



MUNICIPALITY OF HUMACAO, PUERTO RICO
ANNUAL FINANCIAL REPORT
FISCAL YEAR ENDED JUNE 30, 2008



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MUNICIPALITY OF HUMACAO, PUERTO RICO

ANNUAL FINANCIAL REPORT

FISCAL YEAR ENDED JUNE 30, 2008

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ROMAN TORO & CO., PSC

Certificate Public Accountants

Honesty - Integrity - Experience

Members of:
American Institute of Certified Public Accountants
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INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and Members of the
Municipal Assembly
Municipality of Humacao, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of **Municipality of Humacao, Puerto Rico**, as of and for the year ended June 30, 2008, which collectively comprise the Municipality of Humacao, Puerto Rico's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Municipality of Humacao, Puerto Rico'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 the 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 Humacao, Puerto Rico, as of June 30, 2008, and the respective changes in financial position, 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 December 22, 2008, on our consideration of the Municipality of Humacao, Puerto Rico's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

**INDEPENDENT AUDITOR'S REPORT
(CONTINUED)**

The management's discussion and analysis and budgetary comparison information on pages 3 through 14 and 44 through 45, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Roman Toro & Co.
ROMAN TORO & CO., CSP
LICENSE #35 - IN FORCE

Yauco, Puerto Rico
December 22, 2008

Stamp #2373212 was affixed to
the original of this report

MANAGEMENT DISCUSSION AND ANALYSIS

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

The following discussion and analysis of the Municipality of Humacao's financial performance provides an overview of the Municipality's financial activities for the fiscal year ended June 30, 2008. Please read it in conjunction with the financial statements which follow this section.

FINANCIAL HIGHLIGHTS

Highlights for Government-wide Financial Statements

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

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2007 by \$91,546,242 and 2008 by \$102,333,314 (net assets).
- Revenues increased by \$8,641,384 (14.3%) and expenses increased \$5,905,119 (11.3%) in comparison with year 2007.
- Net change in net assets amounted to \$10,787,072, an increase of 34% with respect to prior year (2007) net change.

Highlights for Fund Financial Statements

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

- At the close of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$57,070,118, an increase of \$1,906,269 in comparison with the prior year.
- The General Fund reported an excess of revenues over expenditures of \$4,987,408 and Transfer to Capital Projects the amount of \$3,916,656. Also, \$722,734 was transfer to Debt Service Fund to cover the principal and interests of operating bonds. General Fund reported unreserved fund balance of \$13,394,917, an increased of \$4,106,697 from prior year.

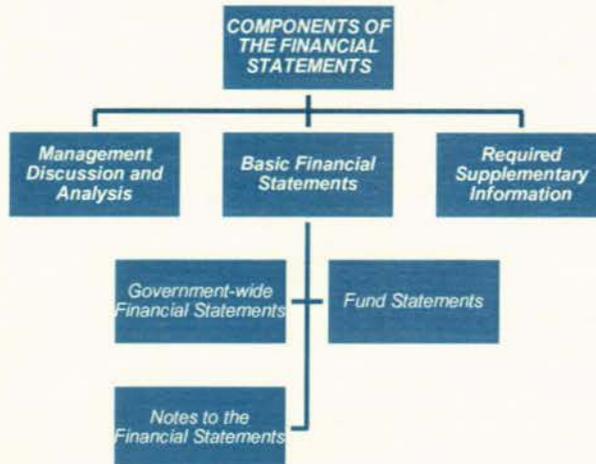
General Financial Highlights

- The investment in net capital assets as of June 30, 2008 was \$67,642,400 (net of related debt).
- Long-Term General and Special Obligations decreased to \$44,259,975 approximately the same as prior year balance, by the issuances of new bonds in the amount of \$2,055,000 for general construction and the payment of \$2,060,262.
- Other long-term debts increases and net reductions from payments amounted to \$1,064,003 and \$409,433, respectively.
- On a budgetary basis, actual revenues exceeded actual expenditures by \$3,148,292, net of \$4,978,397 designated general fund for future expenditures (transfers out to capital project fund and debt service fund).
- Revenues increase (\$9,868,914) was mainly due to \$3,344,707 of new enacted Sales Taxes, \$1,609,978 of volume of business taxes, construction taxes of \$2,185,987, and \$1,358,316 of interest revenues. Expenditures were more than estimated by \$1,031,472, but transfer out to capital project increases the negative variance.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

OVERVIEW OF THE FINANCIAL STATEMENTS

The Municipality's basic financial statements comprise three components: (1) management discussion and analysis (presented here), (2) basic financial statements, and (3) required supplementary information.



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

Basic Financial Statements

- **Government-Wide Financial Statements**

The government-wide statements report information about the Municipality as a whole using accounting methods similar to those used by private-sector businesses. They are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. The first government-wide statement – the *Statement of Net 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 roads and other infrastructure 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.

The government-wide statements reports as governmental activities the Municipality's basic services such as public safety, public works, health and sanitation, culture and recreation, solid waste disposal, human services and 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

- **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 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 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 complies 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 the financial statements**

Provides integral information needed to explain the basis for the numbers used within the Basic Financial Statements and provide more detailed data.

Required supplementary information

Provides additional information to better understand the financial position of the Municipality and contains the Budgetary Comparison Schedule for the General Fund.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

The following table presents a summary of the Statements of Net Assets as of June 30, 2008 and 2007:

Tabla 1			
Commonwealth of Puerto Rico			
Municipality of Humacao, Puerto Rico			
Statement of Net Assets			
June 30,			
	2008	2007	
Current and Non-current Assets	\$ 86,951,566	\$ 84,466,914	
Capital Assets	84,143,298	76,098,572	
Total Assets	171,094,864	160,565,486	
Current liabilities	3,476,415	3,394,211	
Deferred Revenues	12,619,218	13,531,497	
Long-term liabilities	52,665,917	52,093,536	
Total Liabilities	68,761,550	69,019,244	
Net Assets:			
Investment in Capital Assets, Net of Related Debt	67,642,400	62,686,902	
Restricted	25,041,677	23,269,325	
Unrestricted	9,649,237	5,590,015	
Total Net Assets	\$ 102,333,314	\$ 91,546,242	

Net assets (assets over liabilities) may serve over time as a useful indicator of a government's financial position. Net assets for the year increased 10% with respect to prior year as restated.

The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure) for \$67,642,400; total capital assets (\$113,134,520) less accumulated depreciation (\$28,991,222) and less any related outstanding debt (\$16,500,898) 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.

As of June 30, 2008 the Municipality presented unrestricted net assets of \$9,649,237. This balance was affected by long term obligations such as compensated absences \$5,420,149 and other debts for the amount of \$2,836,066 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.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Changes in net assets

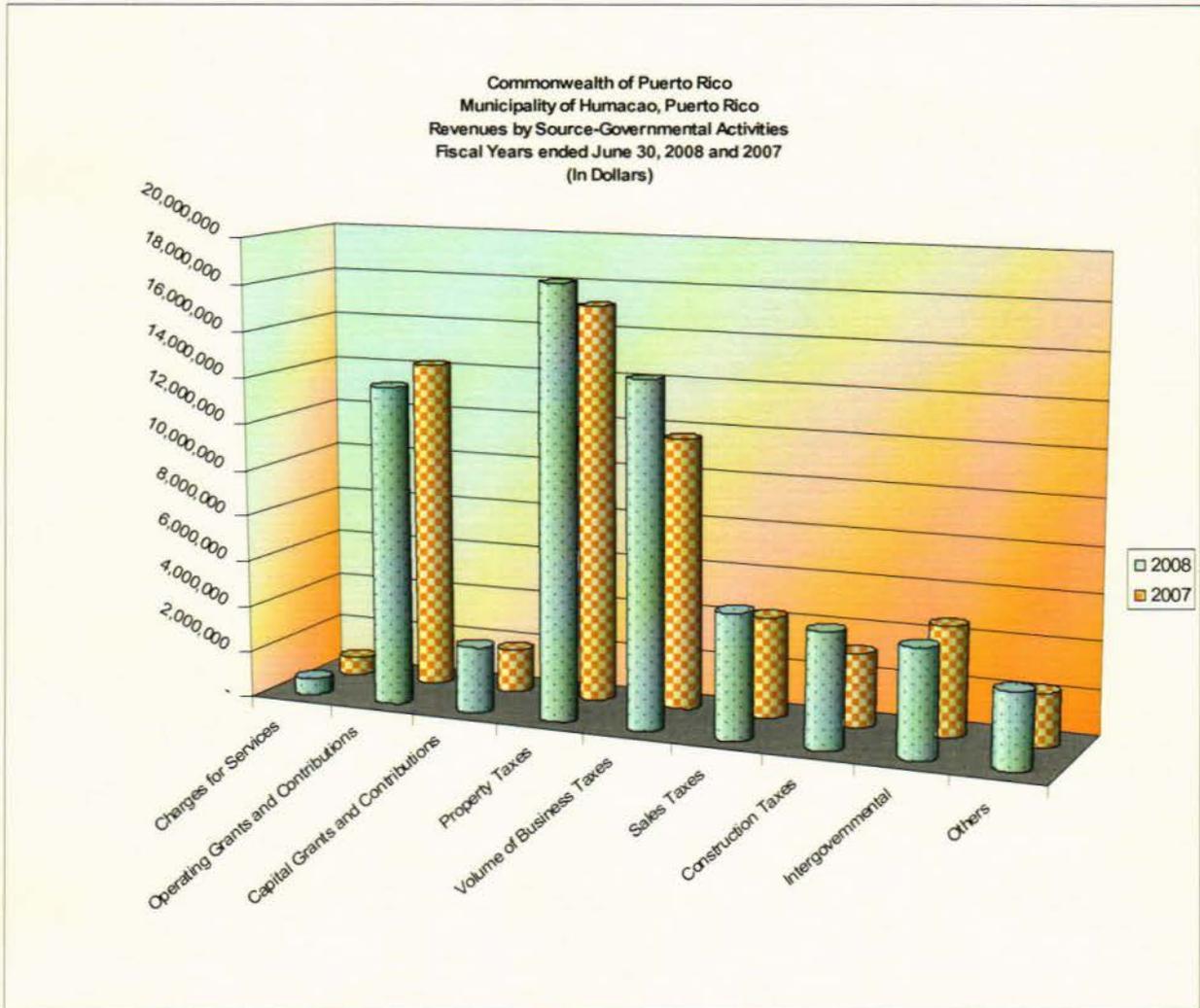
The following table summarizes the changes in net assets for the years ended June 30, 2008 and 2007:

Tabla 2		
Commonwealth of Puerto Rico		
Municipality of Humacao, Puerto Rico		
Change in Net Assets		
For the Fiscal Years Ending June 30,		
	2008	2007
Revenues:		
Program Revenues:		
Changes for Services	\$ 718,756	\$ 781,144
Operating Grants and Contributions	13,773,472	14,226,041
Capital Grants and Contributions	2,847,194	1,866,680
General Revenues:		
Property Taxes	18,529,331	17,172,409
Volume of Business Taxes	14,769,978	11,718,520
Sales Taxes	5,365,707	4,354,861
Construction Taxes	4,955,987	3,168,514
Intergovernmental	4,670,763	4,685,973
Other General Revenues	3,256,923	2,272,585
Total Revenues	<u>68,888,111</u>	<u>60,246,727</u>
Expenses:		
General Administration	27,303,446	20,197,780
Public Safety	2,612,229	2,663,796
Public Works	3,068,679	3,538,710
Culture and Recreation	1,968,021	1,945,079
Health and Sanitation	1,903,279	1,888,692
Education	8,666,599	9,019,632
Solid Waste Disposal	3,480,483	2,886,482
Human Services and Welfare	6,735,616	6,422,210
Urban Development	-	1,885,462
Loss on Disposal of Asset	2,465	-
Interest Costs	2,360,222	1,748,077
Total Expenses	<u>58,101,039</u>	<u>52,195,920</u>
Changes in Net Assets	10,787,072	8,050,807
Net Assets-Beginning	91,546,242	83,495,435
Net Assets-Ending	<u>\$ 102,333,314</u>	<u>\$ 91,546,242</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

