



MUNICIPALITY OF HUMACAO, PUERTO RICO

SINGLE AUDIT REPORT

FISCAL YEAR ENDED JUNE 30, 2009



#03-57

MUNICIPALITY OF HUMACAO, PUERTO RICO

SINGLE AUDIT REPORT

FISCAL YEAR ENDED JUNE 30, 2009

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

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

We have audited the 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, 2009, which collectively comprise the Municipality of Humacao, Puerto Rico's basic financial statements and have issued our report thereon dated December 18, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Municipality of Humacao, Puerto Rico's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Municipality of Humacao, Puerto Rico's financial statements that is more than inconsequential will not be prevented or detected by the Municipality of Humacao, Puerto Rico's internal control. We consider the deficiency identified in the accompanying schedule of findings and questioned costs as 2009-II-1 to be a significant deficiency in internal control over financial reporting.

Internal Control Over Financial Reporting (continued)

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Municipality of Humacao, Puerto Rico's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, we do not believe that the significant deficiency described above is a material weakness.

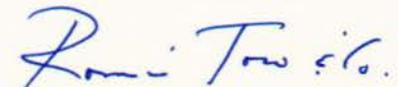
Compliance and Other Matters

As part of obtaining reasonable assurance about whether Municipality of Humacao, Puerto Rico's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Municipality of Humacao, Puerto Rico in a separate letter dated December 18, 2009.

The Municipality of Humacao's response to the findings identified in our audit are described in the accompanying schedules of findings and questioned costs. We did not audit the Municipality of Humacao's response and, accordingly, express no opinion on it.

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


ROMAN TORO & CO., CSP
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Yauco, Puerto Rico
December 18, 2009

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**REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

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

Compliance

We have audited the compliance of **Municipality of Humacao, Puerto Rico** with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2009. Municipality of Humacao, Puerto Rico's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Municipality of Humacao, Puerto Rico's management. Our responsibility is to express an opinion on Municipality of Humacao, Puerto Rico's compliance based on our audit.

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

In our opinion, Municipality of Humacao, Puerto Rico complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009.

Internal Control Over Compliance

The management of Municipality of Humacao, Puerto Rico is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Municipality of Humacao, Puerto Rico's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality of Humacao, Puerto Rico's internal control over compliance.

Internal Control Over Compliance, (Continued)

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

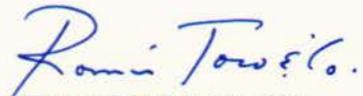
A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

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

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Municipality of Humacao, Puerto Rico, as of and for the year ended June 30, 2009, and have issued our report thereon dated December 18, 2009. Our audit was performed for the purpose of forming our opinions on the financial statements that collectively comprise the Municipality of Humacao, Puerto Rico's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of management, Mayor, others within the entity, Municipal Assembly, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.


ROMAN TORO & CO., CSP
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Yauco, Puerto Rico
December 18, 2009

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009**

FEDERAL GRANTOR / PASS THROUGH GRANTOR / PROGRAM OR CLUSTER TITLE	FEDERAL CFDA NUMBER	PASS-THROUGH ENTITY IDENTIFYING NUMBER	FEDERAL EXPENDITURES
U.S. Department of Agriculture:			
Pass-Through Department of Education: Child and Adult Care Food Program	10.558	N/AV	\$ 86,500
Pass-Through Administration of Families and Children: Child and Adult Care Food Program	10.558	N/AV	805,362
Pass-Through Rural Development: Water and Waste Disposal System for Rural Communities	10.760		<u>340,656</u>
Total U.S. Department of Agriculture			<u>1,232,518</u>
U.S. Department of Housing and Urban Development:			
Community Development Block Grant/Entitlement Grants (CDBG)	14.218		2,516,039
Section 8 Housing Choice Vouchers	14.871		<u>1,875,349</u>
Total U.S. Department of Housing and Urban Development			<u>4,391,388</u>
U.S. Department of Justice:			
Juvenile Justice and Delinquency Program	16.540		<u>24,714</u>
U.S. Department of Transportation:			
Federal Transit – Capital Investment Grants	20.500		<u>16,071</u>
U.S. National Highway Safety Administration:			
Regional Community Program	20.600		<u>3,332</u>
U.S. Department of Homeland Security:			
Pass-Through Governor Office: Public Assistance Grants	97.036	N/AV	7,168
State Domestic Preparedness Equipment Support Program (HSPG) (Cluster)	97.004		<u>392,374</u>
Total U.S. Department of Homeland Security			<u>399,542</u>
U. S. Department of Health and Human Services:			
Pass-Through Elderly Office: Special Programs for the Aging – Title III, Part C – Nutritional Services.	93.045	N/AV	65,451
Pass-Through Administration of Families and Children: Child Care and Development Block Grant	93.575	N/AV	131,616
Direct Program: Early Head Start Program	93.600		1,239,602
Pass-Through Administration of Families and Children: Head Start Program	93.600	N/AV	<u>6,626,977</u>
Total U.S. Department of Health and Human Services			<u>8,063,646</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$14,131,211</u>

See accompanying Notes to Schedule of Expenditures of Federal Awards.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO**

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009**

NOTE 1 GENERAL

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Humacao, Puerto Rico (Municipality) and is presented on the modified accrual basis. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the general-purpose financial statements. The reporting entity is defined in Note (1) (A) to the general-purpose combined financial statements.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- A. The accompanying Schedule of Expenditures of Federal Awards is prepared from Municipality's accounting records and is not intended to present financial position or the results of operations.
- B. The financial transactions are recorded by the Municipality in accordance with the terms and conditions of the grants, which are consistent with accounting principles generally accepted in the United States of America.
- C. Expenditures are recognized in the accounting period in which the liability is incurred, if measurable or when actually paid, which ever occurs first.

NOTE 3 FEDERAL CFDA NUMBER

The CFDA numbers included in this Schedule are determined based on the program name, review of grant contract information and the Office of Management and Budget's Catalogue of Federal Domestic Assistance.

NOTE 4 PASS THROUGH GRANTOR'S NUMBER

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

NOTE 5 RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Expenditures of federal awards are reported in the Municipality's Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Fund as follows: Head Start \$6,687,663 and Other Governmental Funds \$5,964,327.

NOTE 6 MAJOR PROGRAMS

Major programs are identified in the Summary of Auditor's Results Section of the Schedule of Findings and Questioned Costs.

END OF NOTES

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2009**

SECTION I – SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditor's report issued: Unqualified Opinion Qualified Opinion
 Adverse Opinion Disclaimer Opinion

Internal control over financial reporting:

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

Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major programs:

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

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

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

Identification of Major Programs:

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

Dollar threshold used to distinguish between Type A and Type B Programs: \$423,936

Auditee qualified as low-risk auditee? Yes No

END OF SECTION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS, Continued
FOR THE YEAR ENDED JUNE 30, 2009

SECTION II – FINANCIAL STATEMENT FINDINGS

2009-II-1

Type of finding: Financial statement.
Situation: Significant deficiency.
Federal Program: None.
Compliance Requirements: Not applicable.
Prior-Year(s) Audit Finding(s): None.
Questioned Costs: None.

Condition:

The Municipality did not adequately implement its internal controls for property management for several inventory items and dependencies.

Context:

During our review of property internal control system, we encountered the following deficiencies:

1. The Municipality had not accounted part of the construction costs of its Performing Arts Center which were contributed by a state agency, requiring a material adjustment to its accounting records,
2. The Person In-Charge of property had not realized the annual inventory of various dependencies, and
3. Numerous property items were delivered to municipal dependencies without properly identifying them through numbered tags, with some items received for more than 6 months without tagging.

Criteria:

The Municipality must maintain accurate and complete records of its property, must perform an annual inventory of items in all its dependencies, and tag all property items with pre-numbered identifying tags, as required under Chapter VII of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affairs (OCAM). Additionally, the Municipality must maintain adequate records and documentation in order to substantiate account balances and transactions and overall governmental fiscal operations for examination and audit, as required by Article 8.015 of Law #81 of August 30, 1991 and by Law # 5 of December 8, 1955.

Cause:

The Municipality's staff required that the state agency send the detail of construction costs to them for accounting, but we did not find any evidence of the staff efforts to accomplish this. They also informed us that they did not perform the inventories or identify property items received because of lack of transportation to their locations.

Effect:

The Municipality did not have proper safeguard controls for various property items and departments, and had incomplete accounting records of its construction in progress.

Auditor's Recommendation:

The Municipality should impart instructions and provide more resources to its staff to assure that its property records are complete and that all property safeguards are being properly implemented.

Views of responsible officials and corrective actions:

Instructions were given to the Director of Finance and Property Officer in order to take corrective actions assuring the accounting of the constructions in progress. It will require the area of project management and the Office of Federal Programs to provide to the Property Officer all information related to the progress of construction and implementation stages. In addition, to provide the resources to the Property Officer to carry out the tasks required of taking of inventories and the identification of units or property acquired.

END OF SECTION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS, Continued
FOR THE YEAR ENDED JUNE 30, 2009

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None.

END OF SECTION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2009

Year	Finding Number	Finding	CFDA Number	Questioned Cost(s)	Comments
(1) Prior Audit Findings, fully corrected or not noted during our audit:					
2008	2008-3	Incorrect payments made through direct deposits to Section 8 participating tenants and lessors.	14.871	None.	Finding was not noted during the year.
2008	2008-2	Various deficiencies in the preparation and review of the Head Start's program bank reconciliations.	93.600	None.	The situation was corrected, and not noted during the year.

(2) Prior Audit Findings, not corrected or partially corrected:

None.

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

None.

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

None.

END OF SCHEDULE



MUNICIPALITY OF HUMACAO, PUERTO RICO
ANNUAL FINANCIAL REPORT
FISCAL YEAR ENDED JUNE 30, 2009



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HUMACAO
CAPITAL DEL ESTE
CIUDAD AUTÓNOMA

COMISIONADO DE REGlamentACION
E INTERVENCION

MARCELO TRUJILLO PANISSE
ALCALDE

10 MAR 10 PM 1:35

OFICINA DEL ALCALDE

3 de marzo de 2010

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 2009 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

Cartas Of. Alcalde/Envío Single Audit 2009



10-03-090

PO BOX 178
HUMACAO, PR
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TEL. 787.656.0400

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO

CORRECTIVE ACTION PLAN

SINGLE AUDIT REPORT 2008-2009
Fiscal Year Ended June 30, 2009

Designated Officer: Hon. Marcelo Trujillo
Mayor
PO Box 178, Humacao 792-0178

Certification: 
MARCELO TRUJILLO PANISSE

Phone: 1-787- 852-2000

Date: 3/3/10

1-787-852-3066 ex

FINDINGS	CORRECTIVE ACTION	LTS
<p>SECTION II - FINANCIAL STATEMENT FINDINGS</p> <p>Number 2009-II-1</p> <p>FINANCIAL STATEMENT DEFICIENCY</p> <p>The Municipality did not adequately implement its internal controls for properly management for several inventory items and dependencies.</p> <p>During our review of property internal control system, we encountered the following deficiencies:</p> <ol style="list-style-type: none"> 1. The Municipality had not accounted part of the construction costs of its Performing Arts Center which were contributed by a state agency, requiring a material adjustment to its accounting records. 2. The person In-charge of property had not realized the annual inventory of various dependencies, and 3. Numerous property items were delivered to municipal dependencies without properly identifying them through numbered tags, with some items received for more than 6 months without tagging. 	<p>Instructions were given to the Director of Finance and Property Officer in order to take corrective actions assuring the accounting of the constructions in progress. It will require the area of project management and the Office of Federal Programs to provide to the Property Officer all information related to the progress of construction and implementation stages. In addition, to provide the resources to the Property Officer to carry out the tasks required of taking of inventories and the identification of the property units acquired.</p>	<p>Situation Part:</p> <p>Our Office will perform periodical inspections to assure that these situations been correct</p>

MUNICIPALITY OF HUMACAO, PUERTO RICO

ANNUAL FINANCIAL REPORT

FISCAL YEAR ENDED JUNE 30, 2009

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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, 2009, 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.

