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JUAN RIVERA, CPA
Certified Public Accountant

Ave. Del Valle Levittown, P.R. 00949

T. 787-784-2255 / F. 787-784-2250 / jrmelecio@hotmail.com

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO

Independent Auditors' Report

Financial Statements and
Supplemental Schedules

Year Ended June 30, 2011

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO

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JUAN A. RIVERA, CPA
CERTIFIED PUBLIC ACCOUNTANT

Phone: 787-784-2255
Fax: 787-784-2250
Email: jrmelecio@hotmail.com

URB LEVITTOWN, 1818 DEL VALLE AVE, TOA BAJA, PR 00949

Independent Auditors' Report

The Honorable Mayor, Members of the
Municipal Legislature and People of
the Municipality of Maricao
Maricao, Puerto Rico

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

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

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 Maricao of the Commonwealth of Puerto Rico, as of June 30, 2011, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Audit Standards*, we have also issued our report dated December 13, 2011 on our consideration of the Government's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreement and other matters. The purpose of that report is to describe the scope of our testing of internal control over a financial reporting and compliance and the results of that testing, and not to provide and opinion on the internal control over financial reporting compliance. That report is an integral part of an audit performed in accordance with *Government Audit Standards* and should be considered in assessing the results of our audit.

The *Management's Discussion and Analysis* and the *Budgetary Comparison Schedule* on page 3 through 10 and 47 through 48 are not required parts 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Maricao of the Commonwealth of Puerto Rico basic financial statements. The introductory section, combining and individual non-major fund financial statements, and statistical section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of the Municipality of Maricao of the Commonwealth of Puerto Rico, the combining and individual non-major fund financial statements and the schedule of expenditures of federal awards have been subjected to the auditing procedure applied in the audit of the basic financial statements and in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and accordingly we express no opinion on them.


Juan Rivera, CPA
License 2214

December 13, 2011
Toa Baja, Puerto Rico



Stamp No. 2633853 of the Puerto Rico Society of Certified Public Accountants were affixed to the record copy of this report.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

Management of the Municipality of Maricao of the Commonwealth of Puerto Rico (the "Municipality") provides this *Management's Discussion and Analysis* of the Municipality's basic financial statements as an overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2011. We encourage readers to consider the information presented here in conjunction with the additional information that we have furnished in the accompanying basic financial statements.

During fiscal year ended June 30, 2003, the Municipality implemented the new required financial reporting standards established by Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, issued by the Governmental Accounting Standards Board (commonly known as "GASB 34"). According to this statement, significant required changes in content and structure have been made in the accompanying Municipality's basic financial statements as of and for the fiscal year ended June 30, 2011, which make the accompanying basic financial statements not easily comparable to the Municipality's general purpose financial statements issued in years prior to 2003. However, the comparison of years after the adoption of GASB 34 will be more meaningful and will go further in explaining the Municipality's financial position and results of operations.

This Management's Discussion and Analysis (MD&A) is prepared as a result of the requirements of GASB 34, and it has been designed accordingly with the following goals:

- a) Assist the reader in focusing on significant financial issues,
- b) Provide an overview of the Municipality's financial activity,
- c) Identify changes in the Municipality's financial position (its ability to address the next and subsequent year challenges),
- d) Identify any material deviations from the financial plan (the approved budget), and;
- e) Identify individual fund issues or concerns.

Since the MD&A is designed to focus on the current year activities, resulting changes and currently known facts, please read it in conjunction with the accompanying basic financial statements.

FINANCIAL HIGHLIGHTS

- The Municipality net assets increased by \$3,432,314.
- In the Governmental financial statements, general fund balances increased by \$2,341,991.
- Capital expenditures amounted to \$3,160,167

USING THIS ANNUAL REPORT

This annual report consists of a series of new financial statements with a change in the focus from the previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The Municipality's financial statements include three components: (1) the Government-Wide Financial Statements, (2) the Fund Financial Statements, and (3) the Notes to the Financial Statements (collectively known as the "basic financial statements"). This report also contains additional required supplementary information (budgetary schedule) in addition to the basic financial statements themselves. These components are described below:

Government-Wide Financial Statements

The *government-wide financial statements* are designed to provide readers with a broad overview of the Municipality's operations and finance as a whole in a manner similar to private-sector business. These statements provide short-term and long-term information about the Municipality's financial position, which assist the Municipality's management to determine the economic condition at the end of the fiscal year. These financial statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means that these financial statements follow methods that are similar to those used by most businesses. They take into account all revenues and expenses connected with the fiscal year ended June 30, 2011, even if cash involved have not been received or paid. The government-wide financial statements include: (1) the statements of net assets and (2) the statement of activities.

Statement of Net Assets

The statement of net assets presents all of the Municipality's assets and liabilities, with the difference between these two items reported as "net assets" (equity). Over time, increases or decreases in the net assets may serve as a useful indicator of whether the financial position of the Municipality is either improving or deteriorating.

Statement of Activities

The statement of activities presents information showing how the Municipality's net assets changed during the fiscal year ended June 30, 2011. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as uncollected taxes and earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenues for each function of the Municipality.

Both of the abovementioned financial statements present all the governmental activities of the Municipality, which consist mostly of taxes and intergovernmental revenues (such as federal grants). Most services provided by the Municipality fall into this category, including culture and education, general government, health and sanitation, public safety, public housing and welfare, etc.

Fund Financial Statements

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011

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

The fund financial statements focus on: (1) individual parts of the Municipality's government and (2) reporting the Municipality's operations in more detail than the government-wide financial statements. For financial reporting purposes, the Municipality classifies its funds within the following fund categories: (1) general fund, (2) debt service fund, (3) special revenue funds and (4) capital projects funds (collectively known as the "governmental funds").

Governmental funds are used to account for all of the services provided by the Municipality. Governmental funds are used to account for essentially the same functions reported as governmental activities in the governmental-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of expendable resources. They also focus on the balances of expendable resources available at the end of the fiscal year (June 30, 2011). This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the Municipality's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the Municipality, that is, evaluating the Municipality's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the fund information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Municipality's near-term financial decisions. For financial reporting purposes the Municipality has five major funds: (1) the general fund, (2) the debt service fund, (3) the \$3,860,000 Loan fund, (4) the \$3725,000 Loan fund, and, (5) the FEMA (*Lluvias de Octubre 2010*) fund.

Notes to the Basic Financial Statements

The notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and the fund financial statements. The notes to the basic financial statements can be found immediately following the basic financial statements.

Required Supplementary Information

The basic financial statements are followed by a section of required supplementary information consisting of a budgetary comparison between actual operating results with the original budget and the final amended budget for the general fund.

INFRASTRUCTURE ASSETS

Historically, a government's largest group of assets (infrastructure – roads, bridges, traffic signals, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011

governmental financial statements. GASB 34 requires that these assets be valued and reported within the governmental column of the Government-Wide Financial Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (modified approach), which periodically (at least every third year), by category, measures and demonstrates its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statement users in evaluating a local government and its performance over time.

As of July 1, 2003, the Municipality retroactively recorded the historical costs of infrastructure assets. Also the Municipality elected to depreciate infrastructure assets instead of using the modified approach.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

As noted earlier, net assets may serve over time as a useful indicator of the Municipality's financial position. In the case of the Municipality, net assets (excess of assets over liabilities) amounted to \$5,549,696 at June 30, 2011.

The largest portions of the Municipality's net assets are invested in capital assets net of their related debt \$10,045,302. The Municipality's net assets are also composed of net assets amounting to \$5,459,375 that are restricted for (1) future debt service payments and (2) the future acquisition or construction of capital assets. In addition, the Municipality's net assets (deficit) are reported net of an unrestricted net asset (deficit) of \$(9,954,981).

The unrestricted deficit is the consequence of previous budgets, which did not provide funding for incurred long-term obligations such as compensated absences and others. Historically, such obligations have been budgeted on a pay as you go basis without providing funding for their future liquidation. Consequently, the Municipality cannot draw from its existing assets to provide services to its citizens and depends on its taxing ability to continue its operations.

The portion of the Municipality's net assets invested in capital assets such as land, buildings, equipment, etc., less any outstanding related debt used to acquire those assets, are used by the Municipality to provide services to its citizens; consequently these assets are not available for future spending. Although the Municipality's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from the debt service fund, since the capital assets themselves cannot be used to liquidate these liabilities.

The following is a condensed presentation of the Municipality's financial position, as reported in the government-wide financial statements:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

Condensed Statement of Activities:

| | | |
|--|---------------------|---------------------|
| General revenues: | 2011 | 2010 |
| Property taxes | 620,614 | 490,292 |
| Municipal sales tax | 1,336,267 | 1,264,997 |
| Municipal license tax and excise tax | 403,499 | 379,876 |
| Grants and contributions restricted to specific purposes | 7,762,887 | 5,781,709 |
| Interest, fine and penalties | 171,009 | 49,087 |
| Miscellaneous | 79,510 | 433,851 |
| Total revenues | <u>10,373,786</u> | <u>8,399,812</u> |
| Expenses: | | |
| General government | 2,320,050 | 2,775,334 |
| Public safety | 2,347,809 | 3,256,363 |
| Culture | 336,214 | 292,092 |
| Health | 350,861 | 349,899 |
| Public housing and welfare | 377,066 | 303,379 |
| Urban economic development | 602,146 | 349,820 |
| Payment principal | 380,000 | 255,000 |
| Interest on long term debt | 227,326 | 91,667 |
| Total expenses | <u>\$ 6,941,472</u> | <u>\$ 7,673,554</u> |
| Change in net assets | \$ 3,432,314 | \$ 726,258 |
| Net assets-at beginning of year | 1,549,861 | 823,603 |
| Net assets-at beginning of year - Adjustment | 567,521 | |
| Net assets-at end of year | <u>\$ 5,549,696</u> | <u>\$ 1,549,861</u> |

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S GOVERNMENTAL FUNDS

As discussed earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds - The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balance of expendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of fiscal year.

The following is a condensed presentation of the Municipality's balance sheet and results of operations of governmental funds:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

| <u>Condensed Balance Sheet - Governmental funds:</u> | <u>Amount</u> |
|--|-----------------------------|
| Total Assets - Major Funds | \$ 4,553,434 |
| Total Assets - Other Funds | <u>3,043,061</u> |
| Total assets | <u>7,596,495</u> |
| Total Liabilities - Major Funds | 3,587,200 |
| Total Liabilities - Other Funds | <u>64,634</u> |
| Total liabilities | <u>3,651,834</u> |
| Fund Balances - Restricted - Major Funds | 2,778,340 |
| Fund Balances - Restricted - Other Funds | - |
| Fund Balances - Committed - Major Funds | - |
| Fund Balances - Committed - Other Funds | 2,978,427 |
| Fund Balances - Unassigned - Major funds | (1,812,106) |
| Fund Balances - Unassigned - Other funds | <u> </u> |
| Total net assets | <u>\$ 3,944,661</u> |

| <u>Condensed Statement of Operations - Governmental funds:</u> | |
|--|---------------------|
| Total Revenues - Major Funds | \$ 6,451,169 |
| Total Revenues - Other Funds | <u>3,861,994</u> |
| Total revenues | <u>10,313,163</u> |
| Total expenditures - Major Funds | 8,555,962 |
| Total expenditures - Other Funds | <u>4,300,210</u> |
| Total expenditures | <u>12,856,172</u> |
| Revenues Over Expenses - Major | (2,104,793) |
| Revenues Over Expenses - Nonmajor | <u>(438,216)</u> |
| Total Revenues Over Expenses - Nonmajor | <u>(2,543,009)</u> |
| Other financing sources - Major Funds | 3,712,245 |
| Other financing sources - Other Funds | <u>1,172,755</u> |
| Total Other financing resources | <u>4,885,000</u> |
| Revenues and other financing sources over expenses - Major | 2,341,991 |
| Beginning Fund balance | 1,035,147 |
| Prior year adjustment | <u>567,523</u> |
| Ending Fund balance | <u>\$ 3,944,661</u> |

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

GENERAL FUND BUDGETARY HIGHLIGHTS

The accompanying Budgetary Comparison Schedule shows a total negative variance between budgeted revenues and actual revenue results of \$1,067,593.