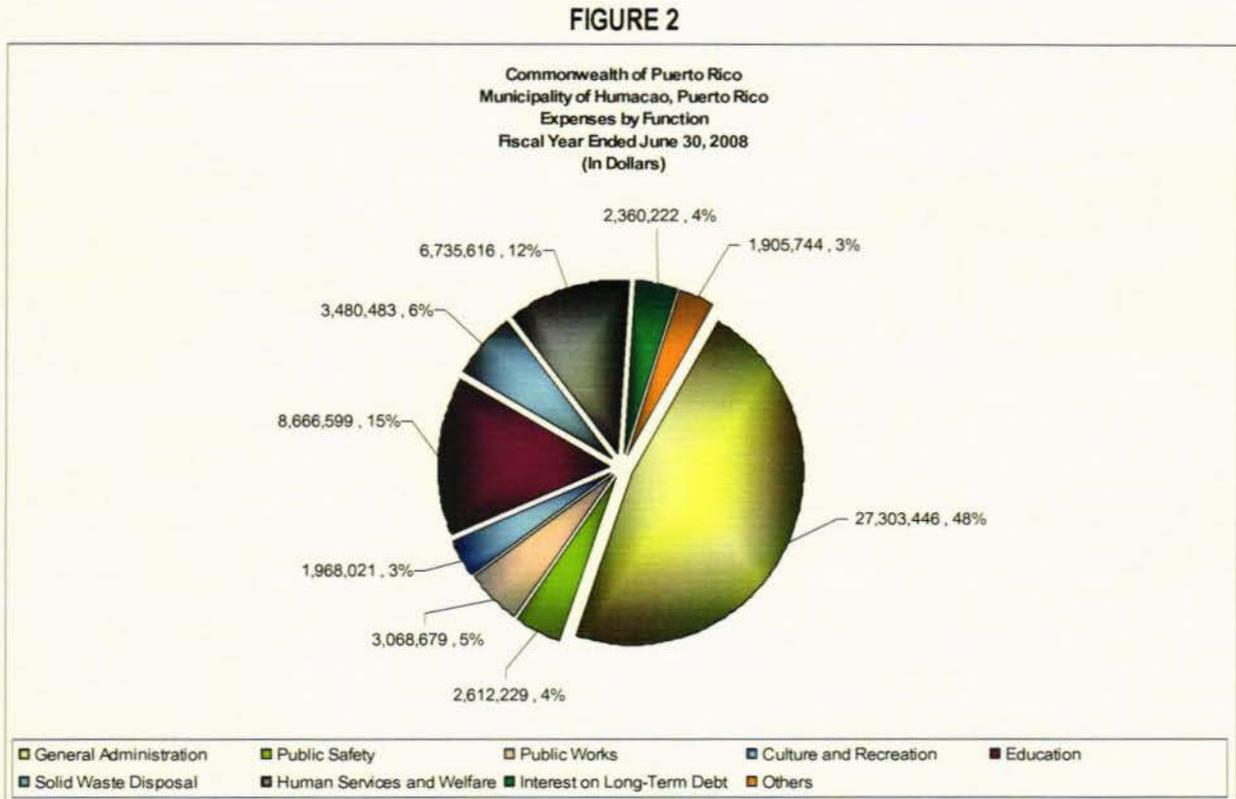
Figure 1 presents revenues comparison by sources of the governmental activities during the past two years:

FIGURE 1



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Figure 2 presents expenses by function of the governmental activities during the fiscal year 2007-2008:



Approximately 24% of the Municipality's revenues came from grants and contributions, 27% from property taxes, volume of business taxes 21% and 28% from other sources. The Municipality's expenses cover a range of services. The largest expenses are general administration with 47%, education with 15%, and human services and welfare with 11.6. Program revenues of the Municipality covered 30% of total expenses.

With respect to prior year, revenues increased by approximately \$8,641,384 or 14.3%, principally due to the new enacted sales taxes (\$5,365,707 millions). Significant increase was in property taxes, volume of business taxes, construction taxes and interest on investments with approximately \$5,850,924 for the promotion on new commercial industries and constructions.

Expenses increased 11.3% or \$5,905,119 in comparison with 2007 year, principally in general administration and interest on long-term debts.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

The following table focuses on the cost of each of the Municipality's largest functions/programs as well as each functions/program's net cost (total cost less fees generated by the programs and program-specific intergovernmental aid):

Tabla 3				
Commonwealth of Puerto Rico				
Municipality of Humacao, Puerto Rico				
Net Cost of Municipality's Governmental Activities				
For the Fiscal Years Ended June 30,				
	Total Cost of Services		Net Cost of Services	
Functions/Programs	2008	2007	2008	2007
General Administration	\$ 27,303,446	\$ 20,197,780	\$ 25,425,953	\$ 19,416,978
Public Safety	2,612,229	2,663,796	2,249,688	2,011,975
Public Works	3,068,679	3,538,710	2,594,344	2,522,999
Culture and Recreation	1,968,021	1,945,079	1,916,416	1,894,466
Education	8,666,599	9,019,632	590,631	132,422
Solid Waste Disposal	3,480,483	2,886,482	3,480,483	2,886,482
Human Services and Welfare	6,735,616	6,422,210	3,804,086	3,582,326
Interest on Long-Term Debt	2,360,222	1,748,077	2,360,222	1,748,077
Others	1,905,744	3,774,154	(1,660,206)	1,126,330
Total	\$ 58,101,039	\$ 52,195,920	\$ 40,761,617	\$ 35,322,055

Some of the cost of governmental activities in 2008 was paid by those who directly benefited from the programs (\$718,756) and other governments and organizations that subsidized certain programs with grants and contributions (\$16,620,666). The \$40,761,617 net cost of services was substantially covered by other general revenues including property, volume of business license taxes, sales taxes and intergovernmental.

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, unreserved fund balance may serve as a useful measure of a Municipality's net resources available at the end of a fiscal year. For the Fiscal year ended June 30, 2008, the governmental funds reported combined ending fund balances of \$57,070,118, a net increase of \$1,906,269 in comparison with the prior year. This increase was caused primarily by a net change in the general fund corresponding to excess of revenues \$9.4 million. Of total combined fund balances, \$13,394,917 (23.4%) constitutes unreserved fund balance of general fund. The remainder of fund balance is reserved to indicate that is not available for new spending.

The general fund is the operating fund of the Municipality. Unreserved fund balance of the general fund represents approximately 89.7% of total ending general fund balance. For the year ended June 30, 2008, the fund balance of the general fund increased by \$4,106,697 when compared with the prior year. The net increase is due to excess of revenues over expenditures, principally by the new enacted sales taxes that provide \$5.4 million of revenues.

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

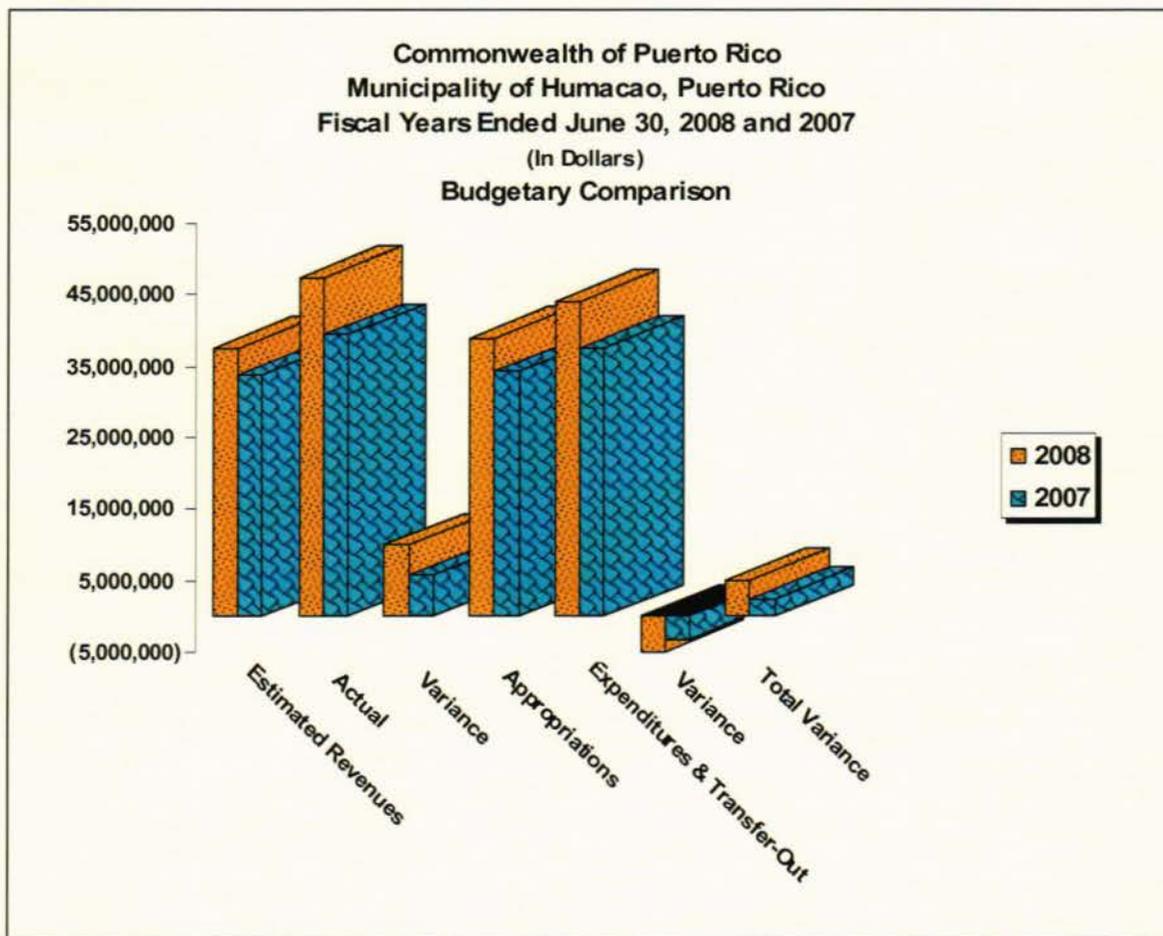
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

GENERAL FUND BUDGETARY HIGHLIGHTS

The general fund original budget for the fiscal period 2007-2008 presented an increase of 11.3% with respect to prior year budget. During the fiscal year budget revenues were increased by \$9,868,914 mainly due to excess in property taxes, volume of business taxes, construction taxes, interest on investment, and the new enacted sales taxes, but the Municipality does not included as an amendment to the original budget. Budget expenditures were amended during the year in accordance with functions estimates. Nevertheless, non budgeted transfers to non-major funds were used to pass economies in appropriations to specific capital projects of \$3.9 millions.

A positive variance of \$4,573,713 between revised budget and actual expenditures was due mainly to additional revenues as explain in the preceding paragraph and economies in some functions, but the transfer out to capital project fund of \$3.9 million reduce the variance. The Municipality reported more expenditure than appropriations in those functions on payments for purchase of supplies, equipment, and professional and nonprofessional services.

FIGURE 3



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets

At the end of the fiscal year, the Municipality has invested \$84,143,298 (net of accumulated depreciation) in a broad range of capital assets, including buildings, parks, roads, bridges, land and equipment. This amount represents a net increase of \$8,044,724 or over 10% from the prior year.