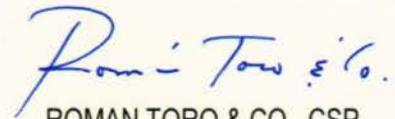
We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and 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, 2009, 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 18, 2009, 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 15 and 51 through 52, 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., CSP
LICENSE #35 - IN FORCE

Yauco, Puerto Rico
December 18, 2009

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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, 2009

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, 2009. 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 2009 by \$120,771,173 and 2008 by \$102,765,438, as restated (net assets).
- Revenues increased by \$15,530,591 (22.5%) and expenses increased \$7,044,052 (12.2%) in comparison with year 2008.
- Net change in net assets amounted to \$18,005,735, an increase of 60.5% with respect to prior year (2008) 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 \$58,721,227, an increase of \$1,233,459 in comparison with the prior year.
- The General Fund reported an excess of revenues over expenditures of \$4,512,874 and Transfer to Capital Projects the amount of \$10,272,375. Also, \$726,163 was transfer to Debt Service Fund to cover the principal and interests of operating bonds. General Fund reported unreserved fund balance of \$7,746,605, a decreased of \$5,948,312 from prior year, due to the transfer to capital projects.

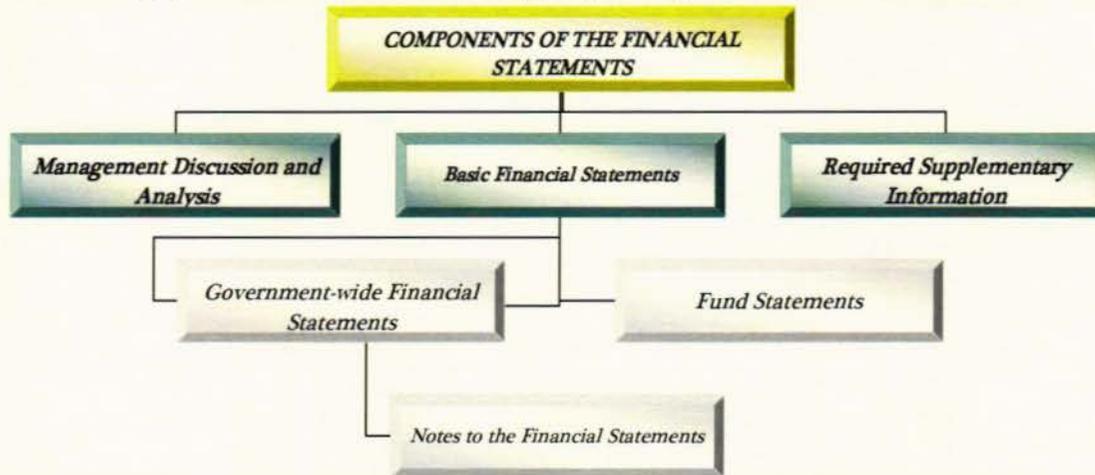
General Financial Highlights

- The investment in net capital assets as of June 30, 2009 was \$83,138,302 (net of related debt).
- Long-Term General and Special Obligations increased to \$52,295,436 an increased of \$8,035,461 in comparison with prior year balance, due to the issuances of new bonds in the amount of \$10,265,836 for general construction and the payment of \$2,230,264.
- Other long-term debts increases and net reductions from payments amounted to \$1,645,368 and \$1,408,833, respectively.
- On a budgetary basis, actual revenues exceeded actual expenditures by \$3,618,206, net of \$10,998,538 designated general fund for future expenditures (transfers out to capital project fund and debt service fund).
- Revenues increase \$3,218,651 was mainly due to \$4,939,497 of volume of business taxes. Expenditures were less than estimated by \$1,167,146, 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, 2009

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, 2009

- ***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, 2009**

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, 2009 and 2008:

Table 1		
Commonwealth of Puerto Rico Municipality of Humacao, Puerto Rico Statement of Net Assets June 30,		
	2009	2008
Current and Non-current Assets	\$ 92,511,775	\$ 86,966,040
Capital Assets	<u>110,172,710</u>	<u>84,143,298</u>
Total Assets	<u>202,684,485</u>	<u>171,109,338</u>
Current Liabilities	7,169,441	3,058,765
Deferred Revenues	13,885,816	12,619,218
Long-Term Liabilities	<u>60,858,055</u>	<u>52,665,917</u>
Total Liabilities	<u>81,913,312</u>	<u>68,343,900</u>
Net Assets:		
Investment in Capital Assets, Net of Related Debt	83,138,302	67,642,400
Restricted	31,995,598	25,056,151
Unrestricted	<u>5,637,273</u>	<u>10,066,887</u>
Total Net Assets	<u>\$ 120,771,173</u>	<u>\$ 102,765,438</u>

Net assets (assets over liabilities) may serve over time as a useful indicator of government's financial position. Net assets for the year increased 17.5% 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 \$83,138,302; total capital assets (\$141,587,961) less accumulated depreciation (\$31,415,251) and less any related outstanding debt (\$27,034,408) 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, 2009 the Municipality presented unrestricted net assets of \$5,637,273. This balance was affected by long-term obligations such as compensated absences \$5,780,162 and other debts for the amount of \$4,887,412 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, 2009

Changes in Net Assets

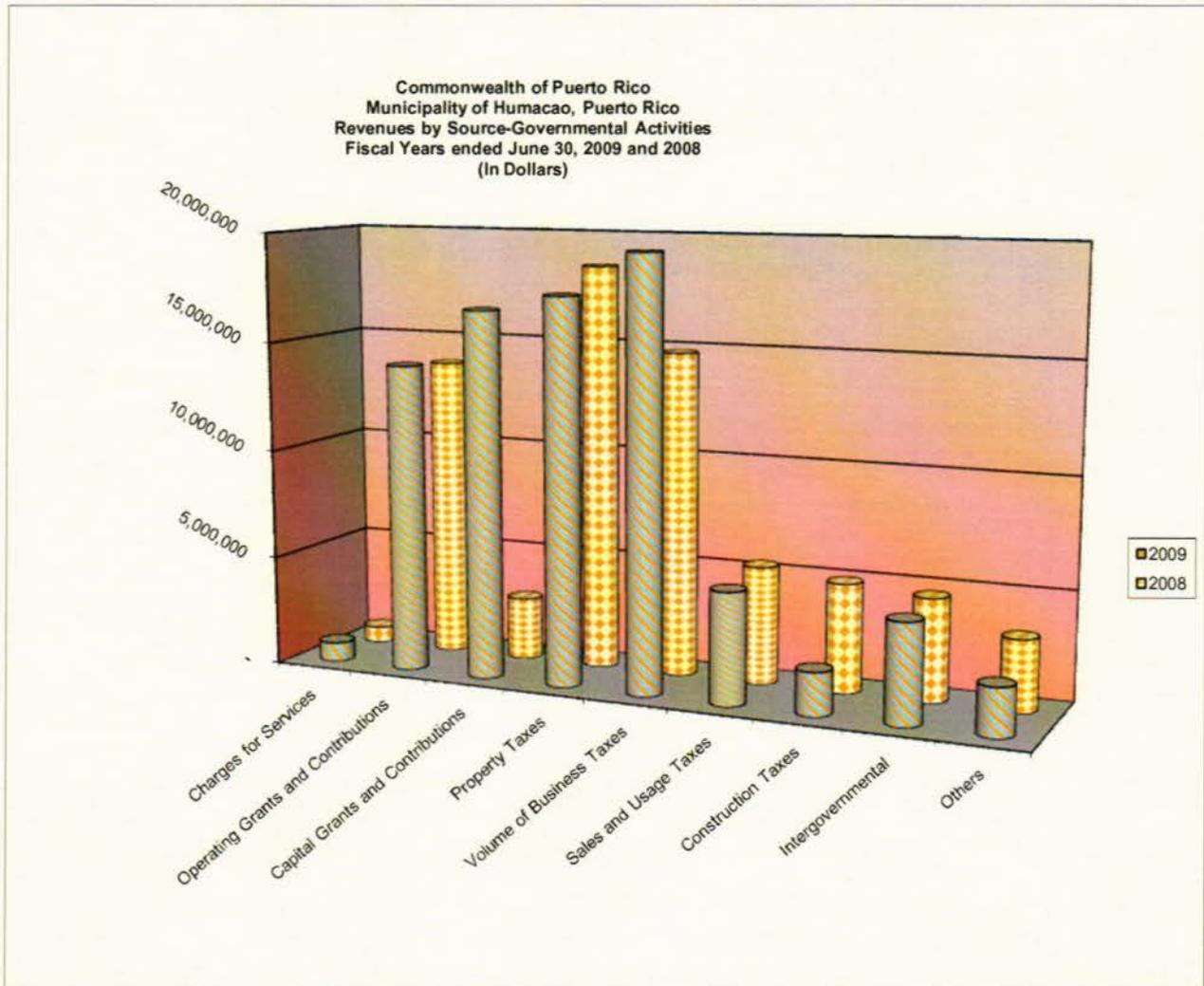
The following table summarizes the changes in net assets for the years ended June 30, 2009 and 2008:

Table 2		
Commonwealth of Puerto Rico Municipality of Humacao, Puerto Rico Change in Net Assets For the Fiscal Years Ending June 30,		
	2009	2008
Revenues:		
Program Revenues:		
Changes for Services	\$ 872,719	\$ 718,756
Operating Grants and Contributions	14,076,342	13,787,946
Capital Grants and Contributions	1,510,948	2,847,194
General Revenues:		
Property Taxes	17,492,516	18,529,331
Volume of Business Taxes	19,484,497	14,769,978
Sales and Use Taxes	5,080,367	5,365,707
Construction Taxes	1,973,471	4,955,987
Intergovernmental	4,535,341	4,670,763
Special Item	15,215,186	-
Other General Revenues	2,191,789	3,256,923
Total Revenues	<u>82,433,176</u>	<u>68,902,585</u>
Expenses:		
General Administration	26,289,993	26,885,796
Public Safety	2,912,807	2,612,229
Public Works	8,021,470	3,068,679
Culture and Recreation	2,351,873	1,968,021
Health and Sanitation	1,715,105	1,903,279
Public Instruction	7,998,508	8,666,599
Solid Waste Disposal	3,543,512	3,480,483
Human Services and Welfare	8,633,222	6,735,616
Urban Development	1,180,831	-
Loss on Disposal of Asset	83,356	2,465
Interest Costs	1,696,764	2,360,222
Total Expenses	<u>64,427,441</u>	<u>57,683,389</u>
Changes in Net Assets	18,005,735	11,219,196
Net Assets-Beginning	102,765,438	91,546,242
Net Assets-Ending	<u>\$ 120,771,173</u>	<u>\$ 102,765,438</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009**