In addition, the accompanying Budgetary Comparison Schedule shows a total negative variance between budgeted expenditures and actual expenditures results of \$921,219.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The accompanying statement of net assets reported total gross capital assets, at cost, amounting to \$22,506,196 of which \$8,738,581 represents building structure assets at June 30, 2011. The related accumulated depreciation and amortization of capital assets amounted to \$5,819,994, of which \$1,878,297 is related to building, structure and building improvements assets at June 30, 2011. This investment in capital assets includes land, buildings, improvements, equipment, infrastructure and construction in progress. Infrastructure assets are items that are normally immovable and of value only to the municipal government, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

Actual costs incurred to purchase or construct capital assets were \$3,160,167 for the year ended June 30, 2011. Depreciation and amortization charges for the year totaled \$404,086.

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

Debt Administration

The laws and regulations of the Commonwealth of Puerto Rico have established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged.

The applicable laws and regulations also require that in order for a municipality to be able to issue additional general obligation bonds and notes, such municipality must have sufficient "payment capacity". Act No. 64 provides that a municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Redemption fund and the annual amounts collected with respect to such municipality's Special Additional Tax (as defined below), as projected by the Government Development Bank for Puerto Rico, will be sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

The Municipality is required under applicable laws and regulations to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2011**

Debt Administration (cont)

obligation municipal bonds and notes to the extent that the Special Additional Tax Levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

ECONOMIC FACTORS, NEXT BUDGETS AND RATES

The Municipality relies primarily on property and municipal license taxes, as well as, federal and state grants to carry out the governmental activities. Historically, property and municipal license taxes have been very predictable with increases not generally exceeding ten percent. Federal grant revenues may vary if new grants are available but the revenue is also very predictable.

Those factors were considered when preparing the Municipality's budget for the 2009-2011 fiscal years. There were no significant changes between the budget for fiscal year 2009-2010 and the one for fiscal year 2010-2011.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayers, customers, investors and creditors) with a general overview of the Municipality's finances and demonstrate the Municipality's' accountability. If you have any questions about the report or need additional financial information, contact the Municipality's Director of Finance, Mr. Modesto Ayala Quiñones at P.O. Box 837, Maricao, Puerto Rico, 00606-0837.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Statement of Net Assets
June 30, 2011

ASSETS

Current Assets:

| | | | |
|---|----|-----------|------------------|
| Cash and cash equivalents (notes 1g and 3) | | | |
| Receivables, net of allowance for doubtful accounts | | | |
| Taxes: | | | |
| Property taxes | \$ | 72,836 | |
| Sales and use tax | | 1,042 | |
| Municipal license taxes | | | |
| Intergovernmental grants and contributions | | | |
| Accrued interest on deposits | | 61 | |
| Other receivables (Federal financial assistance) | | 603,667 | |
| Total receivables | | | 677,606 |
| Restricted assets: | | | |
| Cash in commercial banks | | 1,027,662 | |
| Cash in fiscal agent | | 4,269,732 | |
| Property tax receivable | | | |
| Total restricted assets | | | 5,297,394 |
| Other current assets | | | <u>5,975,000</u> |
| Total current assets | | | <u>5,975,000</u> |

Noncurrent Assets:

| | | | |
|---|--|--------------------|----------------------|
| Capital assets | | | |
| Depreciable capital assets | | 15,200,215 | |
| Non-depreciable capital assets | | <u>7,305,981</u> | |
| Total capital assets | | 22,506,196 | |
| Less: accumulated depreciation and amortization | | <u>(5,819,994)</u> | |
| Capital assets, net of accumulated depreciation | | | 16,686,202 |
| Deferred charges, net of amortization | | | <u>16,686,202</u> |
| Total noncurrent assets | | | <u>16,686,202</u> |
| Total assets | | | <u>\$ 22,661,202</u> |

LIABILITIES

Current liabilities:

| | | | |
|---|--|----------------|------------------|
| Accounts payable and other accrued liabilities (notes 1h) | | 303,962 | |
| Outstanding check s over bank balance | | 66,060 | |
| Intergovernmental (note 1h and 8) | | 581,343 | |
| Accrued interest on bonds and notes payable | | <u>164,288</u> | |
| Total accounts payable | | | 1,115,653 |
| Unearned revenues | | | 595,308 |
| Current portion of long term obligations | | | |
| Bonds payable | | 380,000 | |
| Notes Payable | | 7,465 | |
| Compensated absences | | 361,488 | |
| Obligation under capital leases | | - | |
| Total current portion of long term obligations | | | <u>748,953</u> |
| Total current liabilities | | | <u>2,459,914</u> |

Noncurrent liabilities:

| | | | |
|------------------------------|--|------------|-------------------|
| Bonds payable | | 10,745,900 | |
| Notes Payable | | 3,319,030 | |
| Compensated absences | | 586,662 | |
| Total noncurrent liabilities | | | <u>14,651,592</u> |
| Total liabilities | | | <u>17,111,506</u> |

NET ASSETS (DEFICIT)

| | | | |
|---|--|-----------|----------------------|
| Invested in capital assets, net of related debt | | | <u>10,045,302</u> |
| Restricted for (1j): | | | |
| Debt service | | 1,046,075 | |
| Capital projects | | 4,413,300 | |
| Total restricted net assets | | | <u>5,459,375</u> |
| Unrestricted net deficit | | | <u>(9,954,981)</u> |
| Total net assets | | | <u>5,549,696</u> |
| Total liabilities and net assets | | | <u>\$ 22,661,202</u> |

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Statement of Activities
Year Ended June 30, 2011

| Functions/Programs | Expenditures | Charges for services | Program Revenues | | Net Expenses and Changes in Net Assets |
|--------------------------------------|---------------------|----------------------|------------------------------------|----------------------------------|--|
| | | | Operating Grants and Contributions | Capital Grants and Contributions | |
| Governmental activities: | | | | | |
| General government | \$ 2,700,050 | - | - | - | \$ (2,700,050) |
| Public Work | 2,347,809 | - | - | 1,661,441.00 | (686,368) |
| Health & Sanitation | 350,213 | - | - | - | (350,213) |
| Public safety | 602,146 | - | - | - | (602,146) |
| Education | 648 | - | - | - | (648) |
| Public housing and welfare | 377,066 | - | 332,360 | - | (44,706) |
| Culture, recreation and education | 336,214 | - | - | - | (336,214) |
| Interest on long term obligations | 227,326 | - | - | - | (227,326) |
| Total governmental activities | \$ 6,941,472 | \$ - | \$ 332,360 | \$ 1,661,441 | \$ (4,947,671) |

General revenues:

Taxes:

| | |
|--|---------------------|
| Property taxes (note 5) | 620,614 |
| Municipal Sales Tax | 1,336,267 |
| Municipal license taxes (note 4) | 403,499 |
| Total taxes | 2,360,380 |
| Intergovernmental contributions and reimbursements | 5,175,178 |
| Other revenues | 844,427 |
| Total general revenues | 8,379,985 |
| Net change in net assets | 3,432,314 |
| Other Financial source | |
| Net assets-beginning of fiscal year | 1,549,861 |
| Prior Year adjustment | 567,521 |
| Net assets-beginning of fiscal year, as restated | 2,117,382 |
| Net assets-end of fiscal year | \$ 5,549,696 |

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Balance Sheet
Governmental Funds
June 30, 2011

| | Major Funds | | | | | | Total Governmental Funds |
|--|-----------------------|---------------------|-------------------------|---------------------|--------------------------------|--------------------------------|--------------------------------|
| | General Fund | Debt | | | Other Governmental Funds | Total Governmental Funds | |
| | | Service Fund | Lluvias Octubre 2010 | \$3,860,000 Loan | \$3,725,000 Loan | | |
| ASSETS | | | | | | | |
| Unrestricted cash and cash equivalents | | | | | | \$ 1,027,662 | \$ 1,027,662 |
| Cash with fiscal agent | | \$ 1,589,782 | | | | | 1,589,782 |
| Receivables, net of allow. for doubt. acnts: | | | | | | | - |
| Taxes | | | | | | | - |
| Property taxes | 72,836 | | | | | | 72,836 |
| Municipal Sales Tax | 521 | 521 | | | | | 1,042 |
| Municipal license tax | - | - | | | | | - |
| Interest Receivable | | 61 | | | | | 61 |
| Due from other funds | 8,101 | | | | | 1,674,015 | 1,682,116 |
| Due from governmental entities | 543,045 | | | | | | 543,045 |
| Due from Federal Financial Assistance | | | | | | | - |
| Prepaid Expenses | | | | | | | - |
| Other | | | | | | | - |
| Temporarily restricted cash and cash equivalents | - | - | 561,721 | 1,732,128 | 44,718 | 341,384 | 2,679,951 |
| Total assets | <u>624,503</u> | <u>1,590,364</u> | <u>561,721</u> | <u>1,732,128</u> | <u>44,718</u> | <u>3,043,061</u> | <u>7,596,495</u> |
| LIABILITIES | | | | | | | |
| Bank Overdraft | 66,060 | | | | | | 66,060 |
| Account payable and accrued expenses | 138,137 | | | | 44,582 | | 182,719 |
| Mature bonds due and payable | | 380,000 | | | | | 380,000 |
| Due to other governmental entities | 581,343 | | | | | | 581,343 |
| Due to other funds | 1,627,265 | | | | | 54,851 | 1,682,116 |
| Interest Payable | | 164,288 | | | | | 164,288 |
| Deferred Volume of Business Tax | 23,804 | | | | | | 23,804 |
| Deferred federal fin. assist. revenue | | | 561,721 | | | 9,783 | 571,504 |
| Deferred intergovernmental revenue | | | | | | | - |
| Total Liabilities | <u>2,436,609</u> | <u>544,288</u> | <u>561,721</u> | <u>-</u> | <u>44,582</u> | <u>64,634</u> | <u>3,651,834</u> |
| FUND BALANCES | | | | | | | |
| Non expendable | | | | | | | |
| Restricted | | 1,046,076 | - | 1,732,128 | 136 | | 2,778,340 |
| Committed | | | | | | 2,978,427 | 2,978,427 |
| Assigned | | | | | | | - |
| Unassigned | (1,812,106) | | | | | | (1,812,106) |
| Total fund balances | <u>\$ (1,812,106)</u> | <u>\$ 1,046,076</u> | <u>\$ -</u> | <u>\$ 1,732,128</u> | <u>\$ 136</u> | <u>\$ 2,978,427</u> | <u>\$ 3,944,661</u> |
| Total liabilities and fund balances | <u>\$ 624,503</u> | <u>\$ 1,590,364</u> | <u>\$ 561,721</u> | <u>\$ 1,732,128</u> | <u>\$ 44,718</u> | <u>\$ 3,043,061</u> | <u>\$ 7,596,495</u> |