Commonwealth of Puerto Rico Municipality of Humacao, Puerto Rico Capital Assets, net As of June 30,		
	Governmental Activities	
	2008	(As restated) 2007
Non-Depreciable Assets:		
Land	\$ 11,390,661	\$ 7,418,626
Construction in Progress	23,104,931	18,559,112
Depreciable Assets:		
Buildings	34,241,962	35,234,094
Infrastructure	11,525,706	11,791,894
Motor Vehicles	1,751,358	1,352,607
Equipment	1,957,840	1,435,461
Capital Lease	170,838	306,778
Total	\$ 84,143,296	\$ 76,098,572

The Municipality invested a total of \$10,343,656 in capital assets during the fiscal year 2007-2008. Principal addition is as follows:

- Land acquisition - \$3,974,500
- Construction in Progress - \$4,545,819 -

The principal projects are the following:

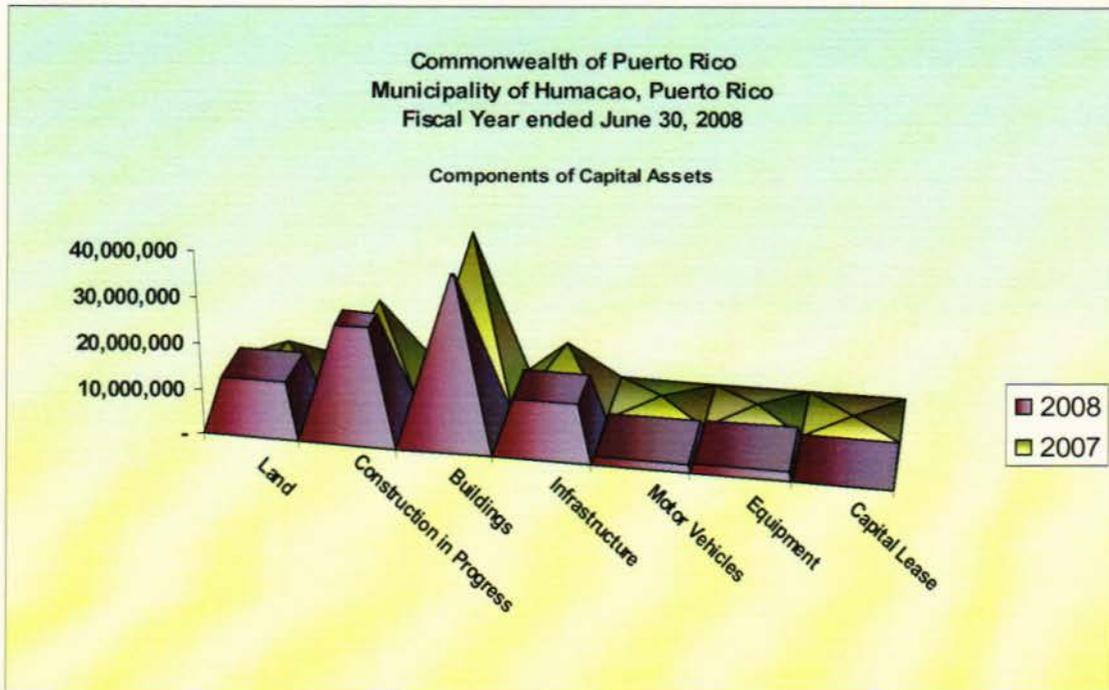
- Design of Exclusive Auto Line (\$862,655)
- Municipal Coliseum (\$1,447,014)
- Casona Artistic Center (\$931,387)
- Various Projects (\$1,304,763)
- Acquisition of Motor Vehicles - \$842,636
- Acquisition of Equipment - \$976,074

Projects in the amount of \$9,548,044 were finished.

Other projects related to repair and maintenance of roads (not capitalized) and facilities was developed during the year 2008.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

FIGURE 4



Long term debt

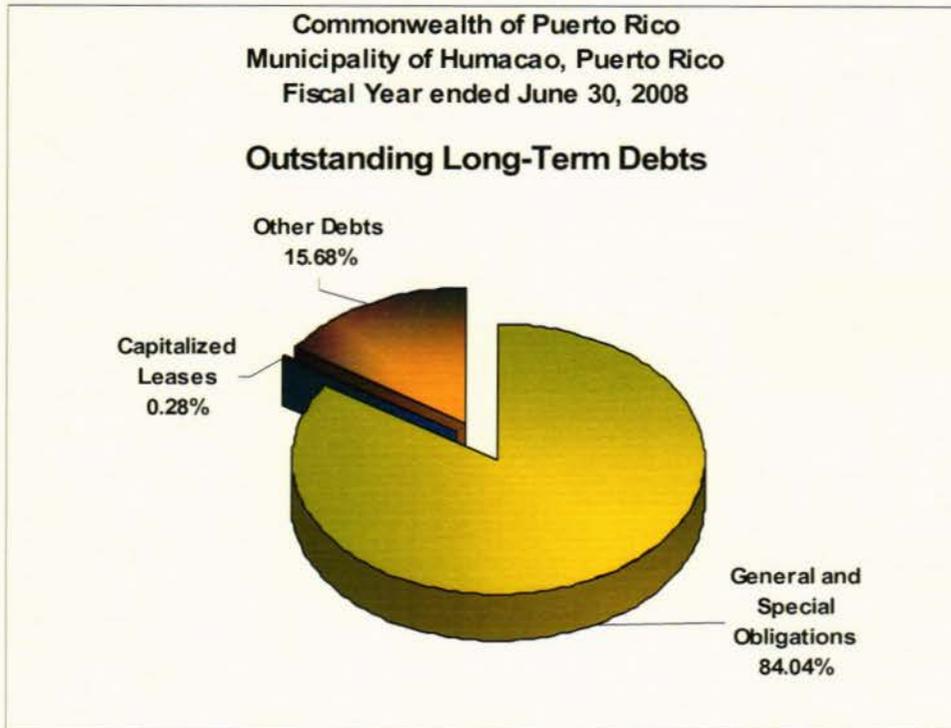
At year-end, the Municipality had \$44,259,975 in general and special bonds and notes, approximately the same as prior year balance, by the issuances of new bonds in the amount of \$2,055,000 for general construction and the payment of \$2,060,262. The following is a summary of the Municipality's outstanding debt as of June 30, 2008 and 2007:

Tabla 5		
Commonwealth of Puerto Rico		
Municipality of Humacao, Puerto Rico		
Outstanding Long-term Debts		
As of June 30,		
	Governmental Activities	
	2008	2007
General and Special Obligation Bonds and Note	\$ 44,259,975	\$ 44,265,237
Capitalized Leases	149,727	226,651
Others Debts	8,256,215	7,601,645
Total	\$ 52,665,917	\$ 52,093,533

The increase in the others debts is due to recognition of property taxes final liquidation, and increase in compensated absences. More detailed information about the Municipality's long-term liabilities is presented in Notes 9 and 10 to the financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

FIGURE 5



ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's selected and appointed officials considered many factors when setting the fiscal year 2007-2008 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 13.8%, which compares with the Commonwealth rate of 12.7%.

The Municipality applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2009 are \$43 million, approximately \$5.5 million more than the fiscal year 2008. The Municipality expects an increase in revenues for the next years due to the new sales tax, volume of business taxes, construction taxes and interest on investments as in the past two years. Also, revenues increases from other sources are demonstrative of the economic development from new commerce and stability of the manufacturing industry. Budgeted expenditures are expected to stabilize accordingly to the projected revenues. Among planned projects, this budget may be adjusted in accordance with economic injection projected when the construction project promoted by the Municipality and others private projects were develop during the year.

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 Finance Department at [(787) 852-2730] or P.O. Box 178, Humacao, Puerto Rico 00792.

BASIC FINANCIAL STATEMENTS

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

STATEMENT OF NET ASSETS

JUNE 30, 2008

	<u>GOVERNMENTAL ACTIVITIES</u>
ASSETS:	
Cash and Investments	\$ 57,417,648
Cash with Fiscal Agent	18,453,808
Receivables (net):	
Property Taxes	79,103
Due from Governmental Units	31,661
Federal Grants	10,034,343
Sales Tax	401,561
Others	304,031
Deferred Charges	229,411
Capital Assets:	
Land, Improvement and Construction in Progress	24,947,548
Other Capital Assets [Net of Depreciation]	<u>59,195,750</u>
TOTAL ASSETS	<u>\$ 171,094,864</u>
 LIABILITIES:	
Accounts Payable and Accrued Expenses	\$ 2,290,885
Accrued Interest	994,383
Due to Governmental Units	191,147
Deferred Revenues	12,619,218
Long-Term Liabilities:	
Due Within One Year	6,633,122
Due in More than One Year	<u>46,032,795</u>
TOTAL LIABILITIES	<u>68,761,550</u>
 NET ASSETS:	
Investment in Capital Assets, Net of Related Debt	67,642,400
Restricted for:	
Capital Project	801,860
Head Start	3,966,055
Debt Service	10,195,553
Community Development Projects	2,676,601
Other Purposes	7,401,608
Unrestricted	<u>9,649,237</u>
TOTAL NET ASSETS	<u>\$ 102,333,314</u>

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

STATEMENT OF ACTIVITIES

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenues (See Next Page)
		Charges For Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
Mayor and Municipal Legislature	\$ 2,616,201	\$ -	\$ -	\$ -	\$ (2,616,201)
General Government	24,687,245	-	1,877,493	-	(22,809,752)
Public Safety	2,612,229	-	362,541	-	(2,249,688)
Public Works	3,068,679	-	474,335	-	(2,594,344)
Culture and Recreation	1,968,021	-	51,605	-	(1,916,416)
Health and Sanitation	1,903,279	718,756	-	-	(1,184,523)
Public Instruction	8,666,599	-	8,075,968	-	(590,631)
Solid Waste Disposal	3,480,483	-	-	-	(3,480,483)
Human Services and Welfare	6,735,616	-	2,931,530	-	(3,804,086)
Urban Development	-	-	-	2,847,194	2,847,194
Loss on Disposition of Asset	2,465	-	-	-	(2,465)
Interest on Long-Term Debt	2,360,222	-	-	-	(2,360,222)
Total Governmental Activities	\$ 58,101,039	\$ 718,756	\$ 13,773,472	\$ 2,847,194	(40,761,617)

General Revenues:

Taxes:

Property Taxes, levied for General Purposes	13,587,982
Property Taxes, levied for Debt Service	4,941,349
Volume of Business Taxes	14,769,978
Sales Taxes	5,365,707
Construction Taxes	4,955,987
Intergovernmental	4,670,763
Rent	84,475
Miscellaneous	414,132
Interest	2,758,316

Total General Revenues and Transfers 51,548,689

CHANGES IN NET ASSETS 10,787,072

Net Assets – Beginning of Year 91,546,242

NET ASSETS – ENDING OF YEAR \$ 102,333,314

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

BALANCE SHEET – GOVERNMENTAL FUNDS

JUNE 30, 2008

	GENERAL FUND	HEAD START FUND	ART CENTER FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS:						
Cash and Investment	\$ 26,759,973	\$ 119,429	\$ 11,206,098	\$ -	\$ 19,332,148	\$ 57,417,648
Cash with Fiscal Agent	562,793	-	10,732	11,110,833	6,769,450	18,453,808
Receivables:						
Property Taxes	-	-	-	79,103	-	79,103
Sales Taxes	401,561	-	-	-	-	401,561
Federal Grants	-	4,735,285	-	-	5,299,058	10,034,343
Due from Other Funds	1,063,616	-	-	-	75,842	1,139,458
Due from Governmental Units	-	-	-	-	31,661	31,661
Other Receivables	-	-	-	-	304,031	304,031
Total Assets	\$ 28,787,943	\$ 4,854,714	\$ 11,216,830	\$ 11,189,936	\$ 31,812,190	\$ 87,861,613
LIABILITIES AND FUND BALANCES:						
Liabilities:						
Account Payable	\$ 1,187,525	\$ 8,000	\$ -	\$ -	\$ 1,095,360	\$ 2,290,885
Bond and Notes	-	-	-	2,125,000	-	2,125,000
Account Interest	-	-	-	994,383	-	994,383
Due to Federal Government	-	-	-	-	136,887	136,887
Due to Governmental Units	54,260	-	-	-	-	54,260
Due to Other Funds	170	178,806	-	-	960,482	1,139,458
Deferred Revenues:						
Volume of Business Tax	12,619,218	-	-	-	-	12,619,218
Others	-	4,267,422	-	-	-	4,267,422
Federal Grants	-	-	-	-	7,163,982	7,163,982
Total Liabilities	13,861,173	4,454,228	-	3,119,383	9,356,711	30,791,495
Fund Balances:						
Reserve For:						
Encumbrances	1,531,853	-	-	-	-	1,531,853
Debt Service	-	-	-	8,070,553	-	8,070,553
Head Start Program	-	400,486	-	-	-	400,486
Capital Projects	-	-	11,216,830	-	-	11,216,830
Other Purposes	-	-	-	-	22,455,479	22,455,479
Unreserved	13,394,917	-	-	-	-	13,394,917
Total Fund Balances	14,926,770	400,486	11,216,830	8,070,553	22,455,479	57,070,118
Total Liabilities and Fund Balances	\$ 28,787,943	\$ 4,854,714	\$ 11,216,830	\$ 11,189,936	\$ 31,812,190	\$ 87,861,613