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

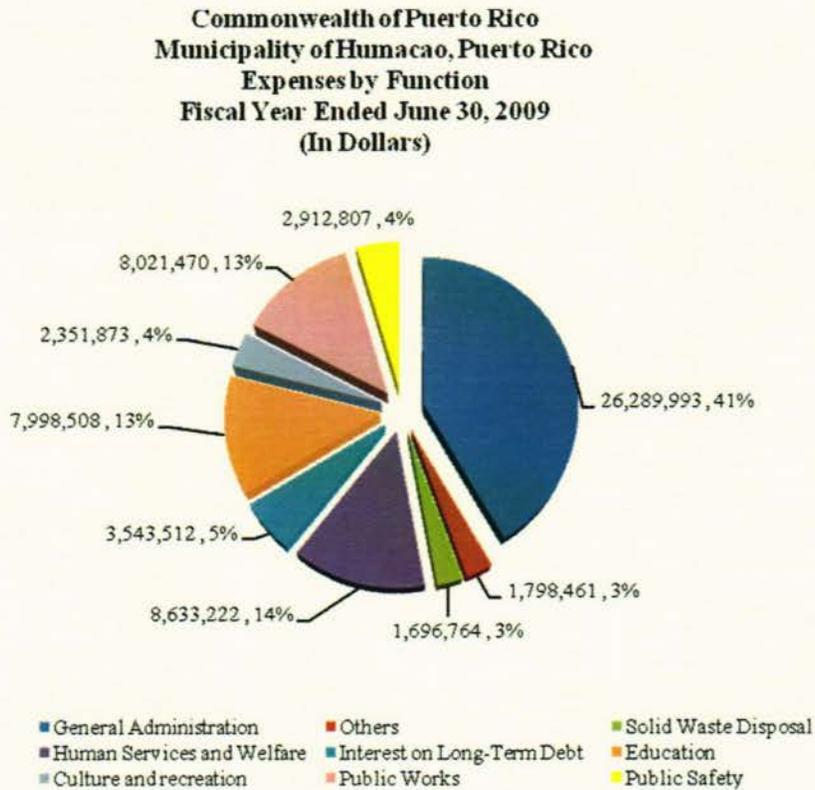
FIGURE 1



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009**

Figure 2 presents expenses by function of the governmental activities during the fiscal year 2008-2009:

FIGURE 2



Approximately 37% of the Municipality's revenues came from grants and contributions, 21% from property taxes, volume of business taxes 24% and 18% from other sources. The Municipality's expenses cover a range of services. The largest expenses are general administration with 41%, education with 12.3%, public works with 12%, and human services and welfare with 13%. Program revenues of the Municipality covered 24% of total expenses.

With respect to prior year, revenues increased by approximately \$13.5 million or 19.6%, principally due to capital grants and contributions (\$13.9 millions) for the construction of the Humacao Performing Arts Center by AFI. Other item with significant increase was the volume of business taxes for approximately \$5.0 million for collection of prior years from some industries and other commercial.

Expenses increased 12.2% or \$7,044,052 in comparison with 2008 year, principally in public works and human services and welfare.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

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):

Table 3

**Commonwealth of Puerto Rico
Municipality of Humacao, Puerto Rico
Net Cost of Municipality's Governmental Activities
For the Fiscal Years Ended June 30,**

Functions/Programs	Total Cost of Services		Net Cost of Services	
	2009	2008	2009	2008
General Administration	\$ 26,289,993	\$ 26,885,796	\$ 25,783,771	\$ 25,008,303
Public Safety	2,912,807	2,612,229	2,495,719	2,249,688
Public Works	8,021,470	3,068,679	7,590,046	2,594,344
Culture and Recreation	2,351,873	1,968,021	2,337,963	1,916,416
Public Instruction	7,998,508	8,666,599	(14,132)	444,814
Solid Waste Disposal	3,543,512	3,480,483	3,543,512	3,480,483
Human Services and Welfare	8,633,222	6,735,616	4,315,901	3,935,429
Urban Development	1,180,831	-	(15,923,040)	(2,847,194)
Interest on Long-Term Debt	1,696,764	2,360,222	1,696,764	2,360,222
Others	1,798,461	1,905,744	925,742	1,186,988
Total	\$ 64,427,441	\$ 57,683,389	\$ 32,752,246	\$ 40,329,493

Some of the cost of governmental activities in 2009 was paid by those who directly benefited from the programs (\$872,719) and other governments and organizations that subsidized certain programs with grants and contributions (\$30,802,476). The \$32,752,246 net cost of services was substantially covered by other general revenues including property, volume of business license taxes, sales and usage 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, 2009, the governmental funds reported combined ending fund balances of \$58,721,227, a net increase of \$1,223,454 in comparison with the prior year. This increase was caused primarily by a net change in the general fund corresponding to excess of revenues \$4.5 million and new issuance of special obligations bonds. Of total combined fund balances, \$7,746,605 (12.6%) constitutes unreserved fund balance of general fund. The remainder of fund balance is reserved to indicate that is not available for new spending.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

The general fund is the operating fund of the Municipality. Unreserved fund balance of the general fund represents approximately 92.6% of total ending general fund balance. For the year ended June 30, 2009, the fund balance of the general fund decreased by \$6.3 million when compared with the prior year due to the transfers to capital projects fund and debt service fund.

Table 4

**Government of Puerto Rico
Municipality of Humacao, Puerto Rico
General Fund
As of June 30,**

Description	<u>2009</u>	<u>2008</u>
Revenues:		
Property Taxes	\$ 13,510,579	\$ 13,587,982
Volume of Business Taxes	19,484,497	14,769,978
Sales and Usage Taxes	4,158,184	4,808,414
Licenses and Permits	1,973,471	4,955,987
Intergovernmental	4,535,341	4,670,763
Interests	1,191,985	2,758,316
Charges for Service	872,719	718,756
Miscellaneous	466,385	498,607
Total Revenues	<u>46,193,161</u>	<u>46,768,803</u>
Expenditures:		
General Government	22,508,047	19,973,045
Public Safety	2,579,774	2,301,877
Public Work	3,120,752	2,764,107
Culture and Recreation	1,857,551	1,395,791
Health and Sanitation	1,715,105	5,373,749
Human Services and Welfare	8,203,839	4,186,650
Urban Development	1,133,744	907,137
Capital Outlay	561,475	998,234
Total Expenditures	<u>41,680,287</u>	<u>37,900,590</u>
Net Transfer In (Out)	(10,541,078)	(4,438,098)
Other Financing Sources	-	-
Net (decrease) increase in Fund Balance	<u>\$ (6,028,204)</u>	<u>\$ 4,430,115</u>

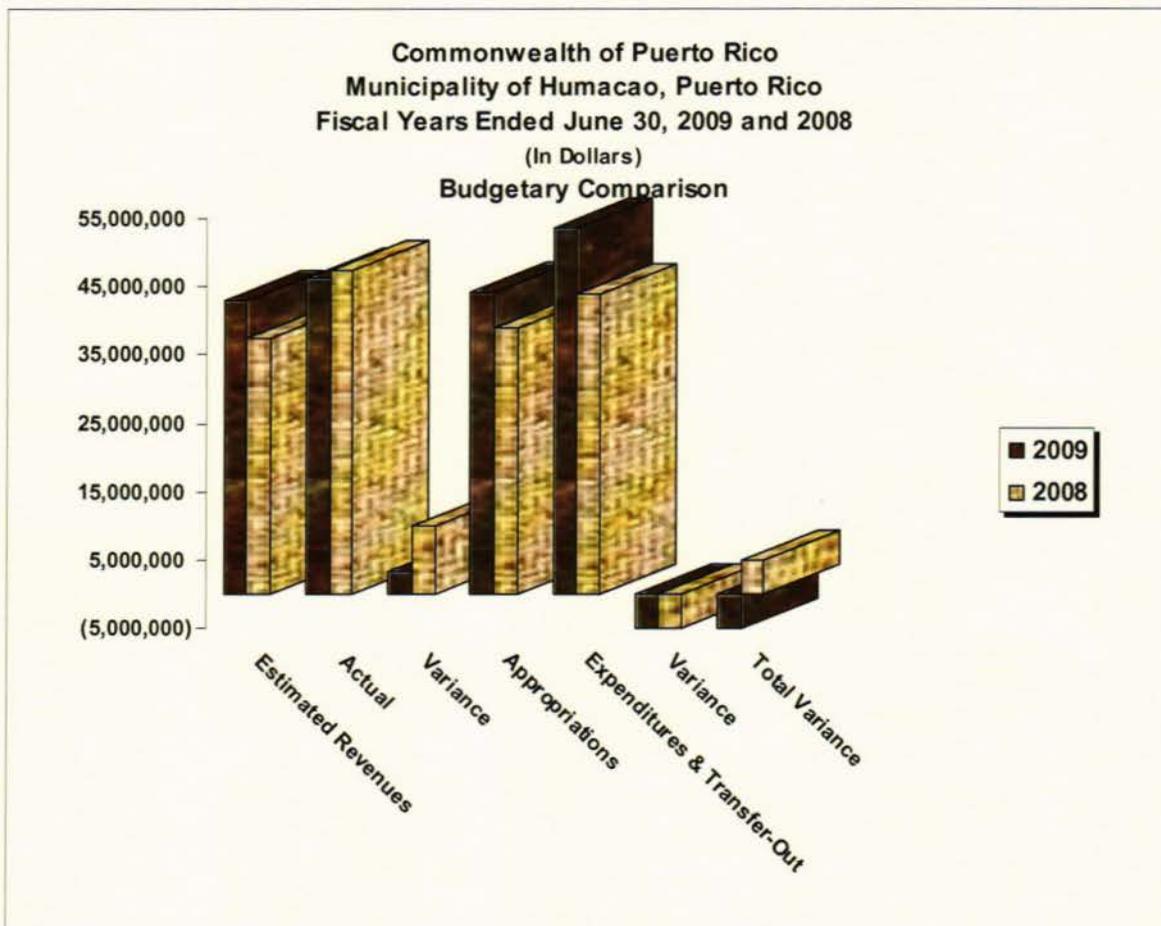
COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

GENERAL FUND BUDGETARY HIGHLIGHTS

The general fund original budget for the fiscal period 2008-2009 presented an increase of 14.7% with respect to prior year budget. During the fiscal year budget revenues were increased by \$3,218,651 mainly due to excess in volume of business 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 \$10.5 million.

A positive variance of \$1,167,146 between final 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 \$10.5 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, 2009**

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At the end of the fiscal year, the Municipality has invested \$110,172,710 (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 \$26 million or over 31% from the prior year.

