



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

***BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY
INFORMATION AND INDEPENDENT
AUDITORS' REPORT
(WITH ADDITIONAL REPORTS REQUIRED
UNDER THE OMB CIRCULAR A-133)***

***AS OF AND FOR THE FISCAL YEAR ENDED
JUNE 30, 2011***



***Hon. Pedro J. García-Figueroa
Mayor***

***Mrs. Miriam Irizarry
Finance Director***

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

TABLE OF CONTENTS

	<u>PAGE</u>
<u>FINANCIAL SECTION</u>	
Independent Auditors' Report	1-2
Management's Discussion and Analysis	3-14
Basic Financial Statements:	
Government-wide Financial Statements:	
Statement of Net Assets	15
Statement of Activities	16
Fund Financial Statements:	
Balance Sheet - Governmental Funds	17
Reconciliation of the Balance Sheet - Governmental Funds to the Statement of Net Assets	18
Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) - Governmental Funds	19
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) - Governmental Funds to the Statement of Activities	20
Notes to Basic Financial Statements	21-51
Required Supplementary Information:	
Budgetary Comparison Schedule – General Fund	52
Notes to Required Supplementary Information - Budgetary Comparison Schedule – General Fund	53-54
Supplementary Information:	
Financial Data Schedule	55-56
Notes to Supplementary Information – Financial Data Schedule	57
<u>SINGLE AUDIT SECTION</u>	
Supplementary Information:	
Schedule of Expenditures of Federal Awards	58
Notes to Schedule of Expenditures of Federal Awards	59-60
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	61-62
Independent Auditors' 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 OMB Circular A-133	63-64
Schedule of Findings and Questioned Costs	65-67
Schedule of Status of Prior Years Audit Findings and Questioned Costs	68

FINANCIAL SECTION

INDEPENDENT AUDITORS' REPORT

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INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Hormigueros (the Municipality), as of and for the year ended June 30, 2011, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Hormigueros, as of June 30, 2011, 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.

In accordance with Government Auditing Standards, we have also issued our report dated March 21, 2012, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provision of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Budgetary Comparison Schedule – General Fund on pages 3 through 14 and 52 through 54 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's financial statements as a whole. The accompanying Schedule of Expenditures of Federal Awards on page 58 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 not a required part of the financial statements. The Schedule of Expenditures of Federal Awards is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The Financial Data Schedule supplementary information on pages 55 and 57 is required by the Uniform Reporting Standards of the Department of Housing and Urban Development. The Schedule of Expenditures of Federal Awards and the Financial Data Schedule supplementary information have been subjected to the auditing procedures applied in the audit of the basic 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 or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the financial statements as a whole.

A handwritten signature in cursive script, appearing to read "C. Harris, Davis & Harting LLP".

San Juan, Puerto Rico
March 21, 2012

Stamp 2632886 was affixed
to the original

MANAGEMENT'S DISCUSSION AND ANALYSIS

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

The discussion and analysis of the Municipality of Hormigueros' financial performance will provide an overall review of the Municipality's financial activities for the fiscal year ended June 30, 2011. The intent of this discussion and analysis is to look at the Municipality's financial performance as a whole; this section should be read in conjunction with the basic financial statements to obtain a better understanding of the financial position and the results of operations of the Municipality. We encourage readers to consider the information presented here in conjunction with the Municipality's financial statements, which follow this analysis.

FINANCIAL HIGHLIGHTS

Highlights for Government-wide Financial Statements

Information reported in the government-wide statements is based on the economic resources measurement focus and the accrual basis of accounting:

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2011 by \$35,202,747 (net assets). This represents an increase of 5% with respect to fiscal year 2010.
- Revenues increased by 8% and expenses decreased by 0.11% in comparison with the previous year.
- Change in net assets increased 264% compared to change in net assets of fiscal year 2010.

Highlights for Fund Financial Statements

Fund financial statements presents information of the most significant funds of the Municipality based on the current financial resources measurement focus and the modified accrual basis of accounting:

- During the year 2011 the Municipality implemented GASB Statement No. 54 Fund Balance Reporting and Governmental Fund Type Definitions ("GASB No. 54"). Certain information from the year 2010 has been restated.
- A net change of (\$597,143) in the fund balances of the Municipality's governmental funds resulted in a reported combined ending fund balances of \$5,011,038 in fiscal year 2011. Approximately 23% of the total combined fund balances is unrestricted (assigned or unassigned).
- For the fiscal year 2011, the General Fund reported an excess of revenues and other financing sources over expenditures and other financing uses of \$570,824. The unassigned fund balance amounts to \$417,501 or 4% of total General Fund Expenditures.

General Financial Highlights

- The investment in capital assets as of June 30, 2011 was \$46,512,631 (net of depreciation).
- Long-term debt decreased to \$18,430,399 or approximately 6% with respect to the prior year.
- On a budgetary basis, actual expenditures exceeded actual revenues by \$114,793.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

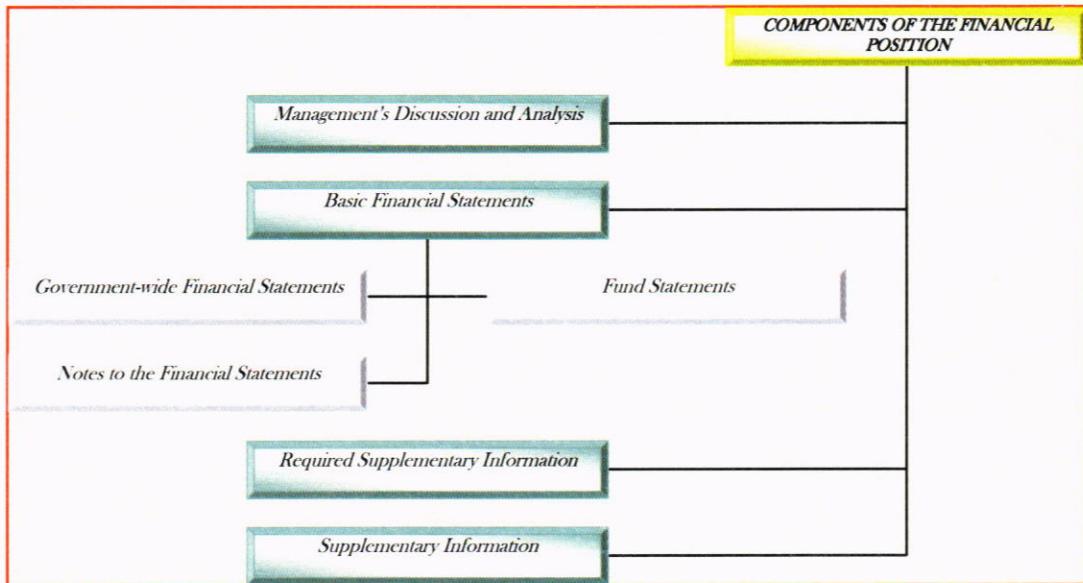
MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

OVERVIEW OF THE FINANCIAL STATEMENTS

The Municipality's financial report comprises four components:

- Management's discussion and analysis (presented here)
- basic financial statements
- required supplementary information
- supplementary information



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

➤ **Government-Wide Statements**

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

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

➤ ***Fund Financial Statements***

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

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

The governmental fund statements focus on major funds. The Municipality's major funds are the general fund (which accounts for the main operating activities of the Municipality) and funds that comply with a minimum criterion (percentage of the assets, liabilities, revenues or expenditures). Funds that do not comply with this criterion are grouped and presented in a single column as other governmental funds.

➤ ***Notes to financial statements***

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

➤ ***Required supplementary information***

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

➤ ***Supplementary information***

The required supplementary information is followed by a financial data schedule containing financial information of the Section 8 Housing Choice Voucher Program administered by the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

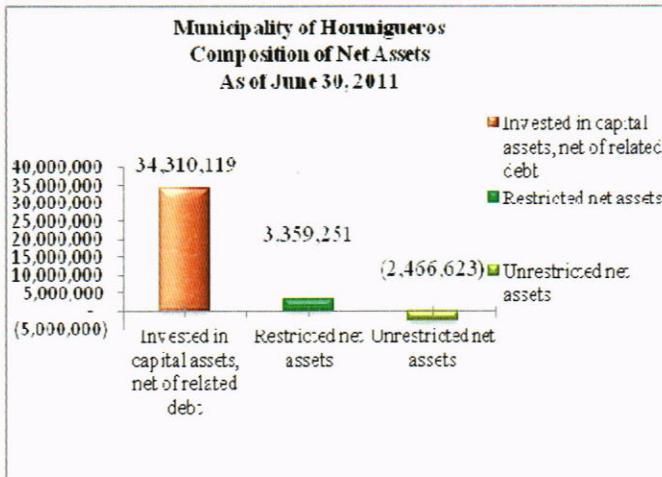
Net Assets

The following table presents a summary of the Statement of Net Assets as of June 30, 2011 and 2010:

TABLE 1

<i>Summary Statement of Net Assets As of June 30,</i>		
	Governmental Activities	
	2011	2010
Assets		
Current and other assets	\$ 9,956,882	\$ 11,110,785
Capital assets	46,512,631	45,042,123
Total assets	<u>\$ 56,469,513</u>	<u>\$ 56,152,908</u>
Liabilities		
Current and other liabilities	\$ 2,836,368	\$ 3,121,623
Long-term liabilities	18,430,399	19,648,160
Total liabilities	<u>21,266,766</u>	<u>22,769,783</u>
Net assets		
Invested in capital assets, net of related debt	34,310,119	32,920,882
Restricted	3,359,251	3,904,480
Unrestricted	(2,466,623)	(3,442,237)
Total net assets	<u>\$ 35,202,747</u>	<u>\$ 33,383,125</u>

Net assets (assets over liabilities) may serve over time as a useful indicator of a government's financial position. At the close of the fiscal year, the assets of the Municipality exceeded its liabilities by \$35,202,747, representing an increase of 5% with respect to fiscal year 2010. The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure) less accumulated depreciation and less any related outstanding debt used to acquire those assets.



The Municipality uses these assets to provide services to its citizens and, consequently, these assets are not available for future spending. The resources needed to repay the debt related to these capital assets must be provided from other sources because capital assets are not generally liquidated for the purpose of retiring debt. Restricted net assets represent resources that are subject to external restrictions on how they may be used. Unrestricted net assets are the part of the net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

As of June 30 2011, the Municipality presented an unrestricted net assets deficit. This deficit primarily arises from long-term obligations such as compensated absences and debts to CRIM for which the Municipality did not provide funding in previous budgets. Historically, such obligations have been budgeted on a "pay as you go" basis without providing funding for their future liquidation. In addition, operational loans and certain general obligation bonds do not have a related capital asset to be reported as invested in capital assets, net of related debt. Therefore, they are reported as part of the unrestricted net assets section.

Changes in net assets

The following table summarizes the changes in net assets for the fiscal years ended 2011 and 2010:

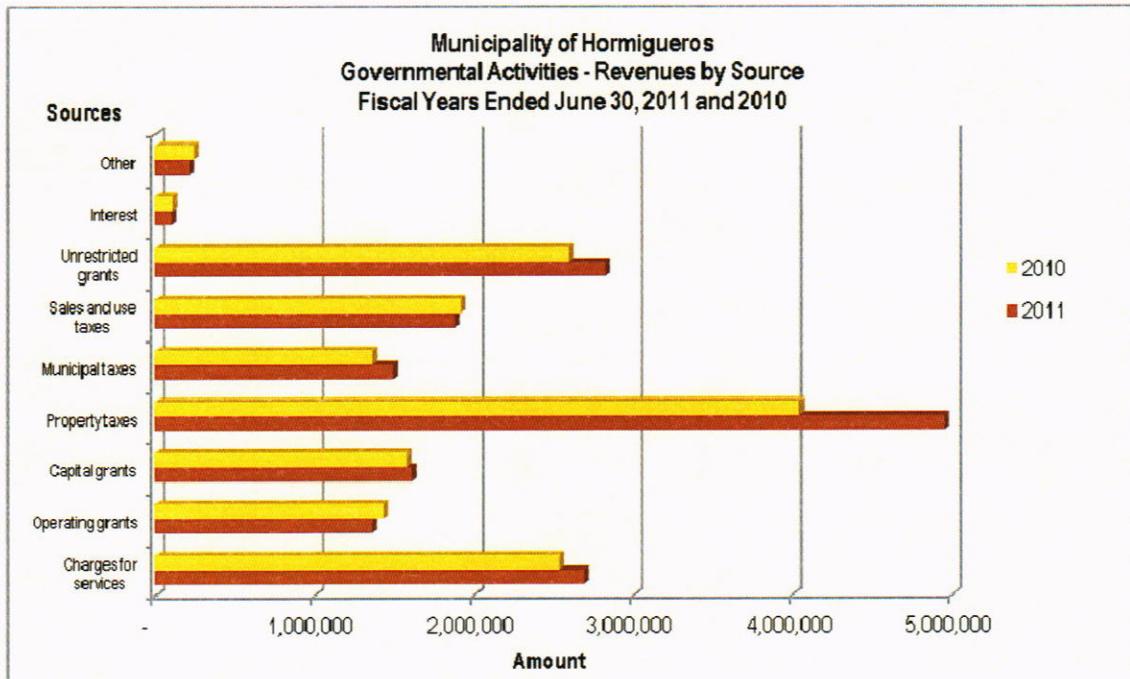
TABLE 2

<i>Summary of Changes in Net Assets As of June 30,</i>			
	Governmental Activities		
	2011	2010	
Program revenues:			
Fees, fines and charges for services	\$ 2,686,880	\$ 2,532,365	
Operating grants and contributions	1,360,438	1,429,310	
Capital grants and contributions	1,607,230	1,576,164	
General revenues:			
Property taxes	4,953,461	4,041,139	
Municipal license taxes	1,491,837	1,363,030	
Sales and uses taxes	1,875,803	1,915,141	
Grants and contributions not restricted to specific programs	2,819,648	2,595,611	
Interest	102,577	111,103	
Other	212,956	244,239	
Total revenues	17,110,830	15,808,102	
Expenses:			
General government	6,553,540	6,579,699	
Public works and sanitation	3,310,518	3,521,556	
Public safety	856,420	774,509	
Culture and recreation	1,271,279	1,357,263	
Health	380,079	370,703	
Housing, welfare and community development	2,211,971	2,017,650	
Education	38,419	31,369	
Interest on long term debt	668,982	654,827	
Total expenses	15,291,208	15,307,576	
Change in net assets	1,819,622	500,526	
Net assets-beginning of year	33,383,125	32,882,599	
Net assets-end of year	\$ 35,202,747	\$ 33,383,125	