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS

JUNE 30, 2008

Total Fund Balances – Government Funds (Page 17) **\$ 57,070,118**

Amount reported for Governmental Activities in the Statement of Net Assets (Page 15)
are different because:

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

Non Depreciable Capital Assets	\$ 24,947,548	
Depreciable Capital Assets	66,183,197	
Infrastructure Assets	22,003,775	
Accumulated Depreciation	<u>(28,991,222)</u>	
Total Capital Assets		84,143,298

Other Assets used in governmental activities are not financial resources and therefore
are not reported in the funds:

Deferred Charges		229,411
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Some of the **Municipality's** revenues will be collected after year-end but are not available
soon enough to pay for the current period's expenditures and therefore are deferred in the funds:

CDBG Program	2,528,075	
Head Start Program	4,267,422	
Early Head Start Program	1,375,414	
Other Major Fund	<u>3,260,493</u>	
Total Deferred Revenues		<u>11,431,404</u>

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

General and Special Obligation Bonds and Note	(42,134,975)	
Capital Leases	(149,727)	
Property Tax Advance - MRCC	(284,976)	
Law Number 146 - MRCC	(701,231)	
LIMS Debt - MRCC	(766,575)	
Law Number 42 - MRCC	(455,208)	
Claims and Judgments	(478,000)	
Employees Retirement Administration	(28,992)	
Unemployment	(121,084)	
Compensated Absences	<u>(5,420,149)</u>	
Total Long-Term Liabilities		<u>(50,540,917)</u>

Total Net Assets of Governmental Activities (Page 15) **\$ 102,333,314**

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE – GOVERNMENTAL FUNDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

	GENERAL FUND	HEAD START FUND	ART CENTER	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
REVENUES:						
Property Taxes	\$ 13,587,982	\$ -	\$ -	\$ 4,941,349	\$ -	\$ 18,529,331
Volume of Business Taxes	14,769,978	-	-	-	-	14,769,978
Sales Taxes	5,365,707	-	-	-	-	5,365,707
Federal Assistances	-	7,051,773	-	-	5,974,154	13,025,927
Intergovernmental	4,670,763	-	-	-	1,387,249	6,058,012
Licenses and Permits	4,955,987	-	-	-	-	4,955,987
Charges for Services	718,756	-	-	-	-	718,756
Interest	2,758,316	-	562,037	-	407,665	3,728,018
Miscellaneous	498,607	-	-	-	3,789	502,396
Total Revenues	<u>47,326,096</u>	<u>7,051,773</u>	<u>562,037</u>	<u>4,941,349</u>	<u>7,772,857</u>	<u>67,654,112</u>
EXPENDITURES:						
Current:						
Mayor and Municipal Legislature	2,284,489	-	-	-	-	2,284,489
General Government	17,688,556	-	-	-	2,284,862	19,973,418
Public Safety	2,301,877	-	-	-	258,200	2,560,077
Public Works	2,764,107	-	-	-	-	2,764,107
Culture and Recreation	1,395,791	-	-	-	192,434	1,588,225
Health and Sanitation	1,893,266	-	-	-	-	1,893,266
Public Instruction	-	6,687,663	-	-	1,978,936	8,666,599
Solid Waste Disposal	3,480,483	-	-	-	-	3,480,483
Human Services and Welfare	4,186,650	-	-	-	2,548,601	6,735,251
Urban Development	907,137	-	-	-	1,562,777	2,469,914
Capital Outlay	998,234	-	-	-	9,345,423	10,343,657
Debt Service:						
Principal	-	-	-	2,675,068	-	2,675,068
Interest and Other Charges	-	-	-	2,360,222	-	2,360,222
Bond Issue Costs	-	-	-	8,067	-	8,067
Total Expenditures	<u>37,900,590</u>	<u>6,687,663</u>	<u>-</u>	<u>5,043,357</u>	<u>18,171,233</u>	<u>67,802,843</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	<u>9,425,506</u>	<u>364,110</u>	<u>562,037</u>	<u>(102,008)</u>	<u>(10,398,376)</u>	<u>(148,731)</u>
OTHER FINANCING SOURCES (USES):						
Proceed of Bonds	-	-	-	-	2,055,000	2,055,000
Transfers – In	540,299	-	-	722,734	3,916,656	5,179,689
Transfers – Out	(4,978,397)	-	-	-	(201,292)	(5,179,689)
Total Other Financing Sources and Uses	<u>(4,438,098)</u>	<u>-</u>	<u>-</u>	<u>722,734</u>	<u>5,770,364</u>	<u>-</u>
Net Change in Fund Balance	<u>4,987,408</u>	<u>364,110</u>	<u>562,037</u>	<u>620,726</u>	<u>(4,628,012)</u>	<u>-</u>
Fund Balance – Beginning	<u>9,939,362</u>	<u>36,376</u>	<u>10,654,793</u>	<u>7,449,827</u>	<u>27,083,491</u>	<u>5</u>
FUND BALANCE – ENDING	<u>\$ 14,926,770</u>	<u>\$ 400,486</u>	<u>\$ 11,216,830</u>	<u>\$ 8,070,553</u>	<u>\$ 22,455,479</u>	<u>\$ -</u>

See accompanying Notes to Basic Financial Statements.

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5/11/09

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Net Change in Fund Balances – Government Funds (Page 19) **\$ 1,906,269**

Amount reported for Governmental Activities in the Statement of Activities (Page 16)
are different because:

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

Capital Assets	\$ 10,343,656	
Depreciation Expense	<u>(2,296,465)</u>	
Excess of Capital Assets over Depreciation Expense		8,047,191

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 1,233,999

Governmental Fund Report the effect of Bond Issuance Costs as Expenditure when Debt is first
issued, and amortized in the Statement of Activities. This amounts is the effect of these differences:

Bond Issuance Costs	14,994	
Amortization of Deferred Charges	<u>(10,535)</u>	4,459

Repayment of long-term principal is expenditure in the governmental funds, but issuing debt
reduced Long-Term Liabilities in the Statement of Net Assets. In the current period
repayments were 2,675,068

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 governmental funds.

These activities consist of:

Increase in Bonds	(2,055,000)	
Increase in Property Tax Advance	(424,196)	
Loss on Disposal	(2,465)	
Increase in Employees Retirement Administration	(28,992)	
Decrease in Unemployment Plan	161,446	
Increase in Compensated Absences	<u>(730,707)</u>	
Total Additional Expenses		<u>(3,079,914)</u>

Change in Net Assets of Governmental Activities (Page 16) **\$ 10,787,072**

See accompanying Notes to Basic Financial Statements.

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

NOTE 1 FINANCIAL REPORTING ENTITY

The Municipality of Humacao, Puerto Rico (Municipality) was founded in the year 1793, and operates as a governmental unit of the Commonwealth of Puerto Rico, under the Law Number 81 of August 30, 1991, known as "Autonomy Municipalities Law of the Commonwealth of Puerto Rico". The governmental system of the Municipality is composed of the executive and legislative bodies. The Mayor is the Chief Executive Officer and is elected every four years in the general elections of the Commonwealth of Puerto Rico. The legislative body consists of 16 Legislators also elected in the general elections of Puerto Rico for a four-year period.

The Municipality provides services such as: health, public works, sanitation, aids and services to low-income and elderly citizens, public safety, housing and urban development, culture and recreation, planning, zoning and other general and administrative services. As a government entity, the Municipality is exempt from both federal and state taxes.

The accounting policies of the Municipality conform to accounting principles generally accepted in the United States of America (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB). The GASB is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards which, along with subsequent GASB pronouncements (Statements and Interpretations) constitutes GAAP for governmental units. The following is a summary of the more significant of such policies.

The accompanying basic financial statements include all departments and organizations units whose funds are under the custody and control of the Municipality. In evaluating the Municipality as a reporting entity, management has addressed all the potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of GASBS No. 14, as amended by GASBS No. 39, *Determining Whether Certain Organizations Are Component Units – an amendment of GASB Statement No. 14*.

GASBS No. 39 provided additional guidance to determine whether certain organization for which the primary government is not financially accountable should be reported as components units. A legally separate, tax-exempt organization should be discretely presented as a component unit if all of the following criteria are met: (a) the economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents; (b) the primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and; (c) the economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

There are two methods of presentation of the component unit in the financial statements: blending – the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balance; and discrete – presentation of the component unit's financial data in column separate from the Municipality's balances and transactions.

The relative importance of each criterion must be evaluated in light of specific circumstances in order to determine which components units are to be included as part of the reporting entity. Our specific evaluations of the criteria applicable to the Municipality indicate no organizations meet the criteria to be included as component units. Accordingly, these basic financial statements present only the Municipality as the reporting entity.

These financial statements present the respective financial position of the governmental and business type activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2008, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

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

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES

A. Financial Statement Presentation

The basic financial statements include both government-wide (based on the Municipality as a whole) and fund financial statements. Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as either governmental or business type.

Government-wide Financial Statements

The government-wide financial statements (the *Statement of Net Assets* and the *Statement of Activities*) report information of all the activities of the Municipality. For most part, the effect of interfund activity has been removed from these financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely, to a significant extent, on fees and charges for support. Business-type activities are not reported since the **Municipality** don't have such activities.

The focus of the *Statement of Net Assets* is designed to be similar to bottom line results for the Municipality's governmental activities and business type activities. This statement combines and consolidates governmental fund's current financial resources (short-term spendable resources) with capital assets and long-term obligations. The *Statement of Net Assets* presents the reporting entities' assets and liabilities, with the difference reported as net assets.

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

The *Statement of Activities* demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services, or privileges provided by a given function or segment, and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Governmental Fund Financial Statements

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

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is on Major Funds, rather than the previous financial model's fund types. This is the manner in which these funds are normally budgeted. This presentation deemed most appropriate to (a) demonstrate legal and covenant compliance, (b) demonstrate the source and use of liquid resources, and (c) demonstrate how the Municipality's actual experience conforms to the budgeted fiscal plan.

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

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

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

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

B. Measurement Focus and Basis of Accounting

Government-wide Financial Statements

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

Governmental Funds Financial Statements

The governmental funds financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purposes, the Municipality considers revenues to be available if they are collected within sixty (60) days of the end of the current fiscal period. Expenditures generally are recorded when liability is incurred, as under accrual accounting. However, expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, volume of business taxes, sale taxes, licenses and permits, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the Municipality.

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

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

Expenditures are generally recognized when the related liability is incurred, as under accrual accounting. The exceptions to this general rule are the compensated absences and claims and judgments, if any, that are recorded only when payment is due.

