal year, restricted and total fund balance reached \$2,671,170.

Debt service fund (DSF)- The DSF's total assets amounted to \$1,506,473 at June 30, 2012, which consist of restricted cash in fiscal agent (\$1,438,829), property taxes receivables (\$10,013) and sales and use tax receivables (\$57,631). The DSF's total liabilities amounted to \$796,188 at June 30, 2012, which are mainly composed of: (1) matured bonds due and payable (\$540,000), and (2) matured interest due and payable (\$256,188). At the end of the current fiscal year, DSF's total and restricted fund balance reached \$710,285.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

Analysis of Operating Results of Governmental Funds

Major Governmental Funds

General fund– The total fund deficit of the GF decreased by \$506,950 during current fiscal year, principally due to the increase in the collections of municipal license tax revenue. Total revenues, expenditures and other financing sources (net) amounted to \$10,552,547, \$9,994,509, and \$51,088, respectively, for the fiscal year ended June 30, 2012.

Approximately 45% (\$4,730,149) of the GF's total revenues for the current fiscal year came from property, municipal license, construction excise and sales and use taxes, while 50% (\$5,281,211) resulted from intergovernmental grants and contributions. Interest revenues and miscellaneous revenues amounting to \$541,187, provided 5% of the total revenues for the current fiscal year.

The largest expenses of the GF for the fiscal year ended June 30, 2012 were related to: general administrative and operating costs (\$3,576,377), which were classified as "general government" and accounted for 36% of total expenses, health and welfare (\$564,883), which accounted for 6% percent of total expenses, public works (\$4,504,112), which accounted for 45% of total expenses, public safety (\$895,298), which accounted for 9% of total expenses, and culture, recreation and education (\$453,839), which accounted for 5% of total expenses.

Special revenue fund – federal grants (SRF-FG)- The total revenues of the SRF-FG for the current fiscal year amounted to \$2,941,086. Total expenditures amounted to \$3,060,900 for the fiscal year ended June 30, 2012.

SRF-FG's total expenditures for the current fiscal year came from health and welfare (\$942,134), public works (\$289,249), public safety (\$179,789), culture, recreation and education (\$305,468), and community development (\$1,344,260).

Special revenue fund – state and local grants (SRF-S&LG)- The total revenues of the SRF-S&LG for the current fiscal year amounted to \$2,228,947. Total expenditures amounted to \$2,634,098 for the fiscal year ended June 30, 2012.

SRF-S&LG's total expenditures for the current fiscal year came from health and welfare (\$2,414,986), public works (\$149,862), public safety (\$68,788), and community development (\$462).

Capital project fund – state and local grants (CPF-S&LG)- The total fund balance of the CPF-S&LG decreased by \$1,946,164 during current fiscal year. Total expenditures amounted to \$1,946,164 for the fiscal year ended June 30, 2012.

CPF-S&LG's total expenditures for the current fiscal year came principally from general government (1,268), health and welfare (\$45,354), public works (\$1,142,277) and culture, recreation and education (\$757,265).

Debt service fund (DSF) – The total fund balance of the DSF decreased by \$137,928 during current fiscal year. Total revenues, expenditures and other financing sources (net) amounted to \$1,038,275, \$1,227,291 and \$51,088, respectively, for the fiscal year ended June 30, 2012.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

Approximately 46% (\$476,988) of DSF's total revenues for the current fiscal year came from restricted property taxes, while 54% (\$560,410) came from restricted sales and use taxes. DSF's total expenditures for the current fiscal year came from principal and interests on bonds payable (\$1,227,291).

BUDGETARY HIGHLIGHTS

a) General Fund

The original and the final budget of the general fund for the fiscal year ended June 30, 2012 amounted to \$11,681,916. Over the course of the fiscal year, the Municipality revised the GF's budget in order to include increases and decreases in revenues that were identified during the course of the fiscal year based on current developments that positively affected the Municipality's finances. The laws and regulations of the Commonwealth mandate a balanced budget.

The total actual revenues (budgetary basis) of the general fund for the fiscal year ended June 30, 2012 were \$10,504,754, which is 10% (\$1,177,162) lower than the budgeted revenues. In addition, the total actual expenditures (budgetary basis) of the general fund for the fiscal year ended June 30, 2012 were \$11,858,049, which is 2% (\$249,433), greater than the budgeted expenditures.

The most significant fluctuations in actual revenues occurred in municipal license taxes and construction and excise taxes which had actual revenues that were \$1,173,970 and \$328,804 lesser than budgeted, respectively.

Also, the most significant fluctuations in actual expenditures and encumbrances occurred in general government and public safety, which had actual expenditures and encumbrances that were \$110,475 and \$104,594 greater than budgeted, respectively.

CAPITAL ASSETS AND DEBT ADMINISTRATION

a) Capital Assets

The Municipality has invested \$55,188,570 in capital assets used in governmental activities, which have an accumulated depreciation and amortization of \$27,474,896 at June 30, 2012. The net capital assets of governmental activities increased during the current fiscal year due to the current fiscal year's capital additions and reclassifications (\$4,852,753), which were partially offset by the depreciation expense and reclassifications (\$3,712,019) for the same period.

The capital additions made to capital assets during the fiscal year ended June 30, 2012 were the following:

Construction in progress	\$ 3,460,322
Buildings	1,183,729
Infrastructure	<u>208,702</u>
Capital additions for the fiscal year ended June 30, 2012	<u>\$ 4,852,753</u>

During the current year, construction in progress amounted to \$1,392,431 was reclassified to building, structures and improvements category.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

b) Debt Administration

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

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

The Municipality finances a significant portion of its construction activities through bond and note issuances, and through state and federal grants. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes.

At June 30, 2012, the Municipality's total bonded debt amounted to \$16,793,000, consisting of bonds payable. Such debt is backed by the full faith and credit of the Municipality. The following is a summary of the debt activity for the fiscal year ended June 30, 2012:

- Bonds payable decreased by 4% (\$698,000) by the effect of total principal payments on bonds made during the current fiscal year.
- The Municipality has also certain outstanding notes payable due to Puerto Rico Department of Treasury (\$1,955,452). Such notes payable decreased by \$130,000 during the current fiscal year mainly due to the principal payments made during the same period.
- The Municipality has also certain outstanding notes payable due to CRIM (\$3,219,888). Such notes payable decreased by \$403,149 during the current fiscal year mainly due to the principal payments made during the same period.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available, but the revenue can be also predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2012-2013.

FINAL COMMENTS

The Municipality of Guayanilla is an autonomous governmental entity whose powers and authority vested on its Executive and Legislative Branches are specifically established in the Municipal Autonomous Act approved in August 1991. By virtue of such powers, it provides a wide range of services to its constituents which includes, among others, public works, education, public safety, public housing, health, community, urban and economic development, recreation, waste disposal, welfare and others. The Municipality's principal sources of revenues are derived from property taxes, sales taxes, municipal license taxes, subsidies from the Commonwealth of Puerto Rico's General Fund and contributions from the Traditional and Electronic Lottery sponsored by said Government. Since the Municipality is significantly dependent on the intergovernmental grants and contributions received from the government of the Commonwealth of Puerto Rico and from property tax advances received from CRIM, the municipality could suffer a significant financial burden for certain scheduled intergovernmental revenues that could not be collected during the fiscal year 2012-2013.

REQUEST FOR INFORMATION

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer at P.O. Box 1875, Guayanilla, PR 00656, call (787) 835-2660, or visit our website at www.guayanillapr.net.

**Basic Financial Statements and
Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012**

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Statement of Net Assets

June 30, 2012

Assets

Current assets:

Cash in commercial banks	\$ 671,495
Cash in fiscal agent	3,593,300
Accounts receivable, net of allowance for doubtful accounts:	
Property taxes	10,013
Intergovernmental	613,038
Sales tax	88,736
Municipal license	3,276
Construction excise taxes	124,580
Interest	9,337
Miscellaneous	281,104
Total current assets	5,394,879

Noncurrent assets:

Capital assets, net of accumulated depreciation and amortization of \$27,474,896	27,713,674
Total noncurrent assets	27,713,674
Total assets	\$ 33,108,553

Current Liabilities (due within one year):

Accounts payable	\$ 1,195,403
Intergovernmental payables	484,536
Accrued interest payable on long-term debt	256,188
Deferred revenues	986,171
Current portion of long-term obligations:	
Bonds payable	654,000
Other debts	392,485
Total current liabilities	3,968,783

Noncurrent liabilities (due in more than one year):

	23,189,803
Total liabilities	\$ 27,158,586

Net assets (liabilities):

Invested in capital assets, net of related debt	\$ 16,375,674
Restricted for:	
Capital projects	2,671,170
Debt service	1,250,285
Other specified purposes	743,854
Unrestricted net assets	(15,091,016)
Total net assets	\$ 5,949,967

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Statement of Activities

Fiscal Year Ended June 30, 2012

<u>Functions/programs</u>	<u>Expenses</u>	<u>Charges for services</u>	<u>Program Revenues</u>		<u>Net Expenses and Charges in Net Assets</u>
			<u>Operating grants and contributions</u>	<u>Capital grants and contributions</u>	
Governmental activities :					
General government	\$ 3,145,874	\$ -	\$ -	\$ -	\$ (3,145,874)
Health and welfare	3,811,724	1,632,502	1,187,762	139,471	(851,989)
Public works	5,575,965	39,853	1,385,039	355,645	(3,795,428)
Public safety	1,173,014	30,929	220,292	-	(921,793)
Culture, recreation and education	1,364,383	57,161	320,390	-	(986,832)
Community Development	1,086,066	-	267,612	1,076,649	258,195
Interest on long-term obligation	624,291	-	-	-	(624,291)
Total governmental activities	<u>\$ 16,781,317</u>	<u>\$ 1,760,445</u>	<u>\$ 3,381,095</u>	<u>\$ 1,571,765</u>	<u>\$ (10,068,012)</u>
General Revenues:					
Taxes:					
					1,900,517
					2,580,888
					948,363
					302,776
					<u>5,732,544</u>
					3,952,938
					186,759
					265,449
					<u>10,137,690</u>
					69,678
					5,880,289
					<u>\$ 5,949,967</u>

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Balance Sheet – Governmental Funds
June 30, 2012

	MAJOR FUNDS					Total Governmental Funds
	General Fund	Special Revenue Fund - Federal	Special Revenue Fund - State &	Capital Project Fund - State & Local	Debt Service Fund	
ASSETS						
Cash in commercial banks	\$ -	\$ 527,193	\$ 142,762	\$ 1,540	\$ -	\$ 671,495
Cash in fiscal agent	26,739	-	-	2,127,732	1,438,829	3,593,300
Account receivable, net of doubtful accounts:						
Property taxes	-	-	-	-	10,013	10,013
Municipal license	3,276	-	-	-	-	3,276
Construction excise taxes	34,440	-	-	-	-	34,440
Sales tax	31,105	-	-	-	57,631	88,736
Interest	9,337	-	-	-	-	9,337
Other	15,706	3,267	262,131	-	-	281,104
Due from other funds	363,325	-	579,309	800,175	-	1,742,809
Due from governmental entities	-	613,019	19	-	-	613,038
Total assets	<u>\$ 483,928</u>	<u>\$ 1,143,479</u>	<u>\$ 984,221</u>	<u>\$ 2,929,447</u>	<u>\$ 1,506,473</u>	<u>\$ 7,047,548</u>
LIABILITIES						
Accounts payable	379,676	491,468	84,198	240,061	-	1,195,403
Intergovernmental	484,536	-	-	-	-	484,536
Due to other funds	1,050,545	278,884	395,164	18,216	-	1,742,809
Deferred revenue	825,300	160,871	-	-	-	986,171
Matured bonds due and payable	-	-	-	-	540,000	540,000
Matured interests due and payable	-	-	-	-	256,188	256,188
Total liabilities	<u>2,740,057</u>	<u>931,223</u>	<u>479,362</u>	<u>258,277</u>	<u>796,188</u>	<u>5,205,107</u>
FUND BALANCE						
Fund balance:						
Restricted	26,739	212,256	504,859	2,671,170	710,285	4,125,309
Committed	-	-	-	-	-	-
Unassigned	(2,282,868)	-	-	-	-	(2,282,868)
Total fund balances (deficit)	<u>(2,256,129)</u>	<u>212,256</u>	<u>504,859</u>	<u>2,671,170</u>	<u>710,285</u>	<u>1,842,441</u>
TOTAL LIABILITIES AND FUND BALANCE (DEFICIT)	<u>\$ 483,928</u>	<u>\$ 1,143,479</u>	<u>\$ 984,221</u>	<u>\$ 2,929,447</u>	<u>\$ 1,506,473</u>	<u>\$ 7,047,548</u>

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Statement of Revenues, Expenditures and Changes in Fund Balances (Deficits) – Governmental Funds
Fiscal Year Ended June 30, 2012

	MAJOR FUNDS					Total Governmental Funds
	General Fund	Special Revenue Fund - Federal Grants	Special Revenue Fund - State & Local Grants	Capital Project Fund - State & Local Grants	Debt Service Fund	
REVENUES						
Taxes:						
Property taxes	\$ 1,423,529	\$ -	\$ -	\$ -	\$ 476,988	\$ 1,900,517
Municipal license	2,580,888	-	-	-	-	2,580,888
Construction excise taxes	212,636	-	-	-	-	212,636
Sales tax	387,953	-	-	-	560,410	948,363
Charges of service	125,143	2,800	1,538,289	-	-	1,666,232
Intergovernmental grants and contributions:						
Federal government	-	2,933,929	-	-	-	2,933,929
State government	5,281,211	-	690,658	-	-	5,971,869
Investment earnings	185,882	-	-	-	877	186,759
Miscellaneous	355,305	4,357	-	-	-	359,662
Total Revenues	<u>\$ 10,552,547</u>	<u>\$ 2,941,086</u>	<u>\$ 2,228,947</u>	<u>\$ -</u>	<u>\$ 1,038,275</u>	<u>\$ 16,760,855</u>
EXPENDITURES						
Current:						
General government	3,576,377	-	-	1,268	-	3,577,645
Health and welfare	564,883	942,134	2,414,986	45,354	-	3,967,357
Public works	4,504,112	289,249	149,862	1,142,277	-	6,085,500
Public safety	895,298	179,789	68,788	-	-	1,143,875
Culture, recreation and education	453,839	305,468	-	757,265	-	1,516,572
Community Development	-	1,344,260	462	-	-	1,344,722
Debt service:						
Principal	-	-	-	-	603,000	603,000
Interest	-	-	-	-	624,291	624,291
Total Expenditures	<u>9,994,509</u>	<u>3,060,900</u>	<u>2,634,098</u>	<u>1,946,164</u>	<u>1,227,291</u>	<u>18,862,962</u>
Excess (Deficiency) of Revenues over expenditures	<u>558,038</u>	<u>(119,814)</u>	<u>(405,151)</u>	<u>(1,946,164)</u>	<u>(189,016)</u>	<u>(2,102,107)</u>
OTHER FINANCING SOURCES (USES)						
Transfer in from other funds	-	-	-	-	51,088	51,088
Transfer out to other funds	(51,088)	-	-	-	-	(51,088)
Total Other Financing Sources (uses)	<u>(51,088)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>51,088</u>	<u>-</u>
NET CHANGE IN FUND BALANCES (DEFICITS)	506,950	(119,814)	(405,151)	(1,946,164)	(137,928)	(2,102,107)
FUND BALANCE (DEFICIT) AT BEGINNING OF YEAR, AS RESTATED	<u>(2,763,079)</u>	<u>332,070</u>	<u>910,010</u>	<u>4,617,334</u>	<u>848,213</u>	<u>3,944,548</u>
FUND BALANCE (DEFICIT) AT END OF YEAR	<u>\$ (2,256,129)</u>	<u>\$ 212,256</u>	<u>\$ 504,859</u>	<u>\$ 2,671,170</u>	<u>\$ 710,285</u>	<u>\$ 1,842,441</u>