Table 5

**Commonwealth of Puerto Rico
Municipality of Humacao, Puerto Rico
Capital Assets, net
As of June 30,**

	<u>Governmental Activities</u>	
	<u>2009</u>	<u>2008</u>
Non-Depreciable Assets:		
Land	\$ 11,594,691	\$ 11,390,661
Construction in Progress	39,312,828	23,104,931
Depreciable Assets:		
Buildings	38,267,209	34,241,962
Infrastructure	16,784,533	11,525,706
Motor Vehicles	2,250,271	1,751,358
Equipment	1,893,746	1,957,840
Capital Lease	69,432	170,838
Total	\$ 110,172,710	\$ 84,143,296

The Municipality invested a total of \$10,720,442 in capital assets during the fiscal year 2008-2009, in addition to a capital contribution of \$17,982,029 received from the state for its Arts Center. Principal additions are as follows:

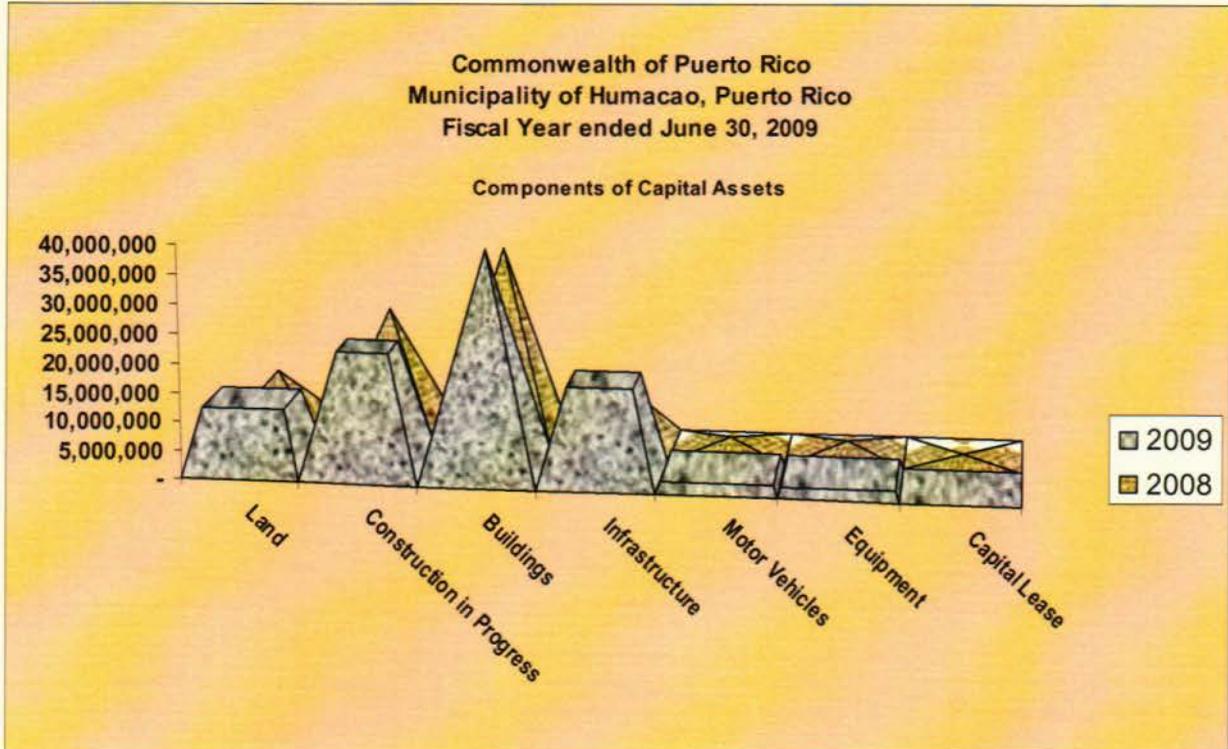
- Land acquisition - \$204,030
- Construction in Progress - \$26,414,887 -
The principal projects are the following:
 - Municipal Coliseum (\$3,750,143)
 - Art Center (\$19,421,528)
 - Various Recreational Facilities (\$3,243,216)
- Acquisition of Motor Vehicles - \$971,716
- Acquisition of Equipment - \$619,838

Projects in the amount of \$658,946 were finished.

Other projects related to repair and maintenance of roads (not capitalized) and facilities were developed during the fiscal year 2009.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

FIGURE 4



Long-Term Debts

At year-end, the Municipality had \$52,295,436 in general and special bonds, an increased of \$8 million, by the issuances of new bonds in the amount of \$10,265,725 for general construction and the payment of \$2,230,264. The following is a summary of the Municipality's outstanding debt as of June 30, 2009 and 2008:

Table 6

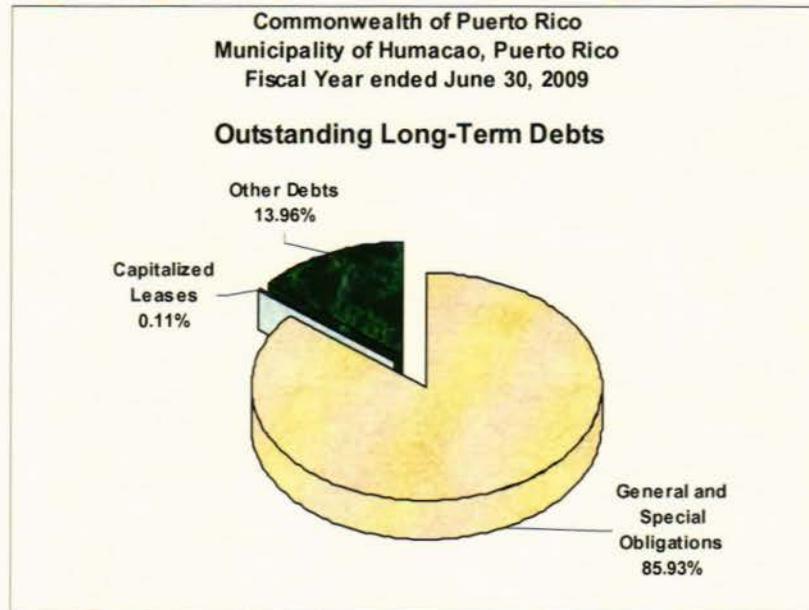
**Commonwealth of Puerto Rico
Municipality of Humacao, Puerto Rico
Outstanding Long-Term Debts
As of June 30,**

	<u>Governmental Activities</u>	
	<u>2009</u>	<u>2008</u>
General and Special Obligation Bonds	\$ 52,295,436	\$ 44,259,975
Capitalized Leases	69,869	149,727
Others Debts	8,492,750	8,256,215
Total	<u>\$ 60,858,055</u>	<u>\$ 52,665,917</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009**

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

FIGURE 5



ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's selected and appointed officials considered many factors when setting the fiscal year 2008-2009 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 19.5%, which compares with the Commonwealth rate of 15.2%.

The Municipality applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2009-2010 are \$40.5 million, approximately \$2.4 million less than the fiscal year 2008-2009. The Municipality expects a decrease in revenues for the next year due to the construction taxes and interest on investments, and to the economic rescission. 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, 2009

	<u>GOVERNMENTAL ACTIVITIES</u>
ASSETS:	
Cash and Investments	\$ 54,504,353
Cash with Fiscal Agent	25,762,640
Receivables (net):	
Property Taxes	672,876
Due from Governmental Units	140,665
Federal Grants	10,783,112
Sales and Use Taxes	337,116
Others	52,172
Total Current Assets	<u>92,252,934</u>
Deferred Charges	258,841
Capital Assets:	
Land, Improvement and Construction in Progress	50,907,519
Other Capital Assets [Net of Depreciation]	59,265,191
Total Capital Assets	<u>110,172,710</u>
TOTAL ASSETS	<u>\$ 202,684,485</u>
LIABILITIES:	
Accounts Payable and Accrued Expenses	\$ 2,966,039
Accrued Interest	652,999
Due to Governmental Units	3,550,403
Deferred Revenues	13,885,816
Long-Term Liabilities:	
Due Within One Year	6,778,362
Due in More than One Year	54,079,693
TOTAL LIABILITIES	<u>81,913,312</u>
NET ASSETS:	
Investment in Capital Assets, Net of Related Debt	83,138,302
Restricted for:	
Capital Project	1,411,779
Head Start	4,387,982
Debt Service	11,963,576
Community Development Projects	1,684,536
Other Purposes	12,547,725
Unrestricted	5,637,273
TOTAL NET ASSETS	<u>\$ 120,771,173</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, 2009

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	\$ 4,163,535	\$ -	\$ -	\$ -	\$ (4,163,535)
General Government	22,126,458	-	506,222	-	(21,620,236)
Public Safety	2,912,807	-	417,088	-	(2,495,719)
Public Works	8,021,470	-	431,424	-	(7,590,046)
Culture and Recreation	2,351,873	-	13,910	-	(2,337,963)
Health and Sanitation	1,715,105	872,719	-	-	(842,386)
Public Instruction	7,998,508	-	8,012,640	-	14,132
Solid Waste Disposal	3,543,512	-	-	-	(3,543,512)
Human Services and Welfare	8,633,222	-	4,317,321	-	(4,315,901)
Urban Development	1,180,831	-	377,737	1,510,948	707,854
Loss on Disposition of Asset	83,356	-	-	-	(83,356)
Interest on Long-Term Debt	1,696,764	-	-	-	(1,696,764)
Total Governmental Activities	\$ 64,427,441	\$ 872,719	\$ 14,076,342	\$ 1,510,948	(47,967,432)
General Revenues:					
Taxes:					
Property Taxes, levied for General Purposes					13,510,579
Property Taxes, levied for Debt Service					3,981,937
Volume of Business Taxes					19,484,497
Sales and Use Taxes					5,080,367
Construction Taxes					1,973,471
Intergovernmental					4,535,341
Rent					87,392
Miscellaneous					378,993
Interest					1,725,404
Special item - Capital contribution for Arts Center (Note 17)					15,215,186
Total General Revenues and Special Item					65,973,167
CHANGES IN NET ASSETS					18,005,735
Net Assets – Beginning of Year, as Restated					102,765,438
NET ASSETS – ENDING OF YEAR					\$ 120,771,173

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
BALANCE SHEET – GOVERNMENTAL FUNDS
JUNE 30, 2009

	GENERAL FUND	HEAD START FUND	ART CENTER FUND	MULTIPLE USES COLISEUM FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS:							
Cash and Cash Equivalents	\$ 22,694,105	\$ 330,284	\$ 11,666,872	\$ 6,633,861	\$ -	\$ 13,179,231	\$ 54,504,353
Cash with Fiscal Agent	5,500	-	235,150	10,623,586	11,943,699	2,954,705	25,762,640
Receivables:							
Property Taxes	-	-	-	-	672,876	-	672,876
Sales and Use Taxes	337,116	-	-	-	-	-	337,116
Federal Grants	-	4,805,538	-	-	-	5,977,574	10,783,112
Due from Other Funds	1,386,093	-	-	-	-	170	1,386,263
Due from Governmental Units	944	-	-	-	-	139,721	140,665
Other Receivables	-	-	-	-	-	52,172	52,172
Total Assets	\$ 24,423,758	\$ 5,135,822	\$ 11,902,022	\$ 17,257,447	\$ 12,616,575	\$ 22,303,573	\$ 93,639,197
LIABILITIES AND FUND BALANCES:							
Liabilities:							
Account Payable	\$ 1,841,933	\$ 84,781	\$ 13,548	\$ 217,513	\$ -	\$ 808,264	\$ 2,966,039
Bond and Notes	-	-	-	-	2,860,000	-	2,860,000
Account Interest	-	-	-	-	652,999	-	652,999
Due to Federal Governmental	-	-	-	-	-	396,669	396,669
Due to Governmental Units	354,566	-	2,766,843	-	-	32,325	3,153,734
Due to Other Funds	170	309,128	-	-	-	1,076,965	1,386,263
Deferred Revenues:							
Volume of Business Tax	13,885,816	-	-	-	-	-	13,885,816
Federal Grants	-	4,308,841	-	-	-	5,307,609	9,616,450
Total Liabilities	16,082,485	4,702,750	2,780,391	217,513	3,512,999	7,621,832	34,917,970

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
BALANCE SHEET – GOVERNMENTAL FUNDS, Continued
JUNE 30, 2009