The Municipality reports the following major governmental funds:

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

Head Start Fund – This is the fund used to account for all transactions of the Head Start Program. The objectives to this program are to provide comprehensive health, educational, nutritional, social and other developmental services primarily to economically-disadvantaged pre-school children and infants and toddlers so that the children will attain school readiness.

Debt Service Fund – This is used to account for the accumulation of resources for, and the payment of, long-term debt principal and interests.

Art Center Fund – This is used to account for the construction of the Art Center in Humacao, Puerto Rico.

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

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

The non-major funds are combined in a single column in the fund financial statements.

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

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

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

C. Stewardship, Compliance, and Accountability

Budgetary Information

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

Encumbrances outstanding at year end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be reappropriated and honored during the subsequent year.

The Municipality follows these procedures, in accordance with law, in order to establish the budgetary data reflected in the Budgetary Comparison – General Fund Schedule:

Original Budget

1. Prior of May 15 of each fiscal year, the Mayor submits to the Municipal Legislature a proposed budget for the fiscal year commencing the following July 1 in addition of a budget message.
2. The budget document is available for public inspection prior to its approval by the Municipal Legislature.
3. The Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law.
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance to be effective on July 1.

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

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

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

Final Budget

The final budgetary data presented in the Budgetary Comparison – General Fund Schedule reflects the following changes to the original budget:

1. Certain annual appropriations are budgeted on a project basis. If such projects are not completed at the end of the fiscal year, unexpended appropriations, including encumbered funds, and unexpended grant appropriations, are carried forward to the following year. In certain circumstances, other regular annual appropriations may be carried forward after appropriate approval. Annually appropriated funds, not authorized to be carried forward, lapse at the end of the fiscal year. Appropriations carried forward from the prior year are included in the final budgetary data.
2. Appropriations may be adjusted during the year with the approval of the Mayor and the Municipal Legislature, e.g. supplemental appropriations. Additionally, the Mayor is authorized to make certain transfer of surplus within the departments. Such adjustments are reflected in the final budgetary data.

The Annual Appropriation Ordinance adopts the budget at the character level of expenditure within departments. As described above, the Mayor is authorized to make certain transfers of appropriations within departments. Accordingly, the legal level of budgetary control by the Municipal Legislature is the department Level.

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

1. Encumbrances are recorded as expenditures under the budgetary basis and as a reserve of fund balances under GAAP.
2. Interfund transactions of the General Fund are not included in the budgetary basis.
3. Certain accrued liabilities and other debts are not included in the budgetary basis.
4. Certain revenues susceptible to accrual, i.e., both measurable and available, are not included in the budgetary data.

The Special Revenue Fund has not been included in the budgetary comparison because balances are not budgeted. Also the budget prepared for the Federal Financial Awards Programs included in the Capital Projects and Special Revenue Funds is based on a program period which is not necessarily the same fiscal year. Accordingly, it's not practical to present an annual comparison of budget for such programs.

D. Cash and Investment, and Cash with Fiscal Agent

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

Cash with fiscal agent in the Debt Service Fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law. Cash with fiscal agent in other governmental funds consists of undisbursed proceeds of certain bonds and notes issued for the acquisition and construction of major capital improvements, or grants which are maintained in a cash custodian account by the Government Development Bank of the Commonwealth of Puerto Rico. This sinking fund is maintained by the Governmental Development Bank of Puerto Rico, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

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

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

E. Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statement as "interfund balances".

Receivable are shown net of an allowances for uncollectible, which are determined upon past collection experience and current economic conditions. Intergovernmental receivables in the general fund represent mostly property tax accounts that are levied by Municipal Revenue Collection Center (MRCC), a governmental entity created by the Commonwealth of Puerto Rico, from grant and contributions from Federal Government, and state appropriations.

Advance between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

F. Inventories

The Municipality used the purchase method to account for the purchases office and printing supplies, gasoline, oil and other expendable supplies held for consumption. This method records items as expenditures, in the appropriate fund, when they are acquired and, accordingly, the inventory is not recorded in the basic financial statements.

G. Capital Assets

Capital assets, which include land, buildings and improvement, machinery and equipment, motor vehicles, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets, other than infrastructure assets, are defined by the government as assets with an initial, individual cost of more than \$500 (amount not rounded) and an estimated useful life in excess of two years. For improvements other than buildings, the capital outlay must be greater than \$10,000, extend the estimated useful life for ten years, and be greater than 10% of the original cost of the asset. The government reports infrastructure assets on a network and subsystem basis. Accordingly, the amounts spent for the construction or acquisition of infrastructure assets are capitalized and reported in the government-wide financial statements regardless of their amount.

In the case of the initial capitalization of general infrastructure assets (i.e., those reported by governmental activities) the government chose to include all such items regardless of their acquisition date or amount. The government was able to estimate the historical cost for the initial reporting of these assets through back trending (i.e., estimating the current replacement cost of the infrastructure to be capitalized and using an appropriate price-level index to deflate the cost to the acquisition year or estimated acquisition year). As the government constructs or acquires additional capital assets each period, including infrastructure assets, they are capitalized and reported at historical cost. The reported value excludes normal maintenance and repairs which are essentially amounts spent in relation to capital assets that do not increase the capacity or efficiency of the item or extend its useful life beyond the original estimate. In the case of donations the government values these capital assets at the estimated fair value of the item at the date of its donation.

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NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

Capital outlay is recorded as expenditures of the General Fund and other governmental funds and as assets in the governmental-wide financial statements to the extent the Municipality capitalization threshold is met. Interest incurred during the construction phase of the capital assets of business-type activities is reflected in the capitalized value of the asset acquired under capital leases is included in depreciation. Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

CAPITAL ASSETS	YEARS
Buildings	50
Improvement Other Than Buildings	50
Infrastructure	10-50
Equipments	10
Furniture	10
Vehicles	5
Machinery	5-10

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

H. Compensated Absences

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

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

In accordance with the above criteria and requirements as established by GASBS No. 16; the Municipality has accrued a liability for compensated absences, which has been earned but not taken by Municipality's employees, including its share of social security and Medicare payments made on behalf of the employees in the accrual for vacation and sick leave pay. All vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements. For the government-wide statements, the current portion is the amount estimated to be used in the following year. For the governmental funds statements, all of the compensated absences are considered long-term and therefore, are not a fund liability and represents a reconciling item between the fund level and government-wide presentations (see Note 9 on page 34).

I. Risk Financing

The Municipality carries commercial insurance to cover property and casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the municipalities of Puerto Rico. Also, principal officials of the Municipality are covered under various surety bonds. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the MRCC for the year ended June 30, 2008 amounted to approximately \$660,919. The current insurance policies have not been cancelled or terminated. In addition, MRCC deducted approximately \$623,595 for workers compensation insurance covering all municipal employees for the same period.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
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NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

J. Long-Term Obligations, Bonds Issuance Costs, Premiums and Discounts

The liabilities reported in the government-wide financial statements include the general and special obligation bonds, long-term notes, other long-term liabilities (e.g., vacation, sick leave, claims and judgments, long-term liabilities to other governmental entities and third parties, and landfill postclosure care costs. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount.

In the fund financial statements, governmental fund types recognize bond premiums and discounts as other financing sources and uses, respectively, and bond issuance costs as debt service expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

K. Fund Equity/Net Assets

Reservations of Fund Equity

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditures or (2) legally segregated for a specific future use. Following is a brief description of the nature of certain reserves.

- *Reserve for Encumbrances* – Encumbrances are recorded as reservations of fund balances because they do not constitute expenditures or liabilities. In certain other governmental funds, this accounting treatment results in a deficit unreserved fund balance. This deficiency is carried forward to the next fiscal year where it is applied against estimated revenues in the year the commitments are expended.
- *Reserve for Debt Service* – The fund balance of the debt service funds is reserved for the payment of debt service in the subsequent years.
- *Reserve for Capital Projects* – Certain assets, primarily cash and investments, and cash with fiscal agent to be invested in capital projects.
- *Reserve for Other Purposes* – Certain assets, primarily cash and investments of grants and contributions that are authorized to be carried over and expended in the ensuing year.

Restricted Net Assets

The governmental-wide and proprietary funds financial statements utilize a net assets presentation. Net assets are categorized as invested in capital assets (net of related debt), restricted, and unrestricted.

- *Invested in Capital Assets, Net of Related Debt* – These consists of capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and amortization, and the outstanding balances for debt that are attributable to the acquisition, construction, or improvement of these assets reduce the balance in this category.
- *Restricted Net Assets* – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- *Unrestricted Net Assets* – These consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

COMMONWEALTH OF PUERTO RICO
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NOTES TO THE BASIC FINANCIAL STATEMENTS
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NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

L. Interfund Transactions

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

Interfund Transfers – Legally required transfers that are reported when incurred as transfers-in by the recipient fund and as transfers-out by the disbursing fund, with receivables and payables presented as amounts due to and due from other funds.

Intra-Entity Transactions – Advances between funds are also presented as amounts due to and due from other funds. However, these transfers and related amounts receivables and payables are considered internal balances and activities that have been eliminated in the government-wide financial statements.

M. Claims and Judgments

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

N. Use of Estimates

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

O. Future Adoption of Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) issued the following pronouncement that does not apply to the Municipality:

GASB Statement No. 49, *Pollution Remediation*. This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of *existing* pollution by participating in pollution remediation activities such as site assessments and cleanups. The scope of the document excludes pollution *prevention* or *control* obligations with respect to current operations, and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and postclosure care and nuclear power plant decommissioning. This Statement are effective for financial statements for periods beginning after December 15, 2007, with measurement of pollution remediation liabilities required at the beginning of that period so that beginning net assets can be restated. However, governments that have sufficient objective and verifiable information to apply the expected cash flow technique to measurements in prior periods are required to apply the provisions retroactively for all such prior periods presented.

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NOTES TO THE BASIC FINANCIAL STATEMENTS
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NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

GASB Statement No. 51, *Intangible Assets*. This Statement requires that an intangible asset be recognized in the statement of net assets only if it is considered identifiable. Additionally, this Statement establishes a specified-conditions approach to recognizing intangible assets that are internally generated. Effectively, outlays associated with the development of such assets should not begin to be capitalized until certain criteria are met. Outlays incurred prior to meeting these criteria should be expensed as incurred. This Statement also provides guidance on recognizing internally generated computer software as an intangible asset. This Statement is effective for financial statements for periods beginning after June 15, 2009. The provisions of this Statement generally are required to be applied retroactively. For governments that were classified as phase 1 or phase 2 governments for the purpose of implementing Statement 34, retroactive reporting is required for intangible assets acquired in fiscal years ending after June 30, 1980, except for those considered to have indefinite useful lives as of the effective date of this Statement and those that would be considered internally generated. Retroactive reporting of these intangible assets by phase 3 governments is encouraged but not required. Retroactive reporting is not required but is permitted for intangible assets considered to have indefinite useful lives as of the effective date of this Statement and those considered to be internally generated.

GASB Statement No. 52, Land and Other Real Estate Held as Investments by Endowments. This Statement establishes consistent standards for the reporting of land and other real estate held as investments by essentially similar entities. It requires endowments to report their land and other real estate investments at fair value. Governments also are required to report the changes in fair value as investment income and to disclose the methods and significant assumptions employed to determine fair value, and other information that they currently present for other investments reported at fair value. This Statement is effective for financial statements for periods beginning after June 15, 2008.

GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. Statement 53 is intended to improve how state and local governments report information about derivative instruments—financial arrangements used by governments to manage specific risks or make investments—in their financial statements. The Statement specifically requires governments to measure most derivative instruments at fair value in their financial statements that are prepared using the economic resources measurement focus and the accrual basis of accounting. The guidance in this Statement also addresses hedge accounting requirements and is effective for financial statements for reporting periods beginning after June 15, 2009, with earlier application encouraged.