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Fiscal year ended June 30, 2011

FIGURE 1



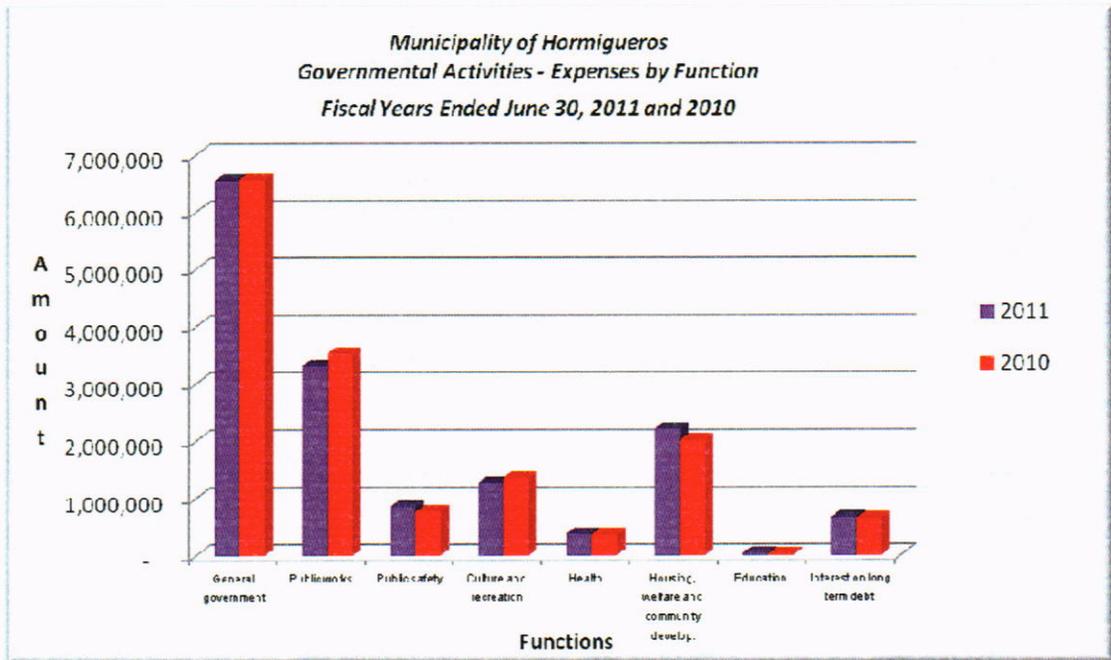
Approximately 29% of the Municipality's revenues came from property taxes, 17% from operating and capital grants, and 16% from grants and contributions not restricted to specific programs. Revenues increased 8% in comparison with fiscal year 2010. This net increase is mostly affected by a combination of the following: (1) an increase in property tax income of 23% as a result of the amnesty, (2) a 13% decrease in other income, (3) a 9% increase in both unrestricted grants and municipal taxes, (4) an 8% decrease in interest revenue due to the decrease in interest from investments and interest from loans, (5) a 6% increase in fees, fines and charges for services because of the increase in PREPA and the rent of former Hormigueros Auto Parts building that was not in the previous years, and (6) the 5% decrease in operating grants.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

FIGURE 2



The Municipality's expenses cover a range of services. The largest expenses are general government representing approximately 43%, public works and sanitation with 22%, and housing, welfare and community development with 14% of total expenses. Program revenues of the Municipality covered 37% of total expenses.

Expenses decreased 0.11% in comparison with previous fiscal year. This includes a combination of changes. There was an increase of 20% in education, an increase in housing, welfare and community of 10%, an increase of 11% in public safety, and a 6% decrease in both Public Works and Culture and Recreation.

As noted previously the increase in revenues, combined with a decrease in expenses, resulted in an increase of net assets of 264% when compared with the net change in net assets reported in fiscal year 2010. The following table focuses on the cost of each of the Municipality's largest programs as well as each program's net cost (total cost less fees generated by the programs and program-specific intergovernmental aid):

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

TABLE 3

<i>Net Cost of Municipality's Governmental Activities Fiscal years ended June 30,</i>				
Functions/Programs	Total Cost of Services		Net Cost of Services	
	2011	2010	2011	2010
General government	\$ 6,553,540	\$ 6,579,699	\$ (3,663,829)	\$ (3,831,736)
Public works and sanitation	3,310,518	3,521,556	(1,926,394)	(2,090,947)
Public safety	856,420	774,509	(832,450)	(769,613)
Culture and recreation	1,271,279	1,357,263	(1,252,694)	(1,323,483)
Housing, welfare and community development	2,211,971	2,017,650	(873,813)	(697,059)
Other	1,087,480	1,056,899	(1,087,480)	(1,056,899)
	<u>\$ 15,291,208</u>	<u>\$ 15,307,576</u>	<u>\$ (9,636,660)</u>	<u>\$ (9,769,737)</u>

Some of the cost of governmental activities was paid by those who directly benefited from the programs (\$2,686,880) and other governments and organizations that subsidized certain programs with grants and contributions (\$2,967,668). The (\$9,636,660) net cost of services was fully covered by other general revenues including property, municipal license, and sales and use taxes.

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

Governmental funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending. Such information is useful in assessing the Municipality's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a Municipality's net resources available at the end of a fiscal year. During the year 2011 the Municipality implemented GASB Statement No. 54 *Fund Balance Reporting and Governmental Fund Type Definitions* ("GASB No. 54"). This statement establishes accounting and reporting standards for all governments that report governmental funds. It also establishes criteria for classifying fund balances into specially defined classifications and clarifies definitions for governmental fund types. Previously classified reserved and unreserved fund balances are now reported as nonspendable, restricted, committed, assigned or unassigned. As a result of the implementation the Law No. 52 special fund was reclassified from the general fund to other governmental funds.

For the fiscal year ended June 30, 2011, the governmental funds reported ending fund balances of \$5,011,038, a net decrease of \$597,143 in comparison with the prior year. This net decrease was caused by the combination of various increases and decreases. Primarily by a decrease of (\$685,842) in the Other Governmental Funds, an increase in General Fund of \$570,824 and a decrease of (\$307,504) in the 3,000,000 Bond Issuance Fund due to the culmination of the fund. Of total fund balances, \$1,149,681 (or 23%) constitutes unrestricted fund balance, which is comprised of funds assigned by the Mayor or the Finance Director as well as unassigned funds. The remainder of the fund balance is restricted to indicate that it is not available for new spending. The general fund is the operating fund of the Municipality. The fund balance of the general fund represents 33% of total ending fund balance. Assigned portions of the unrestricted fund balance are distributed as follows 1) \$13,517 assigned for general public works and sanitation; 2) \$1,024,997 assigned for capital projects; 3) \$177,836 assigned for encumbrances and 4) \$874 assigned for general government and other purposes.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

The remainder of the unrestricted fund balance or \$417,501 is unassigned fund balance, which represents 33% of the total fund balance of the general fund and 4% of total general fund expenditures. For the year ended June 30, 2011, the fund balance of the general fund increased by \$570,823. Of this change \$849,519 pertains to other special funds (with self-imposed restrictions) included as part of the general fund (resources to finance these special funds were provided in current and previous years).

General fund budgetary highlights

The general fund original budget for the fiscal period 2011 presented an increase of 12% with respect to the prior year budget due to an increase in the estimated amount of property tax revenues, intergovernmental revenues and other revenues.

Amendments to the original budget are approved by the Municipal Legislature. During the fiscal year 2011 amendments to budget expenditures for a net amount of \$817,071 were approved. Of this net amount \$751,000 represented a readjustment of current year budget with prior year's budgetary surpluses, \$47,000 were transferred from deposits and sureties payable, and \$19,071 were transferred from the public schools maintenance fund. Actual revenues exceeded the revised budgeted revenues by \$636,554. The most significant variances were \$394,564 from property taxes, \$242,687 from intergovernmental subsidies, (\$96,624) from municipal license taxes, \$93,403 from fees, fines and charges for services, and (\$56,741) from sales and use tax revenue. The Municipality reported a positive variance of \$38,060 between revised budgeted appropriations and actual expenditures primarily due to a positive variance of \$17,386 in general government expenditures, and \$16,391 in Health Expenditures; ending with a total net negative variance of (\$114,793).

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital assets

At the end of the fiscal year, the Municipality has invested \$46,512,631 in a broad range of capital assets, including buildings, parks, roads, bridges, land and equipment. This amount represents a net increase of 3% over the prior year.

TABLE 4

<i>Capital Assets As of June 30,</i>		
	Governmental Activities	
	2011	2010
Non-depreciable assets:		
Land	\$ 8,165,495	\$ 7,702,495
Construction in progress	10,310,004	10,367,690
Depreciable assets (net):		
Land improvements	977,415	657,720
Buildings and buildings improvements	18,735,621	17,279,331
Infrastructure	5,715,749	6,114,474
Vehicles, machinery and equipment	2,608,347	2,920,413
Total	\$ 46,512,631	\$ 45,042,123

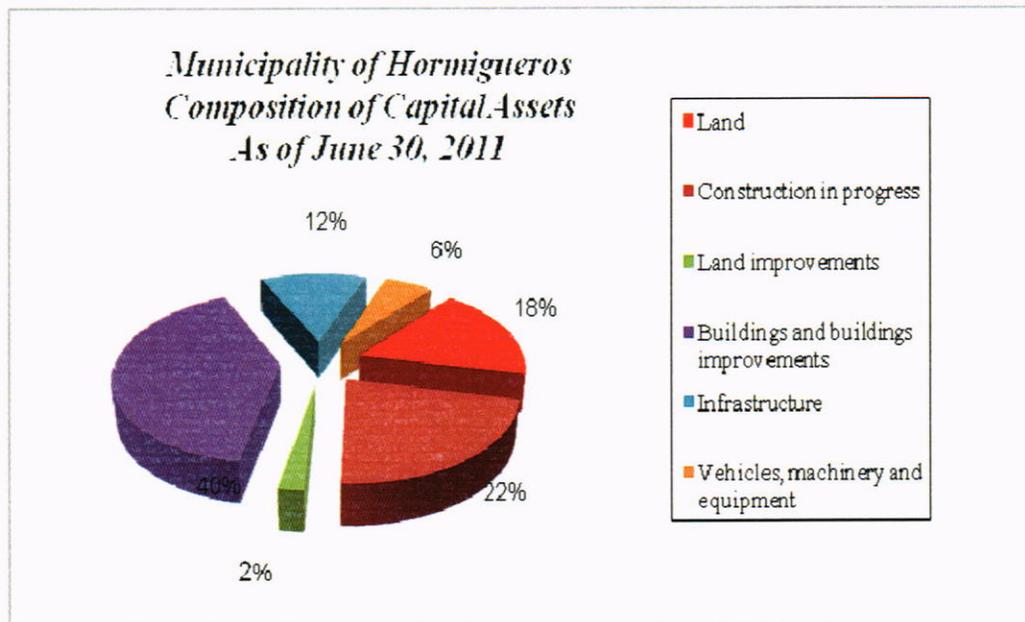
COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

Certain projects are still in construction in progress as of June 30, 2011. The most significant of these projects are the construction of "Lavadero Sanitary Sewer System", the remodeling of the Fine Arts School building, Segundo Ruiz Belvis recreational park, Jose A. Rosas San Romualdo's Multiuse Center, "Vista a la Bahia" plaza, and the construction of a 400 meters race track with reported costs of \$4,830,887, \$1,412,025, \$883,213, \$375,315, \$348,347 and \$1,639,492 respectively.

Figure 3



The Municipality's fiscal year 2011-2012 capital budget calls for a significant amount of new and continuous projects including the continuance of the construction of Lavadero Sanitary Sewer system, which is being financed through grants from USDA Rural Development, P.R. Water and Sewer Authority and Commonwealth's stimulus plan funds. Other projects still in progress in this fiscal year 2012 will include the rehabilitation of the Eureka sugar mill, the access road to San Romualdo community through Santana trail, the improvements to the municipal landfill, and the improvements of various basketball courts in different communities, among others.