50,900

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**
Reconciliation of the Balance Sheet – Governmental Funds
to the Statement of Net Assets
June 30, 2012

Aggregate fund balance reported in the balance sheet - governmental funds	\$ 1,842,441
Governmental activities' amounts reported in the statement of net assets and the balance sheet - governmental funds are different because:	
Accounts receivables not collected 60 days after the closing date are not recognize in Governmental Funds, but these receivable are reported in the Governmental-Wide Statements of Activities and Changes in Net Assests.	90,140
Capital assets (net of accumulated depreciation) used in governmental activities are not financial resources, therefore, are not reported in the governmenal funds	27,713,674
The following liabilities are not due (mature) in the current period, therefore, are not reported in the governmental funds:	
Bonds payable	(16,253,000)
Note payable to Puerto Rico Treasury Department	(1,955,452)
Notes payable to Municipal Revenue Collection Center (CRIM)	(3,219,888)
Compensated absences	<u>(2,267,948)</u>
Net assets as reported in the accompanying statement of net assets	<u>\$ 5,949,967</u>

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Reconciliation of the Statement of Revenues, Expenditures and Changes in
Fund Balances (Deficits) – Governmental Funds and the Statement of Revenues, Expenses
and Changes in Fund Net Assets
Fiscal Year Ended June 30, 2012

Net change in fund balances- total governmental funds \$ (2,102,107)

Governmental activities amounts reported in the statement of activities and the statement of Revenues, expenditures and changes in fund balances governmental funds are different because:

Under the modified accrual basis of accounting used in the governmental funds, expenditures are not recognize for transactions that are not normally paid with expendable financial resources. In the Statements of Activities , however, wich is presented in the accrual basis, expenses and liabilities are presented regardless of when finacial resources are available:

Net change in compensated absences liability 10,478

Governmental funds report capital outlays as expenditures. However in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation and amortization expenses. This the amount by which capital outlays exceed depreciation expenses. 927,157

Accounts receivables not collected 60 days after the closing date are not recognize in Governmental Funds, but these receivables are reported n the Government-Wide Statements of Activities and Change in Net Assets. 90,140

Repayment of principal of long-term obligations is an expenditures in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets 1,144,010

Net changes in net assets reported in the accompayning statements of activities \$ 69,678

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

1. Summary of Significant Accounting Policies

The Municipality of Guayanilla, Commonwealth of Puerto Rico (the Municipality), is a local municipal government constituted in 1833 in the Commonwealth of Puerto Rico. The Municipality has full legislative, fiscal and all other governmental powers and responsibilities expressly assigned by Law 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 municipal governments legally separated from the state government of the Commonwealth of Puerto Rico (the Commonwealth).

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

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

a) Financial Reporting Model

The accompanying basic financial statements present the financial position of the governmental activities, each major governmental fund, and the aggregate remaining fund information of the Municipality as of June 30, 2012, in conformity with Accounting Principles Generally Accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). In addition, the accompanying basic financial statements present the changes in the financial position (results of operations) of the governmental activities, each major governmental fund, and the aggregate remaining fund information for the fiscal year ended June 30, 2012 in conformity with GAAP.

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

RSI consists of: (1) a Management's Discussion and Analysis (MD&A) and (2) a budgetary comparison schedule – general fund. RSI is unaudited supplementary information required by GAAP presented along with, but separate from, the Municipality's basic financial statements.

MD&A is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the fiscal year ended June 30, 2012, based on the Municipality's knowledge of the transactions, events and conditions

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

The *Budgetary Comparison Schedule – General Fund* is a comparison of the actual results (using the budgetary basis of accounting, which differs from GAAP) with the original budget and the final amended budget for the General Fund. A budget to GAAP reconciliation is presented providing information of differences between the budgetary basis of accounting and GAAP.

b) *Financial Reporting Entity*

The accompanying basic financial statements include all departments, agencies and municipal entities that: (1) are under the legal and administrative control of the Mayor, and (2) whose financial resources are under the legal custody and control of the Municipality's Director of Finance and Budget, as prescribed by Act No. 81.

The Municipality's management has considered all potential component units for which it may be financially accountable and other legally separate organizations for which the nature and significance of their relationship with the Municipality may be such that exclusion of their basic financial statements from those of the Municipality would cause the Municipality's basic financial statements to be misleading or incomplete.

Municipality's management has concluded that, bases on the criteria set forth by GASB Statement No. 14 – *The Financial Reporting Entity* (GASB No. 14) and GASB Statement No. 39 – *Determining Whether Certain Organizations are Component Units* (GASB No. 39), there are no legally separate entities or organizations that should be reported as component units of the Municipality as of June 30, 2012 nor for the year then ended.

c) *Government-Wide Financial Statements*

The accompanying GWFS are composed of: (1) the statement of net assets and (2) the statement of activities. These financial statements do not report fund information but rather report information of all governmental activities of the Municipality as a whole. These statements are aimed at presenting a broad overview of the Municipality's finances by reporting its financial position and results of operations using methods that are similar to those used by most private businesses.

The focus of GWFS is on the operational accountability of the Municipality as a single economic unit and not on compliance with budgets, regulatory requirements or on the use of available or currently expendable financial resources (referred to as fiscal accountability). Operational accountability is the Municipality's responsibility to report to the extent to which it has met its operating objectives efficiently and effectively, using all resources available for that purpose. It focuses on the Municipality's principal operating objective, which is to provide services to its citizens.

The accompanying statement of net assets provides short-term and long-term information about the Municipality's financial position by presenting all of the Municipality's assets and liabilities, with the difference between these two items reported as "net assets" (equity) and/or net liabilities (accumulated deficit). This statement assists management in assessing the level of services that can be provided by the Municipality in the future and its ability to meet its obligations as they

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

become due. In addition, this statement reports the extent to which the Municipality has invested in capital assets and discloses legal and contractual restrictions on resources.

Net assets (liabilities) are classified in the accompanying statement of net assets within the following three categories:

- **Invested in capital assets, net of related debt** – This net asset category consists of capital assets, net of accumulated depreciation and amortization, reduced by the outstanding balances of bonds payable, notes payable and other debts that are attributed to the acquisition, construction or improvement of those assets. For the purposes of determining the outstanding debt attributed to capital assets, the total long-term debt related to the acquisition, construction or improvement of capital assets has been reduced by any related unspent debt proceeds and any related unamortized debt issuance costs.
- **Restricted net assets** – This net asset category consists of net resources restricted by external parties (such as creditors, grantors, contributors, laws or regulations of other governments, etc.), or net assets for which constraints are imposed by constitutional provisions or enabling legislation. Enabling legislation consists of legislation that authorizes the Municipality to assess, levy, charge or otherwise mandate payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

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

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

- **Unrestricted net assets** – This category consists of net assets that are neither externally nor legally restricted, nor invested in capital assets. However, assets reported within unrestricted net liabilities often are designated to indicate that management does not consider them to be available for general operations. Assets reported within this category often have constraints that are imposed by management but can be removed or modified.

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

The accompanying statement of activities presents the Municipality's results of operations by showing, how the Municipality's net assets changed during the fiscal year ended June 30, 2012, using a net (expense) revenue format. This statement presents the cost of each function/program as well as the extent to which each of the Municipality's functions, programs or other services either contributes to or draws from the Municipality's general revenues (such as property taxes, municipal license taxes, construction excise taxes, etc.).

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

A function/program describes a group of activities that are aimed at accomplishing a major service or regulatory responsibility. The functions/programs reported in the accompanying basic financial statements are: (1) general government, (2) urban and economic development, (3) public safety, (4) public works, (5) culture, recreation and education, (6) health and welfare and (7) community development. The governmental operations of the Municipality's departments and operational units are classified within the following functions/programs in the accompanying basic financial statements:

General government:

- Municipal legislature
- Mayor's office
- Department of finance
- Department of human resources
- Department of municipal secretary
- Department of internal audit

Urban and economic development:

- Office of federal programs

Public safety:

- Department of emergency management – civil defense
- Department of municipal police

Public works:

- Department of public works
- Department of sanitation
- Department of recycling services
- Department of transportation

Culture, recreation and education:

- Department of sports and recreation

Health and welfare:

- Department of health
- Department of elderly affairs

Community Development:

- Office of federal programs

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

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

- **Charges for services** – These revenues generally consist of exchange or exchange-like transactions involving charges to customers or applicants who purchase, use or directly benefit from the goods, services or privileges provided, or are otherwise directly affected by the services. These revenues include fees charged for specific services, rent, charges for licenses and permits, and fines and forfeitures, among others.
- **Program-specific operating and capital grants and contributions** – These revenues consist of transactions that are either mandatory or voluntary non-exchange transactions with other governments, organizations, or individuals that restrict the resources for use in a particular program. Operating grants and contributions consist of resources that are required to be used to finance the costs of operating a specific program or can be used either for operating or capital purposes of a specific program. Capital grants and contributions consist of revenues or resources that are restricted for capital purposes – to purchase, construct or renovate capital assets associated with a specific program. Restricted operating and capital grants and contributions are program revenues because they are specifically attributable to a program and reduce the net expense of that program to the Municipality. They are reported net of estimated uncollectible amounts.

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

The *general government* function/program reported in the accompanying statement of activities includes expenses that are, in essence, indirect or costs of other functions/programs of the Municipality. Even though some of these costs have been charged to certain funds in the FFS as indirect cost allocations permitted under some federal programs, the Municipality has reported these indirect costs as direct expenses of the general government function. Accordingly, the Municipality generally does not allocate general government (indirect) costs to other functions.

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

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

The Municipality has no fiduciary activities, which are those in which the Municipality would be holding or managing net assets for specific individuals or other external parties in accordance with trust agreements or other custodial arrangements. In addition, the Municipality has no

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

operations or activities that are primarily financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public is financed primarily through user charges.

d) Governmental Fund Financial Statements

A fund is a fiscal and accounting entity consisting of a self-balancing set of accounts used to record assets, liabilities and residual equities, deficits or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with GAAP and/or special regulations, restrictions or limitations.

The accompanying GFFS are composed of: (1) the balance sheet – governmental funds, and (2) the statement of revenues, expenditures and changes in fund balances (deficits) – governmental funds.

These financial statements report the financial position and results operations of the Municipality's governmental funds and fund types by presenting sources, uses and balances of current and non-current financial resources. Some of these financial statements have a budgetary orientation and focus primarily on: (1) the Municipality's major governmental fund and fund types, as defined below, (2) the fiscal accountability and (3) the individual parts of the Municipality's government. Fiscal accountability represents the Municipality's responsibility to justify that its actions in the current fiscal year have complied with public decisions concerning the raising and spending of public moneys in the short term (generally one fiscal year).

The accompanying GFFS segregate governmental funds and fund types according to their intended purpose and are used in demonstrating compliance with legal, financial and contractual provisions. The minimum number of governmental funds and fund types is maintained consistent with legal and self-imposed managerial requirements established by the Municipality. For financial reporting purposes, the Municipality classifies its governmental funds within the following categories:

- **General fund** – The general fund is the Municipality's main operating fund and a major governmental fund, as defined below, used to account for all financial resources and governmental activities not accounted for and reported 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) GAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund.
- **Debt service fund** – The debt service fund is a major governmental fund, as defined below, used by the Municipality to account for all financial resources that are restricted, committed, or assigned to expenditure for 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/or (2) bonds payable or any general long-term debt for which the Municipality is being accumulating financial resources in advance to pay principal and interest payments maturing in future years. During the fiscal year ended June 30, 2012, the financial activity accounted for in the debt service fund was specifically related to bonds payable.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

The outstanding balance of general long-term obligations for which debt service payments do not involve the advance accumulation of resources (such as notes payable, obligations under capital leases, accrued compensated absences, and claims and judgments) are only accounted for in the accompanying statement of net assets. The debt service payments of such debts, as applicable, are generally accounted for in the general fund.

- ***Special revenue funds*** – The special revenue funds are major and non-major governmental funds, as defined below, used by the Municipality to account for the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service and capital projects. The uses and limitations of each special revenue fund are specified by municipal ordinances or federal and state statutes. However, resources restricted to expenditure for purposes normally financed from the general fund are reported in the Municipality's general fund provided that all applicable legal requirements are appropriately satisfied. In this case, a special revenue fund to account for such kind of transactions will be used only if legally mandated.
- ***Capital projects funds*** – Capital projects funds are major and non-major governmental funds, as defined below, used to account for all financial resources that are restricted, committed, or assigned to expenditure for capital outlays. Significant capital outlays financed from proceeds of general obligation, public improvement or special obligation bonds are accounted for also in the capital projects funds.

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

The focus of the GFFS is on major governmental funds and fund types, which generally represent the Municipality's most important funds. Accordingly, the Municipality is required to segregate governmental funds and fund types between major and non-major categories within the GFFS. Major individual governmental and proprietary funds and fund types are reported individually as separate columns in the GFFS, while data from all non-major governmental funds are aggregated into a single column, regardless of fund type.

By definition, the Municipality's general fund is always considered a major governmental fund for financial reporting purposes. In addition, any other governmental fund is classified as a major governmental fund in the GFFS if its total assets, liabilities, revenues or expenditures of that individual governmental fund are at least 10 percent of the corresponding element total (assets, liabilities, revenues or expenditures) for all governmental funds. For the purposes of applying the aforementioned major fund criteria, no eliminations of inter-fund balances have been made. Total revenues for these purposes means all revenues, including operating and non-operating revenues (net of allowances for uncollectible accounts), except for other financing sources. Total expenditures\expenses for these purposes mean all expenditures\expenses, including operating and non-operating expenditures\expenses, except for other financing uses.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

Based on the aforementioned criteria, the Municipality's major governmental funds reported in the accompanying FFS are: (1) the general fund, (2) the debt service fund, (3) the special revenue fund-federal grants, (4) the special revenue fund-state and local grants, and (5) the capital project fund-state and local grants.

The *general fund* is the accounting entity used to account for all financial resources and governmental activities not accounted for and reported in another fund. Its revenues consist mainly of taxes, licenses and permits, intergovernmental revenue, charges for services and others.

The *special revenue fund – federal grants* is the accounting entity in which revenues derived from federal grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

The *special revenue fund – state and local grants* is the accounting entity in which revenues derived from state and local grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or state statutes.

The *capital project fund – state and local grants* is the accounting entity in which revenues derived from local funds and state grants or other restricted revenue sources related to capital projects, is accounted for. The uses and limitations of each capital project fund are specified by Municipality ordinances or state statutes.

The *debt service fund* is the accounting entity in which revenues derived from property and sales taxes are accumulated for the payment of, general long-term debt principal, interest, and related costs.

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

e) Measurement Focus and Basis of Accounting

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

All revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are generally recorded when the exchange takes place. In exchange transactions, each party to the transaction receives and gives up essentially equal values.