NOTE 3 CASH AND CASH WITH FISCAL AGENT

The Municipality's cash and investments at year-end were entirely covered by the Federal Deposit Insurance Corporation (FDIC) coverage, up to a maximum of \$250,000 in each bank, and the excess by collateral provided by the banks and held by the Puerto Rico Treasury Department pursuant the applicable laws and regulations. Cash with fiscal agent is maintained in interest bearing accounts in the Government Development Bank of Puerto Rico and is not collateralized.

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or the Commonwealth of Puerto Rico. The Municipality is also allowed to invest in bank acceptances, other bank obligations and certificates of deposit in financial institutions authorized to do business under the federal and Commonwealth laws.

During the year, the Municipality invested its funds in interest bearing bank accounts. As June 30, 2008 the amount of \$5,000,489, \$20,141,052, and \$9,011,039 was invested in an interest bearing account in Popular Bank of Puerto Rico, Humacao Branch; Eurobank, Humacao Branch; and First Bank, Humacao Branch that generates an annual interest rate of 5.12%, 4.33% and 2.64%, respectively. Also, \$15,834,411 was invested in another account in Popular Bank of Puerto Rico, Trust Division, which generates an annual interest of 5.20%.

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

NOTE 3 CASH AND CASH WITH FISCAL AGENT (continuation)

Custodial Credit Risk Related to Deposits

Custodial credit risk for cash and investments is the risk that, in the event of the failure of a depository financial institution, the Municipality will not be able to recover its cash and investments or will not be able to recover collateral securities that are in the possession of an outside party. Pursuant to the Investment Guidelines for the Commonwealth adopted by GDB, the Municipality may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, banker's acceptance, or in pools of obligations of the municipalities of Puerto Rico, among others.

The Municipality maintains its cash deposits in commercial 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 deposit insurance. All securities pledged as collateral by the Municipality are held by the Secretary of Treasury of Puerto Rico in the Municipality's name. The following tables presented below disclose the level of custody risk assumed by the Municipality based upon how its deposits were insured or secured with collateral at June 30, 2008:

- Category 1: Insured or collateralized with securities held by the Secretary of Treasury agent's in the Municipality's name.
- Category 2: Collateralized with securities held by the pledging financial institution's trust department or its agents in the Municipality's name.
- Category 3: Uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent by not in the Municipality's name.

	CATEGORY			CARRYING AMOUNT	BANK BALANCE
	1	2	3		
Deposits in Commercial Banks	\$ 57,417,648	\$ -	\$ -	\$ 57,417,648	\$ 58,146,854
Deposits in Governmental Banks	-	-	18,453,808	18,453,808	18,453,808
Total	\$ 57,417,648	\$ -	\$ 18,453,808	\$ 75,871,456	\$ 76,600,662
Reconciliation to Government-Wide Statement of Net Assets:					
	UNRESTRICTED	RESTRICTED	TOTAL		
Carrying amount of deposits					
in Commercial Banks	\$ 26,759,973	\$ 30,657,675	\$ 57,417,648		
Carrying amount of deposits					
in Governmental Bank	-	18,453,808	18,453,808		
Total	\$ 26,759,973	\$ 49,111,483	\$ 75,871,456		

As of June 30, 2008, the Municipality's custodial credit risk was approximately \$18.5 million, which is the bank balance of cash deposited at the Government Development Bank of Puerto Rico (GDB). These deposits are exempt from the collateral requirement established by the Commonwealth.

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

NOTE 4 DEFERRED REVENUES

Governmental funds report *deferred revenues* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of *deferred revenue* and *unearned revenue* reported in the governmental funds were as follows:

	UNAVAILABLE	UNEARNED
Volume of Business Taxes	\$ -	\$ 12,619,218
Other Major Funds	7,163,982	-
Head Start Program	4,267,422	-
Total Deferred Unearned Revenue	\$ 11,431,404	\$ 12,619,218

NOTE 5 OTHERS RECEIVABLES

As of June 30, 2008, the amount of \$304,031 corresponds to rent receivable from state agency.

NOTE 6 INTERFUND RECEIVABLE, PAYABLES AND TRANSFERS

A. Interfund Receivable and Payable Balances

Due to/from Other Funds at June 30, 2008 are summarized as follows:

INTERFUND RECEIVABLE	INTERFUND PAYABLE	AMOUNT
General Fund	Other governmental Fund	\$ 884,810
General Fund	Head Start Fund	178,806
Other Major Fund	General Fund	170
Other governmental Fund	Other governmental Fund	<u>75,672</u>
Total		<u>\$1,139,458</u>

B. Interfund Transfers

Transfers are indicative of funding for capital projects or debt service, and subsidies of various operations.

SOURCES	TRANSFER TO	AMOUNT	PURPOSE
General Fund	Debt Services Fund	\$ 714,667	Bond Principal and Interest Payments
Other Major Fund	Debt Services Fund	8,067	Bond Issue Cost
General Fund	Other Major Fund	3,916,656	Budget Specific Project Funding
Other Major Fund	General Fund	<u>540,299</u>	Budget Specific Project Funding
	Total	<u>\$ 5,179,689</u>	

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
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NOTE 7 DUE FROM / TO GOVERNMENTAL UNITS

As of June 30, 2008, balance due from governmental units of the Other Major Fund corresponded to reimbursement of Law 52 and Law 82.

The balance due to governmental units of the General Fund for services rendered to the Municipality consists of AEELA (\$51,460) and General Service Administration (\$2,800).

NOTE 8 CAPITAL ASSETS

Capital Assets activities for the fiscal year ended June 30, 2008 was as follows:

DESCRIPTION	BALANCE JULY 1, 2007	INCREASE	DECREASE	BALANCE JUNE 30, 2008
Non-Depreciable Capital Assets:				
Land	\$ 7,418,626	\$ 3,974,500	\$ (2,465)	\$ 11,390,661
Construction in Progress	18,559,112	4,545,819	(9,548,044)	13,556,887
Total Non-Depreciable Capital Assets	25,977,738	8,520,319	(9,550,509)	24,947,548
Depreciable Capital Assets:				
Buildings	49,600,108	3,934,012	-	53,534,120
Infrastructure	16,385,116	5,618,659	-	22,003,775
Motor Vehicles	6,502,866	842,636	-	7,345,502
Equipment	3,723,254	976,074	(76,514)	4,622,814
Capital Lease	680,761	-	-	680,761
Total Depreciable Capital Assets	76,892,105	11,371,381	(76,514)	88,186,972
Less Accumulated Depreciation:				
Buildings	(14,366,014)	(996,758)	-	(15,362,772)
Infrastructure	(4,593,222)	(266,188)	-	(4,859,410)
Motor Vehicles	(5,150,259)	(443,885)	-	(5,594,144)
Equipment	(2,287,793)	(453,694)	76,514	(2,664,973)
Capital Lease	(373,983)	(135,940)	-	(509,923)
Total Accumulated Depreciation	(26,771,271)	(2,296,465)	76,514	(28,991,222)
Total Depreciable Capital Assets (Net)	50,120,834	9,074,916	-	59,195,750
CAPITAL ASSETS, NET	\$ 76,098,572	\$ 17,595,235	\$ (9,550,509)	\$ 84,143,298

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

NOTE 8 CAPITAL ASSETS (continuation)

Depreciation expenses were charged to governmental functions/programs as follows:

	AMOUNT
Mayor and Municipal Legislature	\$ 321,505
General Government	206,682
Public Safety	183,717
Public Works	711,905
Culture and Recreation	665,975
Human Service and Welfare	114,822
Urban Development	91,859
Total Depreciation Expenses	\$ 2,296,465

NOTE 9 GENERAL LONG-TERM DEBTS

A. General Obligations Bonds and Special Obligations Bonds

The principal long-term obligations of the Municipality are general obligation bonds and special obligation bonds issued to finance the construction and improvements of public facilities and purchase of machinery and equipment. The Municipality's obligations long-term debt retirements are appropriated and paid from resources accumulated in the Debt Service Fund (See Note 10).

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

NOTE 9 GENERAL LONG-TERM DEBTS (continuation)

The following is a summary of general and special obligation bonds and a note of the Municipality as of June 30, 2008:

Type of Obligation and Purpose	Maturity Date	Interest Rate	Amount
General Obligation Bonds:			
\$5,200,000, Series 2003-04 - General Construction	2028	5.00%	\$ 4,810,000
\$4,020,000, Series 2002-03 - General Construction	2027	5.00%	3,630,000
\$1,099,000, Series 1995 - Purchase of Equipment	2013	5.45%	545,000
\$1,485,000, Series 1995 - General Construction	2014	5.17%	880,000
\$8,395,000, Series 1998 - General Construction	2018	6.46%	5,990,000
\$1,950,000, Series 2001 - Purchase of Equipment	2008	7.00%	340,000
\$1,720,000, Series 2005 - General Construction	2030	5.02%	1,650,000
\$370,000, Series 2006 - Land Acquisition	2030	5.02%	355,000
\$10,620,000, Series 2006 - General Construction	2031	5.525%	10,415,000
\$10,620,000, Series 2006 - General Construction	2031	5.525%	10,415,000
\$2,055,000, Series 2007 - Purchase of Equipment	2014	7.50%	2,055,000
Total General Obligations Bonds			<u>41,085,000</u>
Special Obligations Bonds:			
\$4,786,000, Series 1995 - Refinancing Purpose	2013	7.81%	2,365,000
\$2,000,000, Series 1990 - Operational Purpose	2009	8.00%	131,579
Total Special Obligations Bonds			<u>2,496,579</u>
Special Obligation Note:			
\$678,395, Rural Development - General Construction	Unknown	Undetermined	678,395
Total Special Obligation Note			<u>678,395</u>
Total General and Special Bonds, and Note			<u>\$44,259,974</u>

B. Obligation Under Capital Leases

The Municipality is obligated under certain capital leases accounted for in the Statement of Net Assets. The historical cost, accumulated depreciation, future minimum lease payments at June 30, 2008, are as follows:

Cost	\$ 680,760
Accumulated Depreciation	\$ 236,912
Monthly Lease Payments	\$ 7,009
Residual Lease Payments	\$ -
YEAR ENDING	TOTAL
JUNE 30,	PAYMENT
2009	\$ 84,110
2010	56,894
2011	14,245
Total Minimum Lease Payment	155,249
Less: Deferred Interest	5,522
Present Value Minimum Lease Payments	<u>\$ 149,727</u>

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

NOTE 9 GENERAL LONG-TERM DEBTS (continuation)

C. Other Long-Term Debts

Borrowing from MRCC

The total amount of \$284,976 to be paid during fiscal year 2010-2011 without interests corresponded to the Fiscal Year 2007-2008 final liquidation of property taxes.

On July 1, 2007, the Municipality entered into a repayment agreement with the GDB and MRCC to repay the uncollectible property tax sale authorized by the enacted Law Number 146. The original debt was \$730,449 to be paid during 25 years plus annual interest of 6.22%.

On November 28, 2001, the Municipality entered into a repayment agreement with the GDB and MRCC to pay for the proportional debt to cover the Land Information Management System (LIMS), system established by MRCC with the capacity to maintaining cadastre and photos of all real property of Puerto Rico. The original debt was \$1,833,035 to be paid during 10 years plus annual interest of 5.95%.

On July 1, 2002, the Municipality entered into a repayment agreement with the GDB and MRCC to repay the uncollectible property tax sale authorized by the enacted Law Number 42. The original debt was \$492,779 to be paid during 30 years plus annual interest of 6.1875%.

Claims and Judgments

This amount represents the amount accrued for possible claims arising from litigations.

Employees Retirement Administration

On March 2008, the Municipality entered into a repayment agreement with the Employees Retirement Administration to repay a debt amounted to \$48,320 due on February 26, 2010.

Puerto Rico Department of Labor and Human Resources

On April 2006, the Municipality entered into a repayment agreement with the Puerto Rico Department of Labor and Human Resources to repay an unemployment debt amounted to \$534,337 of principal and interests due on March 2009.

