

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**



Oficina del Comisionado
de Asuntos Municipales
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**BASIC FINANCIAL STATEMENTS WITH ADDITIONAL REPORTS AND
INFORMATION REQUIRED BY THE SINGLE AUDIT ACT**

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

**HON. JORGE L. MARQUEZ PEREZ
MAYOR**

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

BASIC FINANCIAL STATEMENTS WITH ADDITIONAL REPORTS
AND INFORMATION REQUIRED BY THE SINGLE AUDIT ACT

FISCAL YEAR ENDED JUNE 30, 2012

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

BASIC FINANCIAL STATEMENTS WITH ADDITIONAL REPORTS
AND INFORMATION REQUIRED BY THE SINGLE AUDIT ACT

FISCAL YEAR ENDED JUNE 30, 2012

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PEDRO C. ORTIZ LEDEE

CERTIFIED PUBLIC ACCOUNTANT

INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and
Members of the Municipal Legislature
Municipality of Maunabo, 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 **Maunabo**, Puerto Rico (Municipality), as of and for the fiscal year ended June 30, 2012, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

The Municipality did not have a complete, updated and accurate accounting records of the capital assets in order to obtain sufficient and competent evidential matter related to the capital assets reported in the accompanying statement of net assets for \$25,701,271, net of accumulated depreciation of \$9,302,929. Also, during the fiscal year the Municipality did not recorded certain capital assets additions and did not reclassify the construction in progress in the accounting records. In addition, because of the inadequacy of the accounting records, we were unable to form an opinion regarding the capital assets reported in the accompanying statement of net assets.

The Municipality did not maintain adequate accounting records of the interfund cash transactions and the corresponding due from and due to account balances. We were unable to obtain sufficient evidence to support and satisfy ourselves about the amounts recorded in the interfund balances in the amount of \$1,651,834, recorded in each major fund and the aggregate remaining fund in the Balance Sheet of the governmental funds.

Because of the significance of the matter discussed in the third paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial position of the governmental activities of the Municipality at June 30, 2012, or the changes in financial position, thereof for the year then ended.

In addition, in our opinion, except for the effects of such adjustments, if any as might have been determined to be necessary regarding the interfund transactions of each major fund and the aggregate remaining fund information, as described in the fourth paragraph, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2012, and the respective changes in financial position thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

In accordance with *Government Auditing Standards*, we have also issued our report dated March 30, 2013, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the budgetary comparison information on pages 3 through 11 and 50 through 51 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's financial statements as a whole. The accompanying schedule of expenditures of federal awards 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 financial statements. The schedule of expenditures of federal awards is the responsibility of management and was derived from and relate directly to underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

P.C. Ortiz Ledee

Pedro C. Ortiz Ledee, CPA
License Number 5200

Guayama, Puerto Rico
March 30, 2013



COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Management of the Municipality of **Maunabo**, Puerto Rico (Municipality) provides this *Management's Discussion and Analysis* (MD&A) to: (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 plan (its ability to address the next subsequent year challenges), (d) identify any material deviations from the financial plan (the approved budget), and (e) identify individual fund issues or concerns. The Management's Discussion and Analysis "MD&A" is focused on the current year activities, resulting changes and currently known facts; therefore, it should be read in conjunction with the Municipality's Basic Financial Statements. This MD&A will provide comparable information to the readers with the Municipality's prior year financial statements. Also, it can assist readers to get more specific understanding of the financial activities regarding the Municipality's Basic Financial Statements for the fiscal year ended June 30, 2012.

FINANCIAL HIGHLIGHTS

The Municipality's Net Assets for the year ended on June 30, 2012 were \$11,158,249 in comparison with the fiscal year 2010-2011 which was \$12,077,852, as restated, a \$(919,603) decreased.

The Municipality's Government Wide Financial Statements show that governmental activities revenues were \$13,385,631 for the fiscal year ended June 30, 2012 in comparison with the prior fiscal year that were \$15,164,516, a decrease of \$1,778,885. The difference is mainly caused in the General Revenues that reported \$1,106,290, less than fiscal year 2010-2011.

The General Fund showed a net change in Fund Balance of \$(698,570) during the course of this year, in comparison with fiscal year 2010-2011 that showed a net change in Fund Balance of \$927,373. The current year revenues were not enough to comply with Municipality's current obligation.

The governmental activities expenditure for the current fiscal year were \$14,305,234, in comparison with the fiscal year ended June 30, 2011 that reported expenditures of \$15,922,176, a decrease over last fiscal year of \$1,616,942. The General Fund total expenditures for the current fiscal year showed a decrease of \$23,773 with the last year's expenditure balance.

USING THIS ANNUAL REPORT

This annual report consists of three components: 1) Management Discussion and Analysis (this section), 2) Basic Financial Statements, and 3) Required Supplementary Information.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the Municipality's financial statements. The Municipality's basic financial statements comprise three components: government-wide financial statements; fund financial statements; and notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide readers with a broad overview of the Municipality's finances, in a manner similar to a private-sector business.

The Statement of Net Assets presents information on all of the Municipality's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

The Statement of Activities presents information showing how the Municipality's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods.

Both of the government-wide financial statements of the Municipality are principally supported by taxes and intergovernmental revenues. The governmental activities of the Municipality include general government, public safety, public works, culture and recreation, health and sanitation, human services and welfare, urban development and education. Property taxes, municipal license tax, state and federal grants finance most of these activities.

FUND FINANCIAL STATEMENTS

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 other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

GOVERNMENTAL FUNDS

The entire Municipality's basic service are reported in the governmental funds, which focus in how money flows out of those funds and the balances left at year-end that are available for future spending. Consequently, the governmental fund financial statements provide a detailed short-term view of the Municipality general information, general operation and the basis service it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs.

These funds are reported using modified accrual basis of accounting, which measures cash and all other financial assets that can readily be converted to cash. Under this method, revenues are recognized when measurable and available. Expenditure is generally recognized when the related fund liability is incurred. This is the manner in which these funds are normally budgeted.

Since the governmental fund statements (current financial resources) are presented on a different measurement focus and basis of accounting than government-wide statements (total economic resources), a reconciliation of the differences are reflected on the page following each statements. The flow of current financial resources will reflect bond proceeds and inter-fund transfer as other financing sources as well as capital expenditure and bond principal payments as expenditure. The reconciliation will eliminate these transactions and incorporate the capital assets and long-term obligation (bonds and other) into the Governmental Activities column (in the Government-Wide Statements).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

INFRASTRUCTURE ASSETS

GASB Statements Number 34 requires that the infrastructure assets be valued and reported within the Governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of assets management designed to maintain the service delivery potential to near perpetuity. If the governmental develops the assets management system (the alternative method), which periodically (at least every third year), by category, measures and demonstrates its maintenance of locally established condition levels, the government may record all expenditure incurred (except for additions and improvements which extend the asset life) in lieu of depreciation. While the Municipality has acquired an asset management system which a) would allow the election to use the alternative methods, and b) will provide valuable management information. Actually the Municipality is not recording in the accounting records the infrastructure assets.

CAPITAL ASSETS INVESTMENTS

During the fiscal year the Municipality did not update its capital assets subsidiary. The depreciation expense was \$ 979,480 for fiscal year 2011-2012. The capital assets at June 30, 2012 consist mainly of construction in progress, buildings, improvements, and infrastructure. Total Investment in Capital Assets, net of related debt was \$16,447,271.

LONG-TERM DEBT

At June 30, 2012 the Municipality had a total of \$14,687,001 in general obligations and others outstanding debts, as shown in **Table 1**. Of this amount, \$8,335,000 comprises debt backed by the full faith and credit of the government and \$6,352,001 are other obligations.

Long Term Debts	Amount
General obligations	\$ 8,335,000
Section 108 Guaranteed Loan	2,499,000
Others	<u>3,853,001</u>
Total Long Term Debts	<u>\$ 14,687,001</u>

The Municipality is required to limit the amount of general obligation debt to 10% of the total assessment of property located within the Municipality in order for the bonds to be repaid with the proceeds of property taxes restricted for debt services. Other obligations include accrued vacation and sick leave, debt agreements, advances of property taxes and others. More detailed information about the Municipality's long-term liabilities is presented in the notes to the financial statements. The Municipality continues to meet its financial needs through prudent use of its revenues and creative debt financing programs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINANCIAL ANALYSIS OF THE GOVERNMENT AS A WHOLE

GOVERNMENT-WIDE FINANCIAL ANALYSIS

GOVERNMENTAL NET ASSETS

The net assets of the Municipality decreased by \$(919,603) during the current fiscal year. The Municipality's net assets include investments in Capital Assets for \$16,447,271, net of related debt, and over \$3,052,983 restricted for future expenses. The Municipality's net assets at the end of the fiscal year ended on June 30, 2012 were \$11,158,249, as detailed on **Table 2**.

Table 2			
Statement of Net Assets	2012	2011	
Current and non-current assets	\$ 3,567,900	\$ 3,259,273	
Capital assets	<u>25,701,271</u>	<u>26,680,751</u>	
Total Assets	<u>29,269,171</u>	<u>29,940,024</u>	
Current liabilities	3,423,921	3,156,597	
Long-term liabilities	<u>14,687,001</u>	<u>14,705,575</u>	
Total Liabilities	<u>18,110,922</u>	<u>17,862,172</u>	
Net assets:			
Investment in capital assets, net of related debt	16,447,271	16,887,751	
Restricted	3,052,983	2,436,707	
Deficit	<u>(8,342,005)</u>	<u>(7,246,606)</u>	
Total Net Assets	<u>\$ 11,158,249</u>	<u>\$ 12,077,852</u>	

NORMAL IMPACTS

There are six basic (normal) transactions that will affect the comparability of the Net Assets summary presentation.

- **Net Results of Activities** – This will impact (increase/decrease) current assets and unrestricted net assets.
- **Borrowing for Capital** – This will increase current assets and long-term debts.
- **Spending Borrowed Proceeds to Paid Statutory Costs** – This will increase current assets and increase current liabilities. There is a second impact, an increase in total liabilities. The Municipality issued two general obligation bonds to paid statutory costs as: Internal Revenue Service, Retirement and Other Operational Costs.
- **Spending of Non-borrowed Current Assets on New Capital** – This will (a) reduce current assets and increase capital assets and (b) will reduce unrestricted net assets and increase invested in capital assets, net of debt.
- **Principal Payment on Debt** – This will (a) reduce current assets and reduce long-term and (b) reduce unrestricted net assets and increase invested in capital assets, net of debt.
- **Reduction of Capital Assets through Depreciation** – This will reduce capital assets and invested in capital assets, net of debt.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

CURRENT YEAR IMPACTS

The following schedule (as detailed on **Table 3**) presents the revenues and expenses for the current fiscal year:

Table 3			
Statement of Activities (in thousands)	2012	2011	
Revenues			
Operating grants and contributions	\$ 1,960,875	\$ 2,856,759	
Capital grants and contributions	2,191,828	1,943,364	
General revenues:			
Property taxes	1,158,698	1,194,574	
Volume of business taxes	157,768	230,654	
Sales taxes	662,321	770,412	
Licenses and permits	282,451	1,150,948	
Intergovernmental	6,011,454	5,711,721	
Charges for services	733,091	758,266	
Other General revenues	227,145	547,818	
Total revenues	13,385,631	15,164,516	
Expenses			
Mayor and Municipal Legislature	284,879	292,075	
General Government	3,309,305	3,931,800	
Public safety	576,821	571,994	
Public works	3,243,325	3,160,831	
Health and sanitation	2,435,782	2,394,013	
Culture and recreation	1,305,917	864,889	
Human services and welfare	1,529,317	1,321,404	
Urban development	1,200,075	2,196,605	
Education	143,152	993,767	
Interest on long-term debts	276,661	194,798	
Total expenses	14,305,234	15,922,176	
Changes in net assets	(919,603)	(757,660)	
Net assets – beginning, as restated	12,077,852	12,835,512	
Net assets – ending	\$ 11,158,249	\$ 12,077,852	

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NORMAL IMPACTS

There are some impacts on revenues and expenses as reflected below.

REVENUES:

- **Economic Condition** – which can reflect a declining, stable or growing economic environment and has substantial impact on property and volume tax revenues as well as public spending habits for building permits, elective user fees and volumes of consumption.
- **Construction Permits** – decreased due to a recession in construction projects in the Municipality.
- **Intergovernmental Revenues** – increased due to a Puerto Rico Electric Power Authority Compensation.
- **Federal Grants and Contributions** – increased mainly due to the reduction of State and Federal Governments contributions to the Municipality.

EXPENSES:

- **Introduction of New Programs** – within the functional expenses categories individual programs may be added or deleted to meet changing community needs.
- **Increase/Decrease in Authorized Personnel** – changes in service demand may cause the Municipality to increase/decrease authorized staffing. Staffing cost (salary and related benefits) represent approximately 60% of the Municipality's operating cost in the General Fund.
- **Salary Increase (cost of living, merit and market adjustments)** – the ability to attract and retain human and intellectual resources requires the Municipality to strive to approach a competitive salary range position in the marketplace.
- **Inflation** – while overall inflation appears to be reasonably modest, the Municipality is a major consumer of certain commodities such as chemical and supplies, fuels and parts. Some functions may experience unusual commodity specific increases.

REAL ESTATE HELD FOR SALE

On July 6, 2009, the Municipality enter into an agreement with the Commissioner of Municipal Affairs to participated in a construction of a eight apartments building, for low and very low income families, financed with funds provided by Neighborhood Stabilization Program. At June 30, 2012, real estate held for sale presented in the governmental wide statement of net assets, related to these constructions, amounted \$821,489.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

The Municipality uses fund accounting to ensure and demonstrate compliance with related legal and contractual requirements.