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Revenues, Expenditures and Changes in Fund Balance
Governmental Funds
Year Ended June 30, 2011

| | Major Funds | | | | | Other Governmental Funds | Total Governmental Funds |
|--|--------------------|-------------------------|-------------------------|---------------------|-------------------------|--------------------------------|--------------------------------|
| | General Fund | Debt Service Fund | Lluvias Octubre 2010 | \$3,860,000 Loan | \$ 3,725,000.00 Loan | | |
| REVENUES: | | | | | | | |
| Taxes: | | | | | | | |
| Property Taxes | \$469,579 | \$ 151,035 | | | | | \$ 620,614 |
| Municipal Sales Tax | 354,236 | 982,031 | | | | | 1,336,267 |
| Volume of Business Tax | 173,632 | | | | | | 173,632 |
| License, permit and fines | 229,867 | | | | | | 229,867 |
| Intergovernmental Revenues | 3,942,368 | | | | | \$ 1,172,188 | 5,114,556 |
| Charges of Service | | | | | | | 0 |
| Federal Financial Assistance | | | | | | 2,587,709 | 2,587,709 |
| Interest | 96,982 | 1,160 | | \$ 29,661 | \$ 15,433 | 27,773 | 171,009 |
| Miscellaneous | 5,186 | | | | | 74,324 | 79,510 |
| Total revenues | \$5,271,850 | \$1,134,226 | \$0 | \$29,661 | \$15,433 | \$3,861,994 | \$10,313,163 |
| EXPENDITURES: | | | | | | | |
| Current: | | | | | | | |
| General Administration | 4,016,389 | | | 29,660 | 15,000 | 982,704 | 5,043,753 |
| Public Works | 2,302,583 | | | | 44,446 | 780 | 2,347,809 |
| Public Safety | 368,961 | | | | | 237,727 | 606,688 |
| Education | | | | | | | - |
| Health | 350,288 | | | | | (75) | 350,213 |
| Environmental Control | | | | | | 648 | 648 |
| Culture and recreation | 219,639 | | | | | 116,575 | 336,214 |
| Public Housing and welfare | 52,149 | | | | | 351,205 | 403,354 |
| Debt Service: | | | | | | | 380,000 |
| Principal (notes 1r and 10) | | 380,000 | | | | | 380,000 |
| Interest on bonds and notes (note 10) | | 222,001 | | | | 5,325 | 227,326 |
| Capital Outlays | | | | | | 2,605,321 | 3,160,167 |
| Total expenditures | 7,310,009 | 602,001 | - | 495,213 | 148,739 | 4,300,210 | 12,856,172 |
| Revenue over (under) expenditures | (2,038,159) | 532,225 | - | (465,552) | (133,306) | (438,216) | (2,543,009) |
| OTHER FINANCING SOURCES (USES): | | | | | | | |
| Proceeds from bond issued | | | | | \$3,725,000 | 1,160,000 | 4,885,000 |
| Operating transfer -in from other funds (note 6) | 4,091,558 | (500,000) | - | - | (3,591,558) | | - |
| Operating transfer-out to other funds (note 6) | (12,755) | | - | - | | 12,755 | - |
| Total other financing sources (uses) | 4,078,803 | (500,000) | - | - | 133,442 | 1,172,755 | 4,885,000 |
| EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER (USES) | | | | | | | |
| | 2,040,644 | 32,225 | - | (465,552) | 136 | 734,539 | 2,341,991 |
| FUND BALANCES AT BEGINNING OF YEAR | | | | | | | |
| | (3,852,750) | 1,013,850 | - | 1,630,158 | - | 2,243,889 | 1,035,147 |
| PRIOR YEAR ADJUSTMENT | | | | | | | |
| | | | | 567,523 | | | 567,523 |
| FUND BALANCES AT END OF YEAR | | | | | | | |
| | \$ (1,812,106) | \$ 1,046,075 | \$ - | \$ 1,732,129 | \$ 136 | \$ 2,978,428 | \$ 3,944,661 |

Official
3/24/2011

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Reconciliation of Statement of Revenues,
Expenditures and Changes in Fund Balances
Governmental Funds to the Statement of Activities
Year Ended June 30, 2011**

Amounts reported for governmental activities in the accompanying statement are different because:

| | |
|---|---------------------|
| Net change in fund balances as reported in the accompanying statement of revenues, expenditures and changes in fund balances - governmental funds | \$ 2,341,991 |
| Add (deduct) | |
| Compensated absence | (7,484) |
| Proceed long term obligation recognized as other Financial resource in governmental fund an L.T.D. in Statement of Net Assets | (4,171,095) |
| Governmental funds report capital outlays as expenditures. However in the statement of activities, the cost of those assets is allocated over their estimated usefull lives as depreciation and amortization expenses. This the amount by which capital outlays | 2,756,081 |
| Some revenues reported in the statements of activities not available for current expenditures, therefore are not reported as revenue in the governmental funds. | 60,622 |
| Some expenses reported in the statements of activities do not require the use of currents financial resources, therefore are not reported as expenditures in the governmental funds.(Resultas and other) | 2,452,199 |
| Net change in net assets as reported in the accompanying statement of activities | <u>\$ 3,432,314</u> |

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

1. GOVERNMENTAL ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Government Background Information

The Municipality of Maricao of the Commonwealth of Puerto Rico (the "Municipality") is a local government constituted in 1874 with full legislative, fiscal and administrative powers to operate as a government. The Municipality assumes responsibility for public safety, health and sanitation, public housing and welfare, culture and education, urban and development and many other general and administrative duties.

The laws and regulations of the Commonwealth of Puerto Rico (the "Commonwealth") provide for separation of powers of the executive, legislative and judicial branches of the Commonwealth's and the Municipality's governments. The executive power of the Municipality is exercised by a Mayor, who is elected every four years and is assisted by the Administrative Cabinet, which is appointed by the Mayor. The legislative power is exercised by the Municipal Legislature, which is also elected every four years. The judiciary power is exercised by the General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality.

B. Financial Reporting Entity

The accounting policies and financial reporting practices of the Municipality conform to the accounting principles generally accepted in the United States of America ("GAAP") as applicable to state and local governments.

According to GAAP, the financial reporting entity for the Municipality consists of: (1) the primary government, which is composed of all municipal departments and units under the legal and administrative control of the Mayor and the Municipal Legislature, and (2) all component units.

In evaluating how to define the Municipality for financial reporting purposes, the Municipality's management has addressed all potential entities and organizations that may be considered component units according to the criteria set forth by Statement No. 14, *The Financial Reporting Entity*, as amended by Statement No. 39, *Determining Whether Certain Organizations are Component Units*, both issued by the Governmental Accounting Standards Board.

GAAP defines component units as those entities that: (1) are legally separate organizations for which the Municipality's elected officials are financially accountable, and (2) other organizations for which the nature and significance of their relationship with the Municipality are such that exclusion of their financial statements from those of the Municipality would cause the Municipality's basic financial statements to be misleading or incomplete. Financial accountability exists if the Municipality appoints a voting majority of the organization's

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

governing body, and if either one of the following conditions exist: (1) the Municipality can impose its will on the organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Municipality.

GASB Statement No. 39, which was early adopted by the Municipality on July 1, 2003, amended the provisions of GASB Statement No. 14 to provide additional guidance to determine whether certain organizations for which the Municipality is not financially accountable should be reported as component units based on the nature and significance of their relationship with the Municipality. Generally, GASB Statement No. 39 requires reporting as a discretely presented component unit, an organization that raises and holds economic resources for the direct benefit of a governmental entity. Such organizations are legally separate, tax-exempt entities that meet all of the three specific criteria that address benefit, entitlement or access, and significance.

The Municipality's management has concluded that, based on the aforementioned criteria, there are no legally separate entities or organizations considered component units of the Municipality according to GAAP as of June 30, 2011, nor for the year then ended.

C. New Financial Reporting Model

On July 1, 2003, the Municipality adopted the provisions of Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (commonly known as "GASB 34"), issued by the Governmental Accounting Standards Board (GASB). This statement, as amended, established a new financial reporting model for state and local governments.

Simultaneously to the adoption of GASB Statement No. 34, the Municipality adopted certain pronouncements issued by FASB and all of its predecessor bodies, such as the Accounting Principles Board (APB), for its governmental activities. In this respect, the Municipality adopted the pronouncements issued by these entities that were issued on or before November 30, 1989, and that do not conflict with GASB pronouncements. Accordingly, on July 1, 2003, the Municipality adopted the provisions of APB Opinion No. 21, *Interest on Receivables and Payables*, to account for non-interest bearing receivables and payables reported in the accompanying basic financial statements.

The effects of implementing the aforementioned pronouncements have been reported as changes in accounting principles in the accompanying basic financial statements. Accordingly, the cumulative effects of such transactions have been reported retroactively as restatements of fund balances at July 1, 2003.

According to the new financial reporting model established by GASB 34, as amended, the minimum required presentation for financial reporting purposes of the Municipality is composed of the following elements:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

1. **Management's Discussion and Analysis ("MD&A")** – MD&A is a required supplementary information used to introduce the basic financial statements and provide an analytical overview of the Municipality's financial activities for the year ended June 30, 2011, based on the Municipality's management knowledge of the transactions, events and conditions reflected in the basic financial statements and the fiscal policies that control the Municipality's operations.
2. **Government-Wide Financial Statements ("GWFS")** – GWFS is a set of financial statements composed of: (1) a statement of net assets and (2) a statement of activities.

The government-wide financial statements are aimed at presenting a broad overview of the Municipality's finances by focusing on operational accountability through reporting the financial position and results of operations of the Municipality as a whole using methods that are similar to those used by most private businesses.

The statement of net assets provides short-term and long-term information about the Municipality's financial position, which assist management to determine the Municipality's economic condition at June 30, 2011, by presenting all of the Municipality's assets and liabilities, with the difference between these two items reported as "net assets" (equity). Net assets are reported in the following three categories:

- **Invested in Capital Assets, Net of Related Debt** – This consist of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
- **Restricted Net Assets** – These result when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally it is the Municipality's policy to use restricted resources first, and then unrestricted resources as they are needed.
- **Unrestricted Net Assets** – These consist of net assets which do not met the definition of the two preceding categories. Unrestricted net assets often are designed 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.

The statement of activities presents financial information showing how the Municipality's net assets changed during the year ended June 30, 2011. The statement of activities demonstrates the degree to which direct expenses of a given function or

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

segments are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function, segment or operational unit. Program revenues include charges to customers or applicants who purchase, use or directly benefit from goods, services or privileges provided by a given function, segment or operational unit. Program revenues also include 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. Resources that are dedicated internally by the Municipality are reported as general revenues rather than as program revenues. The Municipality does not allocate general government (indirect) expenses to other functions.

Under the provisions of GASB 34, all activities carried out by the Municipality are considered governmental in nature for financial reporting purposes. As a result, no business-type activities are reported in the accompanying basic financial statements.

3. **Fund Financial Statements (“FFS”)** – FFS is a set of financial statements composed of: (1) a balance sheet (financial position) and, (2) a statement of revenues, expenditures and changes in fund balances (deficits) of the Municipality’s governmental funds (results of operations).

The fund financial statements focus on: (1) financial accountability, (2) individual parts of the Municipality’s government and (3) reporting the Municipality’s operations in more detail than the government-wide financial statements.

Each fund is considered an independent fiscal entity accounted for within a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenue, and expenditures. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial and contractual provisions.

On March 2009, GASB 54 was issued in an effort to improve the consistency in reporting fund balance components, enhance fund balance presentation, improve the usefulness of fund balance information, and clarify the definitions of the governmental fund types. In summary, GASB 54 introduces entirely new terminology and classification of fund balances in governmental funds. This new standard also establishes a hierarchy of fund classifications as follows:

1. Non-spendable Amounts: That is, the fund balance which cannot be spent as it is associated with assets such as inventory, prepaid expenses, long term receivables or permanent fund principal.

2. Spendable Amounts: These amounts can be spent, but are classified based on the relative strength of the constraints that control the purposes for which

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

specific amounts can be spent. Beginning with the most binding constraints, these classifications are:

- a. Restricted
- b. Committed
- c. Assigned and
- d. Unassigned

How to classify spendable amounts:

Restricted Fund Balance: This balance represents amounts that are constrained for a specific purpose through restrictions of external parties (i.e. creditors, grantors, contributors, or laws or regulations of other governments), or by constitutional provision or enabling legislation, pursuant to the definition of “restricted” in paragraph 34 of GASB 34, as amended by GASB 46.

Committed Fund Balance: This balance represents amounts that are constrained for specific purposes imposed by a formal action of the government’s highest level of decision making authority (i.e. amounts that have been committed by a governing body legislation, ordinance or resolution for a specific purpose). Furthermore, fund balances cannot be sued for other purposes unless the government used the same acting it took to originally commit the amounts.

Assigned Fund Balance: This balance represents amounts that are constrained by the government’s intent to be used for a specific purpose, but are neither restricted nor committed. Intent should be expressed by (1) the governing body itself (2) a body (e.g. a budget committee) or official to whom the governing body has delegated authority to assign amounts to be used for specific purposes. The key distinction between committed and assigned is that committed monies are set by the highest authority (i.e. the board) and such restrictions can only be removed by this authority.

Unassigned Fund Balance: This balance represents the residual amounts for a government’s General Fund; it includes all amounts that are not classified in the previous three categories (restricted, committed and assigned). Furthermore only the General Fund can report unrestricted fund balance.

The minimum number of funds is maintained consistent with legal and self-imposed managerial requirements established by the Municipality. For financial reporting purposes, the Municipality classifies its funds within the following governmental fund categories:

General Fund – The general fund is the chief operating fund used to account for all financial resources and governmental activities of the Municipality, except for financial resources required to be accounted for in another fund type. It is presumed that the

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

Municipality's activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) GAAP requirements or (3) the demands of sound financial administration requiring the use of a fund other than the general fund.

Special Revenue Funds – The special revenue funds are used to account for revenues derived from grants or other revenue sources (other than major capital projects) that are either self-restricted by the Municipality or legally restricted by outside parties for use in specific purposes. The uses and limitations of each special revenue fund are specified by municipal ordinances or federal and state statutes.