The Municipality will continue its public policy of land acquisition for the development of necessary projects and to promote the development of low cost housing, and commercial spaces. Also, the improvement of municipal roads, sidewalks and gutters, and other infrastructure will be continued during 2011-2012. All these projects will be financed through Commonwealth and Federal grants, Commonwealth Legislature and Municipal funds. More detailed information about the Municipality's capital assets and future projects is presented in Note H to the financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

Long term debt

At year-end, the Municipality has \$ 15,249,000 in general and special bonds and notes outstanding, a decrease of 6% with respect to fiscal year 2010. This decrease was due to payment of year principal amounts of previously issued notes. No new debt was acquired for this year.

TABLE 5

<i>Outstanding Long-term Debt Fiscal years ended June 30,</i>		
	Governmental Activities	
	2011	2010
General and special obligation bonds and notes	\$ 15,249,000	\$ 16,160,000
Compensated absences	1,290,609	1,315,771
Payable to CRIM – prior years doubtful accounts	4,186	4,387
Christmas bonus payable	166,521	177,402
Payable to CRIM - LIMS	16,998	49,534
Estimated landfill closing costs	1,249,607	1,212,306
Note payable to SIFC	-	94,711
Property Taxes – current year	89,858	311,847
Payable to PREPA	363,620	322,202
Total	\$ 18,430,399	\$ 19,648,160

The Municipality reported a decrease in other long-term debts of \$1,217,761. This decrease was primarily due to the amount payable to CRIM because of a property tax negative liquidation of CRIM in 2009 that was due and paid this year, and the payment of the outstanding amount of the note payable to SIFC. More detailed information about the Municipality's long-term liabilities is presented in Note J to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's officials considered certain factors when setting the fiscal year 2011-2012 budget. One of these factors is the economy. Among economic areas considered are the population growth estimates, personal income, housing statistics and unemployment rates. The Municipality's unemployment rate now stands at 14% which compares with the Commonwealth rate of 15.2%.

For fiscal year 2011-2012 the Municipality applied a conservative approach in development budget estimates. Amount available for appropriations in the General Fund totals \$10,558,515, a decrease of approximately 0.31% with respect to prior fiscal year estimates. Budgeted expenditures are expected to fall according to the decrease of budgeted revenues. If these estimates are realized, the Municipality's budgetary general fund balance is expected to decrease modestly by the close of 2012 fiscal year. In addition to the general fund estimated budget the Municipality plans to submit Federal and Commonwealth funds proposals for welfare and community development as well as permanent capital improvements and public works.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2011

CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, and creditors with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability for the money it receives. If you have questions about this report or need additional information, contact the Municipality's Director of Finance at P.O. Box 97, Hormigueros, Puerto Rico 00660.

BASIC FINANCIAL STATEMENTS

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

**STATEMENT OF NET ASSETS
JUNE 30, 2011**

ASSETS	Governmental Activities
Cash and cash equivalents	\$ 2,495,254
Receivables, net:	
Municipal license taxes	127,476
Sales and use taxes	112,218
Lease (note C)	188,724
Other	95,197
Due from (note D):	
Commonwealth Government	833,731
Federal Government	354,129
Restricted assets:	
Cash and cash equivalents	1,278,353
Cash with fiscal agents	4,178,544
Investment held with fiscal agent (note B)	73,335
Deferred bond issuance costs, net of accumulated amortization of \$78,672	96,362
Other assets (note F)	123,559
Capital assets (note H):	
Land and construction in progress	18,475,499
Other capital assets, net	28,037,132
Total capital assets, net	<u>46,512,631</u>
Total assets	<u><u>\$ 56,469,513</u></u>

LIABILITIES

Accounts payable and accrued liabilities	\$ 1,401,308
Interest payable	329,569
Due to:	
Commonwealth Government	1,182
Deferred revenues:	
Municipal license taxes	1,029,496
Intergovernmental - Federal grants	74,812
Long term liabilities (note J):	
Due within one year	1,607,163
Due in more than one year	16,823,236
Total liabilities	<u>21,266,766</u>

NET ASSETS

Invested in capital assets, net of related debt	34,310,119
Restricted for:	
Capital projects	643,961
Debt service	2,608,496
Other purposes	106,794
Unrestricted (deficit)	(2,466,623)
Total net assets	<u><u>\$ 35,202,747</u></u>

The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

BALANCE SHEET -
GOVERNMENTAL FUNDS
JUNE 30, 2011

Major Funds

	General	Community Development Block Grant Program	Commonwealth Legislature Resolutions	Debt Service	Lavadero Sanitary Sewer System	\$ 3,000,000 Bond Issuance	Other Governmental Funds	Total Governmental Funds
Assets								
Cash and cash equivalents	\$ 2,495,254	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,495,254
Receivables, net:								
Municipal license taxes	127,476	-	-	-	-	-	-	127,476
Sales and use taxes	112,218	-	-	-	-	-	-	112,218
Lease	188,724	-	-	-	-	-	-	188,724
Other	71,216	-	-	-	-	-	23,981	95,197
Due from:								
Commonwealth Government	557,960	-	23,358	56,805	-	-	195,608	833,731
Federal Government	-	316,581	-	-	-	-	37,548	354,129
Other funds (note E)	296,989	-	-	-	-	-	-	296,989
Restricted assets:								
Cash and cash equivalents	-	65,081	681,761	-	242,300	-	263,455	1,252,597
Cash with fiscal agents	-	-	-	2,889,988	25,756	-	1,288,556	4,204,300
Investment held with fiscal agent	-	-	-	-	-	73,335	-	73,335
Other Asset	-	-	-	-	-	-	1,659	1,659
Total assets	\$ 3,849,837	\$ 381,662	\$ 705,119	\$ 2,946,793	\$ 268,056	\$ 73,335	\$ 1,810,807	\$ 10,035,609
Liabilities and fund balances (deficit)								
Liabilities:								
Accounts payable and accrued liabilities	\$ 310,098	\$ 268,006	\$ 218,465	\$ -	\$ 392,265	\$ 73,335	\$ 139,140	\$ 1,401,309
Matured bonds and interest payable	-	-	-	972,815	-	-	-	972,815
Due to:								
Commonwealth Government	1,182	-	-	-	-	-	-	1,182
Other funds	-	91,411	-	8,812	-	-	196,766	296,989
Deferred revenues (notes C, I, and M):								
Municipal license taxes	1,156,586	-	-	-	-	-	-	1,156,586
Lease	188,724	-	-	-	-	-	-	188,724
Intergovernmental - Commonwealth Government	514,712	-	23,358	-	-	-	36,351	574,421
Intergovernmental - Federal grants	-	295,764	-	-	-	-	92,012	387,776
Other	43,810	-	-	-	-	-	960	44,770
Total liabilities	2,215,112	655,181	241,823	981,627	392,265	73,335	465,228	5,024,571
Fund balances (deficits):								
Restricted	-	16,283	463,296	1,965,166	25,442	-	1,391,170	3,861,357
Assigned	1,217,224	-	-	-	-	-	-	1,217,224
Unassigned	417,501	(289,802)	-	-	(149,651)	-	(45,591)	(67,543)
Total fund balances (deficits)	1,634,725	(273,519)	463,296	1,965,166	(124,209)	-	1,345,579	5,011,038
Total liabilities and fund balances (deficits)	\$ 3,849,837	\$ 381,662	\$ 705,119	\$ 2,946,793	\$ 268,056	\$ 73,335	\$ 1,810,807	\$ 10,035,609

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

**RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS TO THE
STATEMENT OF NET ASSETS
JUNE 30, 2011**

Total governmental fund balances:		\$ 5,011,038
Amounts reported for governmental activities in the Statement of Net Assets are different because:		
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds:		46,512,631
Other assets used in governmental activities are not current financial resources and therefore are not reported in the funds:		
Deferred charges - bond issuance costs	\$ 96,362	
Other assets - cash deposit	121,900	218,262
Other assets are not available to pay current-period expenditures and therefore are deferred in the funds:		
Receivables:		
Lease agreement	188,724	
Municipal licenses and sales tax	132,904	
Municipal properties rent	43,810	
HOPWA participants	960	
Due from Commonwealth Government:		
P.R. Infrastructure Financing Authority	1,386	
P.R. Department of Treasury - Christmas bonus reimbursement	139,277	
Commonwealth Legislature Resolutions	23,358	
P.R. Department of Education	17,489	
P.R. Electric Power Authority (PREPA)	363,620	
Due from Federal Government:		
P.R. Department of Health - HOPWA	4,048	
Federal Transit Administration	10,728	
P.R. Office of the Ombudsman for the Elderly - Titles III-D	2,425	
OCAM - Public Order Code	23,476	
OCAM - CDBG and CDBG - ARRA	295,764	1,247,969
Interest liabilities are not due and payable in the current period and, therefore, are not reported in funds		(92,754)
Long term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the funds:		
General obligation bonds and notes	(14,513,000)	
Note payable to CRIM-LIMS	(16,998)	
Note payable to CRIM-financing of delinquent accounts	(4,186)	
Compensated absences	(1,290,609)	
Christmas bonus payable	(166,521)	
Prior year property tax	(89,858)	
Estimated landfill closing costs	(1,249,607)	
P.R. Electric Power Authority (PREPA)	(363,620)	(17,694,399)
Net assets of governmental activities:		<u>\$ 35,202,747</u>

The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES (DEFICIT) -
GOVERNMENTAL FUNDS
FISCAL YEAR ENDED JUNE 30, 2011

	Major Funds							Total Governmental Funds
	General	Community Development Block Grant Program	Commonwealth Legislature Resolutions	Debt Service	Lavadero Sanitary Sewer System	\$ 3,000,000 Bond Issuance	Other Governmental Funds	
Revenues:								
Taxes:								
Property taxes (note L)	\$ 3,759,422	\$ -	\$ -	\$ 1,194,042	\$ -	\$ -	\$ -	\$ 4,953,464
Municipal license taxes (note M)	1,364,748	-	-	-	-	-	-	1,364,748
Sales and use taxes (note N)	1,496,690	-	-	389,659	-	-	-	1,886,349
Intergovernmental:								
Commonwealth government (note O)	4,227,292	-	75,000	-	-	-	451,741	4,754,033
Federal government	-	1,328,008	-	-	-	-	1,292,642	2,620,650
Fees, fines and charges for services	1,016,763	-	-	-	-	-	31,708	1,048,471
Interest	23,616	-	-	10,544	-	-	68,417	102,577
Other	146,657	-	-	-	-	-	47,128	193,785
Total Revenues	12,035,188	1,328,008	75,000	1,594,245	-	-	1,891,636	16,924,077
Expenditures								
Current:								
General government	6,073,324	123,203	-	-	-	-	247,623	6,444,150
Public works and sanitation	2,261,117	3,186	3,708	-	-	-	221,847	2,489,858
Public safety	701,786	-	-	-	-	-	7,773	709,559
Culture and recreation	753,166	-	-	-	-	-	-	753,166
Health	367,728	-	-	-	-	-	-	367,728
Housing, welfare and community development	579,524	229,882	1,500	-	-	-	1,262,800	2,073,706
Education	18,087	-	-	-	-	-	-	18,087
Capital outlays	354,705	1,038,489	357,197	-	-	307,403	749,948	2,807,742
Debt service:								
Principal	-	-	-	968,000	-	-	-	968,000
Interest	-	-	-	671,446	-	-	-	671,446
Bond issuance costs	-	-	-	-	-	-	-	-
Total expenditures	11,109,437	1,394,760	362,405	1,639,446	-	307,403	2,489,991	17,303,442
Excess (deficiency) of revenues over expenditures	925,751	(66,752)	(287,405)	(45,201)	-	(307,403)	(598,355)	(379,365)
Other financing sources (uses):								
Lease principal payments (note C)	69,806	-	-	-	-	-	-	69,806
Payment of long term debt to P. R. Electric Power Authority	(65,401)	-	-	-	-	-	-	(65,401)
Payment of long term debt to P. R. Department of Treasury	(222,183)	-	-	-	-	-	-	(222,183)
Transfers in	313,584	-	-	450,733	-	-	93	764,410
Transfers out	(450,733)	-	-	(225,996)	-	(101)	(87,580)	(764,410)
Total other financing sources (uses)	(354,927)	-	-	224,737	-	(101)	(87,487)	(217,778)
Net change in fund balances (deficit)	570,824	(66,752)	(287,405)	179,536	-	(307,504)	(685,842)	(597,143)
Fund balances (deficit) at beginning of year, as restated (Note T)	1,063,902	(206,767)	750,701	1,785,630	(124,209)	307,504	2,031,421	5,608,182
Fund balances (deficit) at end of year	\$ 1,634,726	\$ (273,519)	\$ 463,296	\$ 1,965,166	\$ (124,209)	\$ -	\$ 1,345,579	\$ 5,011,038

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The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

RECONCILIATION OF STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND
BALANCES (DEFICIT) - GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FISCAL YEAR ENDED JUNE 30, 2011

Net change in fund balances (deficit) - total governmental funds: \$ (597,143)

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

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

Expenditures for capital assets	\$ 2,807,742	
Less: current year depreciation	<u>(1,792,547)</u>	1,015,195

Governmental funds only report the proceeds received in the disposal of assets. In the Statement of Activities, a gain or loss is reported for each disposal. Thus, the change in net assets differs from the change in fund balance by the cost of the disposed asset:

(7,687)

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

Receivables:

Municipal licenses	127,089	
Sales tax	5,815	
Municipal properties rent	43,810	
Reimbursements from HOPWA participants	904	

Intergovernmental - Commonwealth Government:

P.R. Department of Treasury - Christmas bonus reimbursement (current)	132,590	
P.R. Department of Education	17,489	
Commonwealth Legislature Resolutions	23,176	
P.R. Electric Power Authority (PREPA)	219,335	

