

**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES
ÁREA DE ASESORAMIENTO, REGLAMENTACIÓN E INTERVENCIÓN FISCAL
ÁREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE SALINAS
AUDITORÍA 2011-2012
30 DE JUNIO DE 2012**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION
FISCAL YEAR ENDED JUNE 30, 2012**

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INDEPENDENT AUDITOR'S REPORT

**To the Honorable Mayor and
Municipal Legislative Body
Municipality of Salinas
Salinas, Puerto Rico**

We have audited the financial statements of the governmental activities, each major funds, and the aggregate remaining fund information of the Municipality of Salinas as of and for the year ended June 30, 2012 which collectively comprise the 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 an opinion on these financial statements based on our audit.

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

We were unable to obtain, discussion or evaluation from the Municipality's outside legal counsel of the pending or threatened litigations discussed in note 18 to financial statements.

The Municipality did not have a complete, update and accurate accounting records of capital assets, principally infrastructure assets, and estimated landfill closure and post choice care cost liability in order to obtain sufficient and competent evidential matter related to the capital assets reported in the accompanying statement of net assets for 18,029,540, net of accumulated depreciation of 8,099,325.

Because of the significance of the matters discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements referred to previously.

In addition, in our opinion, except for the effect of such adjustment if any as might have been determined to be necessary had we have been able to obtain a discussion or evaluation of pending or threatened litigation from the Municipality's outside legal council as discussed in the third paragraph. the financial statements referred to previously present fairly, in all material respects, the respective financial position of the each major fund, and the aggregate remaining fund information of the Municipality of Salinas, as of June 30, 2012, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITOR'S REPORT (CONTINUED):

In accordance with Governmental Auditing Standards, we have also issued our report dated January 9, 2013, on our consideration of the Municipality of Salinas 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Governmental Auditing Standards and should be considered in assessing the results of our audit.

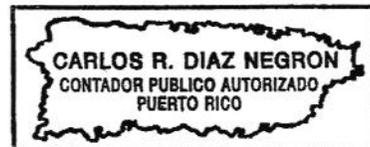
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposed of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and non-Profit Organizations, and is also not a required part of the basic financial statements. Such information is the responsibility of management and was derived form and relates directly to the 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 basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United Sates of America. in my opinion, is fairly presented in all material respects in relation to the general purpose financial statements taken as a whole.

The accompanying financial statements have been prepared assuming that the Municipality will continue as a going concern. As discussed in Note 21 to the financial statements, the Municipality's significant operating losses raise substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 9 and 47 through 49 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.

January 9, 2013
Aguas Buenas, Puerto Rico

License No. 1339
Expire December 1, 2013



The stamp No. **E40866** of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

The management of **Municipality of Salinas**, Puerto Rico (**Municipality**) offers this narrative overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2012. The Management's Discussion and Analysis (MD&A) is designed to focus on the current year activities, resulting changes and currently known facts, and much of the information is comparable to prior year. This MD&A should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements.

The new reporting model required by Governmental Accounting Standards Board Statement No. 34 was implemented during fiscal 2002-2003. This MD&A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

- a broader basis in focusing important issues;
- acknowledgement of an overview of the Municipality's financial activities;
- provide for an evaluation of its financial condition as of the end of the indicated fiscal year, compared with prior year results;
- identification of uses of funds in the financing of the Municipality's variety of activities and;
- assess management's ability to handle budgetary functions.

FINANCIAL HIGHLIGHTS

The following are key financial highlights for the fiscal year:

- ❖ The liabilities of the Municipality exceeded its assets at June 30, 2012 by \$8,319,158, and at June 30, 2011 by \$6,586,178;
- ❖ The Municipality's total deficit increase by a negative net change of \$1,732,980 during fiscal year 2011-2012;
- ❖ As of June 30, 2012, the Municipality's governmental funds reported combined ending deficit of \$4,309,404, an increase \$1,476,982 as restated, from the prior year;
- ❖ At June 30, 2012, the unrestricted deficit was \$28,465,397. During fiscal year 2011-2012, the Municipality issue \$1,685,000 in bonds debt for operational purposes;
- ❖ The Municipality's capital assets inventory increase as a result of this year's operations. Capital assets (net of accumulated depreciation) as of June 30, 2012 was \$18,029,540;
- ❖ The investment in capital assets for this year was \$1,628,350;
- ❖ Loans principal payments were \$1,283,750 and \$1,090,000 in 2012 and 2011, respectively.