	GENERAL FUND	HEAD START FUND	ART CENTER FUND	MULTIPLE USES COLISEUM FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
Fund Balances:							
Reserve For:							
Encumbrances	594,668	-	-	-	-	-	594,668
Debt Service	-	-	-	-	9,103,576	-	9,103,576
Head Start Program	-	433,072	-	-	-	-	433,072
Capital Projects	-	-	9,121,631	17,039,934	-	7,406,879	33,568,444
Other Purposes	-	-	-	-	-	7,274,862	7,274,862
Unreserved	<u>7,746,605</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>7,746,605</u>
Total Fund Balances	<u>8,341,273</u>	<u>433,072</u>	<u>9,121,631</u>	<u>17,039,934</u>	<u>9,103,576</u>	<u>14,681,741</u>	<u>58,721,227</u>
Total Liabilities and Fund Balances	<u>\$ 24,423,758</u>	<u>\$ 5,135,822</u>	<u>\$ 11,902,022</u>	<u>\$ 17,257,447</u>	<u>\$ 12,616,575</u>	<u>\$ 22,303,573</u>	<u>\$ 93,639,197</u>

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, 2009

Total Fund Balances – Government Funds (Page 19) **\$ 58,721,227**

Amount reported for Governmental Activities in the Statement of Net Assets (Page 16)
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	\$ 50,907,519	
Depreciable Capital Assets	68,676,667	
Infrastructure Assets	22,003,775	
Accumulated Depreciation	<u>(31,415,251)</u>	
Total Capital Assets		110,172,710

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

Deferred Charges		258,841
------------------	--	---------

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	1,536,011	
Head Start Program	4,308,841	
Early Head Start Program	1,374,806	
Other Major Fund	<u>2,396,792</u>	
Total Deferred Revenues		9,616,450

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	(49,435,436)	
Capital Leases	(69,869)	
Property Tax Advance - MRCC	(1,015,803)	
Law Number 146 - MRCC	(672,013)	
LIMS Debt - MRCC	(563,358)	
Law Number 42 - MRCC	(446,918)	
Employees Retirement Administration	(14,496)	
Compensated Absences	<u>(5,780,162)</u>	
Total Long-Term Liabilities		<u>(57,998,055)</u>

Total Net Assets of Governmental Activities (Page 16) **\$ 120,771,173**

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, 2009

	GENERAL FUND	HEAD START FUND	ART CENTER	MULTIPLE USE COLISEUM FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
REVENUES:							
Property Taxes	\$ 13,510,579	\$ -	\$ -	\$ -	\$ 3,981,937	\$ -	\$ 17,492,516
Volume of Business Taxes	19,484,497	-	-	-	-	-	19,484,497
Sales and Use Taxes	4,158,184	-	-	-	922,183	-	5,080,367
Federal Assistances	-	6,659,562	-	-	-	7,125,233	13,784,795
Intergovernmental	4,535,341	-	-	-	-	3,631,921	8,167,262
Licenses and Permits	1,973,471	-	-	-	-	-	1,973,471
Charges for Services	872,719	-	-	-	-	-	872,719
Interest	1,191,985	-	389,709	143,710	-	-	1,725,404
Miscellaneous	466,385	-	-	-	-	-	466,385
Total Revenues	<u>46,193,161</u>	<u>6,659,562</u>	<u>389,709</u>	<u>143,710</u>	<u>4,904,120</u>	<u>10,757,154</u>	<u>69,047,416</u>
EXPENDITURES:							
Current:							
Mayor and Municipal Legislature	2,482,202	-	-	-	-	-	2,482,202
General Government	20,025,845	-	-	-	-	1,985,328	22,011,173
Public Safety	2,579,774	-	-	-	-	420,420	3,000,194
Public Works	3,120,752	-	-	-	-	2,302,532	5,423,284
Culture and Recreation	1,857,551	-	-	-	-	10,171	1,867,722
Health and Sanitation	1,715,105	-	-	-	-	-	1,715,105
Public Instruction	-	6,626,976	-	-	-	1,371,532	7,998,508
Solid Waste Disposal	3,543,512	-	-	-	-	-	3,543,512
Human Services and Welfare	4,660,327	-	-	-	-	3,987,105	8,647,432
Urban Development	1,133,744	-	-	-	-	1,389,243	2,522,987
Capital Outlay	561,475	-	19,421,528	3,750,143	-	4,969,325	28,702,471
Debt Service:							
Principal	-	-	-	-	3,421,425	-	3,421,425
Interest and Other Charges	-	-	-	-	1,696,764	-	1,696,764
Bond Issue Costs	-	-	-	-	36,364	-	36,364
Total Expenditures	<u>41,680,287</u>	<u>6,626,976</u>	<u>19,421,528</u>	<u>3,750,143</u>	<u>5,154,553</u>	<u>16,435,656</u>	<u>93,069,143</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	<u>4,512,874</u>	<u>32,586</u>	<u>(19,031,819)</u>	<u>(3,606,433)</u>	<u>(250,433)</u>	<u>(5,678,502)</u>	<u>(24,021,727)</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE – GOVERNMENTAL FUNDS, Continued
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	GENERAL FUND	HEAD START FUND	ART CENTER	MULTIPLE USE COLISEUM FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
OTHER FINANCING SOURCES (USES):							
Proceed of Bonds	-	-	-	10,040,000	-	-	10,040,000
Transfers – In	457,460	-	1,368,516	4,150,000	726,163	4,790,223	11,492,362
Transfers – Out	(10,998,538)	-	-	(36,364)	-	(457,460)	(11,492,362)
Total Other Financing Sources and Uses	(10,541,078)	-	1,368,516	14,153,636	726,163	4,332,763	10,040,000
SPECIAL ITEM							
Capital contribution for Arts Center (Note17)	-	-	15,215,186	-	-	-	15,215,186
Net Change in Fund Balance	(6,028,204)	32,586	(2,448,117)	10,547,203	475,730	(1,345,739)	1,233,459
Fund Balance – Beginning	14,369,477	400,486	11,569,748	6,492,731	8,627,846	16,027,480	57,487,768
FUND BALANCE – ENDING	\$ 8,341,273	\$ 433,072	\$ 9,121,631	\$ 17,039,934	\$ 9,103,576	\$ 14,681,741	\$ 58,721,227

See accompanying Notes to Basic Financial Statements.

OK [Signature]
7/25/2010

**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, 2009**

Net Change in Fund Balances – Government Funds (Page 22) \$ 1,233,459

Amount reported for Governmental Activities in the Statement of Activities (Page 17) 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:

Urban Development and Capital Outlay	\$ 28,702,471	
Depreciation Expense	<u>(2,589,703)</u>	
Excess of Capital Assets over Depreciation Expense		26,112,768

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:

Amortization of Deferred Charges	(10,570)
----------------------------------	----------

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

3,421,425

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

(1,829,426)

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

(83,356)

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 Issue Costs	40,000	
Increase in Bonds	(10,265,725)	
Increase in Claims and Judgments	478,000	
Increase in Property Tax Advance	(730,827)	
Increase in Compensated Absences	<u>(360,013)</u>	
Total Additional Expenses		<u>(10,838,565)</u>

Change in Net Assets of Governmental Activities (Page 17) \$ 18,005,735

See accompanying Notes to Basic Financial Statements.

1. FINANCIAL REPORTING ENTITY

A. Organization

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.

B. Reporting Entity

A reporting entity is comprised of the primary government, component units and other organizations that are included to ensure that financial statements are not misleading. The primary government consists of all funds, departments, boards and agencies that are not legally separate from the Municipality and for which the Municipality is financial accountable.

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

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 activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2009, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Financial Statement Presentation

The basic financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America as applicable to local governmental units (USGAAP). The basic financial statements include both government-wide (based on the Municipality as a whole) and fund financial statements, which provide a more detailed level of financial information. Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as governmental type.

The financial information of the Municipality is presented in this report as follows:

Management's Discussion and Analysis

Management's discussion and analysis is required supplementary information that introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.

Government-wide Financial Statements (GWFS)

The GWFS (the *Statement of Net Assets* and the *Statement of Activities*) report information of all the activities of the Municipality.

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*.

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.

Governmental Funds Financial Statements (GFFS)

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 GFFS are presented in different measurement focus and basis of accounting than the GWFS, reconciliation is presented and separate explanation for each differences.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

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.

Notes to the Basic Financial Statements

The notes to the financial statements provide information that is essential to a user's full understanding of the data provided in the basic financial statements

Required Supplementary Information

The basic financial statements are followed by a section of required supplementary information. This section includes a *Budgetary Comparison Schedule – General Fund*, which includes reconciliation between the statutory fund balance for budgetary purposes and the fund balance for the General Fund as presented in the GFFS.

B. Measurement Focus and Basis of Accounting

Government-wide Financial Statements

The GWFS are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, as are the proprietary funds. Subject to the additional rules and limitations detailed below, revenue (including interest on deposits and investments) is generally recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

All revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are generally recorded when the exchange takes place. In exchange transactions, each party to the transaction receives and gives up essentially equal values. An exchange-like transaction is one in which there is an identifiable exchange and the values exchanged, though related, may not be quite equal. The accompanying GWFS include exchange-like transactions such as license fees, fines, penalties, forfeitures, permits, charges for services, and most miscellaneous revenues, which are recorded as revenues when collected because they are generally not measurable until actually received.

The Municipality groups its non-exchange transactions into the following four classes in the basic financial statements:

Derived Tax Revenues – in this revenue, which result from assessments that the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred.

Imposed Non-exchange Revenues – in this revenue (such as property taxes and volume of business taxes), which result from assessments made by the Municipality on non-governmental entities, including individuals, other than assessments on exchange transactions, receivables are generally recorded in the period when an enforceable legal claim has arisen. Property taxes and volume of business taxes are recognized as revenues (net of amounts considered not collectible) in the fiscal year when resources are required to be used or the first fiscal year that the use of the resources is permitted.

Government Mandated Non-exchange Transactions – in this revenue (such as intergovernmental grants and contributions), receivables and revenues are generally recorded when all eligibility requirements imposed by the provider have been met. For part of the grants, the Municipality must expend resources on the specific purpose or project before the provider reimburses any amounts. Therefore, revenue is generally recognized as qualifying reimbursable expenditures are incurred.

Voluntary Non-exchange Transactions – in this revenue (such as donations and certain grants and entitlements) receivables and revenues are generally accounted for in the same manner as government mandated non-exchange transactions discussed above.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

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

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

Governmental Funds Financial Statements

The GFFS 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. At June 30, 2009, all revenues sources met this availability criterion.

Property taxes, volume of business 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.

In a manner similar to GWFS, but subject to and limited by the availability criteria discussed above, all revenues, expenses, gains, losses, assets and liabilities resulting from exchange, exchange-like transactions are also generally recorded when the exchange takes place while all revenues, expenses, gains, losses and assets resulting from non-exchange transactions are recorded when an enforceable legal claim arises or when all eligibility requirements imposed by the provider have been met, applicable.

The Municipality generally accrues a governmental fund liability and expenditures (including salaries, professional services, supplies, utilities, etc.) in the period in which the government incurs the liability, to the extent that these liabilities are normally expected to be liquidated in a timely manner and in full with current available financial resources. The accompanying balance sheet – governmental funds generally reflects only assets that will not be converted into cash to satisfy current liabilities. Long-Term assets and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying balance sheet – governmental funds. At the same time, long-term liabilities (generally, those unmatured that will not require the use of current financial resources to pay them) are not accounted for in the accompanying balance sheet – governmental funds. Modifications to the accrual basis of accounting include:

- a. Principal and interest on bonds payable are recorded when they matured (when payment is due), except for principal and interest of bonds due on July 1, 2009, which are recorded as governmental fund liabilities of June 30, 2009 which is the date when resources were available in the debt service fund.
- b. Obligations from compensated absences and the estimated liability for municipal solid waste landfill post-closure care costs are recorded only when they mature (when payment is due).