An exchange-like transaction is one in which there is an identifiable exchange and the values exchanged, though related, may not be quite equal. Nevertheless, the exchange characteristics of the exchange-like transaction are strong enough to justify treating it as an exchange for accounting purposes (examples include certain charges for services and miscellaneous revenues, which are recorded as revenues when collected because they are generally not measurable until actually received).

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

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

In the case of *derived tax revenue transactions* (such as municipal license taxes), which result from assessments the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred.

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

Government-mandated non-exchange transactions (such as grants and contributions) result when a government at one level (such as the federal or state government) provides resources to another government (such as the Municipality), and the provider government requires the recipient government to use those resources for a specific purpose or purposes established in the provider's enabling legislation. In these types of transactions, receivables and revenues are generally recorded as follows:

- For reimbursement-type (commonly known as "expenditure-driven awards"), receivables and revenues are recorded when all eligibility requirements imposed by the provider have been met. The Municipality must expend resources on the specific purpose or project before the provider reimburses any amounts. Revenue is, therefore, generally recognized as qualifying reimbursable expenditures are incurred.
- For other types of grants (mainly grants and contributions with purpose restrictions but with no time requirements), receivables and revenues are recorded when all applicable eligibility requirements are met. When the provider is a government (including the government of the United States of America) the applicable recognition period for both, the provider and the recipient, is the provider's fiscal year and begins on the first day of that year.

Voluntary non-exchange transactions (such as donations and certain grants and entitlements) result from legislative or contractual agreements, other than exchanges, willingly entered into by two or more parties. In these types of transactions, receivables and revenues are generally

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

accounted for in the same manner as government-mandated non-exchange transactions discussed above. Events that are neither exchange nor non-exchange transactions are recorded when it is probable that a loss has been incurred and the amount of loss is reasonably estimable.

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

Events that are neither exchange nor non-exchange transactions are recorded when it is probable that a loss has been incurred and the amount of loss is reasonably estimable.

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

Governmental fund financial statements – The accompanying governmental fund financial statements are reported using the current financial resources measurement focus (flow of current financial resources) and the modified accrual basis of accounting. Accordingly, the accompanying statement of revenues, expenditures and changes in fund balances (deficits) – governmental funds, reports changes in the amount of financial resources available in the near future as a result of transactions and events of the fiscal year reported. Therefore, revenues are generally recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current fiscal year or soon enough thereafter to pay liabilities of the current fiscal year. For this purpose, the Municipality considers most revenues to be available if collected generally within 90 days after June 30, 2012, except for property taxes for which the availability period is 60 days. Revenue sources not meeting this availability criterion or collected in advance are recorded as deferred (earned and unavailable) revenues at June 30, 2012.

The principal revenue sources considered susceptible to accrual include property taxes, municipal license taxes, sales and use taxes, construction excise taxes, intergovernmental grants and contributions, interest on deposits and charges for services. These principal revenue sources meet both measurability and availability criteria in the accompanying governmental fund financial statements, except for amounts recorded as deferred (earned and unavailable) revenues.

In a manner similar to the GWFS, but subject to and limited by the availability criteria discussed previously, all revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are also generally recorded when the exchange takes place. Accordingly, certain charges for services and miscellaneous revenues are recorded as revenues when collected because they are generally not measurable until actually received.

All revenues, expenses, gains, losses and assets resulting from non-exchange transactions are recorded in a similar manner to the GWFS, using the previously discussed criteria set forth by GASB No. 33 for non-exchange transactions, but subject to and limited by the availability criteria discussed above. Accordingly, property tax and municipal license tax receivables are also

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

generally recorded in the fiscal year when an enforceable legal claim has arisen while property tax and municipal license tax revenues (net of amounts considered not collectible) are also generally recorded in the fiscal year when resources are required to be used or the first fiscal year that the use of the resources is permitted. Receivables and revenues from federal and state grants and contributions, donations and entitlements are also generally recorded when all eligibility requirements imposed by the provider have been met (generally, as qualifying reimbursable expenditures are incurred for expenditure-driven grants).

Interest on deposits is recorded when earned only if collected within 90 days after the fiscal year-end since these revenues would be considered both measurable and available.

Pursuant to the provisions of GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements* (GASBI No. 6), in the absence of an explicit requirement (i.e., the absence of an applicable modification, discussed below) the Municipality generally accrues a governmental fund liability and an expenditure (including salaries, professional services, supplies, utilities, etc.) in the period in which the government incurs the liability, to the extent that these liabilities are normally expected to be liquidated with current available financial resources. GASBI No. 6 modified the recognition criteria for certain expenditures and liabilities reported under the modified accrual basis of accounting prior to GASB No. 34, and clarified a number of situations in which the Municipality should distinguish between governmental fund liabilities and general long-term liabilities. Therefore, the accompanying balance sheet – governmental funds generally reflects assets that will be converted into cash to satisfy current liabilities. Long-term assets (except for accounts receivables and inter-fund advances) and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying balance sheet – governmental funds. At the same time, long-term liabilities (generally, those unmatured that will not require the use of current financial resources to pay them) are not accounted for in the accompanying balance sheet – governmental funds.

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

- Principal and interest on bonds payable are recorded when they mature (when payment is due), except for principal and interest due on July 1, 2012, which have been recorded as governmental fund liabilities at June 30, 2012, which is the date when resources are available in the debt service fund (generally, June 30).
- Notes payable, obligations under capital leases, compensated absences, and amounts subject to accrued claims and judgments under litigation are recorded only when they mature (when payment is due).
- Certain accrued liabilities not due and payable or not normally expected to be liquidated with current available and expendable financial resources are recorded in the accompanying statement of net assets. Such liabilities are recorded in the governmental funds when they mature.
- Executory purchase orders and contracts are recorded as assignments of fund balance in the governmental funds FFS.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

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

f) Stewardship, Compliance and Accountability

Budgetary Control

According to Law No. 81, the Mayor and its Administrative Cabinet prepare annual budgets each fiscal year for the Municipality's general fund and debt service fund. Such legally adopted budgets are based on expected expenditures by program and estimated resources by source. The annual budgets are developed using elements of performance-based program budgeting and zero-based budgeting, and include estimates of revenues and other resources for the ensuing fiscal year under laws and regulations existing at the time the budgets are prepared.

The Mayor must submit, for each fiscal year commencing on July 1, an annual budgetary resolution project (the Project) to the Commissioner of Municipal Affairs of the Commonwealth (the Commissioner) and the Municipal Legislature no later than the immediately preceding May 31. The Commissioner preliminarily verifies that the Project complies with all the applicable laws and regulations and may provide comments and suggestions to the Mayor on or before the immediately preceding June 15.

The Municipal Legislature has 10 business days, up to the immediately preceding June 13, to discuss and approve the Project with modifications. The Municipal Legislature may amend the budgets submitted by the Mayor but may not increase any items so far to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. After the Municipal Legislature modifies and preliminarily approves the Project, the modified Project is sent back to the Mayor for his approval or rejection within six (6) days. The Mayor may decrease or eliminate any line item but may not increase or insert any new line item in the budgets. The Mayor may also veto the budgets in their entirety and return it to the Municipal Legislature with his objections. If the Mayor rejects the Project, the Municipal Legislature will have up to eight (8) days to adopt or reject the recommendations or objections of the Mayor. The approved Project is sent again to the Mayor, which then would have three (3) days to sign and approve it.

If the budgets are not adopted prior to the end of the deadlines referred to above, the annual budgets for the preceding fiscal year, as approved by the Legislature and the Mayor, are automatically renewed for the ensuing fiscal year until the Municipal Legislature and the Mayor approve new budgets. This regulation permits the Municipality to continue doing payments for its operations and other purposes until the new budgets are approved.

The annual budgets may be updated for any estimate revisions as well as fiscal year-end encumbrances, and may include any additional information requested by the Municipal Legislature. The Mayor may request subsequent amendments to the approved budgets, which are subject to the approval of the Municipal Legislature.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

The Municipality's Department of Finance has the responsibility to ensure that budgetary spending control is maintained. For day-to-day management control purposes, expenditures plus encumbrances may not exceed budgeted amounts at the expenditure-type level of each cost center (activity within a program within a fund). The Mayor may transfer unencumbered appropriations within programs within funds. The Municipal Legislature may transfer amounts among programs within and among funds.

The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriation) is at the function/program level (general government, urban and economic development, public safety, health and sanitation, culture, recreation and education, and public housing and welfare) within a fund.

Under the laws and regulations of the Commonwealth, the appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided.

Budgetary Accounting

The Municipality's annual budgets are prepared using the budgetary (statutory) basis of accounting, which is not in accordance with GAAP.

According to the budgetary basis of accounting, revenue is generally recorded when cash is received. Short-term and long-term borrowings may be used to finance budgetary excess of expenditures over revenues.

The Municipality uses encumbrance accounting to record the full amount of purchase orders, contracts and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control. Accordingly, expenditures are generally recorded when the related expenditure is incurred or encumbered. Available appropriations and encumbrances are established to lapse one fiscal year after the end of the fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment. Unencumbered appropriations and encumbrances lapse at fiscal year-end. Other appropriations, mainly capital projects appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

The accompanying budgetary comparison schedule provides information about the general fund's original budget, the amendments made to such budget, and the actual general fund's results of operations under the budgetary basis of accounting for the fiscal year ended June 30, 2012. Further details of the Municipality's budgetary control at the legal level may be obtained from the Budgetary Liquidation Report for the fiscal year ended June 30, 2012. Copies of that report may be obtained by writing to the Municipality's Director of Finance and Budget.

Because accounting principles applied for the purposes of the developing data on a budgetary basis differ significantly from those used to present the governmental fund financial statements in conformity with GAAP, a reconciliation of the differences between the general and debt service

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

funds' budgetary bases and GAAP actual amounts are presented at the bottom of the respective budgetary comparison schedules.

The Municipality does not legally adopt budgets for the special revenue fund – federal grants and special revenue fund – state and local grants. The financial resources received by these funds are not subject to budgeting by the Municipality since the resources received each year from the respective grantors varies from year to year, and the respective amounts are granted at their discretion.

g) *Unrestricted and Restricted Deposits*

The Municipality's deposits are composed of: (1) cash on hand, (2) demand deposits in commercial banks, (3) demand deposits in the Government Development Bank for Puerto Rico (fiscal agent) and (4) cash equivalents in commercial banks.

The Municipality follows the practice of pooling cash. The balance in the pooled cash account is available to meet current operating requirements and any unrestricted excess, if any, is invested in certificates of deposit with commercial banks. Any deficiency in the pooled cash account is assumed by the general fund and covered through future budgetary appropriations.

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

Cash in commercial banks of the special revenue fund – federal grants, represents the balance of interest bearing and non-interest bearing accounts restricted to finance the operations of certain federal financially assisted programs.

Cash in commercial banks and cash in fiscal agent of the special revenue fund – state and local grants, represents the balance of interest bearing and non-interest bearing accounts restricted to finance the operations of certain state and local financially assisted programs.

Cash in commercial bank and cash in fiscal agent in the capital project fund – state and local grants, consists principally of the balance of interest bearing and non-interest bearing accounts related to state and local grants, and unspent proceeds of bonds, which are restricted for the acquisition, construction or improvement of major capital assets.

Cash in fiscal agent in the debt service fund consists of cash related to property tax and sales and use tax collections, which are restricted for the payment of the Municipality's debt service of bonds payable, as required by law.

h) *Unrestricted and Restricted Accounts and Notes Receivable*

In the accompanying GWFS, receivables consist of all revenues earned but not collected at June 30, 2012. Major receivable balances for the governmental activities include property taxes municipal license and intergovernmental receivables.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

Tax receivables in the general fund represent uncollected property taxes. Restricted tax receivables in the debt service fund consist of uncollected property taxes, which are restricted for the payment of the Municipality's debt service, as established by law.

Intergovernmental receivables are composed of: (1) amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federal and state funded programs (recorded in the general fund, special revenue funds and capital project funds), and (2) contributions in lieu of taxes from the Puerto Rico Electric Power Authority, recorded in the general fund.

These accounts receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience, historical trends, current economic conditions and the periodic aging of accounts receivable.

Activities among funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e. the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds". Advances between funds, as reported in the GFFS, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

i) Other Current Assets

Other current assets in the accompanying statement of net assets and the balance sheet – governmental funds consist principally of prepaid costs, which are capitalized rather than charged to operations.

j) Capital Assets

Capital assets used in governmental activities include land and land improvements, buildings, structures and building improvements, machinery and equipment (including equipment held under capital leases), furniture and fixtures, licensed vehicles, construction in progress, and infrastructure. These assets are capitalized and reported in the accompanying statement of net assets and the statement of net assets – proprietary fund. Infrastructure assets are generally stationary in nature and include roads, bridges, streets and sidewalks, drainage systems and other similar assets.

For financial reporting purposes, the Municipality defines capital assets as assets with an individual cost basis of \$100 or more at the date of acquisition, construction or improvement, and with useful lives extending beyond one year. All assets with individual costs under \$100 or with useful lives not exceeding one year, are charged directly to expense in the government-wide statement of activities and the statement of revenues, expenses and changes in fund net assets. In the governmental funds, all capital assets are recorded as expenditures in the corresponding function/program identified with the asset.

In the statement of net assets and the statement of net assets, all capital assets are recorded at cost or estimated historical cost if actual cost was unavailable, except for donated capital assets, which

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

are recorded at their estimated fair value at the date of donation. Estimated historical costs based on deflated current costs were used to value a portion of the infrastructure constructed or acquired prior to June 30, 2003 and certain lands, buildings, structures and building improvements. The method used to deflate the current costs with an approximate price index was used only in the case of certain items for which the historical cost documentation was not available. Actual historical costs were used to value the infrastructure acquired or constructed after June 30, 2003 as well as, construction in progress, machinery and equipment and licensed vehicles acquired prior or after such date.

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

Depreciation and amortization expense is recorded only in the government-wide statement of activities. However, there is no depreciation or amortization recorded for land and construction in progress. Depreciable capital assets are generally depreciated or amortized over their estimated useful lives under the straight-line method, except for machinery and equipment held under capital leases which is depreciated over the shorter of its estimated useful life or the lease term. The estimated useful lives of major capital asset categories are:

	<u>Years</u>
Building and site improvements	40
Infrastructure	40
Work of art	10
Vehicles	5
Furniture and fixtures	5
Machinery and equipment	3 to 5

Depreciation and amortization expense of capital assets is recorded as a direct expense of the function/program specifically identified with the asset. Depreciation and amortization of infrastructure is not allocated to various functions/programs but reported as direct expenses of the urban and economic development function.

k) Deferred Revenues

In the governmental fund financial statements, deferred revenue arises when one of the following situations occur:

- Potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period (reported as “*earned and unavailable revenue*” in the accompanying balance sheet-governmental funds). As previously discussed, available is defined as due (or past due) at June 30, 2012 and collected within 90 days (60 days for property taxes) thereafter to pay obligations due at June 30. In subsequent periods, when both criteria (measurable and available) are met, the liability for deferred revenue is removed and revenue is recognized.
- The Municipality receives resources before it has a legal claim to them (reported as “*unearned revenue*” in the accompanying balance sheet-governmental funds). In subsequent

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

periods, when the revenue recognition criterion is met, the liability for deferred revenue is removed and revenue is recognized.