Table 4			
Balance Sheet (in thousands)	2012	2011	
Assets:			
Total assets – Major Funds	\$ 2,790,373	\$ 2,168,455	
Total assets – Other Funds	<u>1,607,872</u>	<u>2,487,605</u>	
Combined total assets	<u>4,398,245</u>	<u>4,656,060</u>	
Liabilities:			
Total liabilities – Major Funds	4,305,283	3,071,151	
Total liabilities – Other Funds	<u>887,237</u>	<u>1,911,150</u>	
Combined total liabilities	<u>5,192,520</u>	<u>4,982,301</u>	
Fund Balances (As Restated):			
Restricted	2,099,196	1,902,912	
Committed	132,298	-	
Unassigned	<u>(3,025,769)</u>	<u>(2,229,153)</u>	
Combined total fund balances	<u>(794,275)</u>	<u>(326,241)</u>	
Total liabilities and fund balances	\$ 4,398,245	\$ 4,656,060	

Table 5			
Changes in Fund Balances (in thousands)	2012	2011	
Revenues:			
Total revenues – Major Funds	\$ 11,038,734	\$ 12,493,052	
Total revenues – Other Funds	<u>2,247,607</u>	<u>2,653,989</u>	
Combined total revenues	<u>13,286,341</u>	<u>15,147,041</u>	
Expenditures:			
Total expenditures – Major Funds	12,443,374	12,670,719	
Total expenditures – Other Funds	<u>2,171,001</u>	<u>3,284,559</u>	
Combined total expenditures	<u>14,614,375</u>	<u>15,955,278</u>	
Other financing sources (uses):			
Proceed from issuance of bonds	860,000	-	
Transfer – In	401,232	1,117,817	
Transfer – Out	<u>(401,232)</u>	<u>(1,117,817)</u>	
Combined other financing sources (uses), net	<u>860,000</u>	<u>-</u>	
Net changes in fund balance	(468,034)	(808,237)	
Fund Balance – beginning, as restated	<u>(326,241)</u>	<u>481,996</u>	
Fund Balance – ending	\$ (794,275)	\$ (326,241)	

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

GOVERNMENT FUNDS

The Municipality's Governmental Funds information is useful in assessing the Municipality's financial requirements. At the end of the fiscal year any resource available for spending should be measured by the unassigned fund balance. In the current fiscal year, the Municipality's Governmental Funds reported an ending deficit of \$(794,275).

Restricted and committed fund balance is to cover balances show as follows:

- \$101,835 are restricted to other purpose in general fund;
- \$1,409,024 are restricted to pay debt services;
- \$720,635 are committed (\$30,463) and restricted (\$690,172) for other governmental purpose.

The Municipality's Governmental Funds include the General Fund, which is the Major Operation Fund of the Municipality and as of June 30, 2012, it showed an unassigned deficit of \$(3,025,769). This deficit was caused by the excess of expenditures over revenues during the past years.

GENERAL FUND BUDGETARY HIGHLIGHTS:

The Budgetary Comparison Schedule for budgeted and actual amounts from General Fund is presented in the Municipality's Basic Financial Statement. These schedules show the original adopted budget, the final revised budget, actual results, and variances between final and actual budgeted amounts for the General Fund. An original budget is presented by the Mayor and approved by the Municipality's Legislative Body in an ordinary session, but it may be revised for various reasons and circumstances, or due to unanticipated budgeted issues that arise during the normal course of the fiscal year.

ECONOMIC FACTOR AND NEXT YEAR'S BUDGETS

The Municipality relies primarily on Intergovernmental Revenues as well as Federal Financial Assistance to carry out the Governmental Activities. Historically, these amounts have been predictable for every fiscal year, providing the Municipality with yearly increases. Federal Financial Assistance may vary if new grants are available, but revenue is also predictable.

Local, national and international economics factors may influence the Municipality's revenues, positively or negatively. Positive economic grow is correlated with increased revenues from property taxes, volume of business tax, charges for services, as well as State and Federal Grants. In a local economy, the growth may be monitored by a variety of indicators such as employment growth, unemployment, new constructions, assessed valuation, and other revenues.

All these factors will be considered when preparing the budget for the year ending on June 30, 2012, as well as the increases in property and volume of business tax rates that will be in effect for that fiscal year.

FINAL COMMENTS

On June 16, 2011 the Legislature of the Commonwealth of Puerto Rico approved Act No. 94, to establish an incentive plan for the payment of real and personal property tax dues. This Act provides an amnesty to all property tax payers forgiving all penalties, charges and interests of the unpaid principal of pass-due property tax liability. The period that tax payers have to enjoy for such benefit is for exactly ninety (90) days, beginning during fiscal year 2011-2012.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINAL COMMENTS

On August 11, 2011 the Municipality issued a Special Note in the amount of \$255,000, for the payment of a debt with the Internal Revenue Service. This bond is payable with resources collected through the Municipal Redemption Fund.

CONTACTING THE MUNICIPALITY'S OFFICE OF FINANACIAL MANAGEMENT

This report is designed to provide a general overview of the Municipality's finances and to demonstrate the accountability for the money it receives. If you have any questions about this report or need additional information, contact the Municipality's Finances Department at (787) 861-0825.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

STATEMENT OF NET ASSETS
June 30, 2012

	<u>Governmental Activities</u>
ASSETS:	
Cash	\$ 44,429
Cash with Fiscal Agent	1,884,561
Receivables (net):	
Property Tax	121,347
Sales Tax	66,229
Intergovernmental	180,153
Federal Grants	433,245
Others	16,447
	<u>2,746,411</u>
Real Estate Held for Sale	<u>821,489</u>
Capital Assets:	
Land, Work of Arts, and Construction in Progress	13,863,263
Other Capital Assets, Net of Depreciation	11,838,008
Total Capital Assets	<u>25,701,271</u>
TOTAL ASSETS	<u>29,269,171</u>
LIABILITIES:	
Bank Overdraft	227,804
Accounts Payable and Accrued Expenses	1,574,816
Bonds Payable	265,000
Accrued Interest	109,520
Due to Governmental Units	614,346
Deferred Revenue:	
Volume of Business Tax	119,890
Federal Grants	512,545
Long-Term Liabilities:	
Due within One Year	1,385,410
Due in More than One Year	13,301,591
TOTAL LIABILITIES	<u>18,110,922</u>
NET ASSETS	
Invested in Capital Assets, Net of Related Debt	16,447,271
Restricted for:	
Debt Service	1,409,024
Others Purposes	1,643,959
Unrestricted	(8,342,005)
TOTAL NET ASSETS	<u>\$ 11,158,249</u>

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
Mayor and Municipal Legislature	\$ 284,879	\$ -	\$ -	\$ -	\$ (284,879)
General Government	3,309,305	-	-	-	(3,309,305)
Public Safety	576,821	-	52,485	-	(524,336)
Public Works	3,243,325	-	-	-	(3,243,325)
Culture and Recreation	1,305,917	-	-	90,270	(1,215,647)
Health and Sanitation	2,435,782	730,829	663,391	-	(1,041,562)
Human Services and Welfare	1,529,317	-	552,516	-	(976,801)
Urban Development	1,200,075	-	-	2,101,558	901,483
Education	143,152	2,262	692,483	-	551,593
Interest on Long-Term Debt	276,661	-	-	-	(276,661)
Total Governmental Activities	\$ 14,305,234	\$ 733,091	\$ 1,960,875	\$ 2,191,828	(9,419,440)

General Revenues:

Taxes:

Property, levied for General Purposes	895,939
Property, levied for Debt Services	262,759
Volume of Business	157,768
Sales, levied for Special Purposes	364,567
Sales, levied for Debt Services	297,754
Intergovernmental	6,011,454
Rent	101,636
Licences and Permits	282,451
Miscellaneous	125,509
Total General Revenues	<u>8,499,837</u>

CHANGE IN NET ASSETS

(919,603)

Net Assets - Beginning of Year - Restated

12,077,852

NET ASSETS - END OF YEAR

\$ 11,158,249

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO
BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2012

	General Fund	Debt Service Fund	Municipal Hospital Fund	Community Development Block Grant Funds	Other Governmental Funds	Total Governmental Funds
ASSETS:						
Cash	\$ -	\$ -	\$ 1,447	\$ 29,908	\$ 13,074	\$ 44,429
Cash with Fiscal Agent	101,835	1,749,030	-	-	33,696	1,884,561
Receivables:						
Property Tax	116,765	4,582	-	-	-	121,347
Sales Tax	-	29,932	-	-	36,297	66,229
Intergovernmental	-	-	117,842	-	62,311	180,153
Federal Grants	-	-	-	170,573	262,672	433,245
Due from Other Funds	173,488	-	75,233	203,291	1,199,822	1,651,834
Others	16,447	-	-	-	-	16,447
Total Assets	\$ 408,535	\$ 1,783,544	\$ 194,522	\$ 403,772	\$ 1,607,872	\$ 4,398,245
LIABILITIES AND FUND BALANCES:						
Liabilities:						
Bank Overdraft	\$ 205,913	\$ -	\$ -	\$ -	\$ 21,891	\$ 227,804
Accounts Payable and Accrued Expense Liabilities	963,953	-	194,522	288,310	128,031	1,574,816
Bonds and Notes Payable	-	265,000	-	-	-	265,000
Accrued Interest	-	109,520	-	-	-	109,520
Due to Governmental Units	614,346	-	-	-	-	614,346
Due to Other Funds	1,311,602	-	-	71,593	268,639	1,651,834
Deferred Revenue:						
Volume of Business Tax	119,890	-	-	-	-	119,890
Federal Grants	-	-	-	43,869	468,676	512,545
Property Taxes	116,765	-	-	-	-	116,765
Total Liabilities	3,332,469	374,520	194,522	403,772	887,237	5,192,520
Fund Balances:						
Restricted	-	1,409,024	-	-	690,172	2,099,196
Committed	101,835	-	-	-	30,463	132,298
Unassigned	(3,025,769)	-	-	-	-	(3,025,769)
Total Fund Balances	(2,923,934)	1,409,024	-	-	720,635	(794,275)
TOTAL LIABILITIES AND FUND BALANCES	\$ 408,535	\$ 1,783,544	\$ 194,522	\$ 403,772	\$ 1,607,872	\$ 4,398,245

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	General Fund	Debt Service Fund	Municipal Hospital Fund	Community Development Block Grant Funds	Other Governmental Funds	Total Governmental Funds
REVENUES						
Property Taxes	\$ 796,649	\$ 262,759	\$ -	\$ -	\$ -	\$ 1,059,408
Sales Tax	-	297,754	-	-	364,567	662,321
Volume of Business Taxes	157,768	-	-	-	-	157,768
Federal Assistancess	-	-	-	1,609,881	1,148,698	2,758,579
Intergovernmental	6,011,454	-	662,044	-	723,125	7,396,623
Charges for Services	-	-	730,829	-	2,262	733,091
Licenses and Permits	282,451	-	-	-	-	282,451
Rent	101,636	-	-	-	-	101,636
Miscellaneous	125,509	-	-	-	8,955	134,464
Total Revenues	7,475,467	560,513	1,392,873	1,609,881	2,247,607	13,286,341
EXPENDITURES						
Current:						
Mayor and Municipal Legislature	124,901	-	-	-	-	124,901
General Government	3,752,389	-	-	-	1,400	3,753,789
Public Safety	105,191	-	-	-	398,876	504,067
Public Works	2,820,959	-	-	-	-	2,820,959
Culture and Recreation	543,682	-	-	21,223	684,372	1,249,277
Health and Sanitation	648,946	-	1,716,124	-	-	2,365,070
Human Services and Welfare	581,973	-	-	685,930	643,521	1,911,424
Urban Development	-	-	-	824,747	375,328	1,200,075
Education	143,152	-	-	-	-	143,152
Debt Service:						
Principal	-	265,000	-	-	-	265,000
Interest and Other Charges	-	209,157	-	-	67,504	276,661
Total Expenditures	8,721,193	474,157	1,716,124	1,531,900	2,171,001	14,614,375
Excess (deficiency) of revenues over (under) expenditures	(1,245,726)	86,356	(323,251)	77,981	76,606	(1,328,034)
OTHER FINANCING SOURCES (USES)						
Proceed of Bonds	860,000	-	-	-	-	860,000
Transfers - In	10,407	-	323,251	-	67,574	401,232
Transfers - Out	(323,251)	-	-	(77,981)	-	(401,232)
Total Other Financing Sources and Uses	547,156	-	323,251	(77,981)	67,574	860,000
Net Change in Fund Balances	(698,570)	86,356	-	-	144,180	(468,034)
Fund Balance - Beginning as Restated	(2,225,364)	1,322,668	-	-	576,455	(326,241)
Fund Balances - Ending	\$ (2,923,934)	\$ 1,409,024	\$ -	\$ -	\$ 720,635	\$ (794,275)

*OK
03/04/2013*

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Total Fund Balances – Governmental Funds **\$ (794,275)**

Amounts reported for Governmental Activities in the Statement of Net Assets are different because:

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

Non Depreciable Capital Assets	\$ 13,863,263
Depreciable Capital Assets.....	12,902,846
Infrastructure Assets	8,238,091
Accumulated Depreciation	<u>(9,302,929)</u>

Total Capital Assets..... **25,701,271**

Real Estate Held for Sale is not a current financial resource and
Therefore, is not reported in the funds **821,489**

The Municipal Revenue Collection Center revenues will be collected
Year end, but are not available soon enough to pay for the current period's
Expenditure and therefore, are deferred in the funds..... **116,765**

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

General Bonds and Notes Payable.....	8,335,000
Compensated Absences.....	1,558,486
Property Tax Debt – Law 42	1,224,159
Section 108 Guaranteed Loan.....	2,499,000
State Aqueduct and Sewer Authority – debt agreement.....	255,000
State Department of Labor- debt agreement	21,780
State Retirement System Administration- debt agreement.....	<u>793,576</u>
Total Long-Term Liabilities	<u>(14,687,001)</u>

Total Net Assets of Governmental Activities **\$ 11,158,249**

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

RECONCILIATION OF STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES TO
STATEMENT OF ACTIVITIES

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Net Change in Fund Balances – Total Governmental Funds		\$ (468,034)
Amounts reported for Governmental Activities in the Statement of Activities are different because:		
Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. In the current period, these amounts are:		
Urban Development and Capital Outlay	\$ -	
Depreciation Expense.....	<u>(979,480)</u>	
Excess of Capital Outlay over Depreciation Expense.....		(979,480)
Governmental Funds reports capital outlay of real property held for sale as expenditure. However, in the Statement of Activities, the cost of those assets is capitalized.....		450,905
Revenues in the Statement of Activities that not provide current financial resources are not Reported as revenues in the funds.....		116,765
Revenues in the Statement of Revenues that correspond to prior year resources are Recorded as revenue in the Statement of Activities		(17,475)
Repayment of debt proceeds principal is expenditure in the governmental funds, but the repayment reduces Long-Term Liabilities in the Statement of Net Assets. In the current year the repayments were.....		265,000
Bonds proceeds provide current financial resources to governmental funds, but issuing debt Increase long-term liabilities in the Statement of Net Assets, in the current period, Proceed received was		(860,000)
Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:		
Increase in Compensated Absences	(15,105)	
Increase in State Aqueduct and Sewer Authority – Debt Agreement	(128,858)	
Decrease in Property Tax Debt – Law 42	29,092	
Decrease in LIMS Repayment Plan.....	5,043	
Decrease in CRIM Settlement	33,762	
Decrease in Section 108 Guaranteed Loan.....	167,000	
Decrease in State Department of Labor- Debt Agreement	12,812	
Decrease in Retirement System Administration – Debt Agreement	<u>468,970</u>	
Total Additional Expenditures		<u>572,716</u>
Change in Net Assets of Governmental Activities		\$ (919,603)

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTE TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of **Maunabo**, Puerto Rico (Municipality) was founded in the year 1799, and operates as a local governmental unit of the Commonwealth of Puerto Rico, under the Law Number 81 of August 30, 1991, known as "Autonomy Municipalities Law of the Commonwealth of Puerto Rico". The governmental system of the Municipality is composed of the executive and legislative bodies. The Mayor is the Chief Executive Officer and is elected every four years in the general elections of the Commonwealth of Puerto Rico. The legislative body consists of 12 Legislators also elected in the general elections of Puerto Rico for a four-year period. The General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality, exercises the judiciary power.