Intergovernmental - Federal Government:

OCAM - CDBG and CDBG - ARRA	277,173	
Federal Transit Administration	10,728	
OCAM - Public Order Code	23,476	
P.R. Department of Health - HOPWA	4,048	
P.R. Office of the Ombudsman for the Elderly - Titles III-D	<u>2,425</u>	888,058

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

CRIM - Property tax preliminary settlement	(39,048)	
P.R. Department of Treasury - Christmas bonus reimbursement (prior year)	(141,253)	
P.R. Department of Labor - Law No. 52	(33,371)	
P.R. Infrastructure Financing Authority	(14,707)	
P.R. Infrastructure Financing Authority - PINI Funds	(18,803)	
P.R. Department of Education	(16,600)	
P.R. Department of Treasury - sales and use taxes (Debt Service Fund)	(16,361)	
INSEC-ARRA - Community Services Block Grant	(9,510)	
P.R. Office of the Ombudsman for the Elderly - Titles III-D and E	(7,662)	
P.R. Department of Health - HOPWA	(32,946)	
P.R. Electric Power Authority (PREPA)	(177,917)	
OCAM - CDBG and CDBG - ARRA	(190,486)	
Capital lease principal payment	<u>(51,072)</u>	(749,736)

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

Matured bonds principal payments (net change)		57,000
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Repayment of long term debt is an expenditure in the governmental funds, but reduces long-term liabilities in the Statement of Net Assets:

General Obligation Bonds and Notes	911,000	
Other Long Term Liabilities	<u>1,086,552</u>	1,997,552

Governmental funds report the effect of bond issuance costs as expenditure when debt is first issued, whereas these amounts are deferred and amortized in the Statement of Activities. This amount is the net effect of these differences:

Amortization of deferred charges - bond issuance costs	<u>(9,032)</u>	(9,032)
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Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds:

Christmas Bonus	(166,521)	
P.R. Electric Power Authority (PREPA)	(329,002)	
CRIM - Property tax preliminary settlement	(89,858)	
Estimated landfill closing costs	(37,301)	
Compensated Absences	(157,109)	
Accrued interest (net change)	<u>5,206</u>	<u>(774,585)</u>

Change in net assets of governmental activities: \$ 1,819,622

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Hormigueros was founded in 1874. The Municipality is governed by the executive and the legislative branch elected for a four-year term during the general elections in Puerto Rico. The Mayor is the executive officer and the legislative branch consists of twelve (12) members of the Municipal Legislature. The Municipality engages in a comprehensive range of services to the community such as: general government administration, public works, health, environmental control, education, public security, welfare, housing, community development and culture and recreation activities.

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

1. *Financial reporting entity*

The financial reporting entity included in this report consists of the financial statements of the Municipality of Hormigueros (primary government). To fairly present the financial position and the results of operations of the financial reporting entity, management must determine whether its reporting entity consists of only the legal entity known as the primary government or one or more organizations called component units. The inclusion of a potential component unit in the primary government's reporting entity depends on whether the primary government is financially accountable for the potential component unit or on whether the nature and significance of the relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. There are two methods of presentation of the component unit in the financial statements: (a) blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances and (b) discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

The basic criteria for deciding financial accountability are any one of the following:

- a. Fiscal dependency of the potential component unit on the primary government, or
- b. The primary government appoints a voting majority of the potential component unit's governing body and,
 - 1) The primary government can impose its will on the potential component unit and/or,
 - 2) A financial benefit/ burden exists between the primary government and the potential component unit.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

In addition, a legally separate, tax-exempt organization should be discretely presented as a component unit of a reporting entity if *all* of the following criteria are met:

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

Other organizations should be evaluated as potential component units if they are closely related to, or financially integrated with, the primary government. Professional judgment is applied in determining whether the relationship between a primary government and other organizations for which the primary government is not accountable and that do not meet these criteria is such that exclusion of the organization would render the financial statements of the reporting entity misleading or incomplete.

Based on the above criteria there are no potential component units which should be included as part of the financial statements.

2. *Basis of presentation, measurement focus and basis of accounting*

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

Management Discussion and Analysis

This consists of a narrative introduction and analytical overview of the Municipality's financial activities. This analysis is similar to the analysis the private sector provides in their annual reports.

Basic financial statements

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Government-wide statements

The government-wide statements consist of a Statement of Net Assets and a Statement of Activities. These statements are prepared using the economic resources measurement focus, which concentrates on an entity or fund's net assets. All transactions and events that affect the total economic resources (net assets) during the period are reported. The statements are reported on the accrual basis of accounting. Revenues are recognized in the period earned and expenses recognized in the period in which the associated liability is incurred. Fiduciary activities, if any, whose resources are not available to finance government programs, are excluded from the government-wide statements. The effect of inter-fund activities is eliminated.

The Statement of Net Assets incorporates all capital (long-lived) assets and receivables as well as long-term debt and obligations. The Statement of Activities reports revenues and expenses in a format that focuses on the net cost of each function of the Municipality. Both the gross and net cost of the function, which is otherwise being supported by the general government revenues, is compared to the revenues generated directly by the function. This Statement reduces gross expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. Program revenues must be directly associated with the function.

The types of transactions included as program revenues are: charges for services, fees, licenses and permits; operating grants which include operating-specific and discretionary (either operating or capital) grants; and capital grants which are capital-specific grants. Internally-dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes. Property taxes (imposed nonexchange transactions) are recognized as revenues in the year for which they are levied and municipal license taxes and sales and use taxes (derived tax revenues) when the underlying exchange has occurred. Revenues on both operating and capital grants are recognized when all eligibility requirements (which include time requirements) imposed by the provider have been met. For certain expenditure-driven grants, revenue is recognized after allowable expenditures are incurred. As a policy, indirect expenses in the Statement of Activities are not allocated. The Municipality first uses restricted assets for expenses incurred for which both restricted and unrestricted assets are available.

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

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989 generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The Municipality has elected not to follow subsequent statements and interpretations issued by the FASB after November 30, 1989.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Fund Statements

The financial transactions of the Municipality are recorded in individual funds, each of which is considered an independent fiscal entity. Each fund is accounted for by providing a separate set of self-balancing accounts that comprise its assets, liabilities, reserves, fund equity, revenues and expenditures. Funds are segregated according to their intended purpose which helps management in demonstrating compliance with legal, financial and contractual provisions. Governmental Funds are those through which most governmental functions of the Municipality are financed. The governmental fund statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances with one column for the general fund, one for each major fund and one column combining all non-major governmental funds. Major funds are determined based on a minimum criterion, that is, a percentage of the assets, liabilities, revenues or expenditures or based on the Municipality's official's criteria, if the fund is particularly important to financial statement users (for Commonwealth Legislature Resolutions, Lavadero Sanitary Sewer System and \$3,000,000 Bond Issuance Funds).

The Municipality reports the following major governmental funds:

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

Community Development Block Grant Program Fund (CDBG): CDBG fund (including CDBG - ARRA) is used to account for and report revenue sources for the development of viable urban communities by providing decent housing, a suitable living environment and expanding economic opportunities, principally for persons of low and moderate income.

Commonwealth Legislature Resolutions Fund: This fund is used to account for and report revenue sources from grants provided by the Commonwealth's Legislature for specific purposes which include, among others, acquisition, development and improvements of capital assets.

Debt Service Fund: This fund is used to account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest.

Lavadero Sanitary Sewer System Fund: This fund is used to account for and report revenue sources from a grant provided by the USDA Rural Development for specific purposes, that is, the construction of a sanitary sewer system for the Lavadero's community.

\$3,000,000 Bond Issuance Fund: This fund is used to account for and report the proceeds from a special obligation bond issuance for the acquisition of land and construction of sports facilities.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

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

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

The Municipality reports in the governmental funds statements deferred revenues which arise when potential revenue does not meet both measurable and available criteria for recognition in the current period. In the government-wide statements revenue is recognized as soon as it is earned regardless of its availability. Deferred revenues also arise when resources are received before the Municipality has a legal claim to them or before applicable eligibility requirements are met (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the revenue recognition criteria is met, or when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed from the balance sheet and the revenue is recognized.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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

Notes to Financial Statements

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

Required Supplementary Information:

Required supplementary information consists of the Budgetary Comparison Schedule – General Fund as required by GASB.

3. *Deposits and investments*

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

The laws and regulations of the Commonwealth of Puerto Rico authorize the Municipality to invest only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by the Governmental Development Bank for Puerto Rico ("GDB").

4. *Restricted assets*

Restricted assets are liquid assets which have third-party limitations on their use. Cash and cash equivalents related to Commonwealth and Federal grants (including Commonwealth Legislature Resolutions) are restricted since their use is limited by applicable agreements or required by law. Restricted cash with fiscal agent in the debt service fund consists of the undisbursed balance of property and sales tax collections retained by the Commonwealth of Puerto Rico which are restricted for the repayment of the Municipality's general and special obligation bonds and notes as established by law. Restricted cash with fiscal agent of the other governmental funds represent the undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the GDB or a federal government agency.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

5. *Receivables and due from governmental entities*

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions. Amounts due from federal government represent amounts owed to the Municipality for the reimbursement of expenditures incurred pursuant to federally funded programs. Amounts reported in the debt service fund represent property and sales tax revenues of current fiscal year collected by the CRIM (property tax) and the Puerto Rico Department of Treasury (sales tax) on the subsequent fiscal year.

6. *Interfund receivables and payables*

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

7. *Inventories*

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

8. *Capital assets*

Capital assets reported in the governmental activities in the Statements of Net Assets include property, plant, equipment and infrastructure, (e.g., roads, bridges, sidewalks, and similar items). The Municipality defines capital assets (except for infrastructure assets) as assets that have an individual cost of \$1,000 or more and have a useful life of one or more years. Infrastructure assets are capitalized based on a percentage of the estimated useful life. The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets are capitalized at historical cost or estimated historical cost if historical cost is not available. Donated assets are recorded as capital assets at their estimated fair market value at the date of donation.

All capital assets, other than land and construction in progress, are depreciated using the straight-line method over the following useful lives:

<u>Description</u>	<u>Years</u>
Land improvements	20
Buildings and building improvements	20-50
Infrastructure	10-50
Vehicles, machinery and equipment	5-20

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

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

9. Long-term obligations

Long-term debt and other long-term obligations, which are reported as liabilities in the governmental activities column in the Statement of Net Assets, consist of general and special obligation bonds, liabilities for compensated absences, claims and judgments, and long-term liabilities to other governmental entities.

10. Deferred bond issuance costs

Bond issuance costs are reported as deferred charges and amortized as required by current standards. Governmental fund types recognize bond issuance costs as expenditures during the current period. Those issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the appropriate fund.

11. Compensated absences

The Municipality's employees accumulate vacation, sick leave and compensatory time based on continuous service. Compensated absences are recorded as a liability if (1) are earned on the basis of services already performed by employees, (2) it is probable that will be paid (in the form of paid time off, cash payments at termination or retirement, or some other means) and (3) are not contingent on a specific event (such as illness). The compensated absences are accumulated on the basis of 2½ days per month of vacation and 1½ days per month of sick pay and compensatory time up to a maximum of 60 days of vacations and 90 days of sick leave. Upon separation from employment the accumulated vacations are liquidated up to the maximum number of days. Accumulated sick leave, which is accrued based on all vesting amounts for which payment is probable, is liquidated to employees with 10 years or more service up to the maximum number of days.

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

12. Fund balances and Net Assets

During the year 2011 the Municipality implemented GASB Statement No. 54-Fund Balance Reporting and Governmental Fund Type Definitions ("GASB No. 54"). This statement establishes accounting and reporting standards for all governments that report governmental funds. It also establishes criteria for classifying fund balances into specifically defined classifications and clarifies definitions for governmental fund types. These classifications comprise a hierarchy based primarily on the extent to which the Municipality is bound to observe constraints upon the use of the resources reported. As a result of the implementation a special fund was reclassified from the general fund to other governmental funds. The classifications are as follows:

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

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

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

Assigned: These are amounts intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed. Intent can be expressed by the Mayor or the Finance Director, the official to which the Mayor has also delegated the authority to assign amounts. With the exception of the general fund, this is the residual fund balance of the classification of all governmental funds with positive fund balances. Action taken to assign fund balances may be made after year-end.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

Unassigned: This is the residual classification for the general fund and includes all spendable amounts not restricted, committed or assigned - The general fund is the only fund that reports a positive unassigned fund balance amount. For all other governmental funds the unassigned classification is used only to report a deficit balance resulting for the overspending for specific purposes for which amounts had been restricted, committed or assigned.

The Municipality applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned and unassigned) amounts are available. Similarly, within unrestricted fund balances, committed amounts are reduced first followed by assigned and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used.

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

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

Restricted net assets: Represent net assets (restricted assets net of related debt) that are subject to restrictions beyond the Municipality's control. These include restrictions that are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or restrictions imposed by the law through constitutional provisions or enabling legislation.

Unrestricted net assets: Represent net assets that do not meet the definition of net assets invested in capital assets, net of related debt or restricted. Unrestricted assets are often designated to indicate that management does not consider them to be available for general operations. These types of constraints are internal and management can remove or modify them.

13. *Interfund transactions*

The Municipality reports certain transactions as transfers, which are legally required transfers that are reported when incurred as "Transfers-in" by the recipient fund and as "Transfers-out" by the disbursing fund.