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

l) Compensated Absences

The liability for compensated absences recorded in the accompanying statement of net assets is limited to leave that: (1) is attributable to services already rendered on or before June 30, 2012 and (2) is not contingent on a specific event that is outside the control of the Municipality and the employee (such as illness). Compensated absences that relate to future services or are contingent on a specific event outside the control of the employer or the employee are accounted for in the period when those services are rendered or those events take place.

The liability for compensated absences includes salary-related costs, which are directly and incrementally related to the amount of salary paid to the employee (such as employer's share of social security taxes and medicare taxes).

The vacation policy of the Municipality provides for the accumulation of regular vacations at a rate of 2.5 days per month (30 days per fiscal year) per employee. Employees accumulate regular sick leave at a rate of 1.5 days per month (18 days per fiscal year). Employees accumulate compensatory time at a rate of 1.5 times the overtime worked. All vacation and sick leave days accumulated by employees in excess of 30 days and 90 days, respectively, are paid to employees each fiscal year, if not consumed, as required by law. In the case of compensatory time, the excess of 240 hours is paid to employees each fiscal year, if not consumed.

Upon termination of employment, an employee receives compensation for all accumulated unpaid regular vacation leave at the current rate. In the case of regular sick leave, if the employee terminates his or her employment before reaching 10 years of services, such regular sick leave is not paid to the employee, if not consumed. In addition upon termination of employment, an employee does not receive compensation for compensatory time, if not consumed previously. After 10 years of services, any regular sick leave balance is paid to the employee. Accumulated vacation time is fully vested to the employee at any time.

The liability for compensated absences is in the statement of net assets. A liability for compensated absences is reported in the governmental fund financial statements only when matured (when payment is due), for example, as a result of employee resignations or retirements.

m) Long-term Debt

The long-term liabilities reported in the accompanying statements of net assets include the Municipality's bonds payable, notes payable, obligations under capital leases, accrued compensated absences and accrued legal claims and judgments.

All long-term debt to be repaid from governmental resources is reported as liabilities in the accompanying statement of net assets. Principal and interest payments on bonds due in July 1 of the following fiscal year are recorded as fund liabilities in the GFFS when resources are available

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

in the debt service fund (generally at June 30). In the GFFS, the face amount of debt issued is reported as other financing sources when issued.

n) Accounting for Pension Costs

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

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

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

o) Risk Management

The Municipality carries commercial insurance covering casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Commonwealth's Department of Treasury (the Department of Treasury) on behalf of all municipalities of Puerto Rico. The Department of Treasury pays the insurance premiums on behalf of the Municipality and then is reimbursed each fiscal year through monthly equal payments deducted from the Municipality's gross property tax collections made by the Municipal Revenue Collection Center ("CRIM", by its Spanish acronym), a governmental entity responsible for billing and collecting property taxes on behalf of all municipalities of Puerto Rico.

The Municipality carries insurance coverage for death and bodily injuries caused by automobile accidents. This insurance is obtained through the Automobile Accidents Compensation Administration (ACAA, by its Spanish acronym), a component unit of the Commonwealth. This insurance is compulsory for all licensed vehicles used on public roads and highways in Puerto Rico. The annual premium applicable at June 30, 2012 is \$35 per licensed motor vehicle, which is paid directly to ACAA.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

The Municipality obtains workers' compensation insurance coverage through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth. 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. Workers' compensation insurance premiums are also paid through monthly deductions made by CRIM from the Municipality's gross property tax collections.

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

The Municipality also obtains medical insurance coverage from a health insurance company for its employees. Different health insurance coverage and premium options are negotiated each year by the Municipality. The current insurance policies have not been cancelled or terminated at June 30, 2012. Premiums are paid on a monthly basis directly to the insurance company. In the past three years, the Municipality has not settled claims that exceeded insurance coverage.

p) Fund Balances

On July 1, 2010, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions No. 54* (GASB No. 54). GASB No. 54, which enhanced the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied. Also, this statement establishes fund balance classifications that comprise a hierarchy upon use of the resources reported in governmental funds.

Pursuant to the provisions of GASB No. 54, the accompanying GFFS report fund balance amounts that are considered restricted, committed, assigned, and unassigned, based on the relative strength of constraints that control how specific amounts can be spent. The Municipality has recorded the following types of fund balance classifications in the governmental funds:

- **Restricted** – Represent resources that can be spent only for the specific purposes stipulated by constitutional provisions, external resource providers (externally imposed by creditor or grantors), or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
- **Committed** – Represent resources used for specific purposes, imposed by formal action of the Municipal's highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by a similar law, ordinance or resolution, no later than the end of fiscal year.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

- **Assigned** – Represent resources intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed (generally executive orders approved by the Mayor). Intent can be expressed by the Municipal Legislature, the Mayor or by an official or body to which the Municipal Legislature delegates authority in conformity with the Law No. 81 of August 30, 1991, as amended, known as *Autonomous Municipalities Act of the Commonwealth of Puerto Rico* (Act No. 81). In governmental funds other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed.
- **Unassigned** – Represent the residual classification for the Municipality’s general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

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

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely. However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balance amounts as of and for the fiscal year ended June 30, 2012.

When an expenditure is incurred for purposes for which amounts are available in multiple fund balance classifications, the Municipality uses restricted resources first, and then unrestricted resources. Within unrestricted resources, the Municipality generally spends committed resources first, followed by assigned resources, and then unassigned resources.

q) Inter-fund Activities

The Municipality has the following types of reciprocal and non-reciprocal inter-fund activities recorded among governmental funds in the accompanying GFFS:

- **Inter-fund loans** – Represent resources (assets) provided by one governmental fund to other governmental fund with a requirement and commitment for repayment (reimbursement), which are recorded as “*due from*” in the lender governmental fund and “*due to*” in the borrower governmental fund. For amounts not expected to be collected, inter-fund receivables/payables are reduced to their estimated realizable (settlement) value, and the portion of the inter-fund loan that is not expected to be repaid is reported as a “*transfer-in*” from the governmental fund that provided the loan.
- **Inter-fund transfers (transfers-in/(out))** – Represent flows of assets (permanent reallocation of financial resources among governmental funds) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported as “*other financing uses*” in the governmental fund making transfers and as “*other financing sources*” in the governmental fund receiving transfers.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

- **Inter-fund reimbursements** – Represent repayments (reimbursements) from the governmental fund responsible for particular expenditures or expenses to the governmental fund that initially paid for them.

In the GFFS, inter-fund activity has not been eliminated, as permitted by GAAP.

r) Use of Estimates

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

s) Future Adoption of Accounting Pronouncements

The GASB has issued the following standards that have effective dates after June 30, 2012:

- GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements* (GASB No. 60). The objective of this Statement is to improve financial reporting by addressing issues related to service concession arrangements (SCAs), which are a type of public-private or public-public partnership. This Statement is effective for periods beginning after December 15, 2011.
- GASB Statement No. 61, *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34* (GASB No. 61). The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. The requirements of Statement No. 14, *The Financial Reporting Entity*, and the related financial reporting requirements of Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, were amended to better meet user needs and to address reporting entity issues that have arisen since the issuance of those Statements. This Statement is effective for periods beginning after June 15, 2012.
- GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and IACPA Pronouncements*. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements; 1) Financial Accounting Standard Board (FASB) Statements and interpretations, 2) Accounting Principles Board Opinions, 3) Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. This Statement is effective for periods beginning after December 15, 2011.
- GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

financial position. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2011.

- GASB Statement No. 65, *Previously Reported as Assets and Liabilities*
The objective of this Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012.
- GASB Statement No. 66, *Technical Corrections-2012-an amendment of GASB Statements No. 10 and No. 62 (Issued 03/12)*. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012.
- GASB Statement No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25 (Issued 06/12)*. The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. This Statement replaces the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures*, as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements 25 and 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement and to defined contribution plans that provide postemployment benefits other than pensions.
- GASB Statement No. 68 *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27 (Issued 06/12)*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. This Statement is effective for fiscal years beginning after June 15, 2014.
- GASB Statement No. 69 *Government Combinations and Disposals of Government Operations (Issued 01/13)* This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term government combinations include a variety of transactions referred to as

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

mergers, acquisitions, and transfers of operations. The requirements of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis.

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

2. Deposits

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

On July 1, 2004, 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 credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly, the Municipality is only allowed to invest its obligations of the Commonwealth, obligations of the United States of America, certificates of deposit, 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 is not allowed to invest in marketable securities or any other type of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the credit risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2012.
- **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 investments portfolio at June 30, 2012, (2) limiting the weighted average maturity of its investments to periods of three months or less and (3) keeping most of its banks deposits in interest bearing accounts generating interest at prevailing market rates. At June 30, 2012, the interest rate risk associated with the Municipality's cash and cash equivalent is considered low.
- **Custodial credit risk** – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*, the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC), generally up to a maximum of \$250,000 per depositor. In addition, public funds deposited in commercial banks by the Municipality are fully collateralized for the amounts deposited in excess of the federal depository insurance. All

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

securities pledged as collateral are held in the Municipality's name by the agents of the Commonwealth's Secretary of Treasury. Deposits of GDB, amounting to \$3,593,300 at June 30, 2012, are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2012. It is management's policy to only maintain deposits in banks affiliated to FDIC to minimize the custodial credit risk, except for GDB. Therefore, the Municipality's management has concluded that at June 30, 2012, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

- **Foreign exchange risk** – This is the risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, adopted by the Municipality, the Municipality is prevented from investing in foreign securities or any other types of investments for 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, 2012.

Cash and cash equivalents at June 30, 2012, are classified in the accompanying balance sheet – governmental funds a follows:

	General fund	Special revenue fund – federal grants	Special revenue fund – state & local grants	Capital project fund – State & local grants	Debt service fund	Total
Cash in commercial banks	\$ -	527,193	142,762	1,540	-	\$671,495
Cash in GDB, as fiscal agent	26,739	-	-	2,127,732	1,438,829	3,593,300
Total carrying amount of deposits	\$ 26,739	527,193	142,762	2,129,272	1,438,829	\$4,264,795

3. Municipal License Taxes

The Municipality is authorized by Law No. 81 to impose and collect municipal license taxes to any natural or legal person having trade or business activities within the territory of Guayanilla. This is a self-assessed tax generally based on the business volume of taxpayers, measured by gross revenues. The Municipality establishes the applicable tax rates. At June 30, 2012, the municipal license tax rates imposed by the Municipality were 1.50 percent for financial institutions and 0.50 percent for other types of taxpayers. Any taxpayers that have been granted with a partial tax exemption under any of the tax incentive acts of the Commonwealth ultimately pay municipal license taxes at reduced tax rates, generally between 60 percent and 90 percent under standard rates.

Each taxpayer must assess the corresponding municipal license tax by declaring the volume of business through a tax return to be filed and due five (5) working days after April 15 of each year, based on the actual volume of business (revenues) generated in the preceding calendar year. Taxpayers with a sales volume of \$3 million or more must include audited financial statements with their tax return filings. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration before the due date ended five (5) working days after April 15 of each year. The first installment of the tax covers the six-month period ended December 31, subsequent to the filing date of the declaration, while the second installment of the tax covers the six-month period ended June 30 of the subsequent calendar year. If a taxpayer elects to

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

pay the tax in full on the filing date of the declaration (five (5) working days after April 15), a 5 percent discount is granted automatically on the total tax amount due.

Total municipal license tax receivable, amounted to \$3,276 at June 30, 2012.

Any municipal license taxes collected in advance (that is, pertaining to a future fiscal year) are recorded as deferred revenues in the GWFS and the general fund. Unearned municipal license tax revenues recorded in the accompanying GWFS and the general fund amounted to \$825,300 at June 30, 2012. Those unearned municipal license revenues collected in advance pertain to the general fund's operating budget of the fiscal year 2012-2013, therefore, generally cannot be used to pay obligations of the fiscal year 2011-2012.

The unearned municipal license, recorded in the general fund at June 30, 2012, include municipal license tax revenues of the fiscal year 2012-2013 amounting to \$825,300, which were collected in advance from taxpayers between January and June, 2012 (known in Spanish as "Patente en Suspense").

4. Sales and Use Taxes

The Municipality is authorized by Law No. 117 of July 4, 2006, as amended by Law No. 80 of July 29, 2007, to impose and collect sales and uses taxes of one point five (1.5) percent to substantially all products and services sold or provided within the territorial limits of the Municipality. The mentioned Laws establish the applicable tax rate.

At June 30, 2012, the municipal sales and uses tax rate imposed by the Municipality was 1.50, from which the Municipality collect one (1) percent, and the Puerto Rico Secretary of the Treasury collect the remaining point five (.5) percent without including food and food ingredients as defined in Section 2301(a) of the Act No. 107, on behalf of the Municipality.

The point five (.5) percent collected by the Puerto Rico Treasury Department and belonging to the Municipality it is distributed through three separate funds: municipal development fund (up to .2%, at the discretion of the Municipality), municipal redemption fund (from .2% to .4%, at the discretion of the Municipality) and municipal improvements fund (.1%). The Municipality has elected to restrict a portion of the sales tax amounting .4% for the payment of long-term debt and is recorded in the debt service fund. The remaining portion is recorded in the general fund since is available for general operating purposes.

The tax collected by merchants during a given month is due and must be paid accompanied by a sales and use tax return to the Municipality and to the Puerto Rico Treasury Department on or before the 10th day of the following month.

The resources collected by the Municipality due to this tax assessment will be used in local activities like improvements in health services, improvements in the control and management of solid waste disposal and recycling programs, public improvements, improvements of public safety, and maintenance of all public facilities of the Municipality.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

The sales and use tax receivable is recognized as revenue when it becomes measurable and available base on actual collection during the 30 days following the fiscal year-end related to sales and use tax returns due before year end.

Sales and use tax receivable in the general and debt service funds at June 30, 2012, of \$31,105 and \$57,631, respectively, represent actual collection during the 30 days following the fiscal year-end related to sales and use tax returns due before year end.

5. Property Taxes

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

On July 10, 2009, the Legislature of the Commonwealth of Puerto Rico approved Law No. 37 for the purpose, among others, to: (1) increase the real property assessed value by ten times; (2) decrease the real property tax rate by ten times; and (3) increase the exempt portion of real property tax from the first \$15,000 of the assessed value to \$150,000. These provisions are effective only for fiscal years 2010, 2011 and 2012.

The Municipal Revenue Collection Center (CRIM, by its Spanish acronym) is a governmental entity not related to the Municipality which is responsible for the billings and collections of real and personal property taxes on behalf of the Municipality and all other municipalities in the Commonwealth of Puerto Rico. Prior to the beginning of each fiscal year, CRIM informs to the Municipality the estimated amount of property taxes expected to be collected for the ensuing fiscal year. Throughout the fiscal year, CRIM advances funds (estimated collections) to the Municipality based on the initial estimated (forecasted) collection amounts for the fiscal year. 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 the property tax amounts actually collected from taxpayers on behalf of the Municipality during the fiscal year. This settlement has to be completed on a final basis not later than December 31 following the fiscal year end. If in any given fiscal year, CRIM remits to the Municipality property tax advances that are less than the property taxes actually collected by CRIM on behalf of the Municipality, then CRIM will increase the amount of the monthly property tax advances during for the next fiscal year. However, if advances exceed the amount actually collected by CRIM, then CRIM will reduce the amount of the monthly property tax advances during the next fiscal year.