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.

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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENT-WIDE FINANCIAL STATEMENTS (CONTINUED)

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, solid waste disposal, 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 Municipality's basic services are reported in the government fund financial statements. The government funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted into cash. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions.

The Municipality adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

NOTES TO THE BASIC FINANCIAL STATEMENTS

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

OTHER INFORMATION

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information containing budget to actual comparisons for the general and major funds.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENT-WIDE FINANCIAL ANALYSIS

GOVERNMENTAL NET ASSETS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the Municipality, liabilities exceeded assets by \$8,319,158 as of June 30, 2012 versus \$6,586,178 as of June 30, 2011. Our analysis below focuses on the net assets (**Table 1**) and changes in net assets of the Municipality's governmental activities.

Table 1			
Statement of Net Assets	2012	2011	
Current and non-current assets	\$ 4,455,049	\$ 4,177,261	
Capital assets	<u>18,029,540</u>	<u>17,118,007</u>	
Total Assets	<u>22,484,589</u>	<u>21,295,268</u>	
Current liabilities	8,589,231	7,184,089	
Long-term liabilities	<u>22,214,516</u>	<u>20,697,357</u>	
Total Liabilities	<u>30,803,747</u>	<u>27,881,446</u>	
Net assets:			
Investment in capital assets, net of related debt	15,864,540	14,768,007	
Restricted	4,281,699	4,127,055	
Deficit	<u>(28,465,397)</u>	<u>(25,481,240)</u>	
Total Net Assets	<u>\$ (8,319,158)</u>	<u>\$ (6,586,178)</u>	

The Municipality's net deficit contains a portion that it is invested in capital assets (e.g. land, buildings, machinery and equipment); less any related debt used to acquire those assets still outstanding. These capital assets are used to provide services to citizens; consequently these assets are not available for future spending. It should also be noted that the resources required to repay the related debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. An additional portion of the Municipality's net assets represents resources that are subject to external restrictions on how they may be used.

GOVERNMENTAL ACTIVITIES

Governmental activities decreased the Municipality's deficit. Key elements of this increase are as follows: the Municipality's governmental activities had net expenses of \$15,916,074. However, these services are intended to be primarily funded by taxes, as opposed to charges for services and grants, and those taxes and other general revenues exceed net expenses by \$(1,732,980).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENT-WIDE FINANCIAL ANALYSIS (CONTINUED)

GOVERNMENTAL ACTIVITIES (CONTINUED)

The cost of all governmental activities this year was \$19,017,831. **Table 2** presents the cost of each of the Municipality's largest programs.

Table 2			
Statement of Activities	2012	2011	
Revenues			
Grants and contributions	\$ 2,953,706	\$ 2,623,195	
General revenues:			
Property taxes	3,499,876	3,225,309	
Volume of business taxes	1,632,387	2,255,541	
Sales taxes	1,450,747	1,289,268	
Intergovernmental	5,610,898	5,378,773	
Rent	23,515	53,860	
Licenses and permits	1,618,494	564,224	
Miscellaneous	347,177	689,394	
Charges for services	148,051	72,078	
Total revenues	<u>17,284,851</u>	<u>16,151,642</u>	
Expenses			
General government	6,153,409	5,363,984	
Public safety	1,690,023	1,397,116	
Public works	5,234,174	5,745,115	
Culture and recreation	1,103,321	1,339,956	
Human services and welfare	3,358,852	2,503,642	
Urban development	735,606	915,139	
Education	149,750	151,826	
Interest on long-term debts	592,696	440,466	
Total expenses	<u>19,017,831</u>	<u>17,857,244</u>	
Changes in net assets	(1,732,980)	(1,705,602)	
Net assets – beginning, as restated	(6,586,178)	(4,880,576)	
Net assets – ending	<u>\$ (8,319,158)</u>	<u>\$ (6,586,178)</u>	

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENT FUND FINANCIAL ANALYSIS

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

Table 3

Balance Sheet

	<u>2012</u>	<u>2011</u>
Assets:		
Total assets – Major Funds	\$ 5,300,344	\$ 4,750,388
Total assets – Other Funds	1,287,851	1,307,678
Combined total assets	6,588,195	6,058,066
Liabilities:		
Total liabilities – Major Funds	10,355,567	8,506,865
Total liabilities – Other Funds	542,032	383,623
Combined total liabilities	10,897,599	8,890,488
Fund Balances:		
Restricted	4,281,699	4,169,019
Unrestricted	(8,591,103)	(7,001,441)
Combined total fund balances	(4,309,404)	(2,832,422)
Total liabilities and fund balances	\$ 6,588,195	\$ 6,058,066