14. *Risk financing*

The Puerto Rico Treasury Department (PRDT) acts as an agent, obtaining and determining the coverage for the municipalities of Puerto Rico. The coverage for the Municipality of Hormigueros consists of professional, public responsibility, property and theft, auto and fidelity bond coverage. Insurance policies costs are allocated by PRDT among all the municipalities of Puerto Rico.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

Payment of the Municipality’s insurance premiums is monthly deducted from advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM). Workers compensation insurance is also deducted from the monthly advances by the CRIM. Settled cases have not exceeded insurance coverage for any of the past three years.

15. Use of estimates

The preparation of the basic financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

16. Future adoption of accounting pronouncements

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

<u>Statement</u>	<u>To be adopted in fiscal year ended,</u>
57 OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans	June 30, 2012
60 Accounting and Financial Reporting for Service Concession Arrangements	June 30, 2013
61 The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34	June 30, 2013
62 Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements	June 30, 2013
63 Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position	June 30, 2013
64 Derivative Instruments: Application of Hedge Accounting Termination Provisions—an amendment of GASB Statement No. 53	June 30, 2012

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE B – DEPOSITS AND INVESTMENT

1. Deposits

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The Municipality maintains cash deposits in commercial and governmental banks located in Puerto Rico. Under Commonwealth of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral by the Municipality are held by the Secretary of Treasury of Puerto Rico in the Municipality's name.

At year-end, the Municipality's bank balance of deposits in commercial banks amounting to \$3,835,085 was covered by federal depository insurance or by collateral held by the Secretary of Treasury of Puerto Rico in the Municipality's name. Deposits in governmental banks (all of which are uninsured and uncollateralized), are exposed to custodial credit risk. At year-end the Municipality's bank balance in governmental banks amounts to \$4,176,455.

2. Investment

The investment held with fiscal agent consists of a non-participating investment contract (non-rated guaranteed investment contract, "GIC"). This represents the investment of the undisbursed proceeds of the \$3,000,000 special obligation bond under custody of GDB, the Municipality's fiscal agent, pursuant to the bond purchase agreement. The GIC, with an outstanding balance of \$73,335 as of June 30, 2011 earns interest at a variable rate (.10% rate, accrued interest of \$3.26 as of June 30, 2011) and matures on July 15, 2011. GIC outstanding balance is valued at cost.

NOTE C – RECEIVABLES - LEASE

The Municipality is a lessor of a property, which consists of a building facility, classified as direct financing lease. The lease term is for twenty years under a noncancelable lease agreement. The following lists the components of the net investment in direct financing lease as of June 30:

	Amount
Total minimum lease payments to be received	\$ 215,764
Less: Unearned income	(27,040)
Net investment in direct financing lease	\$ 188,724

At June 30, 2011, minimum lease payments for each of the four succeeding fiscal years are as follows:

Year	Amount
2012	\$ 76,152
2013	76,152
2014	57,114
	\$ 209,418

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE D - DUE FROM (TO) GOVERNMENTAL ENTITIES

Amounts due from governmental entities as of June 30, 2011 follows:

	Commonwealth Government	Federal Government
<u>Major fund - General fund:</u>		
P.R. Electric Power Authority (PREPA)	\$ 363,620	\$ -
P.R. Aqueduct and Sewer Authority (PRASA)	19,938	-
P.R. Department of Treasury – Christmas bonus reimbursement	139,277	-
P.R. Department of Education	12,000	-
P.R. Department of Treasury – sales and use taxes- Municipal Development fund	18,394	-
Others	4,731	-
<u>Major fund – CDBG fund:</u>		
Office of Commissioner of Municipal Affairs – CDBG and CDBG-ARRA	-	316,581
<u>Major fund – Commonwealth Legislature Resolutions fund:</u>		
Commonwealth Legislative Resolutions	23,358	-
<u>Major fund – Debt service fund:</u>		
Municipal Revenue Collection Center (CRIM) – property taxes	16,829	-
P.R. Department of Treasury – sales and use taxes- Municipal Redemption Fund	39,976	-
<u>Other governmental funds:</u>		
P.R. Infrastructure Financing Authority (PRIFA)	1,385	-
P.R. Public Order Code	23,476	-
Solid Waste Authority-Landfill improvements	85,819	-
P.R. Public Works – Improvements 2011	20,000	-
Schools Maintenance	11,489	-
Home Caregivers	23,391	-
P.R. Office of the Ombudsman for the Elderly – Title III-D, E and NSIP	-	9,425
P.R. Public Housing Authority	-	11,913
P.R. Department of Labor – Law No. 52	30,048	-
P.R. Department of Health – HOPWA	-	4,049
Others	-	12,161
	\$ 833,731	\$ 354,129

See note I for detail of amounts due from Governmental Entities recorded as deferred revenue.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE E - INTERFUND TRANSACTIONS

1. Due from/to other funds

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

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General Fund	<u>Major fund:</u>	
	CDBG	\$ 91,411
	<u>Major fund:</u>	
	Debt Service	8,812
	<u>Other governmental funds:</u>	
	\$510,000 Bond Issuance	13,676
	Public Housing	16,334
	\$840,000 Bond Issuance	1,705
	\$425,000 Bond Issuance	512
	\$235,000 Bond Issuance	12,827
	HVP	6,648
	FTA	53
	HOPWA	4,561
	Home Caregivers	23,391
	Schools Maintenance	15,630
	Public Order Code	23,476
	Law 52	32,461
	Title III	4,678
	Ordinance 34 – Valle Hermoso	19,751
	P.R. Public Works – Improvements 2011	15,395
	Others	5,668
Total:		<u><u>\$ 296,989</u></u>

2. Transfers in (out)

Transfers among individual funds were made for operational purposes. Transfers includes interest earned on restricted cash with fiscal agent in the debt service fund, operating and capital improvement loans in other governmental funds which are transferred to the general fund, and principal and interest payments of general long-term debt transferred from the general fund to the debt service fund.

NOTE F- OTHER ASSETS

Other assets include a cash deposit of \$123,559 held in custody of a Commonwealth's court of law for the acquisition of a parcel of land under litigation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE G- FUND BALANCE

1. Fund balance classifications

The governmental fund balance classifications and amounts at June 30, 2011 are shown in the following table:

	General Fund	Community Development Block Grant	Commonwealth Legislative Resolutions	Debt Service	Lavadero Sanitary Sewer System	Other Governmental Funds	Total
<u>Restricted:</u>							
General public works and sanitation	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 90,346	\$ 90,346
Public safety	-	-	-	-	-	99	99
Housing, welfare and community development	-	-	-	-	-	62,276	62,276
Debt Service	-	-	-	1,965,166	-	-	1,965,166
Capital outlays	-	16,283	463,296	-	25,442	1,201,167	1,706,188
General Government and other purposes	-	-	-	-	-	37,282	37,282
	<u>-</u>	<u>16,283</u>	<u>463,296</u>	<u>1,965,166</u>	<u>25,442</u>	<u>1,391,170</u>	<u>3,861,357</u>
<u>Assigned:</u>							
General public works and sanitation	66,885	-	-	-	-	-	66,885
Public safety	619	-	-	-	-	-	619
Housing, welfare and community development	13,551	-	-	-	-	-	13,551
Sports, culture and recreation	873	-	-	-	-	-	873
Capital outlays	1,024,998	-	-	-	-	-	1,024,998
General Government and other purposes	110,298	-	-	-	-	-	110,298
	<u>1,217,224</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,217,224</u>
<u>Unassigned</u>	<u>417,501</u>	<u>(289,802)</u>	<u>-</u>	<u>-</u>	<u>(149,651)</u>	<u>(45,591)</u>	<u>(67,543)</u>
	<u><u>\$ 1,634,725</u></u>	<u><u>\$ (273,519)</u></u>	<u><u>\$ 463,296</u></u>	<u><u>\$ 1,965,166</u></u>	<u><u>\$ (124,209)</u></u>	<u><u>\$ 1,345,579</u></u>	<u><u>\$ 5,011,038</u></u>

2. Fund balance deficits

Certain special funds included in the fund statements disclosed fund balance deficits as follows:

Funds	Fund balance - unassigned amount
<u>Major Funds:</u>	
CDBG	<u><u>\$ 289,802</u></u>
Lavadero Sanitary Sewer System	<u><u>\$ 149,651</u></u>
<u>Other Governmental Funds:</u>	
School Maintenance	\$ 15,490
Public Order Code	15,582
HOPWA	5,509
Others	9,010
	<u><u>\$ 45,591</u></u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE G- FUND BALANCE - Continued

The deficits result from the accrual of expenditures without accruing intergovernmental revenues for reimbursement of expenditures. As required by current standards, the Municipality recorded intergovernmental revenues for reimbursement (expenditure-driven) grants on funds statements when all applicable eligibility requirements have been met and the resources are available.

NOTE H - CAPITAL ASSETS

Capital assets and depreciation activity as of and for the year ended June 30, 2011 is as follows:

	Balance July 1, 2010	Increases	Decreases	Balance June 30, 2011
<u>Governmental activities:</u>				
Capital assets, not being depreciated:				
Land	\$ 7,702,495	\$ 463,000	\$ -	\$ 8,165,495
Construction in progress	10,367,690	2,435,836	2,493,522	10,310,004
Total capital assets not being depreciated:	18,070,185	2,898,836	2,493,522	18,475,499
Capital assets, being depreciated:				
Land improvements	1,046,506	360,200	-	1,406,706
Buildings and building improvements	25,125,288	2,107,060	-	27,232,348
Infrastructure	11,604,061	182,941	-	11,787,002
Vehicles, machinery and equipment	8,253,180	215,224	87,695	8,380,709
Total capital assets being depreciated	46,029,035	2,865,425	87,695	48,806,765
Less accumulated depreciation for:				
Land improvements	388,786	40,504	-	429,290
Buildings and building improvements	7,845,956	650,771	-	8,496,727
Infrastructure	5,489,587	581,666	-	6,071,254
Vehicles, machinery and equipment	5,332,768	519,603	80,008	5,772,363
Total accumulated depreciation	19,057,097	1,792,544	80,008	20,769,634
Total capital assets being depreciated, net	26,971,938	1,072,881	7,687	28,037,132
Governmental activities capital assets, net	\$ 45,042,123	\$ 3,971,717	\$ 2,501,209	\$ 46,512,631

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

Governmental activities:

General government	\$ 232,290
Public works and sanitation	724,332
Public safety	146,861
Culture and recreation	518,112
Health	12,351
Welfare and community development	138,266
Education	20,332
Total depreciation expense, governmental activities	\$ 1,792,544

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE I - DEFERRED REVENUES – GOVERNMENTAL FUNDS

Deferred revenues - Intergovernmental Commonwealth Government represent revenues not available as required by current standards and for Federal Grants represent resources received before allowable expenditures are incurred or resources not available as required by current standards. A detail of these balances follows:

	Commonwealth Government	Federal Grants
<u>Major fund - General fund:</u>		
P.R. Electric Power Authority (PREPA)	\$ 363,620	\$ -
P.R. Department of Treasury – Christmas bonus reimbursement	139,277	-
P.R. Department of Education	6,000	-
P.R. Municipal Sales Tax	5,815	
<u>Major fund – CDBG fund:</u>		
Office of Commissioner of Municipal Affairs – CDBG and CDBG-ARRA	-	295,764
<u>Major fund – Commonwealth Legislature</u>		
<u>Resolutions fund:</u>		
Commonwealth Legislative Resolutions	23,358	-
<u>Other governmental funds:</u>		
P.R. Infrastructure Financing Authority (PRIFA)	1,386	-
P.R. Department of Education - CRE	11,489	-
P.R. Public Order Code	23,476	-
P.R. Department of Housing (PRPHA) – PIH	-	1,069
P.R. Department of Health – HOPWA	-	5,426
P.R. Child Care SENDEC	-	32,106
P.R. Department of Family – ARRA - HPRP	-	30,245
P.R. Department of Family – Title III-D and E	-	2,425
Federal Transit Administration	-	10,728
P.R. Department of Education – Food Program	-	10,013
	\$ 574,421	\$ 387,776

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE J – LONG-TERM DEBT

1. Summary of long-term debt activity

The following summarizes activity in long-term debt for the fiscal year ended June 30, 2011:

	<u>Balance at July 1, 2010</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at June 30, 2011</u>	<u>Due within one year</u>
General, Special Obligations Bonds and Notes	\$ 16,160,000	\$ -	\$ 911,000	\$ 15,249,000	\$ 978,000
Note payable to CRIM- LIMS	49,534	-	32,536	16,998	16,998
Note payable to CRIM- financing of delinquent accounts	4,387	-	201	4,186	199
Note payable to SIFC	94,711	-	94,711	-	-
Compensated absences	1,315,771	157,109	182,271	1,290,609	191,493
Christmas Bonus	177,402	166,521	177,402	166,521	166,521
Estimated Landfill Closing Costs	1,212,306	37,301	-	1,249,607	-
Payable to CRIM- property tax advances	311,847	89,858	311,847	89,858	-
Payable to PREPA	322,202	329,002	287,584	363,620	253,952
	<u>\$ 19,648,160</u>	<u>\$ 779,791</u>	<u>\$ 1,997,552</u>	<u>\$ 18,430,399</u>	<u>\$ 1,607,163</u>