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NOTES TO THE BASIC FINANCIAL STATEMENTS
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NOTE 9 GENERAL LONG-TERM DEBTS (continuation)

Compensated Absences

This amount represents the estimated accrued vacation benefits, accrued sick leave benefits and payroll related benefits, representing the Municipality's commitment to fund such costs from future operations.

Following are the Other Long-Term Debts:

	BALANCE		RETIREMENTS	BALANCE
	JULY 1,	NEW	AND	JUNE 30,
DESCRIPTION	2007	ISSUES	ADJUSTMENTS	2008
Property Taxes-MRCC	\$ -	\$ 284,976	\$ -	\$ 284,976
Law Number 146-MRCC	730,449	-	(29,218)	701,231
LIMS Debt-MRCC	958,217	-	(191,642)	766,575
Law Number 42-MRCC	463,007	-	(7,799)	455,208
Claims and Judgments	478,000	-	-	478,000
Employees Retirement Adm.	-	48,320	(19,328)	28,992
Unemployment	282,530	-	(161,446)	121,084
Compensated Absences	4,689,442	730,707	-	5,420,149
TOTAL	\$ 7,601,645	\$ 1,064,003	\$ (409,433)	\$ 8,256,215

D. CHANGES IN GENERAL LONG-TERM DEBTS

The following is a summary of changes in long-term debts for the year ended June 30, 2008:

	BALANCE		RETIREMENTS	BALANCE	AMOUNTS	AMOUNTS
	JULY 1,	NEW	AND	JUNE 30,	DUE WITHIN	DUE AFTER
DESCRIPTION	2007	ISSUE	ADJUSTMENTS	2008	ONE YEAR	NEXT YEAR
General	\$ 40,685,000	\$ 2,055,000	\$ (1,655,000)	41,085,000	\$ 1,805,000	\$ 39,280,000
Special	3,580,237	-	(405,262)	3,174,975	425,263	2,749,712
Capital Lease	226,651	-	(76,924)	149,727	79,859	69,868
Other Debts	7,601,645	1,064,003	(409,433)	8,256,215	4,323,000	3,933,215
TOTAL	\$ 52,093,533	\$ 3,119,003	\$ (2,546,619)	\$ 52,665,917	\$ 6,633,122	\$ 46,032,795

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

NOTE 9 GENERAL LONG-TERM DEBTS (continuation)

The annual requirements to amortize the long-term debts outstanding as of June 30, 2008 are as follows:

YEAR ENDING JUNE 30,	General Obligation Bonds		Special Obligation Bonds & Note		Other Long-Term Obligation		TOTAL	
	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL	INTEREST
2009	\$ 1,805,000	\$ 2,369,528	\$ 505,122	\$ 192,667	\$ 4,323,000	\$ 103,385	\$ 6,633,122	\$ 2,665,580
2010	1,555,000	2,271,690	431,944	152,698	552,987	99,679	2,539,931	2,524,067
2011	1,665,000	2,173,800	389,241	120,040	267,081	84,296	2,321,322	2,378,136
2012	1,790,000	1,998,310	405,000	89,400	158,543	49,010	2,353,543	2,136,720
2013	1,905,000	1,887,867	440,000	55,600	39,796	62,099	2,384,796	2,005,566
2014-2018	9,330,000	7,721,825	475,000	19,000	209,824	272,388	10,014,824	8,013,213
2019-2023	7,585,000	5,277,808	-	-	232,526	204,252	7,817,526	5,482,060
2024-2028	9,065,000	3,062,346	-	-	263,315	120,361	9,328,315	3,182,707
2029-2032	6,385,000	677,119	-	-	2,209,143	40,840	8,594,143	717,959
Unmatured	-	-	678,395	-	-	-	678,395	-
TOTAL	\$ 41,085,000	\$ 27,440,293	\$ 3,324,702	\$ 629,405	\$ 8,256,215	\$ 1,036,310	\$ 52,665,917	\$ 29,106,008

E. Debt Compliance

There are a number of limitations and restrictions contained in the various bond indentures. The Municipality believes it is in compliance with all significant limitations and restrictions.

NOTE 10 DEBT RETIREMENT

Revenues of the debt service fund consists of the ad-valorem property taxes which are recognized as revenue when collected from taxpayers and reported by the Municipal Revenue Collection Center of the Commonwealth of Puerto Rico to the Municipality (See Note 11).

These property taxes are accumulated by the Municipal Revenue Collection Center in costs of the general obligations bonds issued by the Municipality (See Note 9). Payments are made to the Government Development Bank of the Commonwealth of Puerto Rico from such accumulated funds by the Municipal Revenue Collection Center of Puerto Rico.

NOTE 11 PROPERTY TAXES

The Municipal Revenue Collection Center of the Commonwealth of Puerto Rico is responsible for the assessment of all real and personal property located within the Municipality and for the levy, administration and collection of the corresponding tax contribution.

The personal property tax is self assessed by the taxpayer on a return, which is to be filed and paid in full by May 15 of each year with the MRCC and based on current values as of December 31 of previous year. Real property tax is assessed by the MRCC on each piece of real estate and on each building or residence. The property tax contribution is levied each year over the appraised value of the real property at the beginning of the calendar year. The real property assessment is based on the current value existing in the year 1957.

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

NOTE 11 PROPERTY TAXES (continuation)

The MRCC is responsible for the billing of real property taxes and collections of both, personal and real property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the MRCC informs the Municipality of the estimated amount of property taxes expected to be collected for the ensuing fiscal year. Throughout the year, the MRCC advances funds to the Municipality based on the initial estimated collections. The MRCC is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the MRCC remits to the Municipality property taxes advances, which are less than the tax actually collected, a receivable from the MRCC is recorded at June 30. However, if advances exceed the amount actually collected, a borrowing from MRCC is recorded at June 30. The difference between the advances and the final settlement from MRCC for the fiscal year 2008 resulted in a payable of \$284,976.

The tax rate for fiscal year 2008 is 7.53% for real property and 5.53% for personal property of which 1.03% of both are for the redemption of public debt issued by the Commonwealth of Puerto Rico and 6.50% and 4.50%, respectively, belongs to the Municipality. The Commonwealth of Puerto Rico also contributes an annual tax rate of 0.20% of the property tax collected. The remaining percentage is distributed as follows: (a) 5.25% and 3.25%, respectively, represents the Municipality's basic tax rate that is appropriated for general purposes and therefore accounted for through the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. The remaining portion belonging to the Municipality of 1.25% represents the ad-valorem property taxes withheld by the MRCC and restricted for debt service, which is accounted for through the debt service fund (See Note 12). The Municipality hasn't reached the maximum statutory tax rate limit for the basic tax while there is no limitation for the ad-valorem tax rate.

The Commonwealth of Puerto Rico grants complete real property tax exoneration on the first \$15,000 has assessed valuation on residential units occupied by their owners. However, the Municipality receives the full amount levied, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. As part of Law No. 83 of August 30, 1991, as amended, the exempt amount to be paid by the Puerto Rico Treasury Department to the Municipality was frozen as of January 1, 1992. The Municipal Revenue Collection Center, instead of the property taxpayer, becomes the source of payment in these cases.

In addition, the law grants a complete exemption from personal property taxes up to an assessment value of \$50,000 to retailers with an annual net sales volume of less than \$150,000. The MRCC advances to the Municipality, on monthly payments, 100% of the contribution assessed over property for each fiscal year. In accordance to Law, these advances will be contributions by the MRCC from taxpayers. The MRCC periodically informs to the Municipality the amounts collected from taxpayers and applied to outstanding advances.

The Municipality records as revenue in the general fund the property tax contribution when received from monthly advances from MRCC. Due to the fact that collections of property tax are applied to the advances of property tax paid by the MRCC, the amortization of the advance at end of year was not available due to that is in process of verification by external auditors.

NOTE 12 VOLUME OF BUSINESS TAX

The volume of business tax is levied each year based on the prior year's gross revenues for all commercial and industrial organizations doing business in the Municipality and which are not totally or partially exempt from this tax under the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due five working days after April 15 of each year. Entities with sales volume of \$1 million or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2008, the tax rates were as follows:

- a. 1.50% for financial institutions and savings and loan associations.
- b. 0.50% for all other organizations.

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

NOTE 12 VOLUME OF BUSINESS TAX (continuation)

Taxes are payable in two equal semi-annual installments on July 1 and January 1 following the date of levy. If they are paid with declaration on or before the due date, the taxpayer is granted a 5% of discount. The volume of business tax receivable represents filed tax returns that were uncollected as of June 30, 2008. Collections of taxes during current fiscal year corresponding of the tax return based on the prior year gross sales are applicable to the next fiscal year and recorded as deferred revenues in the General Fund.

NOTE 13 SALES TAXES

Municipality imposes a Sales and Usage Tax of 1.5% (1% to the Municipality and .5% to the Puerto Rico Department of Treasury) on the sales price of a taxable item or on the purchase price of all usage, storage or consumption of a taxable item. Municipality granted exemption to the foods and ingredients of foods as per Ordinance Number 11, Series 2007-2008. All merchants required to collect the Sales and Usage Tax, are required to file a monthly Sales and Use Tax Return Form, no later than the 20th of the following month from the month being reported.

Sales tax receivable represents filed sales tax returns that were collected subsequent to June 30, 2008, but pertaining to the current year period.

As per Ordinance Number 1, Series 2007-2008, the Municipality authorized that one third (1/3) of the sales taxes collected should be appropriated for the investment of Eligible Activities and Infrastructure Fund created by Ordinance Number 44, Series 2006-2007.

NOTE 14 INTERGOVERNMENTAL REVENUES

Intergovernmental revenues consist primarily of funds received from the Commonwealth of Puerto Rico, "in lieu of tax" payments from the Quasi-public Corporation, Puerto Rico Electric Power Authority, and federal financial assistance received from federal government.

Grants and subsidies received from the Commonwealth of Puerto Rico and federal agencies include, among others, a general subsidy for urban development and capital improvements. Intergovernmental revenues are accounted for through the General Fund except for those directly related to urban development and capital improvements, which are accounted for through the Special Revenue and the Capital Project Funds. Federal Financial Assistance is recorded in the Special Revenue Fund.

NOTE 15 PENSION PLAN

Employees of Municipality participate in the Employee's Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (ERS). The ERS is cost-sharing multiple-employer defined benefit pension plan sponsored by the Commonwealth of Puerto Rico under the Act No. 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentalities and of certain municipalities and components units not covered by their own retirement systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Head of Agencies and Public Instrumentalities, Assistants to the Governor, the Comptroller of the Puerto Rico, Gubernatorial Board and Committee appointees and Experimental Service Station employees. ERS provides retirement, death and disability benefits. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

Under the plan, the employees and employer portions are contributed, for which, the employee amount is withheld from salaries. Covered employees are required by Commonwealth statute to contribute 5.775% for the first \$550 of monthly salary plus 8.275% for the excess of this amount, or on the alternative, 8.275% of all salary. The Municipality contributes to the system 9.275% of the participating employee's salaries.

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

NOTE 16 CONTINGENCIES (continuation)

The U.S. Department of Housing and Urban Development has determined that the Municipality's financial management system did not fully comply with applicable HUD requirements. The system did not properly identify the allocate more than \$1.2 million in program income, did not properly allocate more than \$315,500 in administration salaries, allowed the use of more than \$66,500 for ineligible expenditures, and could not account for more than \$79,700 in Block Grant receipts.

The San Juan Office of Community Planning and Development require the Municipality to repay \$102,533 in excessive costs and \$66,593 in ineligible operating expenditures.

NOTE 17 SUBSEQUENT EVENTS

On September 22, 2008, the Municipality Legislature, by means of Ordinance Number 13, Series 2008-2009, approved the acceptance of \$998,844 of the funds provided by the issuance of general obligation bonds of the Commonwealth of Puerto Rico. The funds should be use for general public construction and public assistance.