Personal property taxes are self-assessed by taxpayers every year using the book value of personal property assets owned by the taxpayer at January 1 (assessment date) and reporting such taxable value through a personal property tax return filed on May 15 subsequent to the assessment date. The total personal property tax rate in force at June 30, 2012 was 6.58 percent (of which taxpayers pay 6.38 percent and the remaining 0.20 percent is paid by the Department of Treasury, as a subsidy).

Real property taxes are assessed by CRIM. The assessment on real property is made every January 1 and is based on estimated current values of the property, deflated to 1957 market prices. The total real property tax rate in force at June 30, 2012 was 8.58 percent (of which 8.38 percent is paid by taxpayers and the remaining 0.20 percent is also paid by the Department of Treasury, as a subsidy).

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

Residential real property occupied by its owner (not engaged in trade or business) is exempt from property taxes only on the first \$15,000 of the assessed value (at 1957 market prices). For exempt amounts, the Department of Treasury assumes the payment of the basic tax (4.00 percent and 6.00 percent for personal and real property, respectively), except for property assessed for less than \$3,500 (at 1957 market prices), for which no payment is made by the Department of Treasury.

According to Law No. 81, included within the total personal and real property tax rates of 6.58 percent and 8.58 percent, respectively, there is a levy of an annual special tax of 1.03 percent of the assessed value of all real and personal property not exonerated from taxation. This special tax is levied by the Commonwealth of Puerto Rico but is collected by CRIM. Collections of this special tax are directly remitted by CRIM to the debt service fund of the Commonwealth of Puerto Rico, for the payment of the general long-term debt of the state government.

In addition, included within the total personal and real property tax rates of 6.58 percent and 8.58 percent, respectively, there is a portion of the tax rate in the amount of 1.75 percent that is restricted for the Municipality's debt service requirements of bonds. Such amounts are recorded in the Municipality's debt service fund.

The portion of the property taxes recorded in the general fund is used to finance the operating activities of the Municipality, including the payment of: (1) the insurance premiums acquired through the Puerto Rico Department of Treasury, (2) the monthly contributions to CRIM, which are statutorily required as the Municipality's share of CRIM's operating expenses, (4) statutory contributions to the Puerto Rico Health Services Administration (PRHSA), as the Municipality's share of the cost of the public health insurance coverage provided to qualifying low-income citizens, (5) certain notes payable to CRIM and to the Puerto Rico Department of Treasury and, (6) certain amounts due to certain agencies and component units of the Commonwealth, which are recorded within intergovernmental payables in the accompanying GWFS and GFFS. The 0.20 percent of unrestricted personal and real property taxes paid by the Puerto Rico Department of Treasury as a subsidy is recorded in the Municipality's general fund.

The Additional Lottery System of the Commonwealth of Puerto Rico (the Additional Lottery) is an operational unit reported as an enterprise fund in the Commonwealth of Puerto Rico's basic financial statements, which currently operates several betting alternatives to the citizens of Puerto Rico. The Additional Lottery is required every fiscal year to distribute a portion of its excess of revenues over expenses as follows:

- Thirty five percent of its net earnings (defined as the excess of revenues over expenses less an amount earmarked for the Fund for Rent and Home Improvement Subsidy Program for the Low-Income Qualifying Elderly) is earmarked to the municipalities of the Commonwealth of Puerto Rico, of which a maximum of \$26 million, on an annual basis, is distributed to the Municipal Equalization Fund held by CRIM to cover operating expenses and permanent improvements of the municipalities.
- An additional amount not exceeding \$16 million, on an annual basis, is distributed to the Municipal Equalization Fund, provided it is within the thirty-five percent corresponding to the municipalities of the Commonwealth of Puerto Rico. When the accumulated municipal appropriations from the municipalities' Puerto Rico Health Reform are covered up to June 30, 1997, these resources will be assigned to PRHSA.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

6. Intergovernmental Receivables and Payables

Intergovernmental receivables and payables recorded in the accompanying GWFS and GFFS are as follows:

	<u>General fund</u>	<u>Special revenue fund federal grants</u>	<u>Special revenue fund state & local grants</u>	<u>Total</u>
<i>Intergovernmental receivables:</i>				
Entity:				
Puerto Rico Office of the Commissioner of Municipal Affairs	\$ -	\$ 566,630	-	\$ 566,630
Puerto Rico Administration for Integral Care and Development of Children	-	21,025	-	21,025
Puerto Rico Emergency Management Agency	-	25,294	-	25,294
Puerto Rico Department of Labor	-	-	\$ 19	19
Total intergovernmental receivables	<u>\$ -</u>	<u>\$ 613,019</u>	<u>\$ 19</u>	<u>\$ 613,019</u>
<i>Intergovernmental payables:</i>				
Payroll (general fund):				
Puerto Rico Department of Labor	\$ 102,832	-	-	\$ 102,832
Employees Retirement System of the Government of the Commonwealth of Puerto Rico	175,218	-	-	175,218
Puerto Rico Department of Treasury	16,415	-	-	16,415
Employees Association of the Commonwealth of Puerto Rico	15,272	-	-	15,272
Other services (general fund):				
General Services Administration	1,162	-	-	1,162
Utilities (general fund):				
Puerto Rico Telephone Company	11,105	-	-	11,105
Puerto Rico Aqueduct and Sewer Authority	162,532	-	-	162,532
Total intergovernmental payables	<u>\$ 484,536</u>	<u>-</u>	<u>-</u>	<u>\$ 484,536</u>

Intergovernmental receivables and payables represent the pending settlements of the aforementioned intergovernmental transactions.

This Space Has Been Left Blank Intentionally

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

7. Inter-fund Transactions

The composition of inter-fund balances at June 30, 2012 and for the fiscal year then ended is as follows:

<u>Due/advances to:</u>	<u>Due/advances from:</u>				<u>Total governmental funds</u>
	<u>Major governmental funds</u>				
	<u>General fund</u>	<u>Special revenue fund – federal grants</u>	<u>Special revenue fund – state & local grants</u>	<u>Capital project fund – state & local grants</u>	
<u>Major governmental funds:</u>					
General fund	\$ -	\$ -	\$ 548,549	\$ 501,996	\$ 1,050,545
Special revenue fund – federal grants	263,123	-	15,761	-	278,884
Special revenue fund – state and local grants	96,985	-	-	298,179	395,164
Capital project fund – state & local grants	3,217	-	14,999	-	18,216
Total	\$ 363,325	\$ -	\$ 579,309	\$ 800,175	\$ 1,742,809
<u>Transfers out:</u>					
<u>Transfers in:</u>	<u>General fund</u>	<u>Total governmental funds</u>			
<u>Major governmental funds:</u>					
Debt service fund	\$ 51,088	\$ 51,088			
Total	\$ 51,088	\$ 51,088			

The principal purposes of inter-fund receivables and payables are to recognize in the outstanding balance of the loans granted, the effect of the practice of pooling cash in a current account, and to temporarily cover the payroll and other operating costs of several federally, and local and state funded programs.

The principal purposes of inter-fund transfers are to make a routinary transfer of resources from the general fund to the debt service fund to cover the principal and interest payment on certain bond. These debt service payments were made on January and July 2012.

Inter-fund receivables and payables represent the pending settlements of the aforementioned transfers at June 30, 2012.

This Space Has Been Left Blank Intentionally

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

8. Capital Assets

Capital assets activity for the fiscal year ended June 30, 2012:

a) Governmental Activities

	Cost basis at beginning of fiscal year	Additions	Reductions/ Reclassifications	Cost basis at end of fiscal year
<i>Cost basis:</i>				
Capital assets, not being depreciated:				
Land	\$ 1,720,789	-	-	\$ 1,720,789
Construction in progress	1,392,431	3,460,322	1,392,431	3,460,322
Total capital assets, not being depreciated	3,113,220	3,460,322	1,392,431	5,181,111
Capital assets, being depreciated:				
Buildings	22,429,328	1,183,729	-	23,613,057
Buildings improvements	8,605,806	-	-	8,605,806
Infrastructure	9,381,447	208,702	-	9,590,149
Machinery and equipment, and furniture and fixtures	3,343,406	-	-	3,343,406
Licensed vehicles	4,855,041	-	-	4,855,041
Total capital assets, being depreciated	48,615,028	1,392,431	-	50,007,459
Total cost basis of capital assets	\$ 51,728,248	4,852,753	1,392,431	\$ 55,188,570
	Accumulated Depreciation at beginning of fiscal year	Additions	Reductions/ Reclassifications	Accumulated Depreciation at end of fiscal year
Accumulated depreciation:				
Buildings	\$ 7,620,871	612,086	-	\$ 8,232,957
Buildings improvements	3,527,767	259,970	-	3,787,737
Infrastructure	6,518,393	1,308,486	-	7,826,879
Machinery and equipment, and furniture and fixtures	2,859,159	166,994	-	3,026,153
Licensed vehicles	4,415,541	185,629	-	4,601,170
Total accumulated depreciation	24,941,731	2,533,165	-	27,474,896
Net capital assets, governmental activities	\$ 26,786,517	2,319,518	1,392,431	\$ 27,713,674

The Municipality did not have complete and accurate accounting records of capital assets at June 30, 2012.

This Space Has Been Left Blank Intentionally

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

Depreciation and amortization expense of governmental activities for the fiscal year ended June 30, 2012 was charged to functions/programs in the accompanying statement of activities as follows:

General government	\$	119,717
Public safety		29,139
Economic and urban development		30,653
Health and welfare		65,694
Community development		516,472
Public works		1,223,526
Culture, recreation, and education		547,964
Total depreciation and amortization expense		\$ 2,533,165

9. Deferred Revenues

At June 30, 2012, deferred revenues recorded in the GWFS and the governmental fund financial statements are as follows:

	General fund	Special revenue fund federal grants	Total
<i>Unearned revenues:</i>			
Municipal licenses	\$ 825,300	-	\$ 825,300
Intergovernmental grants and contributions	-	160,871	160,871
Total unearned revenues	825,300	160,871	986,171
Total deferred revenues	\$ 825,300	160,871	\$ 986,171

This Space Has Been Left Blank Intentionally

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

10. Long-Term Obligations

The general long-term debt activity for the fiscal year ended June 30, 2012 is as follows:

	<u>Balance at beginning of fiscal year</u>	<u>Borrowings Or additions</u>	<u>Payments and deductions</u>	<u>Balance at end of fiscal year</u>	<u>Balance due within one year</u>
<u>Governmental activities:</u>					
Bonds payable:					
General obligation and public improvement bonds	\$ 17,491,000	-	698,000	\$16,793,000	\$ 654,000
Notes payable:					
Puerto Rico Department of Treasury:					
Financing agreement to pay legal judgment	7,861	-	7,861	-	-
Financing agreement for payment of the excess of property tax advances over collections through 1992	2,085,452	-	130,000	1,955,452	180,000
Municipal Revenue Collection Center:					
Law No. 42 of January 26, 2000	3,195,521	-	77,358	3,118,163	82,218
Law No. 146 of October 11, 2001 – Delinquent property tax accounts sold Settlement Statement 2010-2011	106,811 320,705	- -	5,086 320,705	101,725 -	5,086
Compensated absences:	2,278,426	1,086,837	1,097,315	2,267,948	125,181
Totals for governmental activities	<u>\$ 25,485,776</u>	<u>\$1,086,837</u>	<u>\$2,336,325</u>	<u>\$24,236,288</u>	<u>\$1,046,485</u>

Historically, the general fund has been used to liquidate the notes payable to CRIM, the Puerto Rico Department of Treasury, compensated absences and any other long-term liabilities other than bonds.

a) Debt Limitation

The Municipal Legislature is legally authorized to approve the contracting of debts of the Municipality. Nevertheless, the laws and regulations of the Commonwealth of Puerto Rico also provide that:

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

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

b) Bonds Payable

The Municipality issues general obligation and public improvement serial bonds to finance the acquisition, construction and improvement of capital assets, as well as, to finance certain operating needs, including the payment to suppliers in certain circumstances.

The laws and regulations of the Commonwealth provide that the Municipality's public debt will constitute a first claim on the available revenue of the Municipality. Public debt is composed of bonds payable. The good faith, credit and taxing power of the Municipality are irrevocably pledged for the prompt payment of the principal and interest of bonds.

As more fully described in Note 5, the Municipality levies an annual additional special property tax of 1.75 percent of the assessed value of personal and real property. The proceeds of this additional special tax are deposited in a sinking fund established at the Government Development Bank for Puerto Rico, fiscal agent, whereby sufficient funds are set aside to redeem the bonds payable of the Municipality in minimum annual and semiannual principal and interest payments. The collections of this special tax are recorded in the Municipality's debt service fund.

As more fully described in Note 4, the Municipality impose and collect sales and uses taxes of one point five (1.5) percent, of which the Municipality has elected to restrict a portion amounting .4% for the payment of long-term bonds. The collections of this sales and use tax are recorded in the Municipality's debt service fund.

For financial reporting purposes, the outstanding balances of bonds represent the total principal to be repaid. Bonds payable is composed as follows at June 30, 2012:

	<u>Outstanding balance</u>
<u>General Obligation and Public Improvement Bonds:</u>	
1988 serial bonds (face amount of \$270,000) due in annual principal installments ranging from \$6,000 to \$20,000; plus interests due in annual installments at fixed rate (5%) through January, 1, 2013.	\$ 20,000
1996 serial bonds (face amount of \$238,000) due in annual principal installments ranging from \$7,000 to \$18,000; plus interests due in annual installments at fixed rate (4.5%) through January, 1, 2020.	125,000
1998 serial bonds (face amount \$122,000) due in annual principal installments ranging from \$3,000 to \$9,000; plus interests due in semiannual installments at fixed rate (4.5%) through January, 1, 2012.	75,000
1998 serial bonds (face amount \$715,000) due in annual principal installments ranging from \$10,000 to \$70,000; plus interests due in semiannual installments at variable rates (4.4% at June 30, 2012) through July 1, 2023.	520,000

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

	Outstanding balance
2001 serial bonds (face amount \$1,300,000) due in annual principal installments ranging from \$20,000 to \$115,000; plus interests due in semiannual installments at variable rates (1.3% at June 30, 2012) through July 1, 2025.	1,000,000
2003 serial bonds (face amount of \$1,230,000) due in annual principal installments ranging from \$20,000 to \$100,000; plus interests due in semiannual installments at variable rates (4.62% at June 30, 2012) through July 1, 2027.	990,000
2003 serial bonds (face amount of \$405,000) due in annual principal installments ranging from \$5,000 to \$30,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2027.	325,000
2003 serial bonds (face amount of \$875,000) due in annual principal installments ranging from \$15,000 to \$65,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2027.	665,000
2004 serial bonds (face amount of \$330,000) due in annual principal installments ranging from \$5,000 to \$25,000; plus interests due in semiannual installments at variable rates (4.62% at June 30, 2012) through July 1, 2028.	270,000
2005 serial bonds (face amount of \$730,000) due in annual principal installments ranging from \$15,000 to \$55,000; plus interests due in semiannual installments at variable rates (4.62% at June 30, 2012) through July 1, 2024.	555,000
2005 serial bonds (face amount of \$525,000) due in annual principal installments ranging from \$35,000 to \$65,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2015.	245,000
2006 serial bonds (face amount of \$835,000) due in annual principal installments ranging from \$15,000 to \$70,000; plus interests due in semiannual installments at variable rates (4.62% at June 30, 2012) through July 1, 2025.	685,000
2007 serial bonds (face amount of \$150,000) due in annual principal installments ranging from \$5,000 to \$10,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2031.	125,000