2. General and special obligation bonds and notes

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2011 amount to \$15,249,000. All of these bonds are serviced by the Governmental Development Bank of Puerto Rico (GDB) maturing at various dates. As required by law, the Commonwealth Government is obligated to collect property taxes for payment of principal and interest on bonds and notes. In addition, .2% of the .5% municipal sales and use tax collected by the P.R. Department of Treasury is deposited in a "Municipal Redemption Fund" to finance loans to Municipalities subject to restrictions imposed by law. Debt service funds have been established for the bonds and notes at GDB with the proceeds of those property and sales and use taxes, whereby sufficient funds must be set aside in order to cover the projected debt service requirements, before any new bonds are issued. Principal and interest payments of \$690,000 Revenue bonds are made through an "Interest Bearing Account" (IBA) maintained by GDB, which is financed with proceeds from lessee's rental payments.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE J – LONG-TERM DEBT – Continued

Principal and interest payments of certain long-term debt issued for operational purposes (special obligation note of \$748,000 and special obligation bonds of \$3,000,000 and \$203,000) are made through withholdings from the advances of property tax and amounts of municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center (CRIM). Principal and interest payments of special obligation notes of \$305,000, \$139,000, \$1,027,000 and \$385,000 are made through the “Municipal Redemption Fund”. A detail of the general and special obligation bonds and notes as of June 30, 2011 follows:

	Outstanding Amount
1994 public improvement bonds of \$125,000 due in annual installments of \$3,000 to \$10,000 through January 1, 2019; bearing interest at 5%	\$ 61,000
1992 public improvement bonds of \$168,000 due in annual installments of \$2,000 to \$17,000 through January 1, 2017; bearing interest at 5%	78,000
1997 general obligation bonds of \$175,000 due in annual installments of \$5,000 to \$15,000 through July 1, 2021; bearing interest at rates ranging from 4.865% to 6.56% (5.94% at June 30, 2011)	105,000
1996 general obligation bonds of \$390,000 due in annual installments of \$5,000 to \$40,000 through July 1, 2020; bearing interest at rates ranging from 4.70% to 6.63% (6.23 % at June 30, 2011)	250,000
1999 general obligation bonds of \$410,000 due in annual installments of \$5,000 to \$35,000 through July 1, 2024; bearing interest at rates ranging from 2.70% to 7.81% (4.40% at June 30, 2011)	310,000
2001 general obligation bonds of \$425,000 due in annual installments of \$5,000 to \$40,000 through July 1, 2025; bearing interest at rates ranging from 2.70% to 6.13% (4.40% at June 30, 2011)	345,000
1999 general obligation bonds of \$736,000 due in annual installments of \$19,000 to \$52,000 through January 1, 2024; bearing interest at 4.75%	520,000
1998 general obligation bonds of \$983,000 due in annual installments of \$23,000 to \$65,000 through January 1, 2024; bearing interest at 4.5%	657,000
2002 general obligation bonds of \$1,000,000 due in annual installments of \$21,000 to \$65,000 through January 1, 2030; bearing interest at 4.50%	850,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE J – LONG-TERM DEBT – Continued

	Outstanding Amount
2000 general obligation bonds of \$1,040,000 due in annual installments of \$27,000 to \$76,000 through January 1, 2025; bearing interest at 5.12%	784,000
1997 general obligation bonds of \$1,538,000 due in annual installments of \$41,000 to \$109,000 through January 1, 2022; bearing interest at 4.75%	962,000
1992 revenue bonds of \$690,000 due in annual installments of \$5,000 to \$25,000 through July 1, 2013; bearing interest at 9%	120,000
2004 general obligation bonds of \$530,000 due in annual installments of \$15,000 to \$40,000 through July 1, 2024; bearing interest at rates ranging from 3.28% to 5.00% (4.62% at June 30, 2011)	420,000
2004 general obligation bonds of \$1,355,000 due in annual installments of \$35,000 to \$85,000 through July 1, 2029; bearing interest at rates ranging from 3.50% to 5.00% (4.62% at June 30, 2011)	1,130,000
2005 special obligation notes of \$748,000 due in annual installments of \$92,000 to \$124,000 through July 1, 2012; bearing interest at rates ranging from 1.53% to 6.60% (1.54% at June 30, 2011)	242,000
2006 general obligation bonds of \$920,000 due in annual installments of \$20,000 to \$70,000 through July 1, 2030; bearing interest at rates ranging from 4.17% to 5.31% (4.62% at June 30, 2011)	820,000
2007 general obligation bonds of \$840,000 due in annual installments of \$10,000 to \$75,000 through July 1, 2031; bearing interest at rates ranging from 1.53% to 7.50% (1.54% at June 30, 2011)	785,000
2007 general obligation notes of \$525,000 due in annual installments of \$60,000 to \$90,000 through July 1, 2014; bearing interest at rates ranging from 1.53% to 7.50% (1.54% at June 30, 2011)	330,000
2008 general obligation notes of \$400,000 due in annual installments of \$45,000 to \$70,000 through July 1, 2014; bearing interest at rates ranging from 1.53% to 7.25% (1.54% at June 30, 2011)	250,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE J – LONG-TERM DEBT – Continued

	<u>Outstanding Amount</u>
2008 general obligation bonds of \$569,000 due in annual installments of \$40,000 to \$77,000 through July 1, 2017; bearing interest at rates ranging from 1.53% to 7.50% (1.54% at June 30, 2011)	440,000
2008 special obligation notes of \$305,000 due in annual installments of \$45,000 to \$60,000 through July 1, 2014; bearing interest at rates ranging from 1.53% to 7.50% (1.54% at June 30, 2011)	215,000
2008 special obligation notes of \$139,000 due in annual installments of \$2,000 to \$11,000 through July 1, 2032; bearing interest at rates ranging from 1.53% to 7.50% (1.54% at June 30, 2011)	135,000
2008 special obligation notes of \$1,027,000 due in annual installments of \$16,000 to \$87,000 through July 1, 2032; bearing interest at rates ranging from 1.54% to 7.25% (1.54% at June 30, 2011)	994,000
2007 special obligation bond of \$3,000,000 due in annual installments of \$60,000 to \$205,000 through July 1, 2032; bearing interest at 5.83%	2,805,000
2007 special obligation bond of \$203,000 due in annual installments of \$14,000 to \$27,000 through July 1, 2017; bearing interest at rates ranging from 1.53% to 7.50% (1.54% at June 30, 2011)	156,000
2008 special obligation notes of \$385,000 due in annual installments of \$5,000 to \$30,000 through July 1, 2033; bearing interest at rates ranging from 1.53% to 7.50% (1.54% at June 30, 2011)	375,000
2010 general obligation bonds of \$510,000 due in annual installments of \$35,000 to \$65,000 through July 1, 2019; bearing interest at 6.50%	475,000
2010 general obligation bonds of \$285,000 due in annual installments of \$5,000 to \$25,000 through July 1, 2034; bearing interest at 6.50%	280,000
2010 general obligation notes of \$160,000 due in annual installments of \$15,000 to \$30,000 through July 1, 2016; bearing interest at rates ranging from 6.0% to 7.50% (6.00% at June 30, 2011)	145,000
2010 municipal obligation notes of \$235,000 due in annual installments of \$25,000 to \$40,000 through July 1, 2016; bearing interest at rates ranging from 6.0% to 6.50% (6.00% at June 30, 2011)	210,000
	<u>\$ 15,249,000</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE J – LONG-TERM DEBT – Continued

The annual requirements to amortize general and special obligation bonds and notes as of June 30, 2010 follows:

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2012	\$ 983,000	\$ 763,431
2013	1,043,000	774,332
2014	948,000	714,112
2015	970,000	656,402
2016	807,000	610,606
2016-2021	3,946,000	3,044,197
2022-2026	3,198,000	1,387,241
2027-2031	2,516,000	586,238
2032-2036	838,000	34,581
Totals	<u>\$ 15,249,000</u>	<u>\$ 8,571,140</u>

3. Other long-term liabilities

Note payable to CRIM (LIMS) - On November 28, 2001 the Municipality entered into a financing agreement with the CRIM in the amount of \$261,009 for the payment of the Municipality's share of the cost of a management information system (**LIMS**) acquired by the CRIM for the management of taxpayer's properties located in Puerto Rico. The note is payable in semiannual installments of \$17,503, including interest of 5.95% and is due on November 28, 2011. The amount will be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of the municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center. Debt service requirements in future years are as follows:

**Outstanding
Amount**

\$ 16,998

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2012	16,998	505
Totals	<u>\$ 16,998</u>	<u>\$ 505</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE J – LONG-TERM DEBT – Continued

Note payable to CRIM (Financing of delinquent accounts) - On March 19, 2002 the Municipality entered into a financing agreement with the CRIM in the amount of \$158,431 to finance delinquent property tax accounts sold to private investors, under the provisions of Law No. 146 of October 11, 2001. The agreement is in the form of a non-revolving line of credit bearing interest of 6.5% for the first five years and variable for the next twenty-five years at 125 points over the London Interbank Offered Rate (LIBOR) and is due on December 1, 2032. As described in Law No. 146, interest payments for the first five years were financed through .48% of the net increase of subsidy provided by the Commonwealth of Puerto Rico’s general fund. Also, during the first five years any collection from those delinquent accounts was credited to the loan principal. After the five-year period the loan outstanding balance would be restructured for a twenty-five year period. The amount would then be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of the municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center. Debt service requirements in future years are as follows:

\$ 4,186

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2012	\$ 199	\$ 257
2013	199	245
2014	199	232
2015	199	220
2016	199	208
2017-2021	998	852
2022-2026	997	543
2027-2031	997	233
2032-2035	199	9
Totals	<u>\$ 4,186</u>	<u>\$ 2,799</u>

Compensated absences - includes accrued vacations, sick leave benefits and other benefits with similar characteristics such as compensatory time; represents the Municipality’s commitment to fund such costs from future operations. The amount is paid with unrestricted funds.

\$ 1,290,609

Christmas Bonus - represents the accrued portion corresponding to fiscal year 2011 of the Christmas bonus to be paid in December 2011 with unrestricted funds.

\$ 166,521

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE J – LONG-TERM DEBT – Continued

Estimated closure and post-closure care costs of Municipal Landfill - The Municipality owns and operates a MSW landfill in Barrio Jaguitas, Hormigueros since about 1977. The Municipality has recognized an estimated liability for future closure and post-closure care costs. (See Note K) \$ 1,249,607

Payable to CRIM, property tax advances – represent the amount reported by CRIM as a result of the settlement of excess of advances over actual collections of property taxes applicable to fiscal year 2011. The amount will be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of the municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center. (See related note L) \$ 89,858

Payable to PREPA - As required by Act No. 83 of May 2, 1941 the Puerto Rico Electric Power Authority (“PREPA”) should annually pay to the Municipalities of Puerto Rico a contribution in lieu of tax (“CELI”) based on certain requirements as specified by the mentioned Act. The amount of CELI obligation is used by the Municipalities to finance the annual electric utility expense payment to PREPA. For fiscal year 2009-2010 the Municipality’s annual energy charges amounted to \$1,126,830 but the CELI obligation amounted to \$797,827. The excess amount of \$329,003 was recorded as a payable and a receivable for the same amount and would be amortized over a three-year period. As of June 30, 2011 the outstanding amount of \$363,620 includes a balance of \$144,285 from fiscal year 2009 and is recognized by the Municipality as a receivable and a liability to PREPA. Debt service requirements in future years are as follows: \$ 363,620

June 30	Principal
2012	\$ 253,952
2013	109,668
Totals	\$ 363,620

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE K - LANDFILL CLOSURE AND POSTCLOSURE CARE COSTS OBLIGATIONS

The Municipality operates a landfill since 1977. Commonwealth and Federal laws and regulations require the Municipality to place a final cover on its landfill when it stops accepting waste and perform certain maintenance and monitoring functions at the landfill site for thirty years after closure. In addition to operating expenses related to current activities of the landfill, an expense provision and related liability should be recognized based on the future closure and post closure care costs that will be incurred near or after the date the landfill no longer accepts waste. The Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to comply with applicable laws and regulations. As a result of this study, the Municipality has recognized an estimated liability for future closure and post-closure care costs. The recognition of this liability is based on the amount of the landfill used during the year. The estimated liability for landfill closure and post-closure care costs has a balance of \$1,249,607 as of June 30, 2011, which is based on 54% usage of the landfill. It is estimated that an additional \$913,892 will be recognized as closure and post-closure care expenditures between the date of the balance sheet and the date the landfill is expected to be filled to capacity (December 2035). The estimated total current costs of the landfill closure and post-closure care (\$2,163,499) is based on the amount that would be paid if all the equipment, facilities and services required to close, monitor and maintain the landfill were acquired as of June 30, 2011. However, the actual cost of closure and post-closure care may be higher due to inflation, changes in technology, or changes in landfill laws and regulations.