END OF NOTES

MUNICIPALITY OF HUMACAO, PUERTO RICO

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED JUNE 30, 2008

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

NOTE 15 PENSION PLAN (continuation)

Members who have attained at least 55 years of age and have completed at least 25 years of creditable service or members who have attained at least 58 years of age and have completed at least 10 years of creditable service are entitled to an annual benefit, payable monthly for life. The amount of the annuity shall be 1.5% of the average salary, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average salary, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month. All employees who at the time of employment are 55 years old or less are eligible to participate in the System. No benefit is payable if the participant receives a refund of his accumulated contributions.

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

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

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

The pension benefit for participants who retire with less than 30 years of service is computed at the rate of 1½% of their average compensation of each year of credit service for the remaining years. The System also provides for death and disability benefits and the assets of the System pertaining to the participant employees.

All employees that do not elect to transfer for the new program and who at the time of employment are 55 years old or less are eligible to participate in the System. Pension benefits for participants with 30 years of service are as follows:

YEARS OF SERVICE	PARTICIPANT'S AGE	PENSION BENEFITS
30 or more	55 or less	65% of the average of the three years of highest salary during the employee's service period.
30 or more	58 or more	75% of the average of the three years of highest salary during the employee's service period.
30 or more	65 or more	75% of the average of the three years of highest salary during the employee's service period (employees started working after April 1, 1990).

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

NOTE 15 PENSION PLAN (continuation)

Disability retirement benefits are available to members for occupational and non-occupational disability up to a maximum benefit of 50% of the average salary, as defined. However, for non-occupational disability, a member must have at least 10 years of creditable service.

The Municipality follows the provisions of GASB Statement No. 27, *Accounting for Pensions Pension by State and Local Governmental Employers*, which requires employers that participate in cost-sharing multi-employer defined-benefits plans to recognize pension expenditures/expense equal to the employer's contractually required contributions and a liability for unpaid contributions.

The total pension expenditures/expenses recorded in the category of administration for the Fiscal Year Ended June 30, 2005 through 2008 was as follow:

FISCAL YEAR	LAW NO. 447	SYSTEM 2000
2008	\$ 601,395	\$ 369,282
2007	596,657	337,863
2006	605,197	335,692
2005	312,000	321,082

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

NOTE 16 CONTINGENCIES

A. CLAIMS AND JUDGMENTS

The Municipality is, at present, a defendant in a number of legal matters that arise from alleged improper application of policies and negligence in the ordinary course of the Municipality's activities. The legal counsel of the Municipality has advised that at this stage in the proceedings of lawsuits he cannot offer an opinion as to the probable outcome.

In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in discovery stage. Certain of these claims are covered by insurance. Legal counsel with the information currently available can not determine the final outcome of these claims. Accordingly, the financial statements do not include adjustment, if any, that could result from the resolution of this legal proceeding. However, it has been the Municipality's experience that such actions are settled for amounts substantially less than the claimed amounts.

B. FEDERAL GRANTS

In the normal course of operations, the Municipality receives grants from various Federal and State agencies. The grant programs are subject to audit by agents of the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. The Community Development Block Grant had a federal audit by Federal Agency and the report presents a liability of \$169,126 of questioned costs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

	Budget Amounts		Actual Amounts	Variance with
	Original	Final	(Budgetary Basis) (See Note A)	Final Budget
BUDGETARY FUND BALANCE, JULY 1, 2007	\$ 7,174,308	\$ 7,174,308	\$ 7,174,308	\$ -
Resources (Inflows):				
Property Taxes	12,891,339	12,891,339	13,587,982	696,643
Volume of Business Taxes	13,160,000	13,160,000	14,769,978	1,609,978
Sales Taxes	2,021,000	2,021,000	5,365,707	3,344,707
Intergovernmental Revenues	4,247,843	4,247,843	4,670,763	422,920
License and Permits	2,770,000	2,770,000	4,955,987	2,185,987
Charges for Services	650,000	650,000	718,756	68,756
Interest	1,400,000	1,400,000	2,758,316	1,358,316
Miscellaneous	317,000	317,000	498,607	181,607
Total Resources (Inflows)	37,457,182	37,457,182	47,326,096	9,868,914
Amounts Available for Appropriation	44,631,490	44,631,490	54,500,404	9,868,914
Charges to Appropriations (Outflows):				
Mayor and Municipal Legislature	2,048,479	2,160,759	2,350,724	(189,965)
General Government	17,324,641	17,630,729	18,193,376	(562,647)
Public Safety	2,358,526	2,352,953	2,311,020	41,933
Public Works	2,754,890	2,802,230	2,944,462	(142,232)
Culture and Recreation	1,399,861	1,436,267	1,411,241	25,026
Health and Sanitation	1,997,776	1,970,277	1,893,266	77,011
Solid Waste Disposal	3,040,000	3,465,543	3,480,483	(14,940)
Human Services and Welfare	4,411,977	4,411,191	4,709,464	(298,273)
Urban Development	846,809	940,653	907,137	33,516
Capital Outlays	628,613	997,333	998,234	(901)
Transfers to Other Funds	645,610	714,668	4,978,397	(4,263,729)
Total Charges to Appropriations	37,457,182	38,882,603	44,177,804	(5,295,201)
BUDGETARY FUND BALANCE, JUNE 30, 2008	\$ 7,174,308	\$ 5,748,887	\$ 10,322,600	\$ 4,573,713

See accompanying Notes to Required Supplementary Information.



Estado Libre Asociado de Puerto Rico • Municipio Autónomo de Humacao
Honorable Marcelo Trujillo Panisse, Alcalde

Box 178, Humacao, PR 00792 • Teléfono: 656-0400

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RECIBIDO
UNIDAD DE CORREO

Call 656-3412

15 de enero de 2009

Sr. Omar E. Negrón Judice
Comisionado
Oficina del Comisionado de Asuntos Municipales
P. O. Box 70167
San Juan, PR 00936-8167

Señor Negrón:

Me place acompañar una (1) copia del "Annual Financial Report" y una (1) copia del "Single Audit Report" del Municipio Autónomo de Humacao para el año fiscal terminado al 30 de junio de 2008 según requerido por el "Single Audit Act of 1984" (Public Law 98-502). Ambos informes fueron preparados por la firma de CPA, Román Toro & CO., PSC. Incluimos además, el Plan de Acción Correctiva que contiene las gestiones que hemos implantado para atender y corregir los hallazgos del informe.

También se incluye una (1) copia del Informe Especial de los Auditores Independientes sobre el cumplimiento con las recomendaciones del Contralor y la corrección de fallas señaladas en los Informes de Auditoría del Contralor Núm. M-06-43 del 10 de abril de 2006.

De tener alguna duda o necesitar información adicional sobre estos informes puede comunicarse con el Sr. José A. Carrasquillo, Director de Finanzas al 852-2730 ó al 852-3066 ext. 2315.

Cordialmente,

Marcelo Trujillo Panisse
Alcalde

c José A. Carrasquillo Jiménez, Director de Finanzas
Luis A. González Rodríguez, Director Auditoría Interna

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE A Explanation of Differences Between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures

	General Fund
Sources/Inflows of Resources:	
Actual Amounts (Budgetary Basis) "Available for Appropriation" from the Budgetary Comparison Schedule (See Page 44)	\$ 54,500,404
Difference – Budget to GAAP:	
The Fund Balance at the Beginning of Year is a budgetary resource but is not a Current-Year Revenue for financial reporting purposes	(7,174,308)
Total Revenues as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 19)	\$ 47,326,096
Uses/Outflows of Resources:	
Actual Amounts (Budgetary Basis) "Total Charges to Appropriation" from the Budgetary Comparison Schedule (See Page 44)	\$ 44,177,804
Difference – Budget to GAAP:	
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes	(1,531,853)
Prior Year Expenditures are not outflows of budgetary resources but are expenditures for financial reporting purposes	233,036
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	(4,978,397)
Total Expenditures as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 19)	\$ 37,900,590

NOTE B Explanation of Differences Between Budgetary Fund Balance and GAAP Fund Balance

Budgetary Fund Balance, June 30, 2008 (See page 44)	\$ 10,322,600
Timing Differences:	
Non-Budgetary Items	1,623,313
Change in Encumbrances	886,211
Designated for Special Revenues	562,793
Unrestricted Fund Balance, June 30, 2008 (See page 17)	\$ 13,394,917

END OF THIS SECTION

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO**

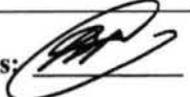
CORRECTIVE ACTION PLAN

Single Audit Report 2007-2008

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Fiscal Year Ended June 30, 2008

FINDINGS	CORRECTIVE ACTION	RESULTS
<p>SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS</p> <p>Number 2008- 3 SECTION 8 HOUSING CHOICE VOUCHERS</p> <p>The Municipality’s internal controls over disbursements of the Section 8 Housing program’s vouchers were significantly deficient in various aspects related to accounting and actual disbursements. Our test disbursements and other audit procedures revealed that the Section 8 direct deposit system had various differences in the transmittal of Section 8 vouchers between the accounting records and tenant files versus the actual disbursements, which were subsequently corrected and adjusted by the Section 8 accountant.</p>	<p>In March of 2008 a special internal audit was assigned to verify this situation. The results were included in a report prepared by our internal auditor that contained several recommendations that were evaluated by our directors of Federal Programs, Finances and the Coordinator of the Section 8 Program. Several irregularities were detected which have been considered and were in corrective process as of now.</p> <p>The recommendation, among others things were the following:</p> <ul style="list-style-type: none"> a. a redistribution of tasks between the area of accounting of the program and the area of finance office of the Department of Finances. b. the revision of the vouchers before the electronic transmission of the payments. c. the identification and notification to the participants who received payments in excess erroneously, determine the amount of these excess and to authorize payment plans to obtain the reimbursement of the funds. <p>Our auditors were instructed in order to make future follow-ups to assure that the recommendations were implemented.</p>	<p>Situation Partially Corrected:</p> <p>A redistribution of accounting tasks and disbursement tasks was made between the personnel from the Federal Program Office and the Finance Department, including additional controls and a close revision of the documents before the electronic transmission of the voucher payments.</p> <p>The Director of Finances will determine the amount that is pending to recover from the participants. Then he was instructed to reimburse the amount to the Section 8 Program with municipality funds. The collection efforts will be continued to the mentioned participants.</p>

Initials: 

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO

CORRECTIVE ACTION PLAN

Single Audit Report 2007-2008

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Fiscal Year Ended June 30, 2008

FINDINGS	CORRECTIVE ACTION	RESULTS
<p>SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS</p> <p>Number 2008-2 CASH MANAGEMENT</p> <p>During our review of the Municipality's bank account reconciliations for the various Head Start Programs, we found various deficiencies:</p> <ol style="list-style-type: none"> 1. 25 monthly bank reconciliations prepared by the program's accountant between 60 and 267 days after the last day of their respective month. 2. 10 monthly bank reconciliations reviewed between 76 and 91 days after preparation. 3. 15 monthly bank reconciliations which were prepared by the program's accountant but not signed by the Finance Director. 4. Unidentified and unexplained differences between the accounting records and the bank statements 5. 7 monthly bank reconciliations which were prepared by the program's accountant whose supporting documentation was not signed by the Finance Director. 	<p>The situation with the bank reconciliations of the Head Start Programs was attended by the Finance Director and the Head Start Program Director. On september 2008 the municipality obtained and assigned two new accountants to the Head Start Program and has distributed the accounting responsibilities among them, including the reconciliation of different bank accounts. The Finance Department has implemented new oversight controls to assure future compliance and a close supervision.</p>	<p>Situation Corrected:</p> <p>The bank reconciliations mentioned in this finding were revised and corrected.</p>

Initials 