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

	Outstanding balance
2007 serial bonds (face amount of \$205,000) due in annual principal installments ranging from \$25,000 to \$35,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2013.	70,000
2008 serial bonds (face amount of \$185,000) due in annual principal installments ranging from \$25,000 to \$35,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2014.	105,000
2007 serial bonds (face amount of \$560,000) due in annual principal installments ranging from \$10,000 to \$50,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2027.	505,000
2008 serial bonds (face amount of \$3,190,000) due in annual principal installments ranging from \$50,000 to \$265,000; plus interests due in semiannual installments at variable rates (6.5% at June 30, 2012) through July 1, 2032.	3,025,000
2009 serial bonds (face amount of \$560,000) due in annual principal installments ranging from \$40,000 to \$75,000; plus interests due in semiannual installments at variable rates (1.55% at June 30, 2012) through July 1, 2018.	430,000
2010 serial bonds (face amount of \$2,760,000) due in annual principal installments ranging from \$40,000 to \$230,000; plus interests due in semiannual installments at variable rates (7% at June 30, 2012) through July 1, 2034.	2,675,000
2010 serial bonds (face amount of \$625,000) due in annual principal installments ranging from \$10,000 to \$65,000; plus interests due in semiannual installments at variable rates (6% at June 30, 2012) through July 1, 2034.	605,000
2010 serial bonds (face amount of \$198,000) due in annual principal installments ranging from \$20,000 to \$38,000; plus interests due in semiannual installments at variable rates (6% at June 30, 2012) through July 1, 2016.	153,000
2011 serial bonds (face amount of \$2,565,000) due in annual principal installments ranging from \$35,000 to \$215,000; plus interests due in semiannual installments at variable rates (6% at June 30, 2012) through July 1, 2035.	2,530,000

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

	Outstanding balance
2011 serial bonds (face amount of \$1,110,000) due in annual principal installments ranging from \$15,000 to \$95,000; plus interests due in semiannual installments at variable rates (6% at June 30, 2012) through July 1, 2035.	1,095,000
Total bonds payable	\$ 16,793,000

Variable interest rates on serial bonds are reviewed periodically by GDB and are based on the fluctuation of GDB's weighted average rate for its commercial paper program. Under this program, GDB issues commercial paper: (1) in the taxable and tax-exempt markets of the United States of America, (2) in the Eurodollar market, and (3) to corporations having tax exemptions under the Commonwealth's Industrial Incentives Acts and, which qualify for benefits provided by the former Section 936 of the U.S. Internal Revenue Code.

Interest expense on bonds payable amounted to \$624,291 for the fiscal year ended June 30, 2012.

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

Fiscal year ending June 30,	Principal	Interest	Total
2013	\$ 654,000	1,107,177	\$ 1,761,177
2014	690,000	1,092,752	1,782,752
2015	682,000	1,048,484	1,730,484
2016	697,000	1,004,198	1,701,198
2017	686,000	957,704	1,643,704
2018-2022	3,654,000	4,083,819	7,737,819
2023-2027	4,225,000	2,759,996	6,984,996
2028-2032	3,345,000	1,441,212	4,686,212
2033-2037	2,160,000	310,938	2,470,938
Totals	\$ 16,793,000	13,806,280	\$ 30,599,280

c) Notes Payable to Puerto Rico Department of Treasury

- **Financing Agreement for Payment of the Excess of Property Tax Advances over Collections** – On August 14, 2002 the Municipality entered into a financing agreement with the Puerto Rico Treasury Department to pay a debt related to the excess of property tax advances over collections made by the Puerto Rico Treasury Department prior to the creation of CRIM in 1993. The face amount of the loan was \$2,421,452, and bears no interest. The note is payable in monthly installments ranging from \$25,452 through December 1, 2023. At June 30, 2017, the balance of this note amounted to \$1,955,452.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

<u>Year Ending June 30,</u>	<u>Principal Amount</u>
2013	\$ 180,000
2014	180,000
2015	180,000
2016	180,000
2017	180,000
2018-2022	930,000
2023	<u>125,452</u>
Total	<u>\$ 1,955,452</u>

d) Notes Payable to Municipal Revenue Collection Center

The Municipality had the following notes payables to Municipal Revenue Collection Center (CRIM, by its Spanish acronym) at June 30, 2012:

- **Act No. 42** – Act No. 42 of January 26, 2000 was enacted to authorize CRIM to enter into a financing agreement of up to \$200 million, for a term not exceeding 30 years. The financing agreement allows for the financing of a debt that the municipalities of Puerto Rico have with CRIM, arising from the final settlements of property tax advances versus actual collections through fiscal year 2000. The amounts that the municipalities will collect from the additional property taxes resulting from the increases in the subsidy from the Commonwealth to the municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238 of August 15, 1999.

In addition, on February 12, 2002, the Municipality entered into a repayment agreement with GDB and CRIM to pay off the remaining excess of property tax advances through fiscal year 2000 and 2001. CRIM retains the principal and interest from the property tax advances of the Municipality. The amounts retained by CRIM are remitted to GDB on July 1 of each year through July 1, 2032. The repayment agreement bears interest at variable rates determined by GDB. The outstanding principal balances of the note payable to CRIM amounted \$3,118,163, at June 30, 2012.

<u>Year Ending June 30,</u>	<u>Principal Amount</u>	<u>Interest Amount</u>
2013	\$ 82,218	\$ 191,684
2014	87,384	186,518
2015	92,875	181,027
2016	98,710	175,192
2017	104,913	172,138
2018-2022	632,125	737,387
2023-2027	857,287	512,224
2028-2032	<u>1,162,651</u>	<u>206,865</u>
Total	<u>\$ 3,118,163</u>	<u>\$ 2,363,035</u>

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

- **Law No. 146 - Financing of delinquent property tax accounts sold** – On September 24, 2002, CRIM, on behalf of the municipalities of Puerto Rico, entered into a financing agreement with GDB pursuant to the provisions of Law No. 146 of October 11, 2001, as amended (Law No. 146). The purpose of this financing agreement was to extinguish in advance certain bonds payable issued by Public Finance Corporation (PFC), a subsidiary of the Government Development Bank for Puerto Rico, which were originally issued to pay certain property tax receivables owned by the municipalities of Puerto Rico through 1996, which were acquired by PFC with recourse.

The original face amount of the note allocated by CRIM to the Municipality was for a term not exceeding 30 years. The note bears interest at 6.50 percent during its first five years. Subsequently, from years 6 through 30, the loan shall bear variable interest at a rate of 125 points over the 5-year LIBOR rate, which will be adjusted every five years. During the first five years of the note, commenced on July 1, 2003, the Municipality shall pay only interest, except for property tax receivables collections related to the transaction explained in the above paragraph, which will be applied as principal payment to reduce the debt balance. At the end of the first five years of the note, the repayment terms and conditions of the note shall be renegotiated to allow the Municipality to pay the outstanding balance of the note in equal installments of principal plus interest, through maturity. Interest payments on this financing agreement are accounted for in the general fund. The outstanding principal of the note payable to CRIM amounted to \$101,725, at June 30, 2012.

<u>Year Ending</u> <u>June 30,</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Amount</u>
2013	\$ 5,086	\$ 6,327
2014	5,086	6,011
2015	5,086	5,694
2016	5,086	5,378
2017	5,086	5,220
2018-2022	25,431	20,564
2023-2027	25,431	12,655
2028-2032	25,433	4,745
Total	\$ 101,725	\$ 66,594

e) *Compensated Absences*

At June 30, 2012, the government-wide statement of net assets – governmental activities includes a liability amounting \$2,388,709, of which \$1,293,012 represents accrued sick leave benefits, and \$1,095,697 represents accrued vacation benefits, representing the Municipality’s commitment to fund such costs from future operations.

This Space Has Been Left Blank Intentionally

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

11. Employees' Retirement Systems

a) Plan Description

The Municipality's employees participate in the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS), a cost-sharing multi-employer (as related to the Municipality's reporting entity) defined pension plan established by the Commonwealth. Substantially all full-time employees of the Commonwealth and substantially all municipalities are covered by ERS under the terms of Public Act No. 447 of May 15, 1951, as amended (Act No. 447). All regular and temporary employees of the Municipality become plan members of ERS at the date of employment, while it is optional for officers appointed.

ERS members, other than those joining it after March 31, 1990, are eligible for the benefits described below:

- ***Retirement Annuity***

ERS members are eligible for a retirement annuity upon reaching the following age:

Policemen and firemen:	Other employees:
50 with 25 years of credited service	55 with 25 years of credited service
58 with 10 years of credited service	58 with 10 years of credited service

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

- ***Merit Annuity***

ERS members are eligible for merit annuity with a minimum of 30 years or more of credited service. The annuity for which the plan member is eligible is limited to a minimum of 65 percent and a maximum of 75 percent of the average compensation.

- ***Deferred Retirement Annuity***

A participating employee who ceases to be an employee of the Municipality after having accumulated a minimum of ten years of credited service qualifies for retirement benefits provided his/her contributions are left in ERS until reaching 58 years of age.

- ***Coordinated Plan***

On the coordinated plan, by the time the employee reaches 65 years old and begins to receive social security benefits, the pension benefits are reduced by the following:

- (a) \$165 per month, if retired with 55 years of age and 30 years of credited service.

MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

- (b) \$110 per month, if retired with less than 55 years of age and 30 years of credited service.
- (c) All other between \$82 and \$100 per month.
- (d) Disability annuities under the coordinated plan are also adjusted at age 65 and in some cases can be reduced over \$165 per month.

- ***Non-Coordinated Plan***

On the non-coordinated plan the participating employee and does not have any change on the pension benefits upon receiving social security benefits.

- ***Reversionary Annuity***

An ERS member, upon retirement, could elect to receive a reduced retirement annuity giving one or more benefit payments to his/her dependents. The life annuity payments would start after the death of the retiree for an amount not less than \$240 per year or greater than the annuity payments being received by the retiree.

- ***Occupational Disability Annuity***

A participating employee, who as a direct result of the performance of his/her occupation is totally and permanently disabled, is eligible for a disability annuity of 50 percent of the compensation received at the time of the disability.

- ***Nonoccupational Disability Annuity***

A participating employee, totally and permanently disabled for causes not related to his/her occupation and with no less than 10 years of credited service, is eligible for an annuity of 1.50 percent of the average compensation of the first 20 years of credited services, increased by 2 percent for every additional year of credited service in excess of 20 years.

- ***Death Benefits***

Occupational:

- (a) **Surviving spouse** – annuity equal to 50 percent of the participating employee's salary at the date of the death.
- (b) **Children** - \$10 per month for each child, minor or student, up to a maximum benefit per family of \$100.

Nonoccupational:

Beneficiary – the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of the death.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

Post-retirement:

Beneficiary with surviving spouse age 60 or over and a child, 18 or under, up to 30 percent (60 percent, if not covered under Title II of the Social Security Act) (increased to 50 percent effective January 1, 2005) of retiree's pension or otherwise the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$750.

- ***Refunds***

A participating employee who ceases his/her employment with the Municipality without the right to a retirement annuity has the right to a refund of the contributions to ERS plus any interest earned thereon.

- ***Cost of Living Adjustment for Pension Benefits***

Public Act No. 10 of May 21, 1992 (Act No. 10) provided for increases of 3 percent every three or more years of retirement. Act No. 10 requires further legislation to grant this increase every three years subject to the presentation of actuarial studies regarding its costs and the source of financing. To protect the financial health of ERS, the increase granted during 2001 and the one granted on January 1, 2005 are being financed by the Municipality and the other participating employers.

To avoid any economic impact on ERS, the employers are responsible for contributing to ERS the amounts to cover the benefit payments and the employer and employee contributions with respect to the participants covered until the participants reach the normal retirement age.

- ***Amendment to Act No. 447 effective January 1, 2000 to create a Defined Contribution Plan***

On September 24, 1999, Public Act No. 305, an amendment to Act No. 447, was enacted to establish a defined contribution plan, known as System 2000, to cover employees joining ERS on or after January 1, 2000.

Employees that participated in the original plan as of December 31, 1999, had the opportunity to elect to either stay in the defined benefit plan or transfer to System 2000. Employees that joined the Municipality on or after January 1, 2000, were only allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there is a pool of plan assets, which is invested by the System, together with those of the cost-sharing multi-employer defined benefit plan. Neither the Commonwealth nor the Municipality guarantee benefits at retirement age. The annuity is based on a formula which assumes that each fiscal year the employee's contribution (with a minimum of 8.28 percent of the employee's salary up to a maximum of 10 percent) is invested as instructed by the employee in an account which either: (1) earns a fixed rate based on the two-year Constant Maturity Treasury Notes, (2) earns a rate equal to 75 percent of the return of the ERS' investment portfolio (net of management fees), or (3) earns a combination of both

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability benefits are not granted under System 2000, rather are provided to those participants that voluntarily elect to participate in a private insurance long-term disability program. The employers' contributions (9.28 percent of the employee's salary) with respect to employees under System 2000 will continue and will be used to fund the cost-sharing multi-employer defined benefit plan.

System 2000 reduced the retirement age from 65 years to 60 for those employees who joined the current plan on or after January 1, 2000.

Historically, the state government of the Commonwealth of Puerto Rico has reported ERS and System 2000 in its basic financial statements as pension trust funds. Accordingly, the Commonwealth is currently assuming any actuarial deficiency that may exist or arise related to the Municipality's participating employees because ERS does not allocate to the Municipality any actuarial deficiencies pertaining to participating municipal employees. The Municipality is only required by law to make statutory contributions at the rates detailed below.

- ***Recent Amendments to Act No. 447***

The Senate and the House of Representatives of the Commonwealth of Puerto Rico have the authority for establishing or amending the contribution requirements of System 2000 by approving the necessary amendments or laws, subject to the final approval of the Governor of the Commonwealth of Puerto Rico.

In June and July 2003, the Governor of the Commonwealth signed three Public Acts that provided the following certain benefits to retirees:

- (a) Increase in minimum monthly pension payments to \$300, effective January 1, 2005.
- (b) Triennial 3 percent increase in all pensions, effective January 1, 2005.
- (c) Increase in widow and/or beneficiaries to 50 percent of the benefit received by the deceased pensioner, effective January 1, 2005.

All the benefits granted will be funded through budgetary assignments in the Municipality's general fund with respect to its retired employees.

The Board of Trustees of ERS approved, effective November 17, 2003, an increase in the amount granted on personal loans to participating employees from \$3,000 to \$5,000.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

b) Funding Policy

The contribution requirement to ERS is established by law and is not actuarially determined. These contributions are as follows:

Municipality and other employers	
Employees:	9.28 percent of applicable payroll
Coordination plan:	5.78 percent of gross salary up to \$6,600 per year, plus 8.28 percent gross salary in excess of \$6,600.
Supplementation plan:	8.28 percent of gross salary. This is the only choice available to policemen, firemen and mayors

The contribution requirement to System 2000 is also established by law and is not actuarially determined. These contributions are as follows:

Municipality and other employers	9.28 percent of applicable payroll
Employees:	5.78 percent of gross salary up to \$6,600 per year, plus 8.28 percent gross salary in excess of \$6,600.

c) Annual Contribution

The actual combined employer and employee contributions to ERS and System 2000 for the current and past two years, which are equal to the statutory required contributions, are as follows:

<u>Fiscal year ended June 30,</u>	<u>Act No. 447</u>	<u>System 2000</u>	<u>Total</u>
2012	\$ 65,742	143,972	\$ 209,714
2011	94,927	152,516	247,443
2010	97,722	123,736	221,458
Totals	<u>\$ 258,391</u>	<u>420,224</u>	<u>\$ 678,615</u>

During the fiscal years ended June 30, 2010, 2011, and 2012, the Municipality and the participating employees contributed at least 100 percent of the required contributions to ERS and System 2000. The authority under which obligations to contribute to ERS and System 2000 by the plans' members, employers and other contributing entities (i.e., state or municipal contributions) are established or may be amended by law by the House of Representatives, the Senate and the Governor of the Commonwealth of Puerto Rico.