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

The accounting policies of the Municipality conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The following is a summary of the more significant policies.

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

In June 1999, GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB No. 34). This statement established new financial reporting requirements for state and local governments. The Municipality adopted the provisions of GASB No. 34 as well as other statements referred to below.

The accompanying basic financial statements present the financial position and the results of operations of the Municipality and its various funds and fund types. The basic financial statements are presented as of June 30, 2012, and for the fiscal year then ended. The more significant of these accounting policies are described below and, where appropriate, subsequent pronouncements will be referenced.

According to the financial reporting model established by GASB No. 34, the minimum required financial statement presentation applicable to the Municipality is composed of the following elements: (1) government-wide financial statements (GWFS), (2) governmental fund financial statements (GFFS), (3) notes to basic financial statements, and (4) required supplementary information (RSI).

The required supplementary information, which consists of a management discussion and analysis (MD&A), is information presented along with, but separate from, the Municipality's basic financial statements. The MD&A is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the year ended June 30, 2012, based on the Municipality's knowledge of the transactions, events and conditions reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Other statements and interpretations were also adopted in conjunction and simultaneously with GASB No. 34. Those statements and interpretations are: (1) GASB Statement No. 33 – *Accounting and Financial Reporting for Nonexchange Transactions*, (2) GASB Statement No. 37 – *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, (3) GASB Statement No. 38 – *Certain Financial Statement Note Disclosures* and (4) GASB Interpretation No. 6 – *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

GASB No. 34 also required that the accounting for all governmental activities reported in the GWFS be based on applicable pronouncements issued by the Financial Accounting Standards Board (FASB) and its predecessor bodies, such as the Accounting Principles Board (APB), issued on or before November 30, 1989, provided those pronouncements do not conflict with or contradict GASB pronouncements. Accordingly, in conjunction and simultaneously with the adoption of GASB No. 34, the Municipality also adopted the following pronouncements: (1) APB Opinion No. 20 – *Accounting Changes*, (2) APB Opinion No. 21 – *Interest on Receivables and Payables*, (3) FASB Statement No. 5 - *Accounting for Contingencies* and (4) FASB Statement No. 16 – *Prior Period Adjustments*. The Municipality has elected to not apply all statements and interpretations issued by FASB after November 30, 1989.

The Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which modified the interpretations of certain terms within the definition of the special revenue funds and the types of activities the Municipality may choose to report in those funds. GASB No. 54 also clarified the capital projects fund type definition for better alignment with the needs of preparers and users. Definitions of other governmental fund types were also modified for clarity and consistency.

A. Financial Reporting Entity

The accompanying basic financial statements include all departments and organizations units whose funds are under the custody and control of the Municipality. In evaluating the Municipality as a reporting entity, management has addressed all the potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of GASBS No. 14.

The basic criteria for including a potential component unit within the reporting entity is if potential component units are financially accountable and other organizations for which the nature and significance of their relationship with the entity are such that exclusion would cause the Municipality's financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) ability of the Municipality to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Municipality.

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

These financial statements present the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2012, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

B. Measurement Focus and Basis of Accounting

Government-Wide Financial Statements

The government-wide financial statements (the Statement of Net Assets and the Statement of Activities) are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grant and similar items are recognized as revenue as soon as all eligibility requirements have been met.

Governmental Fund Financial Statements

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recorded when susceptible to accrual; as soon as it is both measurable and available. "Available" means collectible within the current period or soon enough thereafter, normally within sixty (60) days, to be used to pay liabilities of the current period. Expenditures are generally recognized when the related liability is incurred.

The exception to this general rule is the principal and interest on general obligation long-term debt and compensated absences, if any, are recognized when due.

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

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

Expenditures are generally recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include the following:

- ❖ Employee's vested annual vacation and sick leave is recorded as expenditure when utilized. The amount of accumulated annual vacation and sick leave unpaid at June 30, 2012, has been reported only in the government-wide financial statements.

C. Financial Statement Presentation

The basic financial statements include both government-wide (based on the Municipality as a whole) and fund financial statements. While the previous financial reporting model emphasized fund types (the total of all funds of a particular type), in the new financial model the focus is on either the Municipality as a whole, or major individual funds (within the basic financial statements). Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as either governmental or business type.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

Government-Wide Financial Statements

The government-wide financial statements (the Statement of Net Assets and the Statement of Activities) report information of all the activities of the Municipality. For most part, the effect of interfund activity has been removed from these government-wide financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The focus of the Statement of Net Assets is designed to be similar to bottom line results for the Municipality and its governmental activities. This statement, for the first time, combines and consolidates governmental fund's current financial resources (short-term expendable resources) with capital assets and long-term obligations.

The Statement of Net Assets presents the reporting entities' assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- ❖ **Invested in Capital Assets, Net of Related Debt** – These consists 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 results when constraints are placed on net assets use, which can be either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- ❖ **Unrestricted Net Assets** – These consists of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

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

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

A function/program describes a group of activities that are aimed at accomplishing a major service or regulatory responsibility. The functions/programs reported in the accompanying basic financial statements are: (1) mayor and municipal legislature, (2) general government, (3) public safety, (4) public works, (5) culture and recreation, (6) health and sanitation, (7) human services and welfare, (8) urban development and, (9) education. The governmental operations of the Municipality's departments and operational units are classified within the following functions/programs in the accompanying basic financial statements:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

Mayor and municipal legislature:

Municipal legislature
Mayor's office

General government:

Department of finance
Department of human resources
Department of municipal secretary
Department of internal audit
Administration

Public safety:

Department of emergency management – civil defense

Public works:

Department of public works

Culture and recreation:

Department of sports and recreation
Department tourism and promotion

Health and sanitation:

Department of recycling services
Department of health
Municipal hospital

Human service and welfare:

Youth services
Municipal service center
Multiple services
Public housing

Urban development:

Federal programs office

Education:

Educational services
Child Care Program

The statement of activities demonstrates the degree to which program revenues offset direct expenses of a given function/program or segments. Direct expenses are those that are clearly identifiable with a specific function, segment or operational unit. This statement reports revenues in three broad categories: (1) program revenues, (2) general revenues and, (3) special items.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

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

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

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

Special items – These items consist of revenues arising from significant transactions or other events within the control of management that are either unusual in nature or infrequent in occurrence.

Extraordinary items consist of revenues arising from significant transactions or other events that are both unusual in nature and infrequent in occurrence.

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

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

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

The Municipality has operations and activities that are financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public (expenses, including depreciation) is financed primarily through user charges; and where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Governmental Fund Financial Statements

The fund financial statements (the Balance Sheet and the Statement of Revenues, Expenditures, and Changes in Fund Balances) are, in substance, very similar to the financial statements presented in the financial reporting model before the implementation of the GASB No. 34. Emphasis here is on the major funds in the governmental category. Non-major funds are summarized into a single column.

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is on Major Funds, rather than the previous financial model's fund types. The Governmental Major Fund Statements are presented on current financial resources and modified accrual basis of accounting.

This is the manner in which these funds are normally budgeted. This presentation deemed most appropriate to (a) demonstrate legal and covenant compliance, (b) demonstrate the source and use of liquid resources, and (c) demonstrate how the Municipality's actual experience conforms to the budgeted fiscal plan.

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

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

The model as defined in GASBS No. 34 established criteria (percentage of the assets, liabilities, revenues, or expenditures/expenses of either fund category in the governmental fund) for the determination of major funds. The non-major funds are combined in a single column in the fund financial statements. The Municipality reports the following major funds:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

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

Debt Service Fund – This is the fund used to account for the accumulation of resources for and the payment of, general long-term debt principal, interest, and related costs.

Municipal Hospital Fund – This is the fund used to account for all the transactions of the Municipality's hospital. The primary objectives of this fund is to provide to the community medical services such as emergency doctors and others.

Community Development Block Grant Funds – is used to account for revenues derived from the Department of Housing and Urban Development grants, related to Community Development Block Grants. During the current fiscal year the CDBG funds included in this major fund are CDBG State, Neighborhood Stabilization Program (NSP) and Disaster Recovery.

GASBS No. 34 eliminates the presentation of Account Groups, but provides for these records to be maintained and incorporates the information into the Governmental column in the Government-Wide Statement of Net Assets.

D. Financial Reporting Presentation

The accounts of the Municipality are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures.

The Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which modified the interpretations of certain terms within the definition of the special revenue funds and the types of activities the Municipality may choose to report in those funds. GASB No. 54 also clarified the capital projects fund type definition for better alignment with the needs of preparers and users. Fund types are as follows:

General Fund – is the Municipality main operating fund used to account for and report all financial and reported resources and governmental activities, except for those required to be accounted for in another fund. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) USGAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund. Its revenues consist mainly of taxes, licenses and permits, intergovernmental, charges for services and other.

Special Revenue Fund – is a governmental fund used to account for and report the proceeds of specific revenue sources that are legally restricted, committed or assigned to expenditure for specified purposes other than debt service or capital projects. Resources restricted or committed to expenditure for purposes normally financed from the general fund are generally accounted for in the general fund provided that all applicable legal requirements can be appropriately satisfied and the use of special revenue funds is not required unless they are legally mandated.

Debt Service Fund – is a governmental fund used to account for and report for the accumulation of financial resources that are restricted for, and the payment of, principal and interest for: (1) bonds payable for which debt service payments are legally mandated to be accounted for in a debt service fund and (2) certain special long-term obligations for which the Municipality is being accumulating financial resources in advance to pay principal and interest payments maturing in future years.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. Financial Reporting Presentation (Continued)

Capital Projects Fund – is a governmental fund used to account for and report financial resources that are restricted, committed or assigned to expenditure for capital outlays, including the acquisition or construction of major capital facilities, including those outlays financed by the general obligation bond proceeds (other than those financed by proprietary funds or in trust funds for individuals, private organizations, or other governments). The use of the capital projects funds has been limited to only for major capital acquisitions, construction or improvement activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalizable assets (such as furniture, office equipment, vehicles and other minor capital assets or improvements) have been reported in the governmental fund from which financial resources were used for the payment.

E. Fund Balances

According to the provisions of GASB No. 54, the fund balances are reported in five categories:

- ❖ **Nonspendable** – Amounts that cannot be spent because they are: a) not in spendable form or b) legally or contractually required to be maintained intact. Due to the nature or form of the resources, they generally cannot be expected to be converted into cash or a spendable form.
- ❖ **Restricted** – Amounts are restricted by external parties (creditors, grantors, contributors or law/ regulations) of other governments or restricted by law through constitutional provisions or enabling legislation.
- ❖ **Committed** – Amounts that can only be used for a specific purpose pursuant to constraints imposed by formal action (ordinances or resolutions) of the Municipality's highest level of decision making authority (Municipal Legislature). The formal action must occur prior to the end of the reporting period, however, the amount may be determined in the subsequent period. These are self-imposed limitations on available resources. These committed amounts cannot be used for any other purpose unless the government removes or changes the specified use by taking the same level of action it employed to previously commit those amounts. These committed amounts would be approved and adopted by formal action of the Municipal Legislature.
- ❖ **Assigned** – Amounts that are constrained by the Municipality's intent to be used for specific purposes that are neither restricted nor committed. The intent will be expressed by the Municipal Legislature, the Mayor or by an official to which the Municipal Legislature delegates authority in conformity with the Autonomous Municipalities Law of Puerto Rico.
- ❖ **Unassigned** – Represent the residual classification for the Municipality's General Fund. Therefore, in order to calculate unassigned fund balance, total fund balance less nonspendable, restricted, committed and assigned equals unassigned fund balance. The resulting amount will be available for any purpose.

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

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

E. Fund Balances (Continued)

However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balance amounts as of and for the fiscal year ended June 30, 2012.

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

At June 30, 2012, the accompanying fund financial statements reported fund balances as restricted, committed and unassigned.

F. Budgetary Data

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

The budget columns (original and final budgets) of the Budgetary Comparison – General Fund reflect the original budget and the amended budget (which have been adjusted for legally authorized revisions of the annual budgets during the year). Appropriations, except remaining project appropriations, encumbrances, and unexpended grant appropriations, lapse at the end of each fiscal year.

Amendments to the budget, including transfers, require the approval of the Municipal Legislature. Unencumbered appropriations lapse at the end of the next fiscal year. The Municipality follows these procedures, in accordance with law, in order to establish the budgetary data reflected in the basic financial statements:

1. Prior of May 31 of each fiscal year, the Mayor submits to the Municipal Legislature a proposed budget for the fiscal year commencing the following July 1 in addition of a budget message;
2. The budget document is available for public inspection prior to its approval by the Municipal Legislature;
3. The Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law;
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance;

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

F. Budgetary Data (Continued)

5. 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 Municipal Legislature and the Mayor, is automatically renewed for the ensuing fiscal year until a new budget is approved. This permits the Municipality to continue making payments for its operating and other expenses until the new budget is approved;
6. Subsequent to the enactment of the annual appropriation ordinance, the Municipal Legislature has the authority to make necessary amendments made during the fiscal year and are reflected in the budget information included in the Budgetary Comparison Schedule – General Fund;
7. Budgetary data for the Special Revenue Fund has not been presented in the accompanying basic financial statements as such funds are budgeted over the life of the respective grant or project and not on an annual basis.