Debt Service Fund– The debt service fund is used to account for the accumulation of resources for, and the payment of, principal and interest for: (1) general long-term debt for which debt service payments are legally mandated to be accounted for in a debt service fund, and/or (2) general long-term debt for which the Municipality is being accumulating financial resources in advance, to pay principal and interest payments maturing in future years (such bonds payable and notes payable).

General long-term debts for which debt service payments do not involve the advance accumulation of resources (such as capital leases, compensated absences, claims and judgments, advances from CRIM, and landfill closure and post closure maintenance costs) are accounted for in the general fund.

Long-term debt's principal and accrued interest due on July 1 of the following fiscal year are accounted for as liabilities in the debt service fund at June 30, if resources are available at June 30 for its payment.

Capital Projects Funds – Capital projects funds are used to account for the financial resources used in the acquisition or construction of major capital facilities, other assets and permanent improvements. The use of the capital projects funds has been reserved for major capital acquisitions or construction activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities.

The routine purchase of assets that could be capitalized (such as vehicles and other minor capital assets) has been reported in the general fund.

The Municipality has no significant operations or activities that: (1) are financed and operated primarily in a manner similar to private business enterprises, where the costs of providing goods or services to the general public is financed primarily through user charges, or (2) are fiduciary in nature. As a result, the Municipality does not report proprietary nor fiduciary funds in the accompanying fund financial statements. All Municipalities' funds are classified as governmental for financial reporting purposes.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

Permanent Funds- Accounts for resources that benefit the Government where only the earnings of fund may be used for the Government's related purposed and the principal must remain intact.

4. *Notes to the Basic Financial Statements* – A set of notes that provide information that is essential to a user's understanding of the basic financial statements.
5. *Required Supplementary Information (other than MD&A)* – A set of reports and information reported along with, but separate from, the basic financial statements of the Municipality, such as: (1) Budgetary Comparison Schedule – General Fund, (2) the Notes to Budgetary Comparison Schedule and (3) the Schedule of Funding Progress - Employees' Retirement System of the Commonwealth of Puerto Rico and Its Instrumentalities.

D. Measurement Focus and Basis of Accounting

The term measurement focus refers to what is being expressed in reporting financial position and performance, that is, which resources are being measured in the accompanying basic financial statements. Two different measurement focuses have been applied in the accompanying basic financial statements: (1) the flow of current financial resources and (2) the flow of economic resources. Basis of accounting refers to when transactions have been recognized in the accompanying basic financial statements. GAAP provides for the use of two different bases of accounting, which have been used in the accompanying basic financial statements: (1) the accrual basis and (2) the modified accrual basis.

The accompanying government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Accordingly, revenues are generally recorded when earned and expenses are generally recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. All significant inter-fund activities have been eliminated from these government-wide financial statements.

The accompanying fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are generally recognized as soon as they are both measurable and available (that is, earned and collected or expected to be collected within the next 90 days following the fiscal year-end) to pay liabilities of the current period, except property tax revenues, for which the availability period is 60 days.

In applying the susceptible to accrual concept to intergovernmental revenue in the accompanying fund financial statements, 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, generally recognized as expenditures as

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

incurred. For the other revenue, moneys are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are generally reflected as revenue at the time of receipt or earlier if the susceptible to accrual criteria is met.

In the accompanying fund financial statements, expenditures and related liabilities are generally recorded in the accounting period in which the liability is incurred, except for: (1) principal payment and interest on long-term obligations, which are recorded when due, except for principal and interest due in July 1 of the following fiscal year which are recorded when resources are available in the debt service funds (generally June 30); and (2) vacation leave, sick leave, Christmas bonuses, obligations under capital leases, amounts subject to judgments under litigation, and other long-term obligations, which are recorded under the accrual basis of accounting in the accompanying government-wide financial statements.

In December 1998, the Governmental Accounting Standards Board issued Statement No. 33, *Accounting and Financial Reporting for Non-exchange Transactions* ("GASB 33"), effective for financial statement for periods after June 15, 2000, which the Municipality adopted on July 1, 2003. This statement established accounting and reporting standards for non-exchange transactions involving cash and financial or capital resources (for example, most taxes, grants and private donations). In a non-exchange transaction, a government gives (or receives) value without directly receiving (or giving) equal value in return. This is different from an exchange transaction, in which each party receives and gives up essentially equal values. The statement groups non-exchange transactions of governments into four classes, based on their principal characteristics: (a) derived tax revenue; (b) imposed non-exchange revenue; (c) government mandated non-exchange transactions; and (d) voluntary non-exchange transactions. The adoption of this statement altered significantly the basis of accounting used by the Municipality for the recognition of revenue and expenditures and related assets and liabilities, as described above. The effect of the adoption of this pronouncement has been reported as changes in accounting principles in the accompanying basic financial statements. Accordingly, the cumulative effects of such transactions have been reported retroactively as restatements of fund balances at July 1, 2003.

E. Major and Non-major Funds

Under the provisions of GASB 34, the Municipality is required to segregate funds among major and non-major categories within the fund financial statements. Major individual governmental funds are reported as separate columns in the accompanying fund financial statements, while data from all non-major governmental funds are aggregated into a single column, regardless of fund type. At minimum, a fund is considered major if: (1) it is the primary operating fund of the Municipality (i.e. the general fund) or; (2) meets both of the following criteria:

- (a) Total assets, liabilities, revenues or expenditures of that individual governmental fund are at least 10 percent of the corresponding total for all funds of that category or type; and,

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

- (b) Total assets, liabilities, revenues, or expenditures of the individual governmental fund are at least 5 percent of the corresponding total for all governmental funds combined.

Based on the above-mentioned criteria, the Municipality's general fund, the debt service fund, the \$3,860,000 Loan fund, the \$3725,000 Loan fund, and, (5) the FEMA (*Lluvias de Octubre 2010*) fund are the only five funds that qualify as major funds for the fiscal year ended June 30, 2011, and accordingly, have been reported as major funds in the accompanying fund financial statements. All other governmental funds of the Municipality are considered non-major for financial reporting purposes.

F. Statutory (Budgetary) Accounting

The Municipality's budget is adopted in accordance with a statutory basis of accounting, which is not in accordance with GAAP. Revenue is generally recognized when cash is received.

Expenditures are generally recorded when the related expenditure is incurred or encumbered. Available appropriations and encumbrances are established to lapse one year after the end of the fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment.

Under the statutory basis of accounting, the Municipality uses encumbrance accounting to record the full amount of purchase orders, contracts and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control.

The accompanying budgetary comparison schedule – general fund, only presents the information for the general fund, which is the only Municipality's fund with a legally adopted budget, as required by GAAP. Because accounting principles applied for purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of differences in the deficiency of revenues and other financing sources under expenditures and other uses of financial sources for the year ended June 30, 2011, was presented for the general fund as part of the accompanying budgetary comparison schedule.

G. Cash and Cash Equivalents

The Municipality's cash and cash equivalents are composed of cash on hand, demand deposits, and short-term investments in certificates of deposit with original maturities of three months or less from the date of acquisition.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

The Municipality follows the practice of pooling cash and cash equivalents. The balance in the pooled cash accounts is available to meet current operating requirements and any excess is invested in various interest-bearing deposits with private commercial banks.

Cash with fiscal agent in the debt service fund represents additional property tax collections retained by the Municipal Revenue Collection Center ("CRIM", by its Spanish Acronyms), a municipal corporation (not a component unit of the Commonwealth nor of the Municipality). Such cash balances are restricted for the payment of the Municipality's debt service, as established by law.

H. 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 inter-fund loans).

Tax receivables in the general fund represent amounts owed by taxpayers principally for individual and corporate property taxes, municipal license taxes and construction excise taxes. A portion of these tax receivables is recognized when they become measurable and available based on actual collections during the 90 days (60 days for property taxes) following the fiscal year-end related to tax returns due before year-end. Tax receivables also include amounts owed by taxpayers from taxable years prior to June 30, 2011, estimated to be collectible but not currently available, as a result of the adoption of GASB 33.

Accounts receivables are stated net of estimated allowances for doubtful accounts, which are determined based upon past collection experience and current economic conditions. Intergovernmental receivables mainly represent amounts owed to the Municipality by the Commonwealth and the federal government of the United States of America for: (1) intergovernmental charges, and (2) for reimbursement of expenditures incurred pursuant to federally funded programs, respectively.

In the accompanying government wide financial statements, receivables consist principally of all revenues earned at year-end and not yet received. Allowances for doubtful accounts are based upon historical trends and the periodic aging of accounts receivable. Major receivable balances for the governmental activities include municipal license taxes, property taxes and construction excise taxes, among others.

Non-exchange transactions collectible but not available are deferred in the accompanying fund financial statements in accordance with the modified accrual basis of accounting, but not deferred in the accompanying government wide financial statements in accordance with the accrual basis of accounting. Interest income is recorded when earned only if collected within 90 days after year-end since they would be considered both measurable and available. Allowances for uncollectible accounts receivable are based upon historical trends and the periodic aging of accounts receivable.

COMMONWEALTH OF PUERTO RICO
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I. Inventories and Prepaid Expenses

Inventories consist of materials and supplies held for consumption. Generally, inventories and prepaid expenses are valued at cost and predominantly on the first-in, first-out basis. Governmental fund inventories and prepaid expenses are recorded as expenditures (consumption method) when purchased rather than capitalized as an asset. Only significant amounts of inventory and prepaid expenses at the end of the year would be capitalized, if any, in the governmental funds. However, inventories are always capitalized (purchase method) in the statement of net assets.

J. Temporarily Restricted Assets

Certain cash and cash equivalents set aside by the general fund, the capital projects fund and the special revenue fund are classified as temporarily restricted assets since their use is limited for: (a) the compliance with debt service requirements of bonds and notes payable as established in the respective debt agreements, (b) the funding of construction and permanent improvement projects, and (c) the funding of federal and state sponsored programs. Temporarily restricted cash and cash equivalents amounted to \$5,297,395 (note 3) at June 30, 2011.

K. Deferred Charges

Deferred charges in the accompanying statement of net assets consist of debt bond issuance costs, which are amortized over the term of the related debt using the straight-line method. In the fund financial statements, bond issuance costs are recognized in the current period as expenditure, whether or not withheld from the actual debt proceeds received.

L. Inter-fund Transactions

Permanent reallocations of resources between the Municipality's funds are classified as inter-fund transfers. The Municipality has the following types of transactions recorded among funds in the accompanying fund financial statements:

- ***Operating Transfers*** – Legally required transfers that are reported when incurred as “operating transfers-in” by the recipient fund and as “operating transfer-out” by the disbursing fund.
- ***Inter-fund Payments (Quasi-external Transactions)*** – Charges or collections for services rendered by one fund to another that are recorded as revenue of the recipient fund and as expenditure of the disbursing fund.

For the purposes of the accompanying government-wide statement of activities, all interfund transfers between individual governmental funds have been eliminated.

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M. Capital Assets

The accounting and reporting treatment applied to the capital assets associated with a fund are determined by its measurement focus. General capital assets are long-lived assets of the Municipality as a whole, such as land, land improvements, easements, buildings, building improvements, vehicles, machinery, equipment, works, infrastructure and all other intangible assets that are used in the operations of the Municipality and that have initial useful lives extending beyond a single reporting period (fiscal year). Infrastructure assets are generally immovable in nature and include roads, bridges, streets and sidewalks, drainage systems and other similar assets. In the accompanying government wide statement of net assets, all individual capital assets over the threshold amount of \$500 have been capitalized and depreciated.

In the accompanying government-wide statement of net assets, all capital assets are valued at their historical cost or estimated historical cost if actual is unavailable, except for donated capital assets, which are recorded at their estimated fair value at the date of donation. Estimated historical cost was used to value the majority of the assets acquired prior to June 30, 2011. The costs of normal maintenance and repairs that do not add value to the asset or materially extend capital asset lives are not capitalized.