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

- c. Certain accounts payable, intergovernmental payables and other accrued liabilities not due and payable (unmatured) or not normally expected to be liquidated in full and in a timely manner with available and expendable financial resources, are recorded in the accompanying *Statement of Net Assets*. Such liabilities are recorded in the governmental funds when they mature.
- d. Executory purchase orders and contracts are recorded as a reservation of fund balance in the GFFS.

The measurement focus of the GFFS is on decreases of net financial resources (expenditures) rather than expenses. Most expenditures are measurable and are recorded when the related governmental fund liability is incurred. Allocation of costs, such as depreciation and amortization, are recorded in the accompanying *Statement of Activities*, but are not recorded in the accompanying GFFS.

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.

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

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

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

The non-major funds are combined in a single column in the GGFS.

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 GWFS.

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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For USGAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year. In addition, under the budgetary basis of accounting, revenues are recorded when cash is received.

The unencumbered balance of any appropriation at the end of the year will lapse at the end of such fiscal year. Other appropriations, mainly capital project appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

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

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.

Final Budget

The final budgetary data presented in the Budgetary Comparison Schedule – General Fund 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

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.

B. Assets, Liabilities, and Net Assets

1) Cash and Investment, and Cash with Fiscal Agent

The Municipality's cash and investment are composed of demand deposits in commercial banks, demand deposits in the Governmental Development Bank of Puerto Rico (GDB), and cash equivalents in commercial banks. The Municipality has adopted the *Statement of Uniform Investment Guidelines for the Municipalities of the Government of Puerto Rico*, issued by the GDB as promulgated by Law No. 113 of August 3, 1995. The Finance Director of the Municipality, follow the guidelines, 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 interest bearing commercial bank accounts are recognized as revenue in the General Fund, Art Center Fund and in Multiuses Coliseum Fund in accordance with amount invested. Cash in the Special Revenue 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 Government, deposit in the GDB 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 GDB. This sinking fund is maintained by the GDB, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

2) 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".

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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

Receivables consist of all revenues earned but not collected at June 30, 2009. These account receivables are shown net of estimated allowances for uncollectible accounts, which are determined upon past collection experience, historical trends, and current economic conditions. Intergovernmental receivables in the general fund represent mostly sales and usage taxes, federal grant and contributions, property tax accounts that are levied by Municipal Revenue Collection Center (MRCC), a governmental entity created by the Government. Intergovernmental receivables in the other governmental funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded grant and contributions and state appropriations, and the amount in the debt service fund represents the distribution of property tax collected which is restricted for the debt service.

3) 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.

4) Deferred Charges

Deferred charges in the accompanying *Statement of Net Assets* consist of bond issuance costs, net of accumulated amortization. Deferred charges are amortized over the term of the related debt using the straight-line method. In the GFFS, bond issuance costs are recorded in the current period as expenditures, whether or not withheld from the actual debt proceeds received.

5) 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 GWFS. 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 Municipality 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 Municipality 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

Capital outlay is recorded as expenditures of the General Fund and other governmental funds and as assets in the GFFS 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. Depreciation and amortization expense is recorded only in the GWFS. Depreciable capital assets are generally depreciated or amortized over their estimated useful lives under the straight-line method, except for equipment held under capital leases which is depreciated over the shorter of its estimated useful life or the lease term. No depreciation is recorded for land and construction in progress. The estimated useful lives of major capital asset categories are:

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

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

Impaired capital assets that will no longer be used by the Municipality, if any, are reported at the lower of carrying value or fair value. Impairment losses on capital assets with physical damages that will continue to be used by the Municipality are measured using the restoration cost approach. Impairments of capital assets that are subject to a change in the manner or duration of use, or assets affected by enactment or approval of laws or regulations or other changes in environmental factors or assets that are subject to technological changes or obsolescence, if any, are measured using the service units approach.

The Municipality classifies as capital leases all lease agreements that involve the transfer of substantially all benefits and risks inherent in the ownership of the leased property and meet one or more of the following four criteria: (1) by the end of the lease term, the ownership of the leased property is transferred to the Municipality, (2) the lease agreement contains a bargain purchase option, (3) the lease term is substantially equal (75 percent or more) to the estimated useful life of the leased property, and (4) at the inception of the lease, the present value of the minimum lease payments, with certain adjustments, is 90 percent or more of the estimated fair value of the leased property.

Although the Municipality is prevented legally from entering into obligations extending beyond one fiscal year, most capital lease agreements entered by the Municipality contain fiscal funding clauses or cancellation clauses that make the continuation of the agreements subject to future appropriations.

Leases that meet at least one of the aforementioned four criteria and have a fiscal funding or a cancellation clause have been recorded as capital leases in the accompanying *Statement of Net Assets*, since the likelihood of invoking the provision is considered remote. The Municipality's lease agreements do not include contingent rental payments no escalation clauses.

In the GWFS, the obligation under capital leases is recorded at the lesser of the estimated fair value of the leased property or the present value of the minimum lease payments, excluding any portion representing executory costs and profit thereon to be paid by the lessor. A portion of each minimum lease payment is allocated to interest expense.

In the accompanying GFFS, the net present value of the minimum lease payments at the inception of the capital lease is recorded simultaneously as: (1) expenditures and (2) other financing sources. Minimum lease payments are recorded as expenditures in the governmental fund.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

6) Deferred Revenues

In the GWFS, deferred revenues arise only when the Municipality receives resources before it has a legal claim to them. In the GFFS, arises when one of the following situations occur: (1) potential revenue does not meet both the measurable and available criteria for revenue recognition in the current period (unavailable revenue), and (2) the Municipality receives resources before it has a legal claim to them (unearned revenue).

7) Long-Term Obligations, Bonds Issuance Costs, and Premium or Discount

The liabilities reported in the GWFS 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. 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 GFFS, 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.

8) 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 at the current rate. 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; and (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 GWFS and Proprietary Fund Financial Statements. For the GWFS, the current portion is the amount estimated to be used in the following year. For the GFFS, 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.

9) 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 when the liability is incurred. The Long-Term Liabilities includes, when appropriate, 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

10) Accounting for Pension Costs

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

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

For the purpose of applying the requirements of GASBS No. 27, the state government of the Government is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multiemployer cost-sharing defined benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate. The Municipality is considered a participant, and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Government and the basic financial statements of such retirement systems are part of the financial reporting entity of the Government.

11) Net Assets/Fund Balance

Net Assets

The GWFS and Proprietary Funds Financial Statements utilize a net assets presentation, which are categorized as follow:

- *Invested in Capital Assets, Net of Related Debt* – These consists of capital assets, net of accumulated depreciation and amortization, reduced by the outstanding balances of bonds payable, notes payable and other debts that are attributed to the acquisition, construction or improvements of those assets. For the purposes of determining the outstanding debt attributed to capital assets, the total long-term debt related to the acquisition, construction or improvements of capital assets has been reduced by any related unspent debt proceeds and any related unamortized debt issuance costs. In addition, the outstanding debt attributed to capital assets does not include accrued interest payable, non-capital accrued liabilities, inter-fund loans and other financial assets. Net assets invested in capital assets, net of related debt is comprised of the following:

	<u>Governmental Activities</u>
Capital Assets, Net of Accumulated Depreciation	\$110,172,710
Outstanding Balance on Related Debt.....	(55,132,148)
Unspent Capital Debt Proceeds	<u>28,097,740</u>
Total Invested in Capital Assets, Net of Related Debt	<u>\$ 83,138,302</u>

- *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.

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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

Fund Balance

The GFFS 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* – Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
- *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 under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
- *Reserve for Other Purposes* – Certain assets, primarily cash of grants and contributions that are authorized to be carried over and expended in the ensuing year.

C. 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.

D. 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, 2009 amounted to approximately \$519,162. The current insurance policies have not been cancelled or terminated. In addition, MRCC deducted approximately \$821,767 for workers compensation insurance covering all municipal employees for the same period.

E. Use of Estimates

The preparation of the basic financial statements in conformity with USGAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continuation)

F. Reclassifications

Various reclassifications have been made in the accompanying basic financial statements which affect the comparability with the basic financial statements issued for previous fiscal years.

G. Future Adoption of Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) issued the following pronouncements that have effective dates after June 30, 2009:

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 GASBS No. 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. 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.

GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. Statement 54 is to enhance the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. This Statement establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds.

The initial distinction that is made in reporting fund balance information is identifying amounts that are considered *nonspendable*, such as fund balance associated with inventories. This Statement also provides for additional classification as restricted, committed, assigned, and unassigned based on the relative strength of the constraints that control how specific amounts can be spent. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2010, with earlier application encouraged.

3. CASH AND INVESTMENTS

Cash in Banks

The Municipality's cash and investments at June 30, 2009 are composed of: (1) demand deposits in commercial banks, (2) demand deposits in the Government Development Bank of Puerto Rico (GDB, fiscal agent), and (3) cash equivalents in commercial banks. Cash equivalents of \$80.3 million are deposits in interest bearing commercial bank accounts and GDB, and are recorded at cost, which approximates fair value.

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or Puerto Rico's Government. 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 Government laws.

The Municipality follows the practice of pooling cash. At June 30, 2009, the pool cash account in interest bearing commercial banks accounts had a balance of \$54.5 million of which \$22.7 million in the General Fund, \$330,000 of Head Start Program, \$11.7 million in the Art Center Fund, \$6.6 million in the Multiuses Coliseum Fund, and \$13.2 in Other Governmental Funds of which \$1,563,632, \$20,171,324, \$2,259,990, and \$10,101,688 was invested in an interest bearing account in Popular Bank of Puerto Rico, Humacao Branch; Eurobank, Humacao Branch; Doral Bank, Humacao Branch, and First Bank, Humacao Branch that generates an annual interest rate of 0.30%, 2.99%, 3.00%, and 1.41%, respectively. Also, \$13,213,161 was invested in another account in Popular Bank of Puerto Rico, Trust Division, which generates an annual interest of 1.749%. The balance in the pooled cash account is available to meet current operating requirements and any unrestricted excess, if any, is generally invested in interest bearing accounts with commercial banks. Any deficiency in the pooled cash account is assumed by the general fund and covered through future budgetary appropriation.

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

Cash with fiscal agent in the debt service fund consists principally of property tax collections amounting to \$11.9 million that are restricted for the payment of the Municipality's debt service, as required by law. Cash with Fiscal Agent consist principally of \$10.6 million of unspent proceeds of bonds for the Multiuses Coliseum, \$235,150 for the Art Center, and \$2.9 million in other governmental funds that are restricted for the acquisition, construction or improvement of major capital assets. The amounts deposit in GDB is maintained in interest bearing accounts and is not collateralized.

The Municipality follows the provisions of GASBS No. 40, *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. Accordingly, the following is essential information about credit risk, interest rate risk, custodial credit risk, and foreign exchange exposure of deposits and investments of the Municipality at June 30, 2009:

Credit Risk

This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2009, the Municipality has invested only in cash equivalents of \$54.5 million consisting of deposit in interest bearing commercial bank accounts, which are insured by the FDIC, generally up to a maximum of \$100,000 (actually \$250,000 up to December 2009). As previously mentioned, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the FDIC coverage. No investments in debt of equity securities were made during the Fiscal Year ended June 30, 2009. Therefore, the Municipality's management has concluded that the credit risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2009.