Readers can obtain copies of the audited basic financial statements (GAAP basis) of ERS and System 2000 by writing to Mr. Hector M. Mayol Kauffmann, Executive Director of the Retirement Systems Administration of the Commonwealth of Puerto Rico (the entity that administers ERS and System 2000) at PO Box 42004, Minillas Station, Santurce, Puerto Rico 00940.

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

12. Commitments, Contingencies and Uncertainties

Claims and Judgments

The Municipality is defendant in various legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1955, as amended, persons are allowed to sue the Municipality only for causes of actions set forth in said Act to a maximum amount of \$75,000 or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Municipality may provide its officers and employees with legal representation, as well as assume the payment of any judgment that may be entered against them. There is no limitation on the payment of such judgment.

The Municipality also is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, and other legal matters that arise in the ordinary course of the Municipality's activities. With respects to pending or threatened litigation, the Municipality has reported no liabilities as of June 30, 2012. Management believes, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial resources for its payment.

Federal Financially Assisted Programs

The Municipality receives financial assistance from the federal government in the form of grants and entitlements. Receipts of grants are generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal law and regulations, including the expenditure of resources for eligible purposes. Substantially all grants are subject to audit under Circular A-133 of the Office of Management and Budget of the United States of America (OMB Circular A-133). Disallowance as a result of these audits may become liabilities of the Municipality

Construction Commitments

The Municipality has commitments at June 30, 2012 of approximately \$614,404 for construction, improvements or renovation of certain capital assets.

13. Fund Balance (Deficit)

As of June 30, 2012, fund balance (deficit) is comprised of the following:

Fund balances (deficit)	General fund	Special revenue fund – federal grants	Special revenue fund – state & local grants	Capital project fund – state & local grants	Debt service fund	Total
<i>Restricted for:</i>						
General government	\$ 227	-	-	-	-	\$ 227
Health and welfare	-	212,256	170,137	153,016	-	535,589
Public works	15,907	-	81,190	1,327,131	-	1,424,228
Public safety	-	-	4	-	-	4
Culture and recreation and education	10,605	-	253,034	1,120,125	-	1,383,764
Community development	-	-	-	70,898	-	70,898
Urban and economic development	-	-	314	-	-	314
Debt service	-	-	-	-	710,285	710,285
<i>Unassigned</i>	(2,262,868)	-	-	-	-	(2,262,868)
Total fund balances (deficit)	(\$2,236,129)	212,256	504,589	2,671,170	710,285	\$ 1,862,441

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

14. Restatement

During the current fiscal year, the Municipality revised its fund financial statements and its government-wide financial statements, which resulted in the reclassification of debt balance previously reported as long term debt to fund liabilities, correction of balance of long term debt balance reported in the prior year government wide financial statements, and correction of various accounting errors and omissions reported in the prior year governmental funds, principally in interfund account balances and intergovernmental receivables account balances.

a) Governmental Fund Financial Statements

The following schedule presents a summary of the prior-period adjustments recorded in the accompanying balance sheet – governmental funds, and reconciles the fund balances, as previously reported by the Municipality at June 30, 2011, to the beginning fund balances in the accompanying basic financial statements, as restated:

	<u>Major governmental funds</u>					Total Governmental Funds
	General fund	Special revenue fund federal grants	Special revenue fund - state & local grants	Capital project fund - state & local grants	Debt service Fund	
Assets:						
As previously reported in the audited financial statements at June 30, 2011	\$ 651,044	836,743	1,951,553	5,024,897	1,812,892	\$ 10,277,129
Add/(deduct): prior-period adjustments	(56,913)	-	(394,643)	-	-	(451,556)
Total assets at June 30, 2011, as restated	<u>\$ 594,131</u>	<u>836,743</u>	<u>1,556,910</u>	<u>5,024,897</u>	<u>1,812,892</u>	<u>\$ 9,825,573</u>
Liabilities:						
As previously reported in the audited financial statements at June 30, 2011	\$ 3,357,210	561,586	646,900	407,563	964,679	\$ 5,937,938
Add/(deduct): prior-period adjustments	-	(56,913)	-	-	-	(56,913)
Total liabilities at June 30, 2011, as restated	<u>\$ 3,357,210</u>	<u>504,673</u>	<u>646,900</u>	<u>407,563</u>	<u>964,679</u>	<u>\$ 5,881,025</u>
Fund balance:						
As previously reported in the audited financial statements at June 30, 2011	\$ (2,706,166)	275,157	1,304,653	4,617,334	848,213	\$ 4,339,191
Add/(deduct): prior-period adjustments	(56,913)	56,913	(394,643)	-	-	(394,643)
Total fund balance at June 30, 2011, as restated	<u>\$ (2,763,079)</u>	<u>332,070</u>	<u>910,010</u>	<u>4,617,334</u>	<u>848,213</u>	<u>\$ 3,944,548</u>

**MUNICIPALITY OF GUAYANILLA,
COMMONWEALTH OF PUERTO RICO**

Notes to Basic Financial Statements
Fiscal Year Ended June 30, 2012

b) Government-Wide Financial Statements

The following schedule presents a summary of the prior-period adjustments recorded in the accompanying Statement of Net Assets, and reconciles the total net asset balance at June 30, 2011, as previously reported by the Municipality, to the beginning net assets, as restated in the accompanying GWFS:

	<u>Statement of Net Assets</u>
Assets:	
As previously reported in the audited financial statements at June 30, 2011	\$ 34,931,611
Add/(deduct): prior-period adjustments	(394,643)
Total assets at June 30, 2011, as restated	<u>\$ 34,536,968</u>
Liabilities:	
As previously reported in the audited financial statements at June 30, 2011	\$ 28,656,679
Add/(deduct): prior-period adjustments	-
Total liabilities at June 30, 2011, as restated	<u>\$ 28,656,679</u>
Net assets:	
As previously reported in the audited financial statements at June 30, 2011	\$ 6,274,932
Add/(deduct): prior-period adjustments	(394,643)
Total net assets at June 30, 2011, as restated	<u>\$ 5,880,289</u>

15. Subsequent Events

On January 2013, the Municipality's Legislature approved a Municipal Ordinance to impose a new tax rates on real and personal property located within the jurisdiction of the Municipality of Guayanilla. Such new tax rates will be effective at January 1, 2013.

On April 4, 2013, the Legislature of the Commonwealth of Puerto Rico issued Act No. 3, which amends the previously issued Act 447 of 1951 ("Retirement System Act"). This Act make significant changes to the Employees Retirement System of the Commonwealth of Puerto Rico (the "ERS") trust created by Act 447 of May 15, 1951, as amended, to provide pension and other benefits to retired employees of the government of Puerto Rico and its instrumentalities.

On June 30, 2013, the Legislature of the Commonwealth of Puerto Rico issued Act No. 40, which includes amendments to the sales and use tax sections of the Puerto Rico Internal Revenue Code.

End of Notes to Basic Financial statements

Required Supplementary Information
Budgetary Comparison Schedule – General Fund
Fiscal Year Ended June 30, 2012

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
 Budgetary Comparison Schedule – General Fund
 Fiscal Year Ended June 30, 2012

	Budgeted amounts		Actual amounts (budgetary basis)	Variance with final budget – over (under)
	Original	Final		
Revenues:				
Property taxes	\$ 1,423,529	\$ 1,423,529	\$ 1,423,529	\$ -
Municipal license taxes	3,810,450	3,810,450	2,636,480	(1,173,970)
Sales taxes	400,000	400,000	356,848	(43,152)
Construction excise taxes	507,000	507,000	178,196	(328,804)
Intergovernmental grants and contributions	5,180,937	5,180,937	5,238,990	58,053
Interest on deposits	120,000	120,000	193,940	73,940
Charges for services	100,000	100,000	94,214	(5,786)
Miscellaneous	140,000	140,000	382,557	242,557
Total revenues	11,681,916	11,681,916	10,504,754	(1,177,162)
Expenditures:				
General government	3,995,053	3,995,158	4,105,633	(110,475)
Health and welfare	1,596,254	1,634,840	1,647,481	(12,641)
Public works	4,477,032	4,630,072	4,680,159	(50,087)
Public safety	963,432	826,744	931,338	(104,594)
Culture, recreation and education	576,845	521,802	493,438	28,364
Total expenditures	11,608,616	11,608,616	11,858,049	(249,433)
Excess (deficiency) of revenues over expenditures and encumbrances	73,300	73,300	(1,353,295)	(1,426,595)
Other financing Sources (uses):				
Transfer out to other governmental funds	(73,300)	(73,300)	(51,088)	22,212
Total Other Financing Sources (uses)	(73,300)	(73,300)	(51,088)	22,212
Net change in fund balance (deficit)	\$ -	\$ -	\$ (1,404,383)	\$ (1,404,383)

Reconciliation of differences:

Sources/inflows of financial resources:

Actual amounts (budgetary basis) "available for appropriations" from the budgetary comparison schedule	\$ 10,504,754
Differences - budgetary basis to GAAP:	
Differences in bases of accounting:	
GAAP adjustment to revenues	47,793
Total revenues and as reported on the statement of revenues, expenditures and changes in fund balances	\$ 10,552,547

Uses/outflows of financial resources:

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule (including transfer out to other funds)	\$ 11,909,137
Differences - budgetary basis to GAAP:	
GAAP adjustment to expenses	(1,883,540)
Total expenditures and transfer out to other funds as reported on the statement of revenues, expenditures and changes in fund balances	\$ 10,025,597

**MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO**

Financial Data Schedule
Fiscal Year Ended June 30, 2012

**Balance Sheet
June 30, 2012**

Description	14.871 Housing Choice Vouchers
111 Cash - Unrestricted	\$ 141,494
113 Cash - Other Restricted	87,076
100 Total Cash	228,570
128 Fraud Recovery	36,111
128.1 Allowance for Doubtful Accounts - Fraud	(32,844)
120 Total Receivables, Net of Allowances for Doubtful	3,267
150 Total Current Assets	231,837
164 Furniture, Equipment & Machinery - Administration	26,625
166 Accumulated Depreciation	(23,710)
160 Total Capital Assets, Net of Accumulated Depreciation	2,915
180 Total Non-Current Assets	2,915
190 Total Assets	234,752
312 Accounts Payable <= 90 Days	4,335
322 Accrued Compensated Absences - Current Portion	5,184
333 Accounts Payable - Other Government	15,246
310 Total Current Liabilities	24,765
354 Accrued Compensated Absences - Non Current	15,552
350 Total Non-Current Liabilities	15,552
300 Total Liabilities	40,317
508.1 Invested In Capital Assets, Net of Related Debt	2,915
511.1 Restricted Net Assets	90,343
512.1 Unrestricted Net Assets	101,177
513 Total Equity/Net Assets	194,435
600 Total Liabilities and Equity/Net Assets	\$ 234,752

**MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO**

Financial Data Schedule
Fiscal Year Ended June 30, 2012

**Revenues and Expenses
June 30, 2012**

Description	14.871 Housing Choice Vouchers
70600 HUD PHA Operating Grants	\$ 547,698
71500 Other Revenue	3,428
72000 Investment Income - Restricted	929
70000 Total Revenue	552,055
91100 Administrative Salaries	51,071
91500 Employee Benefit contributions - Administrative	14,529
91600 Office Expenses	21,569
91000 Total Operating - Administrative	87,169
96210 Compensated Absences	3,740
96000 Total Other General Expenses	3,740
96900 Total Operating Expenses	90,909
97000 Excess of Operating Revenue over Operating	461,146
97300 Housing Assistance Payments	583,070
97350 HAP Portability-In	880
97400 Depreciation Expense	903
90000 Total Expenses	675,762
10000 Excess (Deficiency) of Total Revenue Over	\$ (123,707)
11030 Beginning Equity	261,229
11040 Prior Period Adjustments, Equity Transfers and	56,913
11170 Administrative Fee Equity	104,092
11180 Housing Assistance Payments Equity	90,343
11190 Unit Months Available	1752
11210 Number of Unit Months Leased	1669

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYANILLA

Notes to the Financial Data Schedule
Fiscal Year Ended June 30, 2012

NOTE A – BASIS OF PRESENTATION

1. The accompanying Financial Data Schedule (FDS) is a trial balance of the Section 8 Housing Choice Voucher Program, administered by the Municipality. The FDS was created in order to standarize the financial information reported by Public Housing Authorities (PHA) to the Real Estate Assessment Center (REAC), as required by the Uniform Financial Reporting Standards (UFRS). REAC is the US Department of Housing and Urban Development (HUD) national manager center created to assess the condition of HUD owned and assisted properties. The UFRS are rules to implement requirements of 24 CFR, Part 5, Subpart H, for the electronic filing of financial information to HUD.
2. In accordance with the guidelines for reporting and attestation requirements of UFRS, the accompanying FDS is included as information supplementary to the financial statements. It was prepared using the accrual basis of accounting, as required by REAC regulations.

End of Notes to the Financial Data Schedule

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2012

Federal Grantor/Pass-through Grantor/ Program or Cluster Title	CFDA Number	Entity Identifying Number	Federal Expenditures
U.S. Department of Agriculture:			
Pass-through the Department of Education of the Commonwealth of Puerto Rico:			
Child and Adult Care Food Program	10.558	N/AV	\$ 18,883
Subtotal – US Department of Agriculture			18,883
U.S. Department of Housing and Urban Development:			
Direct Program:			
Section 8 Housing Choice Voucher	14.871	N/A	547,968
Pass-through the Office of the Commissioner of Municipal Affairs of the Commonwealth of Puerto Rico			
Community Development Block Grants – State’s Program	14.228	FC-27/AB-27	1,357,526
ARRA- Community Development Block Grant	14.255	08-AB-AR-27-01	230,825
Total Community Development Block Grant Cluster:			1,558,351
Pass-through the Department of the Family of the Commonwealth of Puerto Rico:			
ARRA-Homeless Prevention and Rapid Re-housing Program	14.262	122-2010-000249	56,772
Subtotal – US Department of Housing and Urban Development			2,193,091
U.S. Department of Energy:			
Pass-through the Energy Affairs Administration Office of the Commonwealth of Puerto Rico:			
ARRA-Energy Efficiency and Conservation Block Grant Program	81.128	0013A-027	102,473
Subtotal – US Department of Energy			102,473
U.S. Department of Health and Human Services:			
Pass-through the Governor’s Office for Elderly Affairs of the Commonwealth of Puerto Rico:			
Special Program for Aging – Title III - Part B – Grant for Supportive Services and Senior Centers	93.044	N/AV	114,896

See accompanying Notes to the Schedule of Expenditures of Federal Awards

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2012

Federal Grantor/Pass-through Grantor/ Program or Cluster Title	CFDA Number	Entity Identifying Number	Federal Expenditures
Pass-through the Department of the Family of the Commonwealth of Puerto Rico:			
Child Care and Development Block Grant	93.575	241-2011-000191	275,105
Subtotal – US Department of Health and Human Services			390,001
U.S. Department of Homeland Security:			
Pass-through the Emergency Management Agency of the Commonwealth of Puerto Rico:			
Hazard Mitigation Grant	97.039	N/AV	25,000
Pass-through the Governor’s Authorized Representative Office (GAR) of the Commonwealth of Puerto Rico:			
Disaster Grants – Public Assistance	97.036	N/AV	20,160
Pass-through the Governor’s Office for Public Security Affairs of the Commonwealth of Puerto Rico:			
State Homeland Security Grant Program	97.073	N/AV	179,789
Subtotal – US Department of Homeland Security			224,949
TOTAL EXPENDITURES OF FEDERAL AWARDS			\$2,929,397

See accompanying Notes to the Schedule of Expenditures of Federal Awards

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Notes to the Schedule of Expenditures of Federal Awards
Year Ended June 30, 2012

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Municipality of Guayanilla, Commonwealth of Puerto Rico (the Municipality) for the fiscal year ended June 30, 2012. The Municipality's reporting entity is disclosed in Note 1 to the Municipality's basic financial statements as of and for the fiscal year ended June 30, 2012.