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

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

1. Encumbrances are recorded as expenditures under the budgetary basis and as a reserve of fund balances under GAAP.
2. The non-exonerated portion of the property tax advances are presented as revenue in the budgetary basis and as other financing sources under GAAP.
3. Interfund transactions of the General and Special Revenue Funds are not included in the budgetary basis.
4. Certain accrued liabilities and other debts are not included in the budgetary basis.
5. Certain revenues susceptible to accrual, i.e., both measurable and available, are not included in the budgetary data.

All encumbrance appropriations in the operating budget lapse at the end of the fiscal year. Property taxes collected during the current year by the Municipal Revenue Collection Center (Fiscal Agent) are presented as revenues in the accounting basis but are not considered in the budgetary schedule.

The special funds of the Special Revenue Fund have not been included in the budgetary comparison because balances are not budgeted. Also the budget prepared for the Federal Finance Awards Programs included in the Major and Non Major Funds is based on a program period which is not necessarily a year. Accordingly, it's not practical to present an annual comparison of budget for such programs.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

G. Cash, Cash Equivalent and Investment

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

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

Cash with fiscal agent represents property tax collections retained by the Municipal Revenues Collection Center and undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the Government Development Bank of the Commonwealth of Puerto Rico.

Cash balance recognized in the Debt Service Fund is restricted for the payment of the Municipality's obligations, and others are restricted for specific projects, such as the acquisition or construction of permanent improvements. The sinking fund is maintained by the Governmental Development Bank of Puerto Rico, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

H. Receivables

Receivable are stated net of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions. Receivable from Federal Government represents amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs.

I. Inventories

The General, Special Revenue and Capital Project Funds, purchases office and printing supplies, gasoline, oil and other expendable supplies held for consumption. The cost of purchases is recorded as expenditure in the appropriate fund and the inventory is not recorded in the basic financial statements.

J. Real Estate Held for Sale

Real estate held for sale is a construction project, which consist of nine (9) apartments that are for sale for qualified low and very low income families. This project is subsidized by the federal funds Community Development Block Grant- Neighborhood Stabilization Program. This real estate is carried at cost.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

K. Capital Assets

Property, plant and equipment purchased or acquired is carried at historical cost or estimated historical cost. Contributed assets are recorded at fair market value as of the date received. The Municipality's capitalization levels are \$50 on personal property. For improvements other than buildings, the capital outlay must be greater than \$10,000, extend the estimated useful life for ten years, and be greater than 10% of the original cost of the asset. Other costs incurred for repairs and maintenance is expensed as incurred.

Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

Capital Assets	Years
Buildings and site improvements	40
Infrastructure	40
Vehicles	5
Furniture and fixtures	5
Machinery and equipment	3 to 5

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

L. Long-Term Obligations

The liabilities reported in the government-wide financial statements included general and special obligation bonds and notes, and other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities.

In the fund financial statements, governmental fund types recognize bond issuances cost, during the current period. The face amount of debt issued is reported as other financing sources, while bond issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures.

M. Compensated Absences

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

M. Compensated Absences (Continued)

In accordance with the above criteria and requirements as established by GASBS No. 16; the Municipality has accrued a liability for compensated absences, which has been earned but not taken by Municipality's employees. For the government-wide statements, the current portion is the amount estimated to be used in the following year. For the governmental funds statements, all of the compensated absences are considered long-term and therefore, are not a fund liability and represents a reconciling item between the fund level and government-wide presentations.

The following is a summary of changes in the balance of Compensated Absences for the fiscal year ended June 30, 2012.

<u>BALANCE</u> <u>JULY 1, 2011</u>	<u>NEW ISSUES</u>	<u>RETIREMENTS</u> <u>AND CURRENT</u> <u>MATURATES</u>	<u>BALANCE</u> <u>JUNE 30, 2012</u>	<u>CURRENT</u> <u>PORTION</u>	<u>LONG-TERM</u> <u>PORTION</u>
\$ 1,543,381	\$ 15,105	\$ -	\$ 1,558,486	\$ 222,686	\$ 1,335,800

N. Insurance

The Municipality has insurance coverage for its public facilities, primarily to provide protection from catastrophic losses. Also, principal officials of the Municipality are covered under various surety bonds. The Secretary of the Treasury Department of the Commonwealth of Puerto Rico is the agent commissioned to place all of the Municipality's insurance coverage. Corresponding premiums payable are withheld by the Municipal Revenue Collection Center from quarterly advances of annual property tax and subsidy sent to the Municipality.

O. Interfund Transactions

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

- ❖ **Interfund loans** – Represent amounts provided with a requirement for repayment, which are recorded as "due from" in the lender governmental fund and "due to" in the borrower governmental fund. Interfund receivables, which are not considered currently available financial resources, are reported as advances. For amounts not expected to be collected within a reasonable period, interfund receivables/payables are reduced to the estimated realizable value and the amount that is not expected to be repaid is reported as a transfer from the governmental fund that made the loan.
- ❖ **Interfund transfers** – Represent flows of assets (permanent reallocation of financial resources among governmental funds) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported as other financing uses in the governmental fund making transfers and as other financing sources in the governmental fund receiving transfers.
- ❖ **Interfund reimbursements** – Represent repayments from the governmental fund responsible for particular expenditures or expenses to the governmental fund that initially paid for them.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

P. Claims and Judgments

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

Q. Use of Estimates

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

R. Accounting for Pension Costs

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

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

S. Risk Financing

The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico.

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2012 amounted to \$117,310. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$135,966 for workers compensation insurance covering all municipal employees.

COMMONWEALTH OF PUERTO RICO
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NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

T. FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

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

- ❖ GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*. This statement is effective for periods beginning after December 31, 2012;
- ❖ GASB Statement No. 61, *The Financial Reporting Entity: Omnibus— an amendment of GASB Statements No. 14 and No. 34*. This statement is effective for periods beginning after June 30, 2013;
- ❖ GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre- November 30, 1989 FASB and AICPA Pronouncements*. This statement is effective for periods beginning after December 31, 2012;
- ❖ GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. This statement is effective for periods beginning after December 31, 2011;
- ❖ GASB Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions (an amendment of GASB Statement No. 53)*. This statement is effective for periods beginning after June 30, 2013;
- ❖ GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement is effective for periods beginning after December 15, 2012.
- ❖ GASB Statement No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*. This statement is effective for periods beginning after December 15, 2012.
- ❖ GASB Statement No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25*.
- ❖ GASB Statement No. 68 *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*. This statement is effective for periods beginning after June 15, 2014.
- ❖ GASB Statement No. 69 *Government Combinations and Disposals of Government Operations*. The requirements of this statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis.

Except for GASB Statement No. 63, the Municipality's management has concluded that the future adoption of these GASB Statements will not have a significant impact on the basic financial statements.

NOTE 2 – CASH AND CASH EQUIVALENTS

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

The Municipality adopted the provisions of GASB Statement No. 40 (GASB No. 40), *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. This statement requires that state and local governments disclose essential risk information about deposits and investments. The disclosure requirements cover four main areas: (1) credit risk, (2) interest rate risk, (3) custodial credit risk, (4) foreign exchange exposure.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

Credit risk – This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial and credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2012.

Interest rate risk – This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investment portfolio at June 30, 2012, (2) limiting the weighted average maturity of its investments to three months or less, and (3) keeping most of its bank deposits in interests bearing accounts generating interests at prevailing market rates. At June 30, 2012, the Municipality did not maintain investments in certificates of deposits. Therefore, the Municipality's management has concluded that at June 30, 2012, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

Custodial credit risk – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico* the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$250,000 per depositor. In addition, public funds deposited in commercial banks by the Municipality are fully securities pledged as collateral are held, in the Municipality's name, by the agents of the Commonwealth's Secretary of Treasury. Deposits with GDB are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2012. Therefore, the Municipality's management has concluded that at June 30, 2012 the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

Foreign exchange risk – The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, the Municipality is prevented from investing in foreign securities or any other types of investments in which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2012.

The Municipality's bank balances in commercial banks of \$1,447 in the Municipal Hospital Fund, the \$29,908 in the Community Development Block Grant Funds and the \$13,074 in Other Governmental Funds were fully collateralized at June 30, 2012.

The deposits at GDB of \$101,835 in the General Fund, the \$1,749,030 in the Debt Service Fund, and the \$33,696 in Other Governmental Funds, are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 3 – RECEIVABLES

A. Property Taxes Receivables

Property taxes receivable of \$116,765 and \$4,582 in the General Fund and Debt Service Fund, respectively, represents advances from fiscal year 2011-2012, not collected by the Municipality at June 30, 2012.

B. Sales Tax Receivables

As described below in Note 14, the Municipal Legislature approved the imposition of the municipal sales and use tax during fiscal year 2006-2007. Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the Municipality. Tax is due each 20th day of each month based on tax collected in the preceding month. Therefore sales tax receivable of \$29,932 and \$36,297 in Debt Service Fund and Other Governmental Funds, respectively, represents the amounts due by the taxpayers at June 30, 2012.

C. Intergovernmental Receivables

Intergovernmental receivables of \$117,842 in the Municipal Hospital Fund represent a State contribution owed to the Municipality to cover operational costs. Also, receivables in the Other Governmental Funds represent expenditures incurred not yet reimbursed by the state agencies. Following is a detail of the state government receivables:

Description	Amount
State Department of Labor and Human Resources – Law 52	\$ 35,372
Others	<u>26,939</u>
Total	<u>\$ 62,311</u>

D. Federal Grants Receivable

Federal grants receivable amounting to \$170,573 in the Community Development Block Grant Funds represents expenditures incurred not yet reimbursed by OCAM, the pass-through agency. Also, receivables in Other Governmental Funds represent expenditures incurred not yet reimbursed by the federal agencies or the pass-through grantors. Following is a detail of the federal grants receivable:

Description	Amount
Twenty-First Century Community Learning Centers	\$ 95,349
Child Care and Development Block Grant	66,288
Community Service Block Grant	35,000
Homeland Security Grant	35,000
Puerto Rico Rural Development Corporation	19,000
Puerto Rico Regional Elderly Office	7,003
Emergency Solution Grant	2,633
Child and Adult Care Food Program	<u>2,399</u>
Total	<u>\$ 262,672</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 3 – RECEIVABLES (CONTINUED)

E. Other Receivables

Other receivable in the General Fund, for the amount of \$16,447 represents rental income, solid waste disposal services income and other miscellaneous income due at June 30, 2012.

F. Due From Other Funds

Interfund receivables and payables at June 30, 2012 are summarized as follows:

Receivable Fund	Payable Fund	Purpose	Amount
General Fund	Other Governmental Funds	Payroll and reimbursable expenditures	\$ 101,895
General Fund	Community Development Block Grant Funds	Payroll and reimbursable expenditures	71,593
Other Governmental Funds	Other Governmental Funds	Interfund Loans	166,744
Other Governmental Funds	General Fund	Interfund Loans	1,033,078
Municipal Hospital Fund	General Fund	Interfund Loans	75,233
Community Development Block Grant Funds	General Fund	Interfund Loans	<u>203,291</u>
Total			<u>\$ 1,651,834</u>

NOTE 4 – CAPITAL ASSETS AND REAL ESTATE HELD FOR SALE

REAL ESTATE HELD FOR SALE

On July 6, 2009, the Municipality enter into an agreement with the Commissioner of Municipal Affairs to participated in a construction of a nine (9) apartments building, for low and very low income families, financed with funds provided by Neighborhood Stabilization Program. At June 30, 2012, real estate held for sale presented in the governmental wide statement of net assets, related to these constructions, amounted \$821,489.

CAPITAL ASSETS

Capital assets; those with an estimated useful live of one year or more from the time of acquisition by the Municipality and a cost of \$50 or more, are primarily funded through the issuance of long-term bonds and loans and state and federal assignments. A summary of capital assets and changes occurring in 2012, including those changes pursuant to the implementation of GASB Statement No. 34, follows (Land and construction in progress are not subject to depreciation):

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 4 – CAPITAL ASSETS AND REAL ESTATE HELD FOR SALE (CONTINUED)

Governmental Activities	Balance July 1, 2011	Additions	Retirements / Reclassifications	Balance June 30, 2012
Capital asset, not being depreciated:				
Land	\$ 952,313	\$ -	\$ -	\$ 952,313
Work of Art	90,000	-	-	90,000
Construction in progress	<u>12,820,950</u>	-	-	<u>12,820,950</u>
Total capital assets not being depreciated	<u>13,863,263</u>	-	-	<u>13,863,263</u>
Capital assets, being depreciated:				
Buildings	4,585,285	-	-	4,585,285
Improvements	4,760,769	-	-	4,760,769
Infrastructure	8,238,091	-	-	8,238,091
Machinery and equipment	1,359,931	-	-	1,359,931
Motor vehicles	<u>2,196,861</u>	-	-	<u>2,196,861</u>
Total capital assets being depreciated	<u>21,140,937</u>	-	-	<u>21,140,937</u>
Less accumulated depreciation for:				
Buildings	(2,252,245)	(177,193)	-	(2,429,438)
Improvements	(1,522,751)	(239,133)	-	(1,761,884)
Infrastructure	(1,291,339)	(207,100)	-	(1,498,439)
Machinery and equipment	(1,318,115)	(129,688)	-	(1,447,803)
Motor vehicles	<u>(1,938,999)</u>	<u>(226,366)</u>	-	<u>(2,165,365)</u>
Total accumulated depreciation	<u>(8,323,449)</u>	<u>(979,480)</u>	-	<u>(9,302,929)</u>
Total capital assets being depreciated, net	<u>12,817,488</u>	<u>(979,480)</u>	-	<u>11,838,008</u>
Governmental activities capital assets, net	<u>\$ 26,680,751</u>	<u>\$ (979,480)</u>	<u>\$ -</u>	<u>\$ 25,701,271</u>

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

Governmental activities	Amount
General government	\$ 128,232
Mayor and Municipal	159,978
Public Safety	72,754
Public Works	422,366
Culture and Recreation	56,640
Sanitation	70,712
Human services and welfare	<u>68,798</u>
Total depreciation expenses	<u>\$ 979,480</u>

The Municipality has not maintained complete and adequate records in order to obtain sufficient and competent evidential matter related to the capital assets reported in the governmental activities. In addition, the infrastructure assets recorded in the accompanying statement of net assets do not include a substantial portion of the Municipality's infrastructure assets constructed or acquired by the Municipality from 1980 through June 30, 2012. GASB Statement No. 34 requires to retroactively applying the requirements to major general infrastructure assets within at least four (4) years of the adoption of this pronouncement, which is not later than June 30, 2007. The Municipality has not complied with this requirement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 5 – BANK OVERDRAFT

The bank overdraft of \$205,913 and \$21,891 in General Fund and Other Governmental Funds, respectively, was the result of the adjusted cash balance at June 30, 2012, of the Municipality's bank accounts.