All capitalized assets are depreciated over their estimated useful lives under the straight-line method. All individual capital assets under the above mentioned capitalization threshold are charged directly to expense in the accompanying government-wide statement of activities. The estimated useful lives of major capital asset categories are:

| | <u>Years</u> |
|---|--------------|
| Land improvements | 20 |
| Buildings and building improvements | 30-50 |
| Infrastructure | 20 to 50 |
| Motor vehicles | 8 |
| Furniture and fixtures | 5 to 20 |
| Machinery and equipment (excluding those under capital lease) | 5 to 20 |

Equipment held under capital leases is depreciated under the shorter of the estimated useful life of the assets or the lease term. Capital assets are recorded as capital outlays expenditures in the acquiring fund for the purposes of the accompanying statement of revenues, expenditures and changes in fund balances – governmental funds.

N. Deferred Revenues

The Municipality reports deferred revenue on its basic financial statements. Deferred revenue arises when potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period. Available is defined as due (or past due) at June 30,

COMMONWEALTH OF PUERTO RICO
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2011, and collected within 90 days (60 days for property taxes) thereafter to pay obligations due at June 30. Deferred revenues also arise when the Municipality receives resources before it has a legal claim to them. In subsequent periods, when the revenue recognition criterion is met, or when the Municipality has a legal claim to the resources, the liability for deferred revenue is removed and revenue is recognized. Deferred revenues at the government-wide level arise only when the Municipality receives resources before it has a legal claim to them.

Deferred revenues at June 30, 2011 amounted to \$595,308 in the accompanying government-wide statement of net assets and balance sheet – governmental funds, respectively.

O. Compensated Absences

Compensated absences are accounted for under the provisions of Statement No. 16, *Accounting for Compensated Absences*, issued by the Governmental Accounting Standards Board (GASB 16).

Compensated absences include paid time off made available to employees in connection with vacation, sick leave and compensatory time. According to GASB 16, the liability for compensated absences recorded in the accompanying government-wide statement of net assets is strictly limited to leave that: (1) is attributable to services already rendered on or before June 30, 2011, and (2) is not contingent on a specific event (such as illness) that is outside the control of the Municipality and the employee. The liability for compensated absences, include salary-related costs, which are directly and incrementally related to the amount of salary paid to the employee (such as employer's share of Social Security taxes, Medicare taxes, employer contributions to retirement system and others).

The vacation policy of the Municipality provides for the accumulation of regular vacations at a rate of 2.5 days per month (30 days per year). Employees accumulate regular sick leave at a rate of 1.5 days per month (18 days per year). Employees accumulate compensatory time at a rate of 1.5 times the overtime worked. All vacation and sick leave days accumulated by employees in excess of 30 days and 90 days, respectively, are paid to employees each year if not consumed, as required by law. In the case of compensatory time, the excess of 240 hours is paid to employees each year, if not consumed. Upon termination of employment, an employee receives compensation for all accumulated unpaid regular vacation leave at the current rate. In the case of regular sick leave, if the employee terminates his or her employment with the Municipality before reaching 10 years of services, such regular sick leave days are not paid to the employee. Upon termination of employment, an employee does not receive compensation for compensatory time, if not consumed. After 10 years of services any regular sick leave balance is paid to the employee. Accumulated vacation time is fully vested to the employees at any time. At June 30, 2011, the Municipality has recorded a liability for compensated absences amounting to \$948,150 in the accompanying government-wide statement of net assets.

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P. Claims and Judgments

The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.

Q. Long-Term Debt

All long-term debt to be repaid from governmental resources is reported as liabilities in the government wide statement of net assets, except for principal and interest payment on long-term obligations due in July 1 of the following fiscal year, which is recorded in the fund financial statements when resources are available in the debt service fund (generally at June 30). Bonds and notes premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the debt in the accompanying government-wide financial statements.

Long-term debt for governmental funds is generally not reported as liabilities in the fund financial statements. In the governmental fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of the debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts are reported as other financing uses.

R. Reservations of Fund Balances

Reservations of fund balances represent portions of fund balances that are legally segregated for specific future uses or are not appropriated for expenditure. The Municipality has the following types of reservations of fund balances:

- *Encumbrances* – Represent future expenditures under purchase orders and other commitments. These committed amounts represent reservations of unexpired appropriations and generally will become liabilities in future periods as the goods or services are received.
- *Capital Assets* - Represents net assets available to finance future acquisitions of capital assets.
- *Debt Service* – Represents fund balances available to finance future debt service payments.
- *Advances and Other Specified Purposes* – Represent the reservation of moneys set aside principally for long-term commitments related to federally-funded programs.

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S. Risk Financing

The Municipality purchases commercial insurance covering casualty, theft, tort claims, and other losses. The Commonwealth, through its Department of Treasury, pays the insurance premiums on behalf of the Municipality and then is reimbursed each year through monthly equal payments. The current insurance policies have not been canceled or terminated. For workers' compensation and disability insurance, the Municipality obtains insurance coverage through the State Insurance Fund Corporation (a component unit of the Commonwealth) and the Occupational Disability Fund (which is a trust fund administered by the Department of Labor and Human Resources of the Commonwealth).

T. Total Columns

Total columns on the fund financial statements are presented only to facilitate financial analysis. Data in these columns does not present consolidated financial position or results of operations in conformity with GAAP. Such data is not comparable to a consolidation, since interfund eliminations have not been made in the accompanying fund financial statements.

U. Use of Estimates

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

2. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

The Municipality's general fund is the only governmental fund for which an annual budget is legally adopted. The Municipality's elected Mayor is legally required to prepare and submit to the elected Municipal Legislature an annual balanced budget for the ensuing fiscal year. The annual budget is prepared by the Municipality's Department of Finance, and takes into consideration the advice provided by all municipal departments and divisions. The appropriations made for any fiscal year shall not exceed the total revenues, including available surplus, estimated for said fiscal year, unless the imposition of taxes sufficient to cover said appropriations is provided by law.

The annual budget, which is developed using elements of performance-based program budgeting and zero-based budgeting, includes an estimate of revenues and other financing resources of the ensuing fiscal year under: (1) laws existing at the time the budget is submitted; and (2) municipal legislative measures proposed by the Mayor and submitted with the proposed budget, as well as the Mayor's recommendations as to appropriations that in his judgment are necessary, convenient, and in conformity with the four-year governmental plan adopted by the Municipality.

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The Municipal Legislature may amend the budget submitted by the Mayor but may not increase any items so far to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. Upon approval by the Municipal Legislature, the budget is referred to the Mayor who may decrease or eliminate any line item but may not increase or insert any new line item in the budget. The Mayor may also veto the budget in its entirety and return it to the Municipal Legislature with his objections. If a budget is not adopted prior to the end of the fiscal year, the annual budget for the preceding fiscal year, as approved by the Legislature and the Mayor, is automatically renewed for the ensuing fiscal year until the Municipal Legislature and the Mayor approve a new budget. This permits the Municipality to continue making payments for its operations and other purposes until the new budget is approved.

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with GAAP. Accordingly, for budgetary purposes the Municipality uses encumbrance accounting. The encumbrances (principally purchase orders and contracts) are considered expenditures when a commitment is made. For GAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of budgetary appropriations and GAAP fund balances and do not constitute expenditures or liabilities on a GAAP basis because the commitments will be honored during the subsequent year. The encumbered balance of any appropriation of the general fund at the end of the fiscal year will lapse to the following fiscal year. In addition, the Municipal Legislature may direct that certain revenues be retained and made available for spending within a specific appropriation account.

Generally, expenditures may not exceed the level of spending authorized for an individual department or division of the Municipality. However, the Municipality is statutorily required to satisfy the debt service requirements, regardless of whether such amounts are appropriated or not.

Appropriations are enacted for certain departments and divisions. Appropriations for capital projects are made for each bond/note issue and the authorization continues for the expected construction period.

The Municipality's Finance Department has the responsibility to ensure that budgetary spending control is maintained on an individual department/division basis. The Finance Department may transfer part or all of any encumbered balance within a department to another department subject to approval. Budgetary control is exercised through the Municipality's accounting system. This system ensures that encumbrances or expenditures are not processed if they exceed the department/division's total available spending authorization, which is considered its budget. The legal level of budgetary control is at the individual department level for the general fund expenditures, principal and interest due for the year for the debt service fund, and by bond/note authorization for capital expenditures.

The annual budget, as presented in the accompanying Budgetary Comparison Schedule – General Fund, is the budget ordinance at June 30, 2010, representing the original budget, as amended. There were no supplemental appropriations for the year ended June 30, 2011.

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3. DEPOSITS

The Municipality maintains its deposits of cash in the Government Development Bank for Puerto Rico ("GDB") (a governmental bank and component unit of the Commonwealth) who serves as fiscal agent of the Municipality; and in various commercial banks located in Puerto Rico. The balances deposited in GDB are uninsured and uncollateralized. The balances deposited in commercial banks are insured by the Federal Deposit Insurance Corporation ("FDIC") up to a maximum of \$250,000 per depositor. However, under the laws and regulations of the Commonwealth, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance provided by the FDIC. All securities pledged as collateral are held by an agent of the Secretary of the Treasury of the Commonwealth in the name of the Municipality.

Cash, cash equivalents and investments at June 30, 2011, consist of the following:

| | Debt Service <u>Fund</u> | FEMA (Lluvias de <u>Octubre</u>) | \$3,860,000 <u>Loan</u> | \$3,725,000 <u>Loan</u> | Non Major <u>Funds</u> | <u>Total</u> |
|--|-----------------------------|---|----------------------------|----------------------------|---------------------------|---------------------|
| Restricted Cash in Commercial Banks | | | | | \$ 1,027,662 | \$ 1,027,662 |
| Restricted Cash in GDB or CRIM as Fiscal Agents | 1,589,781 | 561,721 | 1,732,127 | 44,718 | 341,384 | 4,269,732 |
| Total | <u>\$ 1,589,781</u> | <u>561,721</u> | <u>1,732,127</u> | <u>44,718</u> | <u>1,369,046</u> | <u>\$ 5,297,394</u> |

The Municipality's bank balance of deposits and investments with financial institutions are categorized to provide an indication of the level of collateral risk assumed by the Municipality at June 30, 2011. Risk categories are described as follows:

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

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The carrying amount (book balance) and the bank balance of deposits and investments with financial institutions of the Municipality at June 30, 2011, consist of the following:

| | <u>Carrying</u> <u>Amount</u> | <u>Bank</u> <u>Balance</u> |
|--------------------------------|----------------------------------|-------------------------------|
| Deposits in Commercial Banks | \$ 1,027,662 | \$1,019,164 |
| Deposits in Governmental Banks | 4,269,731 | 4,269,731 |
| Total | \$ 5,297,393 | \$ 5,288,895 |

Bank Balances of deposits and investments:

| | | |
|---------------------|--|--------------|
| Category 1 | | \$ 1,019,164 |
| Category 2 | | - |
| Category 3 | | 4,269,731 |
| Total Bank Balances | | \$ 5,288,895 |

4. MUNICIPAL LICENSE TAXES

The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to 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 on April 15 of each year. Entities with sales volume of \$1 million or more must include rates established by the Municipality. At June 30, 2011, the municipal tax rates imposed by the Municipality were 1.50 percent for financing institutions and 0.30 percent for any other taxpayers. Any taxpayers, who have been granted with partial tax exemptions under any of the incentive tax laws of the Commonwealth, ultimately pay municipal license taxes at reduced tax rates, generally between 60 percent and 90 percent under standard rates.

Each taxpayer must assess his/her corresponding municipal license tax by declaring his/her volume of business through a tax return every April 15 based on the actual volume of business generated in the preceding calendar year. The tax can be paid by the taxpayer in two equal installments: (1) the first payment due at the filing date of the return (generally April 15), and (2) January 15 subsequent to the filing of the declaration. The first installment of the tax covers the taxable period (six months) ended December 31 subsequent to the filing date of the declaration, while the second installment of the tax covers the taxable period (six months) ended June 30 of the subsequent calendar year. If a taxpayer

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elects to pay the tax in full on the filing date of the declaration (April 15), a 5 percent discount is granted automatically on the tax amount due.

Any municipal license taxes collected in advance (that is, prior to June 30 but pertaining to the next fiscal year) are recorded as deferred revenues. Deferred municipal license tax revenues recorded in the accompanying GWFS and GFFS amounted to \$23,804 at June 30, 2011, which represents municipal licenses collected in advance for the taxable year 2010-2011.

5. PROPERTY TAXES

The Municipality is authorized by law to impose and collect personal and real property taxes. Personal property taxes can be imposed to any natural or legal person engaged in trade or business that at January 1 of each year is owner of personal property used in trade or business.