NOTE L - PROPERTY TAXES

The Municipal Revenue Collection Center (CRIM) of the Commonwealth of Puerto Rico is responsible for the assessment, collection and distribution of real and personal property taxes. The tax on personal property is self-assessed by the taxpayer. The assessment is made on a return, which must be filed with the CRIM by May 15 of each year and is based on the current value at the date of the assessment. Real property is assessed by the CRIM. The tax is generally assessed on January 1 on all taxable property located within the Municipality and is based on the current value existing in the year 1957. For personal property the tax is due with the return filed on or before May 15. Taxes on real property may be paid on two equal installments, July 1st and January 1st. Total tax rates in force as of June 30, 2011 are 7.03% for personal property and 9.03% for real property. The distribution of these rates follows:

<u>Description</u>	<u>Personal Property</u>	<u>Real Property</u>
Basic property tax rate, which is appropriated for general purposes and accounted for in the Municipality's general fund	4.00%	6.00%
Percent that belongs to the Commonwealth's debt service fund	1.03%	1.03%
Percent that belongs to the Municipality's debt service fund	2.00%	2.00%
Total tax rate	7.03%	9.03%
Discount granted by law to the taxpayers but reimbursed to the Municipality by the P.R. Treasury Department	(.20%)	(.20%)
Total percent to be paid by taxpayers	<u>6.83%</u>	<u>8.83%</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE L - PROPERTY TAXES – Continued

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

The CRIM advances funds to the Municipality based on an estimate of special governmental subsidies and the property taxes to be levied and which are collected in subsequent periods. This distribution includes advances of property tax and amounts of municipal equalization fund from the Commonwealth government. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. The CRIM prepares a preliminary settlement not later than three months after fiscal year-end and a final settlement not later than six months after fiscal year-end. If actual collections exceed the advances a receivable from CRIM is recorded. However, if advances exceed actual collections, a payable to CRIM is recorded. A net payable of \$89,858 resulting from the settlement for fiscal year 2010-11 is recorded as other long-term debt in the government-wide financial statements since it will not be paid with current available financial resources.

On July 2, 2010 the Commonwealth's Legislature approved Act No. 71 which established an incentive plan (amnesty) for the payment of property tax debts. The Act, applicable to tax years 2008-2009 and before, provided participants a 100% interest and penalties waived. Funds would be collected by the CRIM and remitted to the Municipalities. During the year 2010-2011 amnesty collections of \$749,196 and \$47,528 were recorded in the general fund and debt service fund, respectively.

NOTE M - MUNICIPAL LICENSE TAXES

Municipal License taxes are assessed annually by the Municipality to all organizations or entities doing business in the Municipality's location except for entities totally or partially exempt pursuant to certain Commonwealth's statutes. This tax is based generally on volume of business or gross sales as shown in a tax return that should be submitted on or before April 15. During the fiscal year ended June 30, 2011 the tax rates were as follows:

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

The tax is due in two equal installments on July 1 and January 1 of each fiscal year. Tax revenue is recognized at that moment by the Municipality. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year in the amount of \$1,029,497 is recorded as deferred revenues.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE N - SALES AND USE TAXES

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

Section 6189 of the Puerto Rico Internal Revenue Code of 1994, as amended, authorizes the Municipalities in Puerto Rico to impose a sales and use tax to consumers. This tax must be imposed in conformity with the base, exemptions and limitations contained in Subtitle BB of the Code. The municipal sales and use tax is specifically imposed over all sales transactions of taxable items and combined transactions (as defined by the municipal internal regulation) taking place within municipal limits. The municipal sales and use tax is also specifically imposed over the purchase price for the use, storage or consumption of taxable transactions (as defined by the municipal internal regulation) taking place within municipal limits. The Municipal Legislature approved the imposition of the municipal sales and use tax on November 1, 2006 with Ordinance No. 22 Series 2006-2007, effective on November 15, 2006.

On July 29, 2007 the Commonwealth Legislature approved Act No. 80 ("Act 80") which amends Act No. 117 of July 4, 2006 to impose all the Municipalities of Puerto Rico a uniform municipal sales and use tax of 1.5%. Effective August 1, 2007, 1% of the 1.5% is collected by the Municipalities and the remaining .5% of the 1.5% is collected by the Puerto Rico Department of Treasury (PRDT). Act 80 also provides for restrictions on the use of the sales tax, which is required to be invested in solid waste and recycling programs, capital improvements and health and public safety costs.

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

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

The Municipal Legislature approved an amendment to Municipal Ordinance No. 22 Series 2006-2007 to conform to dispositions of Act 80.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE N - SALES AND USE TAXES - Continued

Individuals, organizations and entities collecting the municipal sales and use tax must file a tax return to the Municipality. The tax is due the 10th day of each month based on the tax collected in the preceding month. A total \$106,403 sales and use tax receivable represents the tax collected on June by individuals, organizations and entities but reported and paid to the Municipality on or before July 20, net of uncollectible accounts; \$18,394 and \$39,976 represents amounts of "Municipal Development Fund" and "Municipal Redemption Fund", respectively, collected on June by individuals, organizations and entities but paid by the PRDT subsequent to June 30. No amount related to Municipal Redemption Fund is recorded as deferred revenue since it is not available as required by current standards.

NOTE O - INTERGOVERNMENTAL REVENUES

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

	<u>Amount</u>
Amount of municipal equalization fund sent by CRIM	\$ 2,480,659
Compensation in lieu of tax from the Puerto Rico Electric Power Authority (PREPA)	1,563,781
Reimbursement from P.R. Department of Treasury - Christmas Bonus reimbursement	145,225
Other intergovernmental revenues	37,627
	<u>\$ 4,227,292</u>

NOTE P - RETIREMENT PLAN

1. Plan description

Regular employees of the Municipality contribute to a cost-sharing multiple employer defined benefit retirement plan, administered by the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). ERS covers all regular full-time public employees working for the central government, the municipalities of Puerto Rico and certain public corporations not having their own retirement systems. The system provides retirement pensions, death and disability benefits.

Retirement benefits depend upon age at retirement and number of years of credited service. Disability retirement benefits are available to members of occupational and non-occupational disabilities. Benefits vest after ten years of plan participation. The system was created under Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. Retirement benefits are determined by the application of 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 plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75% of the average compensation. ERS issues a publicly financial report that includes financial statements and required supplementary information of the Plan, which may be obtained from the ERS.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE P - RETIREMENT PLAN - Continued

Law No. 305 of September 24, 1999 amended Act No. 447 of 1951 and was enacted with the purpose of establishing a new pension program (System 2000). The new pension program became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999 may elect either to stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000 will only be allowed to become members of the new program.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. There will be a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. Benefits at retirement age will not be guaranteed by the State government and will be subjected to the total accumulated balance of the savings account. The annuity will be based on a formula, which assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. If the savings accounts balance is \$10,000 or less at time of retirement, the balance will be distributed by the System to the participant as a lump sum. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions have not been granted under the new program. The employer contributions (9.275% of the employee's salary) will be used to fund the current plan. Under System 2000 the retirement age is reduced from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

2. Funding policy

The Act 447, as amended, is the authority under which obligations to contribute to the Plan by the Plan members, employers and other contributing entities are established or may be amended. Plan members are required to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600 except for the Mayor or employee under a supplementation plan, which contributes 8.275% of gross salary. The Municipality is required to contribute 9.275% of gross salary.

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

Fiscal year ended:	Law No. 447	System 2000
2011	<u>\$ 169,857</u>	<u>\$ 189,991</u>
2010	<u>\$ 162,034</u>	<u>\$ 181,676</u>
2009	<u>\$ 170,972</u>	<u>\$ 177,720</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE Q – POSTEMPLOYMENT BENEFITS

In addition to the pension benefits described in Note P, the Municipality is required to cover annually the 3% increase in the retirement plan of its retired employees, as required by Commonwealth's laws. Also, the Municipality is required to finance costs related to the application of certain "Special Laws" issued by the Commonwealth Government. Those Special Laws granted increases in pensions and other benefits to retired employees of the Municipality such as medicines, bonuses, Christmas bonuses and death benefits. For the fiscal year 2010-11, costs related to these post-employment benefits amounted to \$90,306. These benefits are recorded as expenditures in the general fund.

NOTE R - COMMITMENTS

1. *Operating leases*

The Municipality leases office equipment under operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same terms. Rental expenses amounted to \$50,544. Management believes that the summary of the future minimum rental commitments under non-cancelable operating leases with terms exceeding one year is not significant.

2. *Construction*

The Municipality has commitments at June 30, 2011 of \$898,315 for construction, improvements or renovation of certain municipal facilities.

3. *Encumbrances*

As of June 30, 2011 the Municipality has outstanding encumbrances in the general fund of \$177,836 which are assigned for general government purposes (\$110,298), public works (\$53,987) and welfare purposes (\$13,551).

NOTE S - CONTINGENCIES

1. *Federal and Commonwealth grants*

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

2. *Litigations*

The Municipality is, at present, a defendant in a number of legal matters that arise in the ordinary course of the Municipality's activities. There are cases whereby the Municipality is a defendant or codefendant that will be covered by insurance, certain cases whereby the legal counsel has not determined an outcome and other cases that will not be covered by insurance. However, it is the opinion of the Municipality and the legal counsels that, based on their experience, such actions and the potential liabilities will not impair the Municipality's financial position.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE T – NET ASSETS \ FUND BALANCES RESTATEMENTS

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

Description	Fund Balances		
	General Fund	Commonwealth Legislature Resolutions Fund	Other Governmental Funds
Fund Balances at beginning of year, as previously reported	\$ 1,065,554	\$ 715,701	\$ 2,064,769
Reclassification of Law 52 Special Fund to Other Governmental Funds as a result of application of GASB Statement Number 54	(1,652)	-	(33,348)
Correction of error, Commonwealth's legislative resolution recorded in the general fund	-	35,000	-
Fund Balances at beginning of year, as restated	\$ 1,063,902	\$ 750,701	\$ 2,031,421

REQUIRED SUPPLEMENTARY INFORMATION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2011

	Budgeted amounts		Actual Amounts	Variance with
	Original	Final	(Budgetary Basis) (See Note A)	Final Budget Positive (Negative)
Revenues:				
Taxes:				
Property taxes	\$ 2,804,145	\$ 2,804,145	\$ 3,198,709	\$ 394,564
Municipal license taxes	1,500,000	1,500,000	1,403,376	(96,624)
Sales and use taxes	1,564,000	1,564,000	1,507,259	(56,741)
Intergovernmental	3,844,490	3,844,490	3,937,893	93,403
Fees, fines and charges for services	725,500	725,500	968,187	242,687
Interest	80,000	80,000	93,129	13,129
Other	73,000	120,000	119,136	(864)
Total revenues	<u>10,591,135</u>	<u>10,638,135</u>	<u>11,227,689</u>	<u>589,554</u>
Expenditures:				
Current:				
General government	5,368,224	6,206,484	6,189,098	17,386
Public works and sanitation	2,341,077	2,355,281	2,352,516	2,765
Public safety	721,332	702,173	701,602	571
Culture and recreation	767,349	765,820	765,324	496
Health	377,719	384,819	368,428	16,391
Welfare and community development	595,302	577,197	576,759	438
Education	21,800	18,100	18,087	13
Total expenditures	<u>10,192,803</u>	<u>11,009,874</u>	<u>10,971,814</u>	<u>38,060</u>
Excess (deficiency) of revenues over expenditures	398,332	(371,739)	255,875	627,614
Other financing sources (uses):				
Transfers in		19,071	19,071	-
Transfers out	(398,332)	(398,332)	(389,739)	8,593
Total other financing sources (uses)	<u>(398,332)</u>	<u>(379,261)</u>	<u>(370,668)</u>	<u>8,593</u>
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	-	(751,000)	(114,793)	636,207
Readjustment from prior year fund balance (note B)	-	751,000	-	(751,000)
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (114,793)</u>	<u>\$ (114,793)</u>

The accompanying notes to required supplemental information are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION -
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND**

June 30, 2011

NOTE A - BUDGET PROCESS AND BUDGETARY BASIS OF ACCOUNTING

The Municipal budget is prepared for the General Fund following the requirements of the Autonomous Municipal Law of 1981, as amended. It is developed utilizing elements of performance-based program budgeting and zero-based budgeting and includes estimates of revenues and other sources for ensuing fiscal year under laws existing at the time the budget is prepared.

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

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

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

NOTE B - BUDGET READJUSTMENT

The Budgetary Comparison Schedule - General Fund presents a fund balance readjustment of \$751,000. This represents a readjustment of current year budget with prior year's budgetary surpluses, approved by the Municipal Legislature.