NOTE 6 – ACCOUNTS PAYABLE AND ACCRUED EXPENSES LIABILITIES

Accounts payable and accrued expenses liabilities in governmental fund financial statements represent expenditures incurred during fiscal year 2011-2012, and not paid by the Municipality at June 30, 2012. Following is a detail of these accounts payable and accrued liabilities:

Major Governmental Funds	Accounts Payable	Accrued Liabilities	Total
General Fund	\$ 393,957	\$ 569,996	\$ 963,953
Municipal Hospital Fund	194,522	-	194,522
Community Development Block Grant Funds	288,310	-	288,310
Other Governmental Funds	<u>128,031</u>	<u>-</u>	<u>128,031</u>
Total	<u>\$ 1,004,820</u>	<u>\$ 569,996</u>	<u>\$ 1,574,816</u>

NOTE 7 – BONDS AND NOTES PAYABLE

The Municipality issued general and special obligation bonds and notes, principally to provide funds for the acquisition and construction of major capital facilities, to pay debt incurred in prior years and to cover expenditures of special events. At June 30, 2012, the government-wide and fund financial statements presented accounts payable regarding to the outstanding balance of these bond and notes in the amount of \$265,000 and accrued interests of \$109,520.

NOTE 8 – DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2012, balance due to other governmental units consists of the following:

Governmental Agency	Amount
Office of the Commissioner of Municipal Affairs	\$ 402,923
State Retirement System Administration – Special Laws	123,528
State Aqueduct and Sewer Authority	83,845
State Department of Labor	2,894
General Service Administration	<u>1,156</u>
Total	<u>\$ 614,346</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 9 – DEFERRED REVENUES

- A. Volume of business tax** – The deferred revenues of \$119,890 in the General Fund relates to volume of business tax collected in fiscal year 2011-2012 that will be earned in fiscal year 2012-2013.
- B. Federal Grants** – The deferred revenues presented in the Community Development Block Grant Funds and in Other Governmental Funds, amounting to \$43,869 and \$468,676, respectively, represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government in the Other Governmental Funds are as follows:

Program Description	Amount
Homeland Security Department	\$ 362,573
Public and Indian Housing	22,927
Child and Adult Care Food Program	31,170
Homelessness Prevention and Rapid Re-housing Program	27,769
Federal Transportation Administration	8,001
Child Care and Development Block Grants	7,256
Housing Preservation Grant	4,640
Puerto Rico Regional Elderly Office	4,340
Total	<u>\$ 468,676</u>

C. Property Taxes

Property taxes deferred revenues of \$116,765 in the General Fund, relates to an excess of property revenues over advances received from the CRIM during the fiscal year 2011-2012, according to the final settlement statement. In the governmental funds, this receivable was classified as deferred revenues, because was not available to pay liabilities of the current period.

NOTE 10 – GENERAL LONG-TERM DEBTS

Long-term liability activity for the year ended June 30, 2012, was as follows:

Description	Beginning Balance- as restated	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds and Notes Payable	\$ 7,740,000	\$ 860,000	\$ 265,000	\$ 8,335,000	\$ 265,000
Property Tax Debt – Law 42	1,253,251	-	29,092	1,224,159	30,921
Compensated absences	1,543,381	15,105	-	1,558,486	222,686
LIMS Repayment Plan	5,043	-	5,043	-	-
Section 108 Guaranteed Loan	2,666,000	-	167,000	2,499,000	167,000
CRIM Settlement 08-09	33,762	-	33,762	-	-
State Aqueduct and Sewer Authority – debt agreement	126,142	143,858	15,000	255,000	180,000
State Department of Labor- debt agreement	34,592	-	12,812	21,780	15,374
State Retirement System Administration- debt agreement	1,262,546	-	468,970	793,576	504,429
Total	<u>\$ 14,664,717</u>	<u>\$ 1,018,963</u>	<u>\$ 996,679</u>	<u>\$ 14,687,001</u>	<u>\$ 1,385,410</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 10 – GENERAL LONG-TERM DEBTS (CONTINUED)

A. GENERAL OBLIGATIONS BONDS AND NOTES

The Municipality issues general and special obligation bonds and notes, principally, to provide funds for the acquisition and construction of major capital facilities, to pay debt incurred in prior years, and to cover the expenditures of a special event. Bonds and notes payables as of June 30, 2012, are comprised of the following individual issues:

DESCRIPTION	AMOUNT
\$485,000, Series 2008, for purchase of equipment, payable in annual installments ranging from \$50,000 to \$85,000, excluding variable interest from 1.53% to 7.50%, through July 1, 2014	\$ 165,000
\$4,920,000, Series 2008, for construction of public recreational facilities, payable in annual installments ranging from \$70,000 to \$420,000, excluding variable interest from 1.53% to 5.00%, through July 1, 2032	4,595,000
\$1,110,000, Series 2007, for construction of public recreational facilities, payable in annual installments ranging from \$15,000 to \$95,000, excluding variable interest from 3.93% to 6.50%, through July 1, 2032	1,015,000
\$1,030,000, Series 2010, for construction of public recreational facilities, payable in annual installments ranging from \$15,000 to \$90,000, excluding variable interest from 4.75% to 7.50%, through July 1, 2034	980,000
\$820,000, Series 2010, for operational purposes, payable in annual installments ranging from \$20,000 to \$80,000, excluding variable interest from 6.00% to 7.00%, through July 1, 2029	760,000
\$255,000, Series 2011, for operational purposes, payable in annual installments ranging from \$30,000 to \$45,000, excluding variable interest from 6.00% to 6.50%, through July 1, 2018	225,000
605,000, Series 2012, for operational purposes, payable in annual installments ranging from \$10,000 to \$50,000, excluding variable interest from 6.00% to 6.50%, through July 1, 2036	<u>595,000</u>
Total General Obligations – Bonds	<u>\$ 8,335,000</u>

These bonds and notes are payable with the following Municipality's resources:

- ❖ Special ad valorem property tax, which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes and;
- ❖ Municipal sales taxes resources restricted for debt service.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 10 – GENERAL LONG-TERM DEBTS (CONTINUED)

B. BONDS AND NOTES AMORTIZATION

The annual requirements to amortize the general obligations outstanding as of June 30, 2012 are as follows:

Year Ending June 30,	Principal Payment	Interest Payment	Total
2013	\$ 265,000	\$ 346,123	\$ 611,123
2014	305,000	439,625	744,625
2015	250,000	426,575	676,575
2016	280,000	412,525	692,525
2017	290,000	396,725	686,725
2018-2022	1,580,000	1,641,475	3,221,475
2023-2027	2,160,000	1,245,450	3,405,450
2028-2032	2,845,000	572,225	3,417,225
2033-2037	360,000	35,100	395,100
Total	<u>\$ 8,335,000</u>	<u>\$ 5,515,823</u>	<u>\$ 13,850,823</u>

C. PROPERTY TAX DEBT – LAW 42

The Municipality entered into a repayment agreement with the Government Development Bank for Puerto Rico (GDB) and the CRIM, to pay off the excess of property tax advances through fiscal year 2000 and 2001. The CRIM retains the payment from the property tax advances of the Municipality. The amounts retained by the CRIM are remitted to GDB on July 1 of each year through July 1, 2032. The outstanding balance of the note payable to the CRIM at June 30, 2012 amounted to \$1,224,159.

D. COMPENSATED ABSENCES

The government-wide statement of net assets includes \$1,558,486 of accrued sick leave benefits, and accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

E. SECTION 108 GUARANTEED LOAN

On September 14, 2006, the Municipality entered into a loan guarantee commitment of \$3,000,000 with the U.S. Department of Housing and Urban Development (HUD) pursuant to an application under Section 108 of the Housing and Community Development Act of 1974 (Section 108).

The proceeds of \$3,000,000 of the loan guarantee commitment were used by the Municipality to finance the construction of a public recreational facility. The proceeds and uses of the loan guarantee commitment were accounted for in the Section 108 loan guarantee, a fund in the Other Government Funds. The loan guarantee commitment is repaid with grant awards received from the Community Development Block Grants (CDBG), administered by the Puerto Rico pass-through, Office of the Commissioner of Municipal Affairs (OCAM). At June 30, 2012, the outstanding principal balance of the loan guarantee commitment amounted to \$2,499,000.

Actually, the Municipality is not complying with the required annual payments of the Section 108 loan. The amounts not paid by the Municipality during the fiscal years were paid directly by the OCAM. At June 30, 2012, the Municipality owes to OCAM the amount of \$402,923 in accumulated principal and interest payments from current and past years.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 10 – GENERAL LONG-TERM DEBTS (CONTINUED)

F. STATE AQUEDUCT AND SEWER AUTHORITY- DEBT AGREEMENT

In April 4, 2012 the Municipality entered into financing agreement with the State Aqueduct and Sewer Authority, for the payment of the Municipality's debt for water and sewer services at March 31, 2012. The balance at June 30, 2012 of this agreement was \$255,000.

G. STATE DEPARTMENT OF LABOR- DEBT AGREEMENT

The Municipality entered into a financing agreement with the State Department of Labor, for the payment of the Municipality's debt for unemployment benefits. The balance at June 30, 2012 of this agreement was \$21,780.

H. STATE RETIREMENT SYSTEM ADMINISTRATION- DEBT AGREEMENT

In February 25, 2011 the Municipality entered into financing agreements with the State Retirement System Administration, for the payment of the Municipality's debt for retirement benefits of its employees and other special laws. The balances at June 30, 2012 of these agreements were \$339,203 and \$454,373, respectively.

NOTE 11 – DEBT RETIREMENT

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

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

NOTE 12 – PROPERTY TAXES

The Municipality is authorized by Law No. 81 to impose and collect personal and real property taxes. Under the laws and regulations of the Commonwealth, personal property taxes can be imposed to any natural or legal person that at January 1 of each year is engaged in trade or business and is the owner of personal property used in trade or business.

Personal property taxes are self-assessed by taxpayers every year generally using the book value of personal property assets owned by the taxpayer at January 1 (assessment date) and reporting such taxable value through a personal property tax return filed on May 15 subsequent to the assessment date. The total personal property tax rate in force at June 30, 2011 was 6.83% (of which 2.30% belong to the Commonwealth of Puerto Rico and 4.03% belongs to the Municipality).

Real property taxes are assessed by CRIM. The assessment on real property is made every January 1 and is based on estimated current values of the property deflated to 1957 market prices. The total real property tax rate in force at June 30, 2012 was 8.83% (of which 2.30% belongs to the Commonwealth of Puerto Rico and 6.53% belongs to the Municipality).

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 assumes payment of the basic tax (4% and 6% 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 12 – PROPERTY TAXES (CONTINUED)

CRIM is responsible for the billing and collections of real and personal property taxes on behalf of the Municipality. Prior to the beginning of each fiscal year, CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, CRIM advances funds to the Municipality based on the initial estimated collections. CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers.

This settlement has to be completed on a preliminary basis not later than each December 31. If CRIM remits to the Municipality property tax advances, which are less than the property tax actually collected, an additional property tax receivable is recorded at June 30. However, if advances exceed the amount actually collected by CRIM, an intergovernmental payable is recorded at June 30.

Law No. 81 provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation. Such special tax is levied and collected by CRIM. Collections of this special tax are remitted to the Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth.

In addition, 1.50% of the total personal and real property taxes collected by CRIM is restricted for the Municipality's debt service requirements and is retained by GDB for such purposes.

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:

- ❖ 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 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.
- ❖ An additional amount not exceeding \$16 million, on an annual basis, is distributed to the Municipal Equalization Fund, provided it is within the 35% 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.

NOTE 13 – VOLUME OF BUSINESS TAXES

The Municipality is authorized by Law No. 81 to impose and collect municipal license taxes on all trade or business activities operated by any natural or legal person within the territorial area of Maunabo. This is a self-assessed tax generally based on the business volume measured by gross sales. The Municipality establishes the applicable tax rates. At June 30, 2012, the municipal tax rates imposed by the Municipality were 1.50% for financing institutions and 0.50% for other types of taxpayers. Any taxpayers that 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% and 90% under standard rates.

Each taxpayer must assess his/her corresponding municipal license tax by declaring his/her volume of business through a tax return to be filed every April 15 based on the actual volume of business generated in the preceding calendar year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 13 – VOLUME OF BUSINESS TAXES (CONTINUED)

Taxpayers with a sales volume of \$3 million or more must include audited financial statements with their tax returns. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration.

The first installment of the tax covers the six-month period ended December 31, subsequent to the filing date of the declaration, while the second installment of the tax covers the six-month period ended June 30 of the subsequent calendar year. If a taxpayer elects to pay the tax in full on the filing date of the declaration (generally April 15), a 5% discount is granted automatically on the total tax amount due.

Any municipal license taxes collected in advance (that is, pertaining to a future fiscal year) are recorded as deferred revenues in the GWFS and the GFFS (See Note 9).

NOTE 14 – SALES TAXES

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

Section 6189 of the Puerto Rico Internal Revenue Code of 1994, as amended, authorizes the Municipalities in Puerto Rico to impose a sales and use tax to consumers. This tax must be imposed in conformity with the base, exemptions and limitations contained Subtitle BB of the Code. The Municipal Sales Tax is specifically imposed over all sales transactions of taxable items and combined transactions (as defined by the municipal internal regulation) taken place within municipal limits. The Municipal Tax is also specifically imposed over the purchase price for the use, storage or consumption of taxable transactions (as defined by the municipal internal regulation) taken place within municipal limits.