Personal property taxes are self-assessed by taxpayers every year using the book value of personal property assets owned by the taxpayer at January 1 and reporting such taxable value through a personal property tax return filed on May 15 subsequent to the assessment date. At June 30, 2011, the total personal property tax rate in force was 6.38 percent (of which taxpayers pay 6.18 percent and .20 percent is reimbursed by the Department of Treasury of the Commonwealth. Real property taxes are assessed by CRIM. The assessment on real property is made every January 1 and is based on estimated current values of the property deflated at 1957 market prices. At June 30, 2011, the total real property tax rate in force was 8.38 percent (of which 8.18 percent is paid by taxpayers).

Residential real property occupied by its owner is exempt by law from property taxes on the first \$15,000 of the assessed value (at 1957 market prices). For such exempt amounts, the Department of Treasury of the Commonwealth assumes payment of the basic tax (4.00 and 6.00 percent for personal and real property, respectively) to the Municipality, except for property assessed of less than \$3,500 (at 1957 market prices), for which no payment is made. Revenue related to the basic tax on exempt property is recorded in the general fund when collections are received from the CRIM.

CRIM is required to remit 1.03 percent of the personal and real property tax collected to the Municipality to be used for the partial funding of the debt service requirements on general obligations and notes payable of the Municipality. In addition, 1.35 percent of the total personal and real property taxes collected by CRIM is restricted for debt service requirements of the Municipality and is retained by GDB for such purposes. Accordingly, such amount is recorded as revenues in the debt service fund when collected and reported by the CRIM.

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

- i. Thirty five percent (35%) of its net earnings (defined as the excess of revenues over expenses less an amount earmarked for the Fund for Rent and Home Improvement Subsidy Program

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for the Low-Income Qualifying Elderly) is earmarked to the municipalities of the Commonwealth of which a maximum of \$26 million, on an annual basis, is distributed to the Municipal Equalization Fund held by CRIM to cover operating expenses and permanent improvements of the municipalities.

- ii. An additional amount not exceeding \$16 million, on an annual basis, is distributed to the Municipal Equalization Fund, provided it is within the 35 percent corresponding to the municipalities of the Commonwealth. When the accumulated municipal appropriations from the municipalities' Puerto Rico Health Reform are covered up to June 30, 1997, these resources will be assigned to the Health Insurance Administration, a component unit of the Commonwealth.

Total property tax receivable, net of allowance for uncollectible accounts amounted to \$72,836 at June 30, 2011.

6. INTERFUND BALANCES

On July 1, 2001 the Municipality adopted the provisions of Statement No. 38, *Certain Financial Statement Note Disclosures, issued by the Governmental Accounting Standards Board*. This statement requires the disclosure of the flow of resources between funds and to assess the collectibles of inter-fund balances. Inter-fund balances at June 30, 2011 consisted of the following:

| | | COMMONWEALTH OF PUERTO RICO MUNICIPALITY OF MARICAO DUE TO AND DUE FROM | | | | | | |
|-----------------|-------------------------|---|--------------------------------|------------------|------------------|----------------------|------------------|---------------------|
| | | Due From: | | | | | | |
| | | MAJOR FUNDS | | | | | | |
| Due To: | GENERAL FUND | DEBT SERVICE FUND | FEMA (LLUVIAS DE OCTUBRE 2010) | \$3,860,000 LOAN | \$3,725,000 LOAN | OTHER NONMAJOR FUNDS | TOTAL | |
| MAJOR FUNDS: | GENERAL FUND | \$ - | \$ - | \$ - | - | \$ - | \$ 8,101.00 | \$ 8,101.00 |
| NONMAJOR FUNDS: | CONVENIO DTOP | 40,000.00 | - | - | - | - | - | 40,000.00 |
| | JOINT RESOLUTIONS | 859,965.00 | - | - | - | 21,750.00 | - | 881,715.00 |
| | LEY 2 | 45,700.00 | - | - | - | 15,000.00 | - | 60,700.00 |
| | RC 116 | 3,000.00 | - | - | - | - | - | 3,000.00 |
| | QUEBRADA JUAN SANCHEZ | 1,600.00 | - | - | - | - | - | 1,600.00 |
| | RECICLAJE | 1,000.00 | - | - | - | - | - | 1,000.00 |
| | CASA ALCALDIA | 10,000.00 | - | - | - | - | - | 10,000.00 |
| | CANCHA DE BALONCESTO | 3,000.00 | - | - | - | 3,000.00 | - | 6,000.00 |
| | FACILIDADES RECREATIVAS | - | - | - | - | 7,000.00 | - | 7,000.00 |
| | MEJORAS PERMANENTES | 658,000.00 | - | - | - | 5,000.00 | - | 663,000.00 |
| | OTHER FUNDS | - | - | - | - | - | - | - |
| | | <u>1,622,265.00</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>59,851.00</u> | <u>1,682,116.00</u> |

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At June 30, 2011 all amounts due to among funds are considered collectible by the Municipality's management.

7. INTERGOVERNMENTAL RECEIVABLE AND PAYABLE

Intergovernmental receivable and payable

| | Mayor Fund | Other Governmental Fund | Total Governmental Fund | Statement of net assets |
|---|-------------------|-------------------------------|-------------------------------|-------------------------------|
| Intergovernmental receivable: | | | | |
| Puerto Rico Electric Power Authority | 543,045 | | 543,045 | 543,045 |
| SBGP | - | - | - | - |
| Total | <u>\$ 543,045</u> | <u>\$ -</u> | <u>\$ 543,045</u> | <u>\$ 543,045</u> |
| Intergovernmental payable: | | | | |
| General Governmental Services | 19,483 | - | 19,483 | 19,483 |
| Department of Treasury | - | - | 0 | - |
| Employees Retirement System of the Government of Puerto Rico | - | - | 0 | - |
| Department of Labor | 18,815 | - | 18,815 | 18,815 |
| Puerto Rico Aqueduct and Sewer Authority | - | - | 0 | - |
| Puerto Rico Electric Power Authority | 543,045 | - | 543,045 | 543,045 |
| Internal Revenue Service | - | - | - | - |
| Total | <u>\$ 581,343</u> | <u>\$ -</u> | <u>\$ 581,343</u> | <u>\$ 581,343</u> |

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8. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2011, was as follows:

| | Balance at June 30, 2010 | Additions | Reclassifications | Balance at June 30, 2011 |
|--|---|--|--------------------------|---|
| <u>COST BASIS:</u> | | | | |
| Cost basis of capital assets, not subject to depreciation and amortization: | | | | |
| Infrastructure land | \$ 1,290,128 | \$ - | \$ - | \$ 1,290,128 |
| Construction in progress | 4,897,829 | 790,285 | 327,739 | 6,015,853 |
| Total cost basis of capital assets, not subject to depreciation and amortization | <u>6,187,957</u> | <u>790,285</u> | <u>327,739</u> | <u>7,305,981</u> |
| Cost basis of capital assets, subject to depreciation and amortization: | | | | |
| Buildings, structures and building improvements | 7,593,939 | 1,374,641 | (229,999) | 8,738,581 |
| Infrastructure | 2,309,054 | 774,914 | (97,740) | 2,986,228 |
| Land Improvements | 669,713 | - | | 669,713 |
| Licensed vehicles | 2,033,710 | 106,627 | | 2,140,337 |
| Furniture | 2,274 | 14,158 | | 16,432 |
| Machinery and Equipment | 549,382 | 99,542 | | 648,924 |
| Total cost basis of capital assets subject to depreciation and amortization | <u>13,158,072</u> | <u>2,369,882</u> | <u>(327,739)</u> | <u>15,200,215</u> |
| Total cost basis of capital assets | <u>19,346,029</u> | <u>3,160,167</u> | <u>-</u> | <u>22,506,196</u> |
| <u>ACCUMULATED DEPRECIATION AND AMORTIZATION</u> | | | | |
| | Balance at June 30, 2010 | Depreciation Amortization Expense | Reclassifications | Balance at June 30, 2011 |
| Buildings, structures and building improvements | 1,749,208 | 129,089 | - | 1,878,297 |
| Infrastructure | 1,021,666 | 63,400 | - | 1,085,066 |
| Land Improvements | 601,654 | 40,327 | - | 641,981 |
| Licensed vehicles | 1,647,532 | 87,871 | - | 1,735,403 |
| Furniture | 228 | 1,997 | | 2,225 |
| Machinery and equipment | 395,620 | 81,402 | - | 477,022 |
| Total accumulated depreciation and amortization | <u>5,415,908</u> | <u>404,086</u> | <u>-</u> | <u>5,819,994</u> |
| CAPITAL ASSETS, NET | <u>\$ 13,930,121</u> | <u>\$ 2,756,081</u> | <u>\$ -</u> | <u>\$ 16,686,202</u> |

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

Depreciation and amortization expense was charged to functions in the accompanying government-wide statement of activities as follows:

| | | |
|---|----|---------|
| General government | \$ | 131,410 |
| Public safety | | 11,312 |
| Public housing and welfare | | 3,225 |
| Culture, recreation and education | | 7,561 |
| Urban and economic development | | 231,819 |
| Health | | 18,759 |
| | | |
| Total depreciation and amortization expense | \$ | 404,086 |

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

9. EMPLOYEES RETIREMENT SYSTEM

The Municipality's employees participate in the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (the "System"). The System is the administrator of a multi-employer cost-sharing (as related to the Municipality's reporting entity) defined pension plan established by the Commonwealth. The System was created under Act. No. 447 approved on May 15, 1951, as amended, and became effective on January 1, 1952. The System covers all regular employees of the Commonwealth and its instrumentalities, the Municipality and other municipalities of the Commonwealth.

The System is independent, thus assets may not be transferred to another system or used for any purpose other than to benefit each system's participants. The System issues publicly available financial reports that includes its basic financial statements and required supplementary information for each of them, including required six-year trend information. Those reports may be obtained by writing to the administrator of the System.

The System provides for retirement, death and disability benefits. Death and disability retirement benefits are available to members for occupational and non-occupational death and disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after 10 years of plan participation.

Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75 percent of the average compensation.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the System, was enacted with the purpose of establishing a new pension system ("System 2000"). System 2000 became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999, had the option to either stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000, are the only required becoming members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as cash balance plan. Under this new plan, there is a pool of pension assets, which are invested by the System, together with those of the current defined benefit plan. Neither the Commonwealth nor the Municipality will guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employees' contribution (with a minimum of 8.275 percent of the employees' salary up to a maximum of 10.00 percent) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity U.S. Treasury Note; (2) earn a rate equal to 75 percent of the return of the System 2000's investment portfolio (net of management fees); or (3) 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 employer's contributions (9.275 percent of the employees' salary which is applicable to the Municipality) will be used to fund the current plan.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

Funding Policy:

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 |

During the fiscal year ended June 30, 2011, the Municipality, as an employer, did not make any contributions to these retirement systems. On August 12, 2000, Act No. 174 was approved to allow certain participants of the ERS to be eligible for early retirement upon attaining at least age 55 with 25 years of service, provided they made their election on or before April 1, 2001. Those who elected early retirement under this law will receive monthly benefits of 75 percent (if 25 or more year of service and 55, or 30 or more years or services and age 50) or benefits of 65 percent (if 25 years of service by less than age 55) of their average compensation which is computed based on the highest 36 months of compensation recognized by the System. In these cases, the employer (including the Municipality) is responsible for contributing to the System the amount needed to cover the benefit payments and employer contribution with respect to the participants covered until the participants reaches the normal retirement age.

Historically, the Commonwealth has reported the System as a single-employer plan (as relates only to the financial reporting entity of the Commonwealth) in its comprehensive annual financial report. Accordingly, the Commonwealth will assume any actuarial deficiency that may exist or arise related to the Municipality's participating employees since the System does not allocate any actuarial deficiencies pertaining to municipal employees participating in the System.

The Municipality is only required by law to make statutory contributions in the rates mentioned above. As a result, no net pension obligation nor net pension asset that may be allocable to the Municipality's participating employees, if any, has been recorded in the accompanying basic financial statements.