3. CASH AND INVESTMENTS (continuation)

Interest Rate Risk

This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt or equity investments in its investments portfolio at June 30, 2009, (2) limiting the weighted average maturity of its investments in certificates of deposit to periods of three months or less, and (3) keeping most of its banks deposits in certificates of deposit and in interest bearing accounts generating interest at prevailing market rates. Therefore, at June 30, 2009, the interest risk associated with the Municipality's cash and cash equivalent is considered low.

Custodial Credit Risk

This 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 Government adopted by GDB, the Municipality may invest in obligations of the Government, obligations of the United States, certificates of deposit, commercial paper, banker's acceptance, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. At June 30, 2009, the Municipality has balances deposited in commercial banks amounting to \$54.5 million which are insured by the FDIC up to the established limit and the excess are fully collateralized as explained above. Deposits in GDB, amounting to \$25.8 million are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2009. It is management's policy to only maintain deposits in banks affiliated to FDIC to minimize the custodial credit risk, except for GDB. Therefore, the Municipality's management has concluded that at June 30, 2009, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

Foreign Exchange Risk

This is the risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, adopted by the Municipality, the Municipality is prevented from investing in foreign securities or any other types of investments for which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2009.

4. DEFERRED REVENUES

Governmental funds report *deferred revenue* 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	\$ -	\$ 13,885,816
Other Major Funds	5,307,609	-
Head Start Program	4,308,841	-
Total Deferred Unearned Revenue	<u>\$ 9,616,450</u>	<u>\$ 13,885,816</u>

5. OTHERS RECEIVABLES

As of June 30, 2009, the amount of \$42,207 corresponds to rent receivable from state agency and \$9,965 from owners of Section 8 Program.

6. INTERFUND RECEIVABLE, PAYABLES AND TRANSFERS

A. Interfund Receivable and Payable Balances

Due to/from Other Funds at June 30, 2009 are summarized as follows:

INTERFUND RECEIVABLE	INTERFUND PAYABLE	AMOUNT
General Fund	Head Start Fund	\$ 309,128
General Fund	Other Non-Major Funds	1,076,965
Other Non-Major Funds	General Fund	<u>170</u>
Total		<u>\$ 1,386,263</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	\$ 689,799	Bond Principal and Interest Payments
Multiuses Coliseum Fund	Debt Services Fund	36,364	Bond Issue Costs
Other Non-Major Fund	General Fund	457,460	Budget Specific Project Funding
General Fund	Other Non-Major Fund	4,790,223	Budget Specific Project Funding
General Fund	Multiuses Coliseum Fund	4,150,000	Budget Specific Project Funding
General Fund	Art Center Fund	<u>1,368,516</u>	Budget Specific Project Funding
	Total	<u>\$ 11,492,362</u>	

7. DUE FROM/TO GOVERNMENTAL UNITS

As of June 30, 2009, balance due from governmental units of the General Fund is a credit for overpayment to the State Insurance Fund Corporation (\$944) and Other Major Fund corresponded to reimbursement of Law 52 and Law 82 (\$90,288 and \$49,031, respectively), and Simonet Home (\$402) from state appropriation.

The balance due to governmental units of the General Fund for services rendered to the Municipality consists of AEELA (\$54,377), Puerto Rico Water and Sewer Authority (\$296,669) and General Service Administration (\$3,520). Amount due by Art Center Fund is to Authority for the financing of the Infrastructure of Puerto Rico (AFI) for the construction of the Humacao Performing Arts Center (\$2,766,843). Amount due by Other Non-Major Funds are to Municipality of San Juan (\$11,107) for HOPWA reimbursement in excess, and US Department of Housing and Urban Development (\$21,218) for reimbursement of Section 8 Rental Moderate Rehabilitation Programs.

8. CAPITAL ASSETS

Capital Assets activities for the fiscal year ended June 30, 2009 was as follows:

DESCRIPTION	BALANCE				BALANCE JUNE 30, 2009
	JULY 1, 2008	RECLASSIFICATION	INCREASE	DECREASE	
Non-Depreciable Capital Assets:					
Land	\$ 11,390,661	\$ -	\$ 204,030	\$ -	\$ 11,594,691
Construction in Progress	13,556,887	(658,946)	26,414,887	-	39,312,828
Total Non-Depreciable Capital Assets	24,947,548	(658,946)	26,618,917	-	50,907,519
Depreciable Capital Assets:					
Buildings	53,534,120	658,946	492,000	-	54,685,066
Infrastructure	22,003,775	-	-	-	22,003,775
Motor Vehicles	7,345,502	-	971,716	-	8,317,218
Equipment	4,622,814	-	619,838	(249,030)	4,993,622
Capital Lease	680,761	-	-	-	680,761
Total Depreciable Capital Assets	88,186,972	658,946	2,083,554	(249,030)	90,680,442
Less Accumulated Depreciation:					
Buildings	(15,362,772)	-	(1,055,085)	-	(16,417,857)
Infrastructure	(4,859,410)	-	(359,832)	-	(5,219,242)
Motor Vehicles	(5,594,144)	-	(472,803)	-	(6,066,947)
Equipment	(2,664,973)	-	(600,577)	165,674	(3,099,876)
Capital Lease	(509,923)	-	(101,406)	-	(611,329)
Total Accumulated Depreciation	(28,991,222)	-	(2,589,703)	165,674	(31,415,251)
Total Depreciable Capital Assets (Net)	59,195,750	658,946	(506,149)	(83,356)	59,265,191
CAPITAL ASSETS, NET	\$ 84,143,298	\$ -	\$ 26,112,768	\$ (83,356)	\$ 110,172,710

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

	AMOUNT
Mayor and Municipal Legislature	\$ 362,558
General Government	233,073
Public Safety	207,176
Public Works	802,808
Culture and Recreation	751,014
Human Service and Welfare	129,485
Urban Development	103,589
Total Depreciation Expenses	\$ 2,589,703

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).

During February 2009, the Municipality issued special obligation bonds of 2008 in the amount of \$10,040,000 for the construction of the Multiuses Coliseum. The principal and interest at 5.40% for the first installment, and 7.50% for the remaining installments are payable semi-annually ranging from \$955,000 to \$1,595,000 on the 1st days of January and July of each year through July 2016.

The following is a summary of general and special obligation bonds of the Municipality as of June 30, 2009:

Type of Obligation and Purpose	Maturity Date	Interest Rate	Amount
General Obligation Bonds - Property Taxes			
\$5,200,000, Series 2003-04 - General Construction	2028	5.00%	\$ 4,695,000
\$4,020,000, Series 2002-03 - General Construction	2027	5.00%	3,535,000
\$1,099,000, Series 1995 - Purchase of Equipment	2013	5.45%	470,000
\$1,485,000, Series 1995 - General Construction	2014	5.17%	780,000
\$8,395,000, Series 1998 - General Construction	2018	6.46%	5,630,000
\$1,720,000, Series 2005 - General Construction	2030	5.02%	1,615,000
\$370,000, Series 2006 - Land Acquisition	2030	5.02%	345,000
\$10,620,000, Series 2006 - General Construction	2031	5.525%	10,195,000
\$10,620,000, Series 2006 - General Construction	2031	5.525%	10,195,000
\$2,055,000, Series 2007 - Purchase of Equipment	2014	7.50%	1,820,000
Total General Obligations Bonds			39,280,000
Special Obligations Bonds - Property Taxes			
\$4,786,000, Series 1995 - Refinancing Purpose	2013	7.81%	2,045,000
\$904,120, Rural Development - General Construction	Undetermine ¹	Undetermine ¹	904,120
Total Special Obligations Bonds - Property Taxes			2,949,120
Special Obligations Bonds - General Revenues			
\$2,000,000, Series 1990 - Operational Purpose	2009	8.00%	26,316
Special Obligation Bonds - Sales and Usage Taxes			
\$10,040,000, Series 2008 - General Construction	2016	7.50%	10,040,000
Total Special Obligations Bonds			13,015,436
Total General and Special Obligations Bonds			\$ 52,295,436

¹ These terms will be determined by the loan grantor upon completion of the construction activities.

According to Sections 103 and 148 through 150 of the US Internal Revenue Code and Sections 1.148 through 1.150 of the US Treasury Regulation, the Municipality's tax-exempt bonds are subject to the arbitrage rebate requirements. At June 30, 2009, the Municipality had no federal arbitrage liability on bonds since interest income earned from the investment of unspent bond proceeds were made in bank deposits that generate yields lower than the rates applicable to the debt service payments.

9. GENERAL LONG-TERM DEBTS (continuation)

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, 2009, are as follows:

Cost	\$ 680,760
Accumulated Depreciation	\$ 611,329
Monthly Lease Payments	\$ 7,009
Residual Lease Payments	\$ -
YEAR ENDING	TOTAL
JUNE 30,	PAYMENT
2010	\$ 56,894
2011	13,680
Total Minimum Lease Payment	70,574
Less: Deferred Interest	705
Present Value Minimum Lease Payments	\$ 69,869

B. OTHER LONG-TERM DEBTS

Borrowing from MRCC

The total amount of \$284,976 to be paid during fiscal year 2009-2010 without interests corresponded to the Fiscal Year 2007-2008 final liquidation of property taxes.

The total amount of \$730,827 to be paid during fiscal year 2010-2011 without interests corresponded to the Fiscal Year 2008-2009 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%.

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.

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:

DESCRIPTION	BALANCE JULY 1, 2008	NEW ISSUES	RETIREMENTS AND ADJUSTMENTS	BALANCE JUNE 30, 2009	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER NEXT YEAR
Property Taxes-MRCC	\$ 284,976	\$ 730,827	\$ -	\$ 1,015,803	\$ 284,976	\$ 730,827
Law Number 146-MRCC	701,231	-	(29,218)	672,013	29,218	642,795
LIMS Debt-MRCC	766,575	-	(203,217)	563,358	215,487	347,871
Law Number 42-MRCC	455,208	-	(8,290)	446,918	8,810	438,108
Claims and Judgments	478,000	122,000	(600,000)	-	-	-
Employees Retirement Adm.	28,992	-	(14,496)	14,496	14,496	-
Unemployment	121,084	-	(121,084)	-	-	-
Compensated Absences	5,420,149	792,541	(432,528)	5,780,162	3,283,431	2,496,731
TOTAL	\$ 8,256,215	\$ 1,645,368	\$ (1,408,833)	\$ 8,492,750	\$ 3,836,418	\$ 4,656,332

C. CHANGES IN GENERAL LONG-TERM DEBTS

The following is a summary of changes in long-term debts for the year ended June 30, 2009:

DESCRIPTION	BALANCE JULY 1, 2008	NEW ISSUE	RETIREMENTS AND ADJUSTMENTS	BALANCE JUNE 30, 2009	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER NEXT YEAR
General Obligations	\$ 41,085,000	\$ -	\$ (1,805,000)	39,280,000	\$ 1,555,000	\$ 37,725,000
Special Obligations	3,174,975	10,265,725	(425,264)	13,015,436	1,331,316	11,684,120
Capital Lease	149,727	-	(79,858)	69,869	55,628	14,241
Other Debts	8,256,215	1,645,368	(1,408,833)	8,492,750	3,836,418	4,656,332
TOTAL	\$ 52,665,917	\$ 11,911,093	\$ (3,718,955)	\$ 60,858,055	\$ 6,778,362	\$ 54,079,693

9. GENERAL LONG-TERM DEBTS (continuation)

D. 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.

The annual requirements to amortize the general and special obligations outstanding as of June 30, 2009 are as follows:

YEAR ENDING JUNE 30,	General Obligation Bonds		Special Obligation Bonds & Note		Other Long-Term Obligations		TOTAL	
	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL	INTEREST
2010	\$ 1,555,000	\$ 2,271,690	\$ 1,386,944	\$ 381,695	\$ 3,836,418	\$ 99,679	\$ 6,778,362	\$ 2,753,064
2011	1,665,000	2,173,800	1,424,241	642,002	3,494,639	84,296	6,583,880	2,900,098
2012	1,790,000	1,998,310	1,515,000	562,125	158,543	68,093	3,463,543	2,628,528
2013	1,905,000	1,887,867	1,635,000	475,688	39,796	62,099	3,579,796	2,425,654
2014	2,035,000	1,769,199	1,760,000	382,688	40,460	59,617	3,835,460	2,211,504
2015-2019	9,290,000	7,150,127	4,460,000	517,874	213,829	259,297	13,963,829	7,927,298
2020-2024	7,205,000	4,866,641	-	-	237,957	189,734	7,442,957	5,056,375
2025-2029	9,270,000	2,552,470	-	-	270,681	111,577	9,540,681	2,664,047
2030-2032	4,565,000	418,862	-	-	200,426	25,285	4,765,426	444,147
Unmatured	-	-	904,120	-	-	-	904,120	-
TOTAL	\$ 39,280,000	\$ 25,088,966	\$ 13,085,305	\$ 2,962,072	\$ 8,492,749	\$ 959,677	\$ 60,858,054	\$ 29,010,715

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.