The Municipal Legislature approved the imposition of the municipal sales and use tax, effective on July 1, 2006. Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the Municipality. Tax is due each 20th day of each month based on tax collected in the preceding month. The Municipal Ordinance does not impose specific restrictions or limitations on the use of the municipal sales and use tax resources. Resources are recorded in the general fund of the Municipality.

NOTE 15 – INTERGOVERNMENTAL REVENUES

Intergovernmental revenues consist primarily of funds received from the Commonwealth of Puerto Rico, "in lieu of tax" payments from the Quasi-public Corporation, Puerto Rico Electric Power Authority, and federal financial assistance received from federal government. Grants and subsidies received from the Commonwealth of Puerto Rico and federal agencies include, among others, a general subsidy for urban development and capital improvements.

Intergovernmental revenues are accounted for through the General Fund except for those directly related to urban development and capital improvements, which are accounted for through the State Assignment, Loans and CDBG Funds.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 16 – INTERFUND TRANSFERS

Interfund transfers during the fiscal year ended at June 30, 2012, are summarized as follows:

Transfer Out	Transfer In	Purpose	Amount
General Fund	Municipal Hospital Fund	To cover operating expenditures	\$ 323,251
Community Development Block Grant Funds	Other Governmental Funds	Debt retirement	67,574
Community Development Block Grant Funds	General Fund	To cover payroll and operating expenditures	<u>10,407</u>
Total			<u>\$ 401,232</u>

NOTE 17 – EMPLOYEE'S RETIREMENT PLAN

The Employee's Retirement System of the Government of Puerto Rico and its instrumentality (ERS) is the administrator of a cost-sharing multiple-employer retirement system established by the Commonwealth of Puerto Rico. The ERS was created under the Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentality and of certain municipalities and components units not covered by their own retirement systems.

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

The Municipality adopted the requirements of GASBS No. 25 for all the career employees that are covered under the Commonwealth of Puerto Rico Employee's Retirement System, a multiple-employer public employee retirement system, established by State Laws.

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

Law Number 305 of September 24, 1999, amends the Act Number 447 that establish a savings program. All employees active in the system as of December 31, 1999 may elect to transfer from defined contribution programs to the new savings program (a defined contribution plan). Employees in the savings program may now contribute from a minimum of 8.275% up to a maximum of 10% of their monthly salary, and will be invested in an account which will either: (a) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (b) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (c) earn a combination of both alternatives. If at time of retirement accumulated benefits amount to \$10,000 or less may elect to receive a lump sum distribution up to the accumulated benefits. Under the new program the retirement age is reduced from 65 to 60 for those employees who joined the current plan on or after April 1, 1990.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 17 – EMPLOYEE'S RETIREMENT PLAN (CONTINUED)

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

A variety of significant actuarial assumptions are used to determine the standard measure of the pension benefit obligation and these assumptions are summarized below:

- ❖ The present value of the future pension payments was computed by using a discount of 9%.
- ❖ Future pension payments reflect an assumption of a 6% salary increase.

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

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

The amount of the total pension benefit obligation is based on a standardized measurement established by GASBS No. 27, *Financial Reporting for Defined Benefit Pension Plans and Notes Disclosure for Defined Contributions Plans*. The standardized measurement is the actuarial present value of estimated defined pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee services performed to date. The measure is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among other public retirement systems. The measure is independent of the actuarial funding method used to determine contributions to the plan.

The membership of retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits, but not yet receiving benefits, and active employees and the distribution of active employees between vested and non-vested is not readily available.

Contributions in 2006 and prior years were made based on percentages established by the law. Such percentage has not been based on actuarial studies, as required by accounting principles generally accepted in the United States of America. An actuarial compilation of the annual contribution applicable to the Municipality has not been prepared. Accordingly, the accounts by which the actual contributions differ from the required actuarial contributions are not known.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 17 – EMPLOYEE'S RETIREMENT PLAN (CONTINUED)

The total pension expenditures recorded in the category of administration for the fiscal year ended on June 30, 2010, 2011 and 2012 were, approximately, \$114,900, 300,300 and \$256,200, respectively. All employees who at the time of employment are 55 years old or less are eligible to participate in the System. No benefit is payable if the participant receives a refund of his accumulated contributions.

The historical trend information regarding the accumulation of assets and pension benefit obligation in the ERS is not available. For the ten-year trend information, refer to the separately issued financial statements of the ERS as of and for the fiscal year ended June 30, 2012. The P.R. Retirement Plan Administration provides additional information of the ERS. They issue a public available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Commonwealth of Puerto Rico. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, P.R. 00940.

NOTE 18 – COMMITMENTS AND CONTINGENCIES

A. CLAIMS AND JUDGMENTS

The Municipality is, at present, a defendant in a number of legal matters that arise from alleged improper application of policies and negligence in the ordinary course of the Municipality's activities.

It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial resources for its payment.

In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in discovery stage. Certain of these claims are covered by insurance. Legal counsels with the information currently available can not determine the final outcome of these proceeding. However, it has been the Municipality's experience that such actions are settled for amounts substantially less than the claim amounts.

B. FEDERAL GRANTS

In the normal course of operations, the Municipality receives grants from various Federal and State agencies. The grant programs are subject to audit by agents of the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds.

C. CONSTRUCTION

The Municipality had commitments at June 30, 2012 of approximately \$1,160,000 for the construction, improvements, or renovation of several capital facilities and the capital assets.

D. OTHER COMMITMENTS

At June 30, 2012 the General Fund had commitments of approximately \$530,000 for purchase orders or contracts that will be honored during the subsequent year.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 19 – FUND BALANCE (DEFICIT)

As of June 30, 2012, the fund balance (deficit) classifications are as follows:

Fund Balance	General Fund	Debt Service Fund	Other Governmental Fund	Total
Committed for:				
General Government	\$ 101,835	\$ -	\$ 11,905	\$ 113,740
Urban Development	-	-	18,558	18,558
Restricted for:				
General Government	-	-	59,022	59,022
Public Safety	-	-	219,036	219,036
Public Works	-	-	6,772	6,772
Human Services and Welfare	-	-	17,377	17,377
Urban Development	-	-	381,955	381,955
Culture and Recreation	-	-	6,010	6,010
Debt Service	-	1,409,024	-	1,409,024
Unassigned	<u>(3,025,769)</u>	<u>-</u>	<u>-</u>	<u>(3,025,769)</u>
Total Fund Balance	<u>\$ (2,923,934)</u>	<u>\$ 1,409,024</u>	<u>\$ 720,635</u>	<u>\$ (794,275)</u>

NOTE 20 – ACCOUNTING CHANGES AND RESTATEMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

The following restatements have been made in the governmental fund financial statements, which are reported as an adjustment to the beginning fund balances:

Description	General Fund	Debt Service Fund	Municipal Hospital Fund	Community Development Block Grant Funds	Other Governmental Funds	Total Governmental Funds
Fund balance, beginning	\$ (2,678,351)	\$ 1,322,668	\$ -	\$ -	\$ 576,455	\$ (779,228)
Adjustment to the inter-fund balance with the Public Housing Fund according to the pass-through entity final resolution	326,845	-	-	-	-	326,845
Reclassification of the State Aqueduct and Sewer Authority- debt agreement	<u>126,142</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>126,142</u>
Fund balance, beginning as restated	<u>\$ (2,225,364)</u>	<u>\$ 1,322,668</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 576,455</u>	<u>\$ (326,241)</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 20 – ACCOUNTING CHANGES AND RESTATEMENTS (CONTINUED)

A. GOVERNMENTAL WIDE FINANCIAL STATEMENTS

The following restatements have been made in the governmental wide financial statements, which are reported as an adjustment to the beginning net assets:

Description	Total
Net assets, beginning	\$ 11,751,007
Adjustment to the inter-fund balance with the Public Housing Fund according to the pass-through entity final resolution	<u>326,845</u>
Net assets, beginning as restated	<u>\$ 12,077,852</u>

NOTE 21 – ACCUMULATED DEFICIT

The Municipality has accumulated deficit of \$2,923,934 in the General Fund. Among the actions currently taken by management to reduce the accumulated deficit are; the inclusion of an account for the amortization of the accumulated deficit in the 2012-2013 operational budget, a reduction of the transitory employees maintain in the General Fund, an operational cost reduction plan and an implementation of increasing collection effort over the accounts receivables. In addition, in the months of July and August 2012, the Municipality issued two special notes in the amount of \$2,405,000 with the Government Development Bank, for the payment of outstanding debts with various state agencies and suppliers of the Municipality.

NOTE 22 – SUBSEQUENT EVENTS

The Municipality's executive branch approved Ordinance No. 14, Serie 2011-2012, and Ordinances 1 and 2, Serie 2012-2013, authorizing the issuance of a General Obligation Bonds in the amount of \$1,965,000, \$260,000 and 655,000, respectively. These bonds are payable with resources collected through the Municipal Redemption Fund, and were disbursed by the Governmental Development Bank (GDB) during August 2012.

Also, the Municipality's executive branch approved Resolution No. 40, Serie 2011-2012, authorizing the issuance of a General Obligation Note in the amount of \$440,000. This bonds are payable with resources collected through the Municipal Redemption Fund, and were disbursed by the Governmental Development Bank (GDB) during August 2012.

Management has evaluated subsequent events through March 30, 2013, the date the financial statements were available to be issued.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

**BUDGETARY COMPARISON SCHEDULE- GENERAL FUND
(SEE NOTES TO BUDGETARY COMPARISON SCHEDULE)**

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>Budgeted Amounts</u>		<u>Actual Amounts (Budgetary Basis)</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
REVENUES:				
Property taxes	\$ 796,649	\$ 796,649	\$ 796,649	\$ -
Volume of Business Taxes	175,000	175,000	157,768	(17,232)
Intergovernmental Revenues	6,116,742	6,116,742	6,011,454	(105,288)
Licenses, permits and other local taxes	300,000	300,000	282,451	(17,549)
Rent of Property	100,000	100,000	101,636	1,636
Miscellaneous	<u>1,531,609</u>	<u>1,531,609</u>	<u>125,509</u>	<u>(1,406,100)</u>
Total revenues	<u>9,020,000</u>	<u>9,020,000</u>	<u>7,475,467</u>	<u>(1,544,533)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
Mayor and Municipal Legislature	145,790	145,790	132,886	12,904
General government	4,793,583	4,893,269	3,560,726	1,332,543
Public safety	109,712	106,512	105,191	1,321
Public works	2,010,115	1,898,529	2,820,959	(922,430)
Culture and Recreation	592,245	569,345	543,682	25,663
Health and Sanitation	612,540	611,140	648,946	(37,806)
Human Service and Welfare	<u>756,015</u>	<u>795,415</u>	<u>725,125</u>	<u>70,290</u>
Total expenditures, encumbrances and other financing uses	<u>9,020,000</u>	<u>9,020,000</u>	<u>8,537,515</u>	<u>482,485</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)	<u>\$ -</u>	<u>\$ -</u>	<u>\$(1,062,048)</u>	<u>\$(1,062,048)</u>

EXPLANATION OF DIFFERENCE BETWEEN BUDGETARY INFLOWS AND OUTFLOWS AND GAAP REVENUES AND EXPENSES

Sources/inflows of resources:	
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule	\$ 7,475,467
Differences-budget to GAAP	<u>-</u>
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$ 7,475,467</u>
Uses/outflows of resources:	
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule	\$ 8,537,515
Differences-budget to GAAP:	
Prior year expenditure are not outflows of budgetary resources, but are expenditure for financial purposes	152,883
Encumbrances for supplies and equipment ordered, but not received, are reported in the year the order is placed for budgetary reporting purposes	(334,950)
Adjustment to expenditures	<u>365,745</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$ 8,721,193</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

NOTES TO BUDGETARY COMPARISON SCHEDULE- GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE A – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. BUDGETARY CONTROL

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with GAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

The Municipality prepares its annual budget including the operations of the General Fund.

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2012 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2012.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF AGRICULTURE:			
Direct Program:			
Rural Housing Preservation Grants	10.433		\$ 5,501
Pass-through State - Department of Education:			
Child and Adult Care Food Program	10.558	N/AV	41,014
Total U.S. Department of Agriculture			46,515
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Pass-Through State - Office of the Commissioner of Municipal Affairs:			
Community Development Block Grants – State's Program	14.228	11-AB 10-AB-FC 09-AB-FC 08-NSP1 08-DR-AB-FC 08-AB-FC 07-AB-FC	1,578,251
Pass-Through State – State Department of Family:			
ARRA – Homelessness Prevention and Rapid Re- Housing Program (Recovery Act Funded)	14.257	272-1220000-04F- 2009-S08DC720001	46,836
Emergency Solutions Grant Program	14.231	N/AV	2,437
Pass-Through State – Puerto Rico Housing Administration:			
Public and Indian Housing	14.850	2008-000290-A/ B	325,502
Total U.S. Department of Housing and Urban Development			1,953,026
U.S. DEPARTMENT OF ENERGY:			
Pass-through State – Office of the Energy Affairs Administration:			
ARRA – Energy Efficiency and Conservation Block Grant Program (Recovery Act Funded)	81.128	0013A-006	111,493
Total U.S. Department of Energy			111,493

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF EDUCATION:			
Pass-through the Commonwealth of Puerto Rico - Department of Education:			
Twenty-First Century Community Learning Centers	84.287	2012-AF0037	148,423
Total U.S. Department of Education			148,423
U.S. DEPARTMENT OF HOMELAND SECURITY:			
Pass-Through State – Office of the Governor:			
Disaster Grants- Public Assistance	97.036	N/AV	222,405
Total U.S. Department of Homeland Security			222,405
CORPORATION FOR NATIONAL & COMMUNITY SERVICE:			
Direct Program:			
Volunteers in Service to America Americorps Vista	94.013		10,425
Total Corporation for National & Community Service			10,425
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICE			
Pass-Through State – Office of Governor, Regional Elderly Office:			
Special Program for Aging, Title III, Part B	93.045	120294R2	30,751
Pass-Through State – Administration of Children and Families:			
Child Care and Development Block Grant	93.575	241-2012-000106	493,046
Total U.S. Department of Health and Human Service:			523,797
TOTAL EXPENDITURES OF FEDERAL AWARDS			\$ 3,016,084

See notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – GENERAL

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

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

NOTE 3 – FEDERAL CFDA NUMBER

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

NOTE 4 – PASS-THROUGH GRANTOR'S NUMBER

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

NOTE 5 – LOAN OUTSTANDING

The Municipality had an outstanding loan balance under program Section 108 Loan Guarantee Assistance (CFDA No. 14.248), for which the grantor does not impose continuing compliance requirements. The outstanding balance of the loan at June 30, 2012 was \$2,499,000.