The Municipality's actual contributions for the current and the previous two fiscal years, which are equal to the statutory required contributions, were as follows:

| Fiscal Year ended June 30 | Act No. 447 | System 2000 |
|------------------------------|-------------|-------------|
| 2010 | \$ 99,933 | \$ 16,799 |
| 2011 | \$ 391,468 | \$ 62,189 |

10. LONG-TERM DEBT

The Municipality's Legislature is legally authorized to determine the contracting of debts of the Municipality. Nevertheless, the laws and regulations of the Commonwealth also provide that:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

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

In addition, before any new bonds or notes are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. At June 30, 2011, the Municipality is in compliance with the debt limitation requirements.

The general long-term debt activity for the year ended June 30, 2011, was as follows:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
Year Ended June 30, 2011

| | Balance at June 30, 2010, as restated | Borrowings or Additions | Payments or Deductions | Balance at June 30, 2011 | Due Within One Year |
|--|---|----------------------------|---------------------------|-----------------------------|------------------------|
| Bonds Payable | 6,526,800 | 4,885,000 | (285,900) | 11,125,900 | 412,600 |
| Notes payable to: | | | | | |
| Puerto Rico Treasury Department: | | | | | |
| Financing agreement for the excess of property tax advances over collections | - | | | - | |
| CRIM | | | | | |
| Lims | 28,592 | | (21,127) | 7,465 | 7,465 |
| Act No. 42 - Financing agreement for the excess of property tax advances over collections through fiscal year 2000 | 3,391,562 | | (72,472) | 3,319,090 | 77,047 |
| Compensated Absences | 955,634 | | (7,484) | 948,150 | 361,488 |
| Total | \$ 10,902,588 | \$ 4,885,000 | \$ (386,983) | \$ 15,400,605 | \$ 858,600 |

a) Bonds Payable

The Municipality issues general and special (public improvements) obligations bonds and notes to provide for the acquisition and construction of major capital facilities and equipment, as well as, to cover certain operating needs. Long-term debt at June 30, 2011, is composed of the following debts:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

| <u>General obligation bonds:</u> | Outstanding Amount |
|--|-------------------------------|
| 2003 serial bonds due in annual installments ranging from \$10,000 to \$50,000; plus interest due in semiannually installments at variable rates (5.00% to 7.25% at June 30, 2011), through July 1, 2028 | 540,000 |
| Serial bond approved under ordinance number 8 of 2009-10 due in semiannual. Installments ranging from \$5000 to \$19,000 plus interest due in semiannually payments at variable rates (4.75% to 7.5%). Due in January 1, 2017 | 145,000 |
| Serial bond approved under ordinance number 5, 2009-10. Installments ranging from \$5,000 to \$19,000 plus interest at 4.37% until cancellation. This bonds due in 1-1-2017. | 105,000 |
| Serial bond approved under ordinance number 4, 2009-2011. Required installments ranging from \$15,900 to \$20, 500 through 1-1-207; and semiannually interest payment calculated in 4.37% | 110,900 |
| Subtotal General Obligations: | <u>900,900</u> |
| <u>Public Improvement Bonds: (sales taxes)</u> | |
| 2008- Serial bond, original issued amount of \$3,860,000 due in annually principal installments ranging from \$115,000 to \$ 380,000, plus interest due in semiannually installments at variable rates from 1.53% to 7.50% at June 30, 2011 through July 1, 2025 | 3,615,000 |
| 2008- Serial bond, original issued amount of \$160,000 due in annually principal installments ranging from \$5,000 to \$10,000, plus interest due in semiannually installments at variable rates from 1.53% to 7.50% at June 30, 2011 through July 1, 2023. | 150,000 |
| 2008- Serial bond, original issued amount of \$870,000 due in annually principal installments ranging from \$70,000 to \$110,000, plus interest due in semiannually installments at variable rates from 1.53% to 7.50% at June 30, 2011 through July 1, 2018. | 725,000 |
| 2010- Serial bond, original issued amount of \$880,000 due in annually principal installments ranging from \$50,000 to \$380,000, plus interest due in semiannually installments at variable rates from 1.53% to 7.50% at June 30, 2011 through July 1, 2018 | 0 |
| 2011- Serial bond, original issued amount of \$280,000 due in annually principal installments ranging from \$30,000 to \$50,000, plus interest due in semiannually installments at variable rates from 6.00% to 7.50% at June 30, 2011 through July 1, 2017 | 280,000 |
| 2011- Serial bond, original issued amount of \$3,725,000 due in annually principal installments ranging from \$50,000 to \$310,000, plus interest due in semiannually installments at variable rates from 6.00% to 7.50% at June 30, 2011 through July 1, 2035 | 3,725,000 |
| Subtotal Public Improvement Bonds: | <u>9,375,000</u> |

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

| | |
|--|----------------------------|
| <u>Operational Bonds Payable</u> | |
| 2002 Serial bonds due in annual principal installments ranging from \$10,000 to \$80,000; plus interest due in semiannually installments at variable rates 1.28% to 6.00% at June 30, 2003 through July 1, 2026 | <u>850,000</u> |
| Total Bonds | <u>11,125,900</u> |
| <u>Loan Payable to CRIM (Law 42)</u> | |
| 2001 operating loan with the Department of Treasury due in monthly principal installments ranging from \$3,566 to \$23,358; which includes implicit interest due in monthly installments at 6.30% through July 1, 2033 | 3,319,090 |
| <u>Lims</u> | |
| On November 28, 2001 the Agency (CRIM) financed the Real Property Digitalization System that must be used in the Island. The total cost of this System was distributed among all Municipalities. The share of this cost assigned to the Municipality of Maricao amounted to \$ 114,634, financed for 10 years at a 5.95% interest rate, payable in semi-annual installments. At June 30, 2011, the outstanding balance amounted to \$ 7,465. | 7,465 |
| <u>Provision for accrued compensated absence</u> | <u>948,150</u> |
| Total bonds, note payable and compensated absence | <u>\$15,400,605</u> |

These bonds are payable from the ad valorem property tax of 1.0% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

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

The Municipality levies an annual additional special tax of 1.40% of the assessed value of personal and real property. The proceeds of this additional special tax are deposited in a sinking fund established at GDB whereby sufficient funds must be set aside to redeem the bonds in minimum annual or biannual principal and interest payments. The proceeds of this special tax are recorded in the debt service fund.

Interest rates on serial bonds subject to variable rates are reviewed periodically by GDB and are based on the fluctuation of GDB's weighted average rate for its commercial paper program, not to exceed 8%. Under this program, GDB issues commercial paper in the U.S. taxable and tax-exempt markets, in the Eurodollar market and to corporations that have tax exemption under the Commonwealth Industrial Incentives Act.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

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

| <u>Year ended</u> <u>June 30</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|-------------------------------------|----------------------|---------------------|----------------------|
| 2012 | \$ 412,600 | \$ 357,753 | \$ 770,353 |
| 2013 | 453,300 | 768,657 | 1,221,957 |
| 2014 | 485,000 | 735,113 | 1,220,113 |
| 2015 | 511,800 | 699,469 | 1,211,269 |
| 2016 | 558,700 | 661,159 | 1,219,859 |
| 2017-2021 | 2,634,500 | 2,705,259 | 5,339,759 |
| 2022-2026 | 3,130,000 | 1,696,294 | 4,826,294 |
| 2027 -2031 | 1,540,000 | 804,294 | 2,344,294 |
| 2032-2036 | 1,400,000 | 275,625 | 1,675,625 |
| | <u>\$ 11,125,900</u> | <u>\$ 8,703,623</u> | <u>\$ 19,829,523</u> |

b) Notes Payable to CRIM

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

In addition, on February 12, 2003, the Municipality entered into a repayment agreement with GDB and CRIM to pay off the remaining \$3,814,820 of excess of property tax advances through fiscal year 2000 and 2001. CRIM retains the principal and interest from the property tax advances of the Municipality. The amounts retained by CRIM are remitted to CDB on July 1 of each year through July 1, 2032. The repayment agreement bears interest at variable rates determined by GDB. The outstanding principal balances of the note payable to CRIM amounted \$3,319,090, at June 30, 2011. The principal and interest maturities are as follows:

| <u>Year ended</u> <u>June 30</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|-------------------------------------|---------------------|---------------------|---------------------|
| 2012 | 77,047 | 204,195 | 281,242 |
| 2013 | 81,888 | 199,354 | 281,242 |
| 2014 | 87,033 | 194,209 | 281,242 |
| 2015 to 2019 | 524,398 | 881,273 | 1,405,671 |
| 2020 to 2024 | 711,188 | 695,022 | 1,406,211 |
| 2025 to 2029 | 964,513 | 441,698 | 1,406,211 |
| 2030 to end | 873,022 | 111,326 | 984,348 |
| | <u>\$ 3,319,090</u> | <u>\$ 2,727,076</u> | <u>\$ 6,046,166</u> |

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Basic Financial Statements
June 30, 2011

Financing of delinquent property tax accounts sold – On April 22, 2002, the Municipality entered into a financing agreement with CRIM in the amount of \$83,620 for the payment of delinquent property tax account sold to private investors. The financing agreement is in the form of a line of credit, bearing interests at 6.50% during the first 5 years, and variable interests 125 points over LIBOR rate during the next 25 years. At June 30, 2011, the outstanding principal balances amounted to \$38,581. The principal and interest maturities are based on collections.

6. *Compensated Absences*

At June 30, 2011, the liability for compensated absences is composed as follows:

| | Due within one year | Due after one year | Total |
|-------------------|--------------------------------|-------------------------------|--------------|
| Vacations | \$ 171,657 | \$ 144,278 | \$ 315,935 |
| Sick leave | 139,638 | 400,694 | 540,332 |
| Compensatory time | 24,504 | | 24,504 |
| | 335,799 | 544,972 | 880,771 |
| Fringe Benefits | 25,689 | 41,690 | 67,379 |
| Total | \$ 361,488 | \$ 586,662 | \$ 948,150 |

11. COMMITMENTS AND CONTINGENCIES

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

With respects to pending or threatened litigation, the Municipality has reported liabilities of \$375,018 or awarded and anticipated unfavorable judgments as of June 30, 2011. This amount was reported within claims and judgments liabilities in the government-wide statement of net assets. Management believes that the ultimately liability in excess of amounts provided, if any, would not be significant.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
 Budgetary Comparison Schedule – General Fund
 Year Ended June 30, 2011

| | Budgeted Amounts | | Actual Amounts (Budgetary Basis) (See Note 1) | Variance with Final Budget - Positive (Negative) |
|--|---------------------|---------------------|---|---|
| | Original | Final | | |
| Revenues: | | | | |
| Property taxes | \$ 434,249 | \$ 434,249 | \$ 425,143 | \$ (9,106) |
| Municipal sales tax | 650,000 | 650,000 | 607,532 | (42,468) |
| Municipal license taxes | 370,813 | 370,813 | 379,836 | 9,023 |
| Charges for services | 500 | 500 | - | (500) |
| Intergovernmental grants and contributions | 3,740,291 | 3,740,291 | 3,640,826 | (99,465) |
| Investments earnings | 18,000 | 18,000 | - | (18,000) |
| Miscellaneous | 427,800 | 427,800 | 371,102 | (56,698) |
| | <u>5,641,653</u> | <u>5,641,653</u> | <u>5,424,439</u> | <u>(217,214)</u> |
| Expenditures: | | | | |
| General government | 2,395,460 | 2,395,460 | 2,395,460 | - |
| Public Safety | 361,405 | 361,405 | 368,662 | (7,257) |
| Urban and economic development | 2,220,813 | 2,220,813 | 2,124,122 | 96,691 |
| Environmental Control Health | 350,414 | 350,414 | 349,899 | 515 |
| Culture, Recreation and Education | 226,820 | 226,820 | 219,789 | 7,031 |
| Public, Housing and welfare | 86,741 | 86,741 | 85,185 | 1,556 |
| | <u>\$ 5,641,653</u> | <u>\$ 5,641,653</u> | <u>\$ 5,543,117</u> | <u>\$ 98,536</u> |

Explanation of Differences:

Sources/inflows of financial resources:

| | |
|--|---------------------|
| Actual amounts (budgetary basis) "available for appropriations" from the budgetary comparison schedule | \$ 5,424,439 |
| Differences - budget basis to GAAP: | |
| Decrease in receivable | - |
| Non budgetary revenue from operational expenditures account | - |
| Other | - |
| Total revenues as reported on the statement of revenues, expenditures and changes in fund balances - governmental funds | <u>\$ 5,424,439</u> |