The accompanying schedule of expenditures of federal awards is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

NOTE B - FEDERAL CFDA NUMBER

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.

NOTE C - PASS -THROUGH GRANTOR'S NUMBER

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 federal awards received as a subrecipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

End of Notes to the Schedule of Expenditures of Federal Awards



MENDOZA & RAMOS
Contadores Públicos Autorizados, C.S.P.

P.O. Box 35 • Guayama, Puerto Rico 00785

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

**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**

We have audited the financial statements of the governmental activities and each major fund of the Municipality of Guayanilla, Puerto Rico (the "Municipality") as of and for the fiscal year ended June 30, 2012, which collectively comprise Municipality of Guayanilla's basic financial statements and have issued our report thereon dated July 18, 2013. The report's opinion on governmental wide financial statement was disclaimed because does not maintained adequate records regarding capital assets, accumulated depreciation and related depreciation expense reported in the governmental activities. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of the Municipality of Guayanilla, Puerto Rico, is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit we considered the Municipality's internal control over financial reporting as basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Municipality's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we considered to be 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 misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We

INDEPENDENT AUDITOR'S REPORT
MUNICIPALITY OF GUAYANILLA

consider the deficiencies identified as finding 12-01 in the accompanying schedule of findings and questioned costs to be material weakness.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies identified as finding 12-02 in the accompanying schedule of findings and questioned costs to be significant deficiencies.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matter that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as findings 12-01 and 12-02.

We noted certain matters that we reported to management of the Municipality in a separate letter dated July 18, 2013.

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

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

Mendoza & Ramos CPA's

MENDOZA & RAMOS
CERTIFIED PUBLIC ACCOUNTANTS, C.S.P.

Guayama, Puerto Rico
July 18, 2013

Stamp number 2573192 was
affixed to the original of this
report.





MENDOZA & RAMOS
Contadores Públicos Autorizados, C.S.P.

P.O. Box 35 • Guayama, Puerto Rico 00785

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

REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND
MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH THE OMB CIRCULAR A-133

Compliance

We have audited the compliance of the Municipality of Guayanilla, Puerto Rico (the "Municipality") with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2012. 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. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on the Municipality's compliance based on our audit.

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

As described in the accompanying Schedule of findings and questioned costs, the Municipality did not comply with the requirements that are applicable to its major programs, as follows:

Reference Number	Compliance Requirement	Major Program
12-03	Procurement, Suspension and Debarment	Community Development Block Grant / State's Program
12-04	Procurement, Suspension and Debarment	Community Development Block Grant / State's Program

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

INDEPENDENT AUDITOR'S REPORT
MUNICIPALITY OF GUAYANILLA

In our opinion, except for the noncompliance described above, the Municipality complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

INTERNAL CONTROL OVER COMPLIANCE

The management of the Municipality is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Municipality's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with *U. S. Office of Management and Budget (OMB) Circular A-133*, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weakness.

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 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 a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 12-03 and 12-04 to be material weaknesses.

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

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

Mendoza & Ramos CPA's

MENDOZA & RAMOS
CERTIFIED PUBLIC ACCOUNTANTS, C.S.P.

Guayama, Puerto Rico
July 18, 2013

Stamp number 2573193 was affixed
to the original of this report.



**MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO**

Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION I-FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Financial Statements

Type of auditors' report issued:

- Unqualified Opinion, except for disclaimer opinion for government-wide financial statement
- Qualified Opinion
- Adverse Opinion
- Disclaimer Opinion

Internal control over financial reporting:

- Material weakness (es) identified? Yes No
- Significant deficiencies identified that are not considered to be material weakness (es)? Yes None Reported
- Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major programs:

- Material weakness (es) identified? Yes No
- Significant deficiencies identified that are not considered to be material weakness (es)? Yes None Reported

Type of auditors' report issued on compliance for Major Programs:

- Unqualified Opinion
- Qualified Opinion
- Adverse Opinion
- Disclaimer

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

- Yes No

The Municipality's major programs were:

CFDA Number	Name of Federal Program
14.228	Community Development Block Grant / State's Program
14.255	ARRA- Community Development Block Grant / State's Program
14.871	Section 8 Housing Choice Vouchers

Dollar threshold used to distinguish between Type A and Type B Programs:

\$300,000

Auditee qualified as low-risk auditee?

- Yes No

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING	12-01
CATEGORY	INTERNAL CONTROL
NONCOMPLIANCE	CAPITAL ASSETS
TOPIC SENTENCE	FIXED \ CAPITAL ASSETS AND EXPENDITURES – SUBSIDIARY LEDGER.
CONDITION	The Municipality has not maintained complete and adequate records in order to obtain sufficient, competent evidential matter with respect to the Capital Assets reported in governmental activities and, accordingly, the amount by which this departure would affect the assets, net assets, and expenses of the governmental activities is not determinable.
CRITERIA	Chapter IX, Article 9.002 of State Act Number 81 of August 30, 1991 states that the municipality should maintain updated property accounting records. Also the GASB Statements No. 34 <i>Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments</i> require that all capital assets, including infrastructure, must be presented in the Statements of Net Assets and that these assets must be depreciated during its useful life. Also, provisions of GASB Statement No. 42, <i>Accounting and Financial Reporting of Impairments of Capital Assets and for Insurance Recoveries</i> , requires the Municipality to evaluate prominent events or changes in circumstances affecting capital assets to determine whether an impairment of a capital asset has occurred. Furthermore, provisions of GASB Statement No. 51, <i>Accounting and Financial Reporting for Intangible Assets</i> , require that all intangible assets not specifically excluded by its scope provisions be classified as capital assets.
CAUSE	Competent and sufficient evidential matter related to the capital assets was not available to support the value, completeness and ownership of these assets.
EFFECT	The Municipality’s Government Wide Financial Statements do not present fairly, the financial position of the governmental activities, and the change in financial position of the Municipality.
RECOMMENDATION	We recommend that the Municipality should continue the compilation of documents to support the value, completeness and ownership of its capital assets, to comply with the requirements of the GASB Statement No. 34, GASB Statement No. 42 and GASB Statement No.51.
QUESTIONED COSTS	NONE

**MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO**
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING

12-01 (CONTINUED)

**MANAGEMENT RESPONSE
AND CORRECTIVE ACTION PLAN**

Actually, the Municipality's Finance Department staffs continue updating the capital assets subsidiary ledger in order to comply with the GASB No. 34 capital assets requirements for the fiscal year ended on June 30, 2012.

Implementation Date: August 31, 2013

Responsible Person: Mr. Adán Feliciano
Finance Department Director

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING	12-02
CATEGORY	INTERNAL CONTROLS
TOPIC SENTENCE	ACCOUNTING SYSTEM
CONDITIONS	The accounting system and manuals used by the Municipality to account and register the financial transactions during the fiscal year does not provide for the summarization of transactions that permit the preparation of Municipality's financial statements in conformity with the General Accepted Accounting Principles of the United States of America (GAAP).
CRITERIA	According to Article 8.010 (a) and (b) of Law Num. 81 for the Municipalities of Puerto Rico, the computerized system and the procedures of accounting and property will be design so that it allows the Municipality to carry out its functions, at the same time as they serve to maintain an uniform and coordinated accounting, that provide a complete picture of the financial operations of the Municipality and the necessary financial information that assist the Municipality Legislature, the Governor, and the Secretary of the Puerto Rico Treasury Department in the performance of its respective responsibilities. Municipalities accounting will be based on funds, Generally Accepted Accounting Principles and the requirements established by the Governmental Accounting Standard Board. Also the pronouncements of the National Committee on Governmental Accounting and the "Blue Book" will be used to design municipalities' accounting systems and fiscal procedures.
CAUSES	Municipality's accounting system and financial reports are subject to State's agencies requirements which does not allow nor provide the Municipality with the necessary tools capable of recapturing the financial information and provide financial statements.
EFFECT	<p>The lack of an adequate accounting system which can captures all the financial information and generates Municipality's financial statements for each fiscal year affect the Municipality ability to measure the financial and nonfinancial performance of programs and activities; adequately safeguard significant assets and properly record various transactions; and hinder the Municipality from having reliable financial information to operate in an economical, efficient, and effective manner.</p> <p>Sound decisions on the current results and future direction of vital programs and policies are made more difficult without timely, reliable and useful financial performance information.</p>

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING	12-02 (CONTINUED)
RECOMMENDATION	The Municipality should establish and implement the necessary measures that allow the summarization of the financial transactions in order to prepare the financial statements in conformity with GAAP.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>We are considering alternatives to for the acquisition of a new accounting software, and therefore, we will hope to solve our accounting system condition in a near future. But in a short term, we implemented the Peachtree accounting software as an alternate tool in order to maintain monthly reconciled records of all of our funds.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Adán Feliciano Finance Department Director</p>

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-03
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/STATE'S PROGRAM (CFDA NO. 14.228) / ARRA- COMMUNITY DEVELOPMENT BLOCK GRANT/STATE'S PROGRAM (CFDA NO. 14.255) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	INTERNAL CONTROL / COMPLIANCE
NONCOMPLIANCE	PROCUREMENT STANDARDS
TOPIC SENTENCE	LACK OF REQUIRED CONTRACT CLAUSES AND PROCUREMENT DOCUMENTATION
CONDITION	<p>In testing compliance with the procurement requirement, we examined 6 contracts for construction projects which were paid during the fiscal year 2011-12. In relation to such examination we determined the following:</p> <p>1. Absence of contract clauses required by the program regulation, as follows:</p> <ul style="list-style-type: none">• three contracts did not include clauses regarding contractual legal remedies when contractor violates term and termination by grantee for default.• one contract did not includes a provision for granting access to GAO and other federal agencies to books and documents.• four contracts did not include clauses regarding retention of all required records for three years after grantees makes final payment and all other pending matters are closed.• any of the reviewed contracts include provisions for suspension and debarment, Clear Air and Clear Water Act, and Energy Policy and Conservation Act.
CRITERIA	Code of Federal Regulations, Subpart C, 24 CFR Section 85.36 (i) (1-13) states that subgrantee's contract must contain provisions in paragraph (i) of these Sections. Federal agencies are permitted to require changes, remedies, changed conditions, access and records retention, suspension of work, and other clauses approved by the Office of Procurement Policy.

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-03 (CONTINUED)
CAUSE	The Municipality did not maintain appropriate procurement standard procedures in order to assure that contractor complies with program requirements.
EFFECT	Municipality is not in compliance with the mentioned federal regulations.
RECOMMENDATION	We recommend management to update contract model according with the federal requirement and establish internal controls to assure compliance with procurement requirements.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	To correct this condition, we will modify our master contract to include all the general clauses required by Federal and State laws. Implementation Date: August 31, 2013 Responsible Person: Mrs. Lumari Torres Pérez Federal Programs Department Director

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-04
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/STATE'S PROGRAM (CFDA NO. 14.228) / ARRA- COMMUNITY DEVELOPMENT BLOCK GRANT/STATE'S PROGRAM (CFDA NO. 14.255) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	INTERNAL CONTROL / COMPLIANCE
NONCOMPLIANCE	SUSPENSION AND DEBARMENT
TOPIC SENTENCE	ABSENCE OF CONTROLS TO ASSURE COMPLIANCE WITH SUSPENSION AND DEBARMENT
CONDITIONS	In testing procurement, suspension and debarment, we did not find evidence indicating that the Municipality performs procedures to assure that the individuals and entities which are granted with contracts are not suspended or debarred from participation in federal programs.
CRITERIA	As stated in 24 CFR 85.35 grantee and subgrantee must not make any award or permit any award (subgrant or contract) at any tier to any party which is debarred or suspended or is otherwise excluded from or ineligible for participation in Federal assistance programs under Executive Order 12549, "Debarment and Suspension".
CAUSE	The Municipality has no policies and procedures for the use of the List of Parties Excluded from federal procurement or non-procurement programs to assure that they do not award assistance to listed parties.
EFFECT	As a result of this deficiency, the Municipality could have procured goods or services from organizations and individuals that are suspended or debarred which could result in cost disallowances by the federal awarding agency.
RECOMMENDATION	The Municipality should amend their procurement procedures and include a step to verify whether or not the individual or entity is on the list of parties excluded from federal participation in procurement and non-procurement programs. The Municipality should also require the entities or individuals to submit a certification stating that they are not suspended or debarred or add a clause or condition to the covered transaction with that entity.

**MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO**
Schedule of Findings and Questioned costs
Year Ended June 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 12-04 (CONTINUED)

QUESTIONED COSTS None

MANAGEMENT RESPONSE

AND CORRECTIVE ACTION PLAN

We will include in our procurement procedures a step to verify through the electronic version available on the Internet whether or not the individual or entity is on the list of parties excluded from federal participation in procurement and non-procurement programs.

Implementation Date: August 31, 2013

Responsible Person: Mrs. Lumari Torres Pérez
Federal Programs Department Director

END OF SCHEDULE

MUNICIPALITY OF GUAYANILLA
COMMONWEALTH OF PUERTO RICO
 Schedule of prior Audit's Findings and Questioned costs
 Year Ended June 30, 2012

(1) Audit Findings that have been Fully Corrected:

Finding Number	CFDA	Questioned Cost	Comments
11-04 Davis Bacon Act	14.228	None	Corrected
11-07 Special Tests and Provisions	14.228	None	Corrected
10-04 Davis Bacon Act	14.228	None	Corrected
09-04 Davis Bacon Act	14.228	None	Corrected
05-III-08 Davis Bacon Act	14.228	None	Corrected

(2) Audit Findings not corrected or Partially Corrected:

Finding Number	CFDA	Questioned Cost	Comments
11-03 Cash Management	14.228	None	Partially Corrected
11-05 Suspension and Debarment	14.228	None	Situation Still Prevails
11-06 Procurement	14.228	None	Situation Still Prevails
10-03 Suspension and Debarment	14.228	None	Situation Still Prevails
10-05 Procurement	14.228	None	Situation Still Prevails
10-06 Procurement	14.228	None	Situation Still Prevails
09-03 Suspension and Debarment	14.228	None	Situation Still Prevails

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

NONE

(3) Audit findings is no longer valid:

NONE

END OF SCHEDULE