NOTE 6 – MAJOR PROGRAMS

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

PEDRO C. ORTIZ LEDEE
CERTIFIED PUBLIC ACCOUNTANT

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

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Municipality of **Maunabo**, Puerto Rico (Municipality), as of and for the fiscal year ended June 30, 2012, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated March 30, 2013. The report on the governmental fund financial statements was qualified for the interfund balances. We did not express an opinion on the governmental wide financial statements because we were unable to obtain sufficient and competent evidential matter related to the capital assets. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not design to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses. Findings 12-II-02 and 12-II-03.

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompany Schedule of Findings and Questioned Costs to be significant deficiencies. Finding 12-II-01 and 12-II-04.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed 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 Findings 12-II-02 and 12-II-03.

We noted certain other matters that we reported to management of the Municipality in a separate letter dated March 30, 2013.

The Municipality's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the Municipality's response and, accordingly, we express no opinion on it.

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


Pedro C. Ortiz Ledée, CPA
License Number 5200

Guayama, Puerto Rico
March 30, 2013



PEDRO C. ORTIZ LEDEE
CERTIFIED PUBLIC ACCOUNTANT

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

To the Honorable Mayor and
Member of the Municipal Legislature
Municipality of Maunabo, Puerto Rico

Compliance

We have audited Municipality of **Maunabo**, Puerto Rico (Municipality) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Municipality's major federal programs for the fiscal year ended June 30, 2012. The Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on Municipality's compliance based on our audit.

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

As described in items 12-III-06, 12-III-09, 12-III-10 and 12-III-11 in the accompanying Schedule of Findings and Questioned Costs, the Municipality did not comply with requirements regarding Allowable Activities, Procurement and Suspension and Debarment, Program Income and Reporting that are applicable to its Community Development Block Grants – State's Program. Compliance with such requirement is necessary, in our opinion, for the Municipality to comply with the requirements applicable to that program.

As described in item 12-III-13 in the accompanying Schedule of Findings and Questioned Costs, the Municipality did not comply with requirement regarding Reporting that is applicable to its Public and Indian Housing. Compliance with such requirement is necessary, in our opinion, for the Municipality to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraphs, the Municipality complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the fiscal year ended June 30, 2012. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items 12-III-05, 12-III-07, 12-III-08, 12-III-12, and 12-III-14.

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONTINUED)

Internal Control over Compliance

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

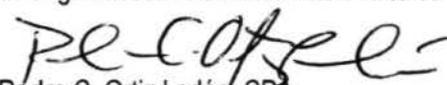
Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance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

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 12-III-06, 12-III-09, 12-III-10, 12-III-11 and 12-III-13 to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We considered the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned costs as items 12-III-05, 12-III-07, 12-III-08, 12-III-12, and 12-III-14 to be significant deficiencies.

The Municipality's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the Municipality's responses and, accordingly, we express no opinion on the responses.

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


Pedro C. Ortiz Ledée, CPA
License Number 5200

Guayama, Puerto Rico
March 30, 2013



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION I – SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued:	Qualified for fund financial statement and disclaimer of opinion for governmental-wide financial statements	
Internal control over financial reporting:		
Material weakness identified?	Yes X	No
Significant deficiencies identified?	Yes X	No reported
Noncompliance material to financial statements noted?	Yes X	No

Federal awards

Internal Control over major programs:		
Material weakness identified?	Yes X	No
Significant deficiencies identified?	Yes X	No reported
Type of auditor's report issued on compliance for major programs:	Unqualified, for Child Care Development Block Grant	
	Qualified, for Community Development Block Grants – State's Program and Public and Indian Housing	
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes X	No

Identification of major programs

CFDA Number	Name of Federal Program or Cluster
14.228	Community Development Block Grants/ State's Program
14.850	Public and Indian Housing
93.575	Child Care and Development Block Grant

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING	12-II-01
REQUIREMENT	ACCOUNTING RECORDS AND REPORTING SYSTEM
CONDITION	The Municipality did not maintain an accounting system that generates accurate accounting information for the preparation of the financial statements in conformity with generally accepted accounting principles (GAAP).
CONTEXT	<p>During our examination of the accounting cycle, we noted that the Municipality's accounting records are maintained in the cash and budgetary basis and at the end of year, personnel of the Finance Department and external consultants summarized in electronic worksheets the revenues, expenditures, capital assets transactions, accounts receivables, accounts payable and long term-debts. These worksheets are used for the preparation of the financial statements.</p> <p>Also, we noted the following conditions during our evaluation of the accounting cycle for the fiscal year 2011-2012:</p> <ol style="list-style-type: none">Accounting transactions are currently accounted simultaneously through a manual and a computerized accounting system for which no reconciliation procedures are made among them. These accounting systems does not provide for a self balancing set of accounts for each fund operated by the Municipality;Both accounting systems does not help management to distinguish between expenditures incurred and encumbrances and does not provide reliable financial information of transactions related with capital assets, accounts receivables, accounts payables and long-term debts;The accounting personnel does not maintained a Model 4a (the manual accounting system that summarized the cash transactions of the Municipality) for the monthly cash transactions of the General Fund and the special revenue funds of the Municipality;No adequate year-end closing entries procedures were made.
CRITERIA	Article 8.010 (b) of State Act Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico</i> of August 30, 1991, states that the Municipality must maintain its fund accounting in accordance with GAAP. In addition, Article 8.010 (c) states that the system used must produce reliable reports and financial statements, provide complete information about the results of operations and include the necessary internal controls to account for all funds, capital assets and other assets.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING	12-II-01 (CONTINUED)
REQUIREMENT	ACCOUNTING RECORDS AND REPORTING SYSTEM (CONTINUED)
CAUSE	The Municipality has not established effective internal control procedures over the preparation of the financial statements and the transactions recorded on its accounting records.
EFFECT	The Municipality is not in compliance with Articles 8.010 (b) and (c) of the State Law Number 81 of August 30, 1991.
RECOMMENDATION	We recommend management to establish the necessary internal controls and procedures in order to maintain a complete accounting system that provides for the preparation of financial statements in accordance with GAAP.
MANAGEMENT RESPONSE	We will continue implementing our accounting system in order to generate reliable accounting information for the financial statement preparation. Responsible person: Finance Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING	12-II-02
REQUIREMENT	ACCOUNTING RECORDS- CAPITAL ASSETS
CONDITION	The Municipality does not have an effective system to account for capital assets, including the infrastructure assets.
CONTEXT	During our examination of the property records, we noted that the Municipality does not have adequate internal controls and procedures to ensure that all capital outlay expenditures and dispositions are recorded in the capital assets subsidiary ledger. In addition, the Municipality did not have adequate procedures to reclassify the finished accumulated construction in progress to buildings or infrastructure. Also, the Municipality has not recorded the infrastructure assets, accordingly, has not recorded depreciation expenses for those assets. These infrastructure assets should be reported as part of the capital assets of the Municipality according to Statement No. 34 of the Governmental Accounting Standards Board (GASB 34). In addition, the Municipality did not performed periodical physical inventories of its capital assets.
CRITERIA	Article 8.010 (c) (3) of the State Law Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico de 1991</i> of August 30, 1991, stated that Municipality should maintain updated property accounting records. Also, GASB 34 requires that all capital assets, including infrastructure, must be presented in the statement of net assets and that there must be depreciated during its useful life.
CAUSE	The Municipality did not maintain an adequate control of the accountability of its capital assets including the infrastructure.
EFFECT	The Municipality is not in compliance with Article 8.010 (c) (3) of the State Law Number 81 of August 30, 1991 and GASB 34.
RECOMMENDATION	We recommend management and the Property Division of the Municipality to make an inventory of the capital assets and reconcile it with the capital assets subsidiary ledger. In addition, the Municipality should implement adequate internal control procedures to improve the accountability of infrastructure assets.
MANAGEMENT RESPONSE	We gave instructions to our employee assigned to the property division of the Municipality, to continue updating the capital assets, in order to reconcile it with the property ledger.

Responsible person: Finance Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-03
REQUIREMENT	ACCOUNTING RECORDS- INTERFUND TRANSACTIONS
CONDITION	The Municipality does not maintain an accurate record over the special revenue funds transactions and the interfund transactions of all Municipalities' funds.
CONTEXT	During our examination of the accounting records, we noted that the Municipality does not maintain adequate controls over the interfund transactions. This situation caused that various special revenue funds (Federal funds and other special revenue funds), were used as loans, to paid operational costs of the General Fund and other funds. In addition, the Municipality did not maintain proper records of the interfund cash transactions and the corresponding due from and due to accounts balances presented in the Balance Sheet, for the fiscal Years 2011-2012 and previous balances.
CRITERIA	Article 8.004 (c) of the State Law Number 81 - <i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico de 1991</i> - August 30, 1991, states that the restricted funds received by the Municipality should be only used for the purposes established by these resources. In addition, Article 8.010 (c) (2) and (3) of State Act Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico</i> of August 30, 1991, states that Municipality should maintain accurate accounting records and funds controls.
CAUSE	The Municipality did not maintain an adequate control of the accountability of the interfund transactions and the due from and due to account balances.
EFFECT	The Municipality is not in compliance with Articles 8.004 (c) and 8.010 (c) (2) and (3) of the State Law Number 81 - <i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico de 1991</i> - August 30, 1991.
RECOMMENDATION	We recommend management to implement procedures in order to obtain and maintain all the required documentation regarding the interfund transactions.
MANAGEMENT RESPONSE	We gave instructions to the Finance Director to avoid the transfer of funds between bank accounts without adequate supporting documentation. Responsible person: Finance Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-04
REQUIREMENT	ACCOUNTING RECORDS- BANK RECONCILIATIONS
CONDITION	The Municipality does not have effective internal control procedures to ensure that the bank reconciliations were reconciled with the accounting records.
CONTEXT	During our cash test, we noted that the reconciliation process of the current cash account and the other accounts of the Municipality consists only of including the ending bank balance, less the outstanding checks of the month. There was not a reconciliation process with the accounting records.
CRITERIA	Chapter IV, Section 12 of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affairs (OCAM), establishes that the accounting system of the municipalities shall provide for the timely and accurate preparation of bank reconciliations. In addition, the Municipality shall prepare a monthly report of revenues and disbursements, which has to be reconciled with the bank reconciliations.
CAUSE	The Municipality's internal control procedures failed to assure that the bank reconciliations were prepared in a complete manner and reconciled with the accounting records.
EFFECT	The Municipality is not in compliance with Chapter IV, Section 12 of the Municipal Administration Regulatory Manual of the OCAM.
RECOMMENDATION	We recommend management to continue improving the internal control procedures over the preparation of the bank reconciliations and assure that accounting records are reconciled with these bank reconciliations within a reasonable amount of time in order to maintain proper control over cash.
MANAGEMENT RESPONSE	Our external consultant reviewed in a monthly basis the bank reconciliations and corrects the errors that were found during his examination. Responsible person: Finance Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-05
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE COST
CONDITION	During the fiscal year 2011-2012, the Program disbursed funds without the appropriate supporting documentation established by the Federal Regulation.
CONTEXT	<p>During our grant disbursement test, we examined thirty-seven (37) non payroll payments vouchers and noted the following conditions:</p> <ul style="list-style-type: none">a. In eleven (11) payments, the purchase orders were prepared after the services and the invoices were received by the Program. In addition, for one (1) payment the purchase order was not available for our examination;b. In three (3) payments, we did not found evidence of the original invoices.
CRITERIA	24 CFR, Section 85.20 (b) (6) has established that accounting records must be supported by source documentation such as canceled checks, paid bills, payrolls, time and attendance records, contracts, sub-grant awards documents, and others. Also, CFR 24 Subtitle A, Section 85.20 (b) (3) states that effective control and accountability must be maintained for all grant and subgrant cash, real and personal property and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.
CAUSE	The Program failed to maintain an adequate control over the maintenance of the documents that justify the disbursement.
EFFECT	The Program is not in compliance with 24 CFR, Section 85.20 (b) (3) and (6).