Uses/outflows of financial resources:

| | |
|--|---------------------|
| Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule | \$ 5,543,117 |
| Differences - budget basis to GAAP: | |
| Increase in debt with governmental entity | - |
| Prior year expenditures(Resultas) | - |
| Expenditures transfer from operational expenditures account | 1,529,955 |
| Other expenditures | - |
| Total expenditures as reported on the statement of revenues, expenditures and changes in fund balances - governmental funds | <u>\$ 7,073,072</u> |

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
 Schedule of Federal Awards
 June 30, 2011

| FEDERAL GRANTOR / PASS THROUGH GRANTOR | FEDERAL CFDA | |
|--|-------------------------|---------------------------|
| <u>PROGRAM TITLE</u> | <u>NUMBER</u> | <u>EXPENDITURES</u> |
| US DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT | | |
| Direct Programs: | | |
| Section 8 Vouchers and Portability | 14.871 | 275,954 |
| Indirect Program: | | |
| Passed through PR Office of Municipal Affairs | | |
| State Block Grant Program (SBGP) | 14.228 | MP . 842,497 |
| Homeless Prevention Program | 14.729 | 31,385 |
| Neighborhood Stabilization Program | 14.264 | <u>818,946</u> |
| Total HUD | | <u>1,968,782</u> |
| Passed through the Elderly Commission Office | | |
| Title III, Part B- Grants for Supportive Services and Seniors Centers | 93.44 | <u>144,395</u> |
| FEDERAL MANAGEMENT EMERGENCY ASSISTANCE | | |
| Direct Programs: | | |
| Public Disaster Assistance | 97.036 | <u>20,410</u> |
| TOTAL FEDERAL FINANCIAL ASSISTANCE | | <u><u>\$2,133,587</u></u> |

MP = Major Program

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Notes to Schedule of Federal Awards
June 30, 2011

1. GENERAL

The accompanying schedule of expenditures of federal awards presents the expenditure of all the federal financial assistance programs of the municipality of Maricao (the Municipality). The Municipality's reporting entity is defined in note 1 to the Municipality's general-purpose financial statements.

2. BASIS OF ACCOUNTING

The accompanying schedule of expenditures of federal awards is presented using modified-accrual accounting basis of accounting, which is described in note 1 to the Municipality's general-purpose financial statements.



JUAN A. RIVERA, CPA
CERTIFIED PUBLIC ACCOUNTANT

Phone: 787-784-2255
Fax: 787-784-2250
Email: jrmelecio@hotmail.com

URB LEVITTOWN, 1818 DEL VALLE AVE, TOA BAJA, PR 00949

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

To the Honorable Mayor and
the Municipal Assembly
Municipality of Maricao
Maricao, Puerto Rico

We have audited the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Maricao as of and for the year ended June 30, 2011, which collectively comprise the Municipality of Maricao basic financial statements and have issued our report thereon dated December 13, 2011. We conducted our audit in accordance with auditing standards generally accepted in 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 Maricao internal control over financial reporting as a basis for designing our auditing procedures for the purpose for the purpose of expressing our opinions of the financial statements but not for the purpose of expressing an opinion on the effectiveness of the Municipality of Maricao 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 Maricao 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 Maricao financial statements that is more than inconsequential will not be prevented or detected by Municipality of Maricao internal control. We consider the deficiencies described in the accompanying schedule of internal control over financial reporting. (2011-1 and 2011-2)

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 Maricao internal control.

Our consideration of the internal control over financial reporting was for the limited purpose describe in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and accordingly would not necessarily disclose all significant deficiencies

that are also considered to be material weaknesses. However we believe that none of the significant deficiencies described above is a material weakness.

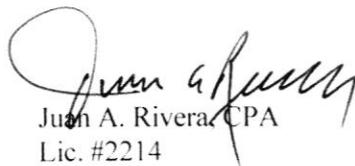
Compliance

As part of obtaining reasonable assurance about whether the Municipality of Maricao financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing and opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such as an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items (2011-1 and 2011-2)

We noted certain matters that we reported to management of Municipality of Maricao, in a separate letter dated December 13, 2011.

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

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


Juan A. Rivera, CPA
Lic. #2214

Toa Baja, Puerto Rico
December 13, 2011



Stamp NO. 2633854 of the Puerto Rico Society of Certified Public Accountants was affixed to the original report.

JUAN A. RIVERA, CPA
CERTIFIED PUBLIC ACCOUNTANT

Phone: 787-784-2255
Fax: 787-784-2250
Email: jrmelecio@hotmail.com

URB LEVITTOWN, 1818 DEL VALLE AVE, TOA BAJA, PR 00949

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

To the Honorable Mayor and
the Municipal Assembly
Municipality of Maricao
Maricao, Puerto Rico

We have audited the compliance of Municipality of Maricao 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, 2011. The Municipality of Maricao major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Municipality of Maricao management. Our responsibility is to express an opinion on the Municipality of Maricao compliance based on our audit.

Compliance

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

As described in item Section II in the accompanying schedule of findings and questioned costs, the Municipality of Maricao did not comply with requirements regarding administrative requirements that are applicable to its SBGP Program. Compliance with such requirement is necessary for the Municipality of Maricao to comply with the federal regulations. Also we want to emphasize that this requirement has not been complied in prior years.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality of Maricao 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, 2011.

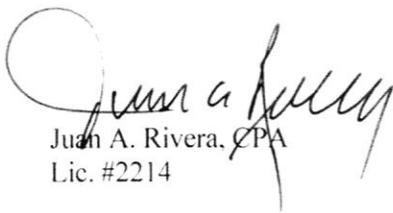
Internal Control Over Compliance

The management of the Municipality of Maricao is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grant applicable to federal programs. In planning and performing our audit, we considered the Municipality of Maricao internal control over compliance with 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 and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Municipality of Maricao ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs in Section II.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

However, we believe that none of the reportable conditions described above is a material weakness. This report is intended for the information of the audit committee, the Municipality's management, the Department of Housing and Urban Development (Cognizant Agency), and federal awarding agencies and pass-through entities. However, this report is not intended to be and should not be used by anyone other than these specified parties.


Juan A. Rivera, CPA
Lic. #2214

December 13, 2011
Toa Baja, Puerto Rico



Stamp No. 2633855 of the Puerto Rico State Society of Certified Public Accountants was affixed to the original report

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2011

Section II – Schedule of Financial Statements Findings and Questioned Costs

FINDING NUMBER 11-01

Accounting and Reporting System

During the performance of our audit procedures the following exceptions were noted:

- The Municipality's accounting system provides only for the recording of revenues, expenditures and other limited transactions. In addition, the accounting records are not integrated and do not provide for, a self balancing set of accounts for each fund operated by the Municipality, recording cash and other financial resources, together with all related assets, liabilities and residual equities or balances, and changes therein. Additionally, we noted that certain records in use were not adequately maintained.
- Accounting records do not provide for segregation between expenditures and encumbrances.

Criteria

A municipality's accounting system must make it possible to present fairly and with full disclosure the financial position and results of financial operations of the funds and account groups of the governmental unit in conformity with accounting principles generally accepted in the United States of America and determine and demonstrate compliance with finance, legal and contractual provisions as established in the Autonomous Municipalities' Law Chapter 215§ 4360.

Cause

The Municipality of Maricao has not established the accounting procedures, controls and records necessary to provide accurate information to prepare the financial statements and federal reports in conformity with accounting principles generally accepted in the United States of America, the governmental accounting and financial reporting principles issued by the Governmental Accounting Standards Board (GASB), and the related grant agreements.

Effect

Due to the deficiencies mentioned above, the examination of the general-purpose financial statements for the year ended June 30, 2011, was more difficult and less efficient than would have been in ordinary circumstances. Since the accounts and other records are not designed to provide the information as it is presented in the financial statements, was necessary to obtain such information from various departments and persons within the Municipality and from numerous accounting records, which are not integrated. This situation can cause the financial statements not to present all the assets, liabilities, revenues and expenditures of the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2011

FINDING NUMBER 11-01- (cont)

Accounting and Reporting System

Recommendation

In order to streamline the accounting and reporting systems and provide proper closing of records and adequate and timely information, we recommend the Municipality to consider the acquisition of new accounting systems. The Municipality should implement a new accounting system that allows the preparation of monthly and year-end financial statements in accordance with Accounting Principles Generally Accepted in the United States of America applicable to government entities. This plan should provide for the following:

Accounting and Reporting System

- Adequate training to all accounting personnel in order to improve the understanding of the system.
- The implementation of a double entry accounting system and the integration of all subsidiary ledgers.
- The preparation of periodic financial reports to be submitted to the Finance Director, the Mayor and the Municipal Assembly.
- Reconciliation of financial with the reports prepared and submitted to the Federal government, and the preparation of the general purpose financial statements in accordance to Accounting principles generally accepted in the United State of America.

Auditee Response

The governmental agency known as 'OCAM' who is in charge of the accounting system of the municipalities is evaluating the actual system with the intention of perhaps changing to another system. The Municipality is awaiting instructions from such agency.

III. Federal Awards Findings and Questioned Costs

Compliance findings:

Our examination of compliance with federal requirements for the Municipality of Maricao for the year ended June 30, 2011, disclosed that grants funds were generally administered in a satisfactory manner, except for the following situations:

FINDING NUMBER 11-02

General Fund

The Municipality obtained funds from the Central Government and included them in Annual Budget, but at the time of receiving the funds they were deposited into Special Funds.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2011**

FINDING NUMBER 11-02- (cont)

Criteria

In the Article 7.001 of the Law 81, as amended, establish that the Municipality will set a self balanced budget of income and expenditures. In the revised regulations on Fundamental Standards of the Municipalities of Puerto Rico, a similar provision is established.

Cause

In General Fund, the Municipality budgeted \$400,000 of allocations from the Central Government for operating expenses of the Municipality. However, when the Municipality received the funds, they were deposited in the Special Funds.

Effect

The Municipality does not follow the procedures established by federal law. It created an operational deficit of \$400,000 in General Fund.

Recommendation

Establish procedures to identify money received and deposit it in the appropriated fund according to budget.

Auditee Response

The Mayor and the Finance Director accept the recommendation of the auditor.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Schedule of Prior Year Findings and Questioned Costs
For the Year Ended June 30, 2011

| Program | Finding/ Compliance | Status |
|--|--|---------------|
| All Federal Program | Condition 07-01 Accounting and Reporting System | |
| | <p>During the performance of our audit procedures the following Exceptions were noted:</p> <ul style="list-style-type: none"> The Municipality's accounting system provides only for the recording of revenues, expenditures and other limited transactions. In addition, the accounting records are not integrated and do not provide for, a self balancing set of accounts for each fund operated by the Municipality, recording cash and other financial resources, together with all related assets, liabilities and residual equities or balances, and changes therein. Additionally, we noted that certain records in use were not adequately maintained. | Still prevail |
| All funds 2002-2007 | <p>Accounting records do not provide for segregation between expenditures and encumbrances</p> <p>Accounting System-</p> | |
| | <p>We noted that the Municipality of Maricao is not keeping an accounting system as required by General Accepted Accounting Principles.</p> | Still prevail |
| SBGP – 2002-2007 | <p>Cash Management time elapsing as required code of Federal Regulation</p> | Corrected |
| <u>Accounting and Reporting System</u> | <u>FINDING NUMBER 10-01</u> | |
| | <p>During the performance of our audit procedures the following exceptions were noted:</p> <ul style="list-style-type: none"> The Municipality's accounting system provides only for the recording of revenues, expenditures and other limited transactions. In addition, the accounting records are not integrated and do not provide for, a self balancing set of accounts for each fund operated by the Municipality, recording cash and other financial resources, together with all related assets, liabilities and residual equities or balances, and changes therein. Additionally, we noted that certain records in use were not adequately maintained. | Still prevail |
| | <p>Accounting records do not provide for segregation between expenditures and encumbrances</p> | |

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MARICAO
Schedule of Prior Year Findings and Questioned Costs
For the Year Ended June 30, 2011

| Program | Finding/ Compliance | Status |
|---------|--|----------------|
| SBGP | <u>FINDING NUMBER 10-02 - Cash Management</u> | |
| | The SBGP bank account maintained balance over program regulation. | corrected |
| | <u>FINDING NUMBER 10-03 - General Fund</u> | |
| | The Municipality obtained funds from the Central Government and included them in Annual Budget, but at the time of receiving the funds they were deposited into Special Funds. | Still prevails |