11. PROPERTY TAXES

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

The MRCC 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.

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 2009 resulted in a receivable of \$672,876 for the Debt Service Fund and a payable (long-term) in the General Fund [See Note 9 (C)].

The tax rate for fiscal year 2009 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.

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 \$3.0 million or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2009, the tax rates were as follows:

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

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, 2009. 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.

13. SALES AND USE TAXES

Municipality imposes a Sales and Use Taxes 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 Use Taxes, are required to file a monthly Sales and Usage Taxes Return Form, no later than the 10th of the following month from the month being reported.

Sales and Use Taxes receivable represents filed Sales and Use Taxes returns that were collected subsequent to June 30, 2009, 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.

14. CONSTRUCTION EXCISE TAXES

Municipality imposes and collects municipal construction excise taxes to most natural and legal persons and any governmental instrumentality that carry out activities related to construction, expansion, major repairs, relocations, alterations and other types of permanent improvements to residential, commercial and industrial buildings, and any structures within the territorial area of the Municipality. The tax is also applicable to infrastructure projects, the installation of machinery, equipment and fixtures, and other types of construction-related activities.

The construction excise tax generally is a self-assessed tax imposed over the cost of the project, net of certain exemptions such as the costs associated with the acquisition of land, existing buildings and improvements, project design and other engineering fees, licenses and permits, consulting and legal fees. The tax is paid by the taxpayer before the beginning of the construction project. The activities covers by this tax and the exemption granted are as follows:

- a. All construction of a single-family residential construction projects not related to housing development projects, condominiums, or any similar projects, with a total cost exceeding \$50,000, will pay 5% of construction excise taxes. This project is exempt of the construction excise taxes for the first \$50,000 of the project construction costs.
- b. All construction projects related to improvement to a single-family residential using as principal residence are exempt of the construction excise taxes for the first \$10,000 of the project construction costs. The swimming pool is not considered and improvement to a single-family residential, accordingly, is not exempt of the construction excise taxes.
- c. All construction projects carried out by philosophic and humanistic organization have full exemption to the construction excise taxes.
- d. All construction projects carried out by state, federal and municipal governments have full exemption to the construction excise taxes if such projects are performed by administration.

15. 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.

16. PENSION PLAN

Description of the Plan

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

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

Members who have attained at least 55 years of age and have completed at least 25 years of creditable service or members who have attained at least 58 years of age and have completed at least 10 years of creditable service are entitled to an annual benefit, payable monthly for life. The amount of the annuity shall be 1.5% of the average salary, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average salary, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

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

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

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

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

16. PENSION PLAN (continuation)

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

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

Funding Policy

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

Contribution requirements are established by law and are as follows:

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

Annual Contribution

Total employee contributions to the above-mentioned plans during the year ended June 30, 2009, 2008 and 2007 amounted to approximately \$2,367,778. The Municipality's contributions during those years are recognized as total pension expenditures/expenses in the category of administration as follow:

FISCAL YEAR	LAW NO. 447	SYSTEM 2000
2009	\$ 606,470	\$ 478,662
2008	601,395	369,282
2007	596,657	337,863

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

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

17. NONMONETARY TRANSACTION

SPECIAL ITEM

During the year, the Municipality recorded \$17,982,029 of construction costs for its Arts Center as a result of a capital contribution received from the Puerto Rico Authority for the Financing of Infrastructure (AFI) where AFI incurred and paid such costs for the Municipality. The construction costs are recorded as an increase to construction in progress under its capital assets in the Government-Wide Statement of Net Assets and as a capital outlay in the Statement of Revenues, Expenditures, and Changes in Fund Balance – Governmental Funds. Of this amount, \$2,766,843 was incurred by AFI in excess of the original capital contribution agreement, resulting in a liability for the Municipality to cover such excess. The \$15,215,186 capital contribution is recorded as a special item in the Government-Wide Statement of Activities and in the Statement of Revenues, Expenditures, and Changes in Fund Balance – Governmental Funds.

18. 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 San Juan Office of Community Planning and Development of the U.S. Department of Housing and Urban Development require the Municipality to repay to the Community Development Block Grant the amount of \$396,669 of questioned costs for excessive costs and ineligible operating expenditures. This amount was paid by the Municipality on August 27, 2009.

19. COMMITMENTS

A. Operating Leases

The Municipality leases real property, buildings, and equipment under various operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same term. Rental expenditures/expenses recorded in the general fund and in other governmental funds for the year ended June 30, 2009, amounted to approximately \$245,000. Management believes that the summary of the future minimum rental commitments under noncancelable real property and equipment lease with terms exceeding one year is not material to the basic financial statements taken as a whole.

B. Construction

The Municipality had commitments at June 30, 2009 of approximately \$29.2 million for the construction, improvements, or renovation of several municipal facilities.

C. Other Commitments

At June 30, 2009, the nonmajor miscellaneous special revenue funds had a deficit of \$124,445 which will be covered with future budgetary appropriations of the general fund, if necessary.

20. NET ASSETS/FUND BALANCES RESTATEMENTS

A. Net Assets Restatements

During the year, the Municipality adjusted the governmental net assets for unrecognized revenues. The following schedule reconciles the June 30, 2008 Net Assets, as previously reported to Beginning Net Assets, as restated, for Governmental Activities.

	NET ASSETS
Net Assets, as Previously Reported, June 30, 2008	\$ 102,333,314
Cancelation of prior year accounts payable	417,650
Adjustments to Revenues not recognized Head Start	92,172
Adjustments to Revenues not recognized Early Head Start	53,645
Adjustments to Revenues recognized prior year as Other Governmental Funds	(131,343)
Adjustment to Capital Assets	-
Beginning Net Assets, as Restated	<u>\$ 102,765,438</u>

B. Fund Balances Restatements

The following reconciles the June 30, 2009 Fund Balance, as previously reported to Beginning Fund Balance, as restated, for the various funds:

	GENERAL FUND	ART CENTER FUND	MULTIUSES COLISEUM FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS
Fund Balance, as Previously Reported, June 30, 2008	\$ 14,926,770	\$ 11,216,830	\$ -	\$ 8,070,553	\$ 22,455,479
Transfer of Multiuses Coliseum Fund Balance	-	-	6,492,731	-	(6,492,731)
Transfer of Cash for Sales and Usage Taxes	(557,293)	-	-	557,293	-
Transfer of Fund Balance related to Art Center	-	352,918	-	-	(352,918)
Cancelation of Prior Year Accounts Payable	-	-	-	-	301,982
Cancelation of Prior Year Accounts Payable for FTA Fund	-	-	-	-	115,668
Beginning Net Assets, as Restated	<u>\$ 14,369,477</u>	<u>\$ 11,569,748</u>	<u>\$ 6,492,731</u>	<u>\$ 8,627,846</u>	<u>\$ 16,027,480</u>

END OF NOTES

MUNICIPALITY OF HUMACAO, PUERTO RICO

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED JUNE 30, 2009

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF HUMACAO, PUERTO RICO
REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	Budget Amounts		Actual Amounts (Budgetary Basis) (See Note A)	Variance with Final Budget
	Original	Final		
BUDGETARY FUND BALANCE, JULY 1, 2008	\$ 10,611,933	\$ 10,611,933	\$ 10,611,933	\$ -
Resources (Inflows):				
Property Taxes	13,510,579	13,510,579	13,510,579	-
Volume of Business Taxes	14,545,000	14,545,000	19,484,497	4,939,497
Sales Taxes	3,810,000	3,810,000	4,158,184	348,184
Intergovernmental Revenues	4,402,601	4,402,601	4,535,341	132,740
License and Permits	4,270,000	4,270,000	1,973,471	(2,296,529)
Charges for Services	700,000	700,000	872,719	172,719
Interest	1,500,000	1,500,000	1,191,985	(308,015)
Miscellaneous	236,330	236,330	466,385	230,055
Total Resources (Inflows)	42,974,510	42,974,510	46,193,161	3,218,651
Amounts Available for Appropriation	53,586,443	53,586,443	56,805,094	3,218,651
Charges to Appropriations (Outflows):				
Mayor and Municipal Legislature	2,244,632	2,403,607	2,601,990	(198,383)
General Government	19,989,000	21,234,511	20,130,456	1,104,055
Public Safety	3,216,022	2,781,391	2,596,452	184,939
Public Works	3,349,888	3,179,363	3,407,894	(228,531)
Culture and Recreation	1,809,020	2,110,089	1,878,202	231,887
Health and Sanitation	1,812,605	1,792,605	1,715,105	77,500
Solid Waste Disposal	3,000,000	3,294,132	3,543,512	(249,380)
Human Services and Welfare	5,189,788	5,156,809	4,706,125	450,684
Urban Development	1,263,929	1,224,577	1,133,744	90,833
Capital Outlays	614,000	565,017	561,475	3,542
Transfers to Other Funds	485,626	485,627	10,998,538	(10,512,911)
Total Charges to Appropriations	42,974,510	44,227,728	53,273,493	(9,045,765)
BUDGETARY FUND BALANCE, JUNE 30, 2009	\$ 10,611,933	\$ 9,358,715	\$ 3,531,601	\$ (5,827,114)

See accompanying Notes to Required Supplementary Information.

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, 2009

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

	<u>General Fund</u>
Sources/Inflows of Resources:	
Actual Amounts (Budgetary Basis) "Available for Appropriation" from the Budgetary Comparison Schedule (See Page 51)	\$ 56,805,094
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	<u>(10,611,933)</u>
Total Revenues as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 21)	<u>\$ 46,193,161</u>
Uses/Outflows of Resources:	
Actual Amounts (Budgetary Basis) "Total Charges to Appropriation" from the Budgetary Comparison Schedule (See Page 51)	\$ 53,273,493
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	(594,668)
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	<u>(10,998,538)</u>
Total Expenditures as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 21)	<u>\$ 41,680,287</u>

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

Budgetary Fund Balance, June 30, 2009	\$ 3,531,601
Timing Differences:	
Non-Budgetary Items	3,277,819
Change in Encumbrances	<u>937,185</u>
Unrestricted Fund Balance, June 30, 2009	<u>\$ 7,746,605</u>

END OF THIS SECTION