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-05 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE COST
RECOMMENDATION	We recommend management to continue strengthening the internal controls and procedures designed to appropriately review the payments vouchers and all the supporting documentation prior to the issuance of a payment or the transfer funds.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	To correct this finding, we gave instructions to the Federal Program Department and the Finance Department to assure that every payment has adequate supporting documents before the issuance of the check. Responsible person: Federal Program Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-06
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE ACTIVITIES
CONDITION	The Program transfer funds to other bank accounts without adequate supporting documentation.
CONTEXT	During our examination, we noted that during fiscal year 2011-2012, the Program transfer funds amounting to \$203,291 in excess of reimbursable expenditures to other bank accounts. Adequate supporting documentation that approved those transfers of funds was not available for our examination.
CRITERIA	24 CFR, Section 85.20 (b) (6) has established that accounting records must be supported by source documentation such as canceled checks, paid bills, payrolls, time and attendance records, contracts, sub-grant awards documents, and others. Also, CFR 24 Section 85.20 (b) (3) states that effective control and accountability must be maintained for all grant and subgrant cash, real and personal property and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.
CAUSE	The Program failed to maintain an adequate control over the maintenance of the documents that justify the disbursement.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24 Section 85.20 (b) (6) and (b) (3).
RECOMMENDATION	We recommend management to continue strengthening the internal controls and procedures designed to appropriately review the payments vouchers and all the supporting documentation prior to the issuance of a payment or the transfer funds.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	We gave instructions to the Finance Director to avoid the transfer of funds between bank accounts that administers Federal funds, unless the transfers are adequately supported. Responsible person: Finance Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-07
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE ACTIVITIES- HOUSING REHABILITATION
CONDITION	The Program failed to maintained appropriate supporting documentation regarding the Housing Rehabilitation.
CONTEXT	<p>As part of our grant disbursement test, we examined six (6) Housing Rehabilitation participant's files and noted the following conditions:</p> <ul style="list-style-type: none">▪ We did not found evidence that the evaluation visit forms and the result evaluation forms were completed for each participants;▪ We did not found evidence of the rehabilitation contracts formalized between the participants and the Municipality;▪ We did not found evidence of the follow-up and final visits made by the Program to the participants, to verify the completeness of the works.
CRITERIA	Code of Federal Regulation 24, Section 570.506 (b) (9) established the documentation that the Municipality shall maintain for residential rehabilitation. The Operational Guide of Housing Rehabilitation (the guide) provided by the Office of Commissioner of Municipal Affairs, the pass through entity, states that the Municipality has to conduct an initial unit inspection to determine if the unit is eligible to be rehabilitating under the criteria of the program.
CAUSE	The Program's internal controls procedures failed to assure that all required information regarding participants were obtained and that the required interviews, visits and inspections to monitor the services were realized in accordance to the pass-through operational guide.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-07 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE ACTIVITIES- HOUSING REHABILITATION
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Sections 570.506 (b) (9) and with the operational guide of housing rehabilitation.
RECOMMENDATION	We recommend management to implement adequate internal controls and procedures in order to assure that the Program's staff completes all the required forms and to inspect and monitor the services in accordance with the regulations and the operational guide.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	We gave instructions to the Housing Rehabilitation Coordinator that complete all the required forms, update all the files and inspect the progress of the services provided. Responsible person: Federal Program Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-08
FEDERAL PROGRAMS	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	CASH MANAGEMENT
CONDITION	The Program did not minimize the time between the receiving of the request of funds from the pass-through entity and the disbursement of funds.
CONTEXT	During our Cash Management test, we examined twenty-two (22) requests of funds made by the Program to the pass-through agency and found that seven (7) requests took between six (6) and ninety one (91) days from the moment the funds were deposited and the issuance of the checks or transfers for the disbursements. In addition, we noted that the Program maintained an average bank overdraft of approximately \$3,721 during the fiscal year 2011-2012.
CRITERIA	Code of Federal Regulations 24, Section 570.489 (c) (1) states that units of general local governments shall use procedures to minimize the time elapsing between the transfer of funds by the state and disbursement made by the grantee.
CAUSE	The Federal Programs and Finance Department of the Municipality did not maintain appropriate cash management procedures in order to request funds to the pass-through agency only for immediate needs.
EFFECT	The Program is not in compliance with Code of Federal Regulations 24, CFR 570.489 (c) (1).
RECOMMENDATION	We recommend management to strengthen its disbursements procedures to minimize the time between the transfer of funds by the pass-through and disbursement made by the Municipality.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	We gave instructions to the Federal Program Director and Finance Director issue the checks immediately after the receipt of the funds. Responsible person: Federal Program Director and Finance Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-09
FEDERAL PROGRAMS	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	PROCUREMENT, SUSPENSION AND DEBARMENT
CONDITION	The Program disbursed funds during fiscal year 2011-2012 not in accordance with the adequate procurement process established by the Federal and State regulations.
CONTEXT	During our grant disbursements test, we noted that there was no evidence of an adequate analysis of the acquisition process (procurement) for five (5) contracts for construction services formalized during the fiscal year 2011-2012.
CRITERIA	Code of Federal Regulation 24, Section 85.36 (b) (9) states that grantees and subgrantees will maintain records sufficient to detail the significant history of a procurement. These records will include, but are not necessarily limited to the following: rationale for the method of procurement, selection of contract type, contractor selection or rejection and the basis for the contract price.
CAUSE	The Program does not performed an appropriate procurement process because failed to document adequately the acquisition process.
EFFECT	The Program is not in compliance with Code of Federal Regulations 24, Section 85.36 (b) (9).
RECOMMENDATION	We recommend management to implement procedures in order to obtain and maintain all the required documentation regards the acquisition process (procurement) to comply with this requirement.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	We gave instructions to the Federal Program Director that the procurement process has to be done for every purchase made with Federal funds. Responsible person: Federal Program Director and the Municipal Secretary

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-10
FEDERAL PROGRAMS	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	PROGRAM INCOME
CONDITION	The Program did not comply with the program income requirement.
CONTEXT	During the fiscal year 2011-2012, the Program received \$81,214 of rental income, from a property that was constructed with CDBG funds. During our program income test, we found that the transactions related with this program income were not recorded in the accounting records of the Program and was not reported as program income to the pass-through entity during the fiscal year 2011-2012.
CRITERIA	Code of Federal Regulations 24, Section 570.504 (a), states that the receipts and expenditures of program income shall be recorded as part of the financial transactions of the grant program.
CAUSE	The Program does not maintained appropriate accounting records over the program income transactions.
EFFECT	The Program is not in compliance with Code of Federal Regulations 24, Subpart J, Section 570.504 (a).
RECOMMENDATION	We recommend management to implement adequate procedures to ensure that the financial transactions related to the program income are properly recorded in the accounting records of the Program.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	We gave instructions to the Finance Department to notify the Federal Programs Director, the revenues received of the projects that generate program income in order to report it to the pass-through entity. Responsible person: Federal Program Director and Finance Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-11
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
CONDITION	The Program did not maintain accurate accounting records of the financial transactions and did not reconcile, the cash account with the quarterly reports submitted to the pass-through entity.
CONTEXT	During our reporting test, we noted that the Program did not maintain adequate accounting records and did not summarize the information of all the financial transactions related to assets, liabilities, revenues and expenditures of the Program, in a formal general ledger or other accounting system. Also, we found that the disbursements reported in the quarterly reports, submitted to the pass-through entity (OCAM), were not traceable to reliable financial information. In addition, the cash balance at June 30, 2012, reported in the quarterly reports, does not agree with the bank reconciliation. Finally, the Municipality did not maintain adequate internal controls and did not maintain adequate supporting documentation over the interfund cash transactions and the corresponding due from and due to account balances.
CRITERIA	Code of Federal Regulations 24, Section 85.20(a) (1) requires that fiscal control and accounting procedures must be sufficient to permit preparation of reports. Code of Federal Regulations 24, Section 85.20(b) (2) requires that grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially- assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.
CAUSE	The Program failed to establish adequate internal controls over the accounting records and the accurate submission of the monthly reports to the pass-through entity.
EFFECT	The Program did not submit accurate quarterly reports to the pass-through entity in order to comply with the Federal regulation.
QUESTIONED COSTS	None

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-11 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
MANAGEMENT RESPONSE	We gave instructions to the Federal Program Director to update the accounting records in order to include all the financial information of the Program. Also, the Program is instructed to reconcile the quarterly reports with the accounting records. Responsible person: Federal Program Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-12
FEDERAL PROGRAM	PUBLIC AND INDIAN HOUSING – (CFDA 14.850) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – PUBLIC HOUSING ADMINISTRATION
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ELEGIBILITY
CONDITION	The Program failed to document properly the eligibility process.
CONTEXT	<p>During our evaluation, we selected a sample of twenty-five (25) participants' files to test the eligibility process and noted the following conditions:</p> <ul style="list-style-type: none">a. For one (1) participant, we did not find evidence of the annual reexamination during the fiscal year 2011-2012;b. For one (1) participant that was subject to annual reexamination, the Enterprise Income Verification (EIV) System was not available for examination.c. In four (4) participants, the incomes reported in the Form 50058, did not agree with third party income verification. Also, for one (1) participant, the family members included in the Form 50058, did not agree with the third party income verification.
CRITERIA	Code of Federal Regulation 24, Section 982.516 (a) (1) states that the PHA must conduct a reexamination of family income and composition at least annually; (2) the PHA must obtain and document in the tenant file third party verification of the following factors or must document in the file why third party verification was not available: (A) reported family annual income; (B) the value of assets; (C) expenses related to deductions from annual income; and (D) other factors that affects the determination of adjusted income.
CAUSE	The Program failed to maintain adequate internal controls that assure that annual reexaminations were calculated using the information obtain from third parties. Also, the Program has not established adequate internal controls over the use of the EIV System during the mandatory annual and interim reexamination as a third party income verification of the family income.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 982.516 (a) (1) and (2).

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-12 (CONTINUED)
FEDERAL PROGRAM	PUBLIC AND INDIAN HOUSING – (CFDA 14.850) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – PUBLIC HOUSING ADMINISTRATION
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ELEGIBILITY
RECOMMENDATION	We recommend to management that the HAP calculations made during the annual reexaminations are prepared using the third parties verifications. We also recommend strengthening the internal controls and procedures designed to verify the family income and composition using the EIV system in each mandatory reexamination of the participants.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	We will continue improving our internal controls and procedures designed to verify the family income during the reexamination of the participants. Responsible person: PHA Administrator and Public Housing Coordinator

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF MAUNABO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-13
FEDERAL PROGRAM	PUBLIC AND INDIAN HOUSING – (CFDA 14.850) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – PUBLIC HOUSING ADMINISTRATION
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
CONDITION	The Program did not maintain accurate accounting records of the financial transactions.
CONTEXT	During our Reporting test, we noted that the Program did not maintain adequate accounting records and did not summarize the information of all the financial transactions related to assets, liabilities, revenues and expenditures of the Program, in a formal general ledger. In addition, we noted that the Program did not maintain proper records and documentation for the interfund cash transactions and the corresponding due from and due to account balances. At June 30, 2012 the Program maintained an interfund balance of \$23,856.
CRITERIA	Code of Federal Regulations 24, Section 85.20 (a) (1) requires that fiscal control and accounting procedures must be sufficient to permit preparation of reports. Code of Federal Regulations 24, Subpart C, Section 85.20 (b) (2) requires that grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially- assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.
CAUSE	The Program failed to establish adequate internal controls over the accounting records and the accurate submission of the monthly reports to the pass-through agency.
EFFECT	The monthly reports submitted to the pass-through entity are not supported with adequate accounting records.
RECOMMENDATION	The Program should implement a set of accounting records in which all the financial transactions of the program are registered. In addition, these records should be reconciled with the monthly reports.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-13 (CONTINUED)
FEDERAL PROGRAM	PUBLIC AND INDIAN HOUSING – (CFDA 14.850) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – PUBLIC HOUSING ADMINISTRATION
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING (CONTINUED)
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	<p>We gave instructions to the Finance Director to maintain on a monthly basis, a general ledger that includes all the financial documentation related to assets, liabilities, revenues and expenditures of the Program.</p> <p>Responsible person: PHA Administrator and PHA Housing Coordinator</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-14
FEDERAL PROGRAM	PUBLIC AND INDIAN HOUSING – (CFDA 14.850) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – PUBLIC HOUSING ADMINISTRATION
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- DEPOSITORY AGREEMENTS
CONDITION	The Municipality failed to enter in a depository agreement with its financial institution.
CONTEXT	During our evaluation, we did not identify evidence of a depository agreement in the form required by HUD with the depository institution of the Municipality.
CRITERIA	Code of Federal Regulation 24, Section 982.156 (a) states that unless otherwise required or permitted by HUD, all program receipts must be promptly deposited with a financial institution selected as depository by the PHA in accordance with HUD requirements. In addition, Code of Federal Regulations 24, 982.156 (c) states that the PHA must enter into an agreement with depository in the form required by HUD.
CAUSE	The Municipality's management failed to enter into agreements in the form required by HUD with its financial institution.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Subpart D, Section 982.156 (a) and (c).
RECOMMENDATION	We recommend management to contact its financial institution and formalize, as soon as possible, the depository agreement in the form established by HUD.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	We will make the necessary arrangements with our financial institution to formalize the depository agreement. Responsible person: Finance Director

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MUNICIPALITY OF MAUNABO

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
11-III-05	Allowable Activities	14.228	\$87,891	No corrective action has been taken. Finding Reference 12-III-06.
11-III-06	Allowable Activities- Housing Rehabilitation and Housekeeper Services	14.228	None	Partially corrective action has been taken. We improved our internal controls of the Housekeepers files. Finding Reference 12-III-07.
11-III-07	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-08.
11-III-08	Procurement, Suspension and Debarment	14.228	None	Partially corrective action has been taken. The auditor issued a finding related to the procurement process. Finding Reference 12-III-09.
11-III-09	Reporting	14.228	None	No corrective action has been taken. Finding Reference 12-III-11.
11-III-10	Allowable Activities	14.850	None	No corrective action has been taken. Finding Reference 12-III-13.
11-III-11	Elegibility	14.850	None	No corrective action has been taken. Finding Reference 12-III-12.
11-III-12	Reporting	14.850	None	No corrective action has been taken. Finding Reference 12-III-13.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
11-III-13	Special Test- Depository Agreement	14.850	None	No corrective action has been taken. Finding Reference 12-III-14.
11-III-14	Allowable Activities	93.575	None	Full corrective action taken. We improved our systems and procedures over the transfer of funds.
11-III-15	Allowable Activities	93.575	None	Full corrective action taken. We improved our systems and procedures over the procurement process.
10-III-05	Allowable Activities	14.228	None	No corrective action has been taken. Finding Reference 12-III-05.
10-III-06	Allowable Activities- Housing Rehabilitation and Housekeeper Services	14.228	None	Partially corrective action has been taken. We improved our internal control procedures over the Housekeepers. Finding Reference 12-III-06
10-III-07	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-08.
10-III-08	Procurement, Suspension and Debarment	14.228	None	No corrective action has been taken. Finding Reference 12-III-09.
10-III-10	Reporting	14.228	None	No corrective action has been taken. Finding Reference 12-III-11.

COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
10-III-11	Reporting	14.850	None	No corrective action has been taken. Finding Reference 12-III-13.
09-III-05	Allowable Activities	14.228	None	Partially corrective action has been taken. Finding Reference 12-III-05.
09-III-06	Allowable Activities	14.850	\$19,505	No corrective action has been taken. Finding Reference 12-III-06.
09-III-07	Allowable Activities	14.228	None	No corrective action has been taken. Finding Reference 12-III-07.
09-III-08	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-08.
09-III-10	Reporting	14.228/ 14.248	None	No corrective action has been taken. Finding Reference 12-III-11.
09-III-11	Reporting	14.850	None	No corrective action has been taken. Finding Reference 12-III-13.
08-III-01	Reporting- Accounting System	All Federal Programs	None	No corrective action has been taken. Finding Reference 12-III-11 and 12-III-13.
08-III-04	Reporting- Bank Reconciliations	All Federal Programs	None	No corrective action has been taken. Finding Reference 12-III-11 and 12-III-13.