NOTE C - BUDGET TO GAAP RECONCILIATION

The accompanying budgetary comparison schedule presents comparisons of the original and final legally adopted budget with actual data on a budgetary basis. Since accounting principles applied for the purposes of developing data on a budgetary basis differ significantly from those used to present accounting principles generally accepted in the United States, the following budget to GAAP reconciliation is presented:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION -
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND**

June 30, 2011

NOTE C - BUDGET TO GAAP RECONCILIATION - Continued

Excess of revenues and other financing sources over expenditures and other financing uses (budgetary basis):	\$	(114,793)
Budget to GAAP differences:		
Entity differences:		
Non-budgeted funds recorded as revenues for financial reporting purposes		843,834
Non-budgeted funds recorded as expenditures for financial reporting		(219,315)
Non-budgeted transfers-in		225,000
Basis of accounting differences:		
Revenues recorded for financial reporting purposes but not in budgetary basis		534,473
Revenues recorded in budgetary basis but not for financial reporting purposes		(431,003)
Expenditures recorded in budgetary basis but not for financial reporting purposes		217,267
Expenditures recorded for financial reporting purposes but not in budgetary basis		(411,330)
Timing differences:		
Current year encumbrances recorded as expenditures for budgetary reporting purposes		5,942
Prior year encumbrances recorded as expenditures for financial reporting purposes		(79,251)
Net change in fund balance (GAAP basis)	\$	<u>570,824</u>

SUPPLEMENTARY INFORMATION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2011

Line Item No.	Description	14.871 Housing Choice Vouchers
Balance Sheet		
111	Cash - unrestricted	\$ 38,588
113	Cash - other restricted	\$ 51,450
100	Total cash	\$ 90,038
121	Accounts receivable - PHA projects	\$ 9,631
122	Accounts receivable - HUD other projects	\$ -
125	Accounts receivable - miscellaneous	\$ 11,060
126.2	Allowance for doubtful accounts - other	\$ -
128	Fraud recovery	\$ 351
128.1	Allowance for doubtful accounts - fraud	\$ -
120	Total receivables, net of allowance for doubtful accounts	\$ 21,042
142	Prepaid Expenses and Other Assets	\$ 1,062
144	Inter program - due from	\$ -
150	Total Current Assets	\$ 112,142
164	Furniture, equipment and machinery - administration	\$ 19,872
166	Accumulated depreciation	\$ (19,644)
160	Total capital assets, net of accumulated depreciation	\$ 228
180	Total Non-current Assets	\$ 228
190	Total Assets	\$ 112,370
312	Accounts payable <= 90 days	\$ 11,245
322	Accrued compensated absences - current portion	\$ 3,349
331 - 030	Accounts payable - HUD PHA programs - Other	\$ -
332	Accounts Payable - PHA Projects	\$ 925
333	Accounts payable - other government	\$ 6,648
341	Tenant security deposits	\$ -
342	Deferred revenue	\$ -
345	Other current liabilities	\$ 1,479
347	Inter-program - due to	\$ -
348	Loan Liability - current	\$ -
310	Total Current Liabilities	\$ 23,646
353	Non-current liabilities - other	\$ 6,831
354	Accrued compensated absences - non current	\$ 8,473
350	Total Non-current Liabilities	\$ 15,304
300	Total Liabilities	\$ 38,950
508.1	Invested in Capital Assets, Net of Related Debt	\$ 228
511.1	Restricted Net Assets	\$ 39,591
512.1	Unrestricted Net Assets	\$ 33,601
513	Total Equity/Net Assets	\$ 73,420
600	Total Liabilities and Equity/Net Assets	\$ 112,370
Income Statement		
70600-010	Housing assistance payments	\$ 505,810
70600-020	Ongoing administrative fees earned	\$ 72,995
70600-070	Admin fee calculation description	
70600	HUD PHA operating grants	\$ 578,805
71500	Other revenue	\$ 47,565
700	Total Revenue	\$ 626,370
91100	Administrative salaries	\$ 49,471
91200	Auditing fees	\$ 5,000
91500	Employee benefit contributions- administrative	\$ 17,242
91600	Office expenses	\$ 10,421
91800	Travel	\$ 445
91000	Total Operating - Administrative	\$ 82,579
96200	Other general expenses	\$ 1,430
96210	Compensated absences	\$ 1,023
96600	Bad debt - other	\$ 344
96000	Total Other General Expenses	\$ 2,797
96900	Total Operating Expenses	\$ 85,376
97000	Excess Revenue Over Operating Expenses	\$ 540,994

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2011

Line Item No.	Description	14.871 Housing Choice Vouchers
97300-020	Home-Ownership	\$ 1,212
97300-050	All Other	\$ 522,743
97300	Housing assistance payments	\$ 523,955
97350	HAP Portability-in	\$ 33,664
97400	Depreciation expense	\$ 164
97500	Fraud losses	\$ 437
900	Total Expenses	\$ 643,596
10000	Excess (Deficiency) of Revenue Over (Under) Expenses	\$ (17,226)
11030	Beginning equity	\$ 90,646
11770-001	Administrative Fee Equity - Beginning Balance	\$ 32,910
11170-010	Administrative Fee Revenue	\$ 72,995
11170-020	Hard to House Fee Revenue	\$ -
11170-021	FSS Coordinator Grant	\$ -
11170-030	Audit Costs	\$ -
11170-040	Investment Income	\$ -
11170-045	Fraud Recovery Revenue	\$ -
11170-050	Other Revenue	\$ 47,565
11170-051	Comment For Other Revenue	This amount corresponds to the administrative fees earned on the portability-in vouchers administered by the Municipality (\$3,738) plus the reimbursement received from the initial PHAs of the HAP rent payments made on behalf of the portability-in units during 10-11 (\$33,664); and FSS salaries reimbursement received from another Municipality (\$10,163).
11170-060	Total Admin Fee Revenues	\$ 120,560
11170-080	Total Operating Expenses	\$ 85,376
11170-090	Depreciation	\$ 164
11170-095	Housing Assistance Portability In	\$ 33,664
11170-100	Other Expenses	\$ 437
11170-101	Comment For Other Expense	This amount corresponds to the fraud losses.
11170-110	Total Expenses	\$ 119,641
11170-002	Net Administrative Fee	\$ 919
11170-003	Administrative Fee Equity - Ending Balance	\$ 33,829
11170	Administrative Fee Equity	\$ 33,829
11180-001	Housing Assistance Payments Equity - Beginning Balance	\$ 57,736
11180-010	Housing Assistance Payments Revenues	\$ 505,810
11180-015	Fraud Recovery Revenue	\$ -
11180-020	Other Revenue	\$ -
11180-021	Comment For Other Revenue	
11180-025	Investment Income	\$ -
11180-030	Total HAP Revenues	\$ 505,810
11180-080	Housing Assistance Payments	\$ 523,955
11180-100	Total Housing Assistance Payments Expenses	\$ 523,955
11180-002	Net Housing Assistance Payments	\$ (18,145)
11180-003	Housing Assistance Payments Equity - Ending Balance	\$ 39,591
11180	Housing Assistance Payments Equity	\$ 39,591
11190-210	Total ACC HCV Units	1,236
11190	Unit Months Available	1,236
11210	Unit Months Leased	1,223

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTE TO SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE

June 30, 2011

NOTE A – BASIS OF PRESENTATION

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 standardize 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 management 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.

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.

SINGLE AUDIT SECTION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FISCAL YEAR ENDED JUNE 30, 2011

Federal Grantor/Pass Through Grantor/Program Title	Federal CFDA Number (note B)	Pass-Through Entity Identifying Number (note B)	Federal Expenditures (notes A and B)
<u>U.S. Department of Agriculture</u>			
Passed-through program from:			
<u>P.R. Department of Education</u> Child and Adult Care Food Program	10.558	CCC-029	\$ 20,180
<u>U.S. Department of Housing and Urban Development</u>			
Direct programs:			
Shelter Plus Care	14.238	PR46C603010	30,422
Section 8 Housing Choice Vouchers Program	14.871	RQ035	578,805
Passed-through programs from:			
<u>Office of Commissioner of Municipal Affairs:</u>			
CDBG - State-Administered Small Cities Program Cluster:			
Community Development Block Grant / State's Program (State-Administered Small Cities Program)	14.228	FC-30, AB-30 ADM-30	1,345,120
ARRA - Community Development Block Grant / State's Program (State-Administered Small Cities Program)	14.255	AR - 30	49,640
Total CDBG - State-Administered Small Cities Program Cluster:			<u>1,394,760</u>
<u>P.R. Department of Health:</u>			
Housing Opportunities for Persons with AIDS (HOPWA)	14.241	2010-V00038	43,082
<u>P.R. Department of Family:</u>			
ARRA - Homeless Prevention and Rapid Re-Housing Program Technical Assistance	14.262	122-2010-000229	123,938
<u>P.R. Department of Housing - (Puerto Rico Public Housing Administration "PRPHA"):</u>			
Public and Indian Housing	14.850	RQ-00500106D	143,964
Subtotal U.S. Department of Housing and Urban Development			<u>2,314,971</u>
<u>U.S. Department of Transportation</u>			
Direct program:			
Federal Transit_Formula Grants	20.507	PR-90	65,726
<u>U.S. Department of Health and Human Services</u>			
Passed-through programs from:			
<u>P.R. Office of the Ombudsman for the Elderly:</u>			
Special Programs for the Aging_Tittle III Part D_Disease Prevention and Health Promotion Services	93.043	110029R2, 110310R2, 110198R2, 110165R2	6,872
National Family Caregiver Support, Title III, Part E	93.052	110005R2	35,919
Nutrition Services Incentive Program	93.053	110310R2, 110198R2	28,529
<u>P.R. Department of Family - Families and Children Administration:</u>			
CCDF Cluster:			
Child Care and Development Block Grant	93.575	2010-2011-241-2011-000275	130,552
ARRA - Child Care and Development Block Grant	93.713	G-0901-PRCCD7	25,753
Total CCDF Cluster:			<u>156,305</u>
<u>"Instituto Socio-economico Comunitario, Inc.":</u>			
ARRA - Community Services Block Grant	93.710	VII-35-09-10-EMP-ARRA-009	25,819
Subtotal U.S. Department of Health and Human Services:			<u>253,444</u>
Total Expenditures of Federal Awards			<u><u>\$ 2,654,321</u></u>

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2011

NOTE A – BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality under programs of the federal government for the year ended June 30, 2011. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments and Nonprofit Organizations*. Therefore, some amounts presented in this schedule may differ from the amounts presented in, or used in the preparation of, the basic financial statements. Because the schedule presents only a selected portion of the operations of the Municipality, it is not intended to and does not present the financial position and changes in net assets of the Municipality.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported on the modified accrual basis of accounting. Such expenditures are recognized when the related liability is incurred following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

The Catalog of Federal Domestic Assistance (CFDA) Number is a program identification number. The first two digits identify the federal department or agency that administers the program and the last three numbers are assigned by numerical sequence.

State or local government redistributions of federal awards to the Municipality, known as “pass-through awards”, should be treated by the Municipality as though they were received directly from the federal government. OMB Circular A-133 requires the schedule to include the name of the pass-through entity and the identifying number assigned by the pass-through entity for the federal awards received as a subrecipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

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

<u>Description</u>	<u>Community Development Block Grant Program Fund</u>	<u>Other Governmental Funds</u>
10.558	\$ -	\$ 20,180
14.238	-	30,422
14.871	-	578,805
14.228	1,345,120	-
ARRA – 14.255	49,640	-
14.241	-	43,082
ARRA – 14.262	-	123,938
14.850	-	143,964
20.507	-	65,726
93.043	-	6,872
93.052	-	35,919
93.053	-	28,529

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2011

NOTE C – RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE BASIC FINANCIAL STATEMENTS – Cont.

<u>Description</u>	<u>Community Development Block Grant Program Fund</u>	<u>Other Governmental Funds</u>
93.575	-	130,552
ARRA – 93.713	-	25,753
ARRA – 93.710	-	25,819
Total federal awards expenditures	1,394,760	1,259,561
Total non-federal awards expenditures	-	1,230,430
Total expenditures, fund statements	<u>\$ 1,394,760</u>	<u>\$ 2,489,991</u>

VALDES, GARCIA , MARIN & MARTINEZ, LLP

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS
MEMBER OF THE AICPA PRIVATE COMPANIES PRACTICE SECTION

P.O. Box 364831
SAN JUAN, P.R. 00936-4831

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

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Hormigueros (the Municipality), as of and for the year ended June 30, 2011, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated March 21, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Municipality's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions 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.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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

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 grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Municipality's management, the Honorable Mayor, Members of the Municipal Legislature, the Commonwealth of Puerto Rico, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



San Juan, Puerto Rico
March 21, 2012

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VALDES, GARCIA , MARIN & MARTINEZ, LLP

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INDEPENDENT AUDITOR'S 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 OMB CIRCULAR A-133

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

Compliance

We have audited the Municipality of Hormigueros' (the Municipality) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Municipality's major federal programs for the year ended June 30, 2011. The Municipality's major federal programs are identified in the summary of auditors' 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 other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Municipality's compliance with those requirements.

In our opinion, 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, 2011.

Internal Control over Compliance

Management of the Municipality is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered 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 the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

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

This report is intended solely for the information and use of the Municipality's management, the Honorable Mayor, Members of the Municipal Legislature, the Commonwealth of Puerto Rico, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, appearing to read "Jose Luis Torres" followed by some initials or a flourish.

San Juan, Puerto Rico
March 21, 2011

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FISCAL YEAR ENDED JUNE 30, 2011

Section I - Summary of Audit Results

A. Summary of audit results:

Part I - Financial Statements

1. Type of audit report: Unqualified opinion Qualified opinion
 Adverse opinion Disclaimer of opinion
2. Significant deficiencies Yes No
3. Significant deficiencies reported as material weaknesses Yes None reported
4. Material noncompliance disclosed Yes No

Part II - Federal Awards

1. Significant deficiencies Yes No
2. Significant deficiencies reported as material weaknesses Yes None reported
3. Type of auditors' report on compliance major programs Unqualified opinion Qualified opinion
 Adverse opinion Disclaimer of opinion
4. Audit findings required to be reported under Section 510(a) of Circular A-133 Yes No

5. Major programs

CFDA Number(s)	Name of Federal Program or Cluster
14.228	Community Development Block Grants/State's Program
14.255	ARRA - Community Development Block Grants/State's Program
14.850	Public and Indian Housing
14.871	Section 8 Housing Choice Vouchers

6. Dollar threshold used to distinguish Type A and Type B programs: \$300,000
7. Auditee qualified as low-risk auditee? Yes No

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FISCAL YEAR ENDED JUNE 30, 2011

Section II - Financial Statements Findings

Finding No matters reported.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FISCAL YEAR ENDED JUNE 30, 2011

Section III - Federal Awards Findings and Questioned Costs

Finding

No matters reported.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HORMIGUEROS**

**SCHEDULE OF STATUS OF PRIOR YEARS AUDIT
FINDINGS AND QUESTIONED COSTS**

FISCAL YEAR ENDED JUNE 30, 2011

No matters reported.