Table 4

Changes in Fund Balances

	<u>2012</u>	<u>2011</u>
Revenues:		
Total revenues – Major Funds	\$ 14,275,411	\$14,134,283
Total revenues – Other Funds	2,851,276	2,180,695
Combined total revenues	17,126,687	16,314,978
Expenditures:		
Total expenditures – Major Funds	17,284,185	16,495,143
Total expenditures – Other Funds	3,299,484	2,763,675
Combined total expenditures	20,583,669	19,258,818
Other financing sources (uses):		
Proceed from issuance of bonds	1,980,000	3,760,000
Transfer – In	332,741	294,420
Transfer – Out	(332,741)	(292,420)
Combined other financing sources (uses), net	1,980,000	3,760,000
Net changes in fund balance	(1,476,982)	816,160
Fund Balance – beginning, as restated	(2,832,422)	(3,648,582)
Fund Balance – ending	<u>\$ (4,309,404)</u>	<u>\$ (2,832,422)</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENTAL FUNDS

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of its fiscal year. At June 30, 2012, the Municipality's governmental funds reported combined ending deficit of \$(4,309,404), an increase of \$1,476,982 from the prior year.

The Municipality has an unassigned deficit of \$8,591,103 in its General Fund. The remainder of the balance is restricted to indicate that it is not available for new spending because it has already been restricted; (a) to pay debt service \$1,739,890 and (b) for other restricted purposes \$2,541,809.

BUDGETARY HIGHLIGHTS

Budget and actual comparison schedules are provided in the Basic Financial Statements for the General Fund. The Budgetary Comparison Schedule of the General Fund shows the original adopted budgets, the final revised budget, actual results, and variance between the final budget and actual results for the general and major special revenue funds.

After the original budget is approved, it may be revised for a variety of reasons such as unforeseen circumstances and other unanticipated revenues. Differences between the original 2012 budget and the final amended budget for the General Fund were relatively minor and can be summarized as follows:

- ❖ The original budget was amended during the fiscal year 2011-2012 by changes between the expenditures accounts.

CAPITAL ASSETS AND DEBT ADMINISTRATION

The Municipality's investment in capital assets for its governmental type activities as of June 30, 2012 amounted to \$18,029,540 (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements, machinery and equipment, parks, roads, highways, and bridges. The total increase in the Municipality's investment in capital assets for the current fiscal year was \$1,628,350. Additions during the fiscal year was principally for building and infrastructure construction and purchase of new vehicles and equipment, necessary to provides services to our citizens. **Table 5** present the major classes of capital assets.

Table 5	
Capital Assets (net of depreciation)	Amount
Construction in progress	\$ 160,796
Land	5,893,658
Buildings	6,810,058
Infrastructure	4,768,477
Vehicles	279,348
Machinery and equipment	<u>117,203</u>
Total Assets	<u>\$18,029,540</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

LONG-TERM DEBT

At June 30, 2012 the Municipality had total of \$22,214,516 in general obligations and others outstanding debts, as shown in **Table 6**. Of this amount, \$13,530,000 comprises debt backed by the full faith and credit of the government and \$8,684,516 is other obligations.

Table 6	
Long Term Debts	Amount
General obligations	\$13,530,000
Others	<u>8,684,516</u>
Total Long Term Debts	<u>\$22,214,516</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 and advances of property taxes. 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.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Local, national and international economic factors influence the Municipality's revenues. Positive economic growth is correlated with increased revenues from property taxes, volume of business taxes, sales taxes, charges for services, as well as state and federal grants. Economic growth in the local economy may be measured by a variety of indicators such as employment growth, unemployment, new construction, assessed valuation, and other revenues.

All of these factors were considered in preparing the Municipality's budget for the 2012 fiscal year. Some cost reductions helped fund improvements of existing facilities, public safety and works, economic development initiatives and human service improvements.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Municipality's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional information contact the Municipality's Finance Department at (787) 824-3060.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
STATEMENT OF NET ASSETS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

	Governmental Activities
ASSETS:	
Cash and Investments.....	\$ 98,209
Cash with Fiscal Agent.....	3,693,218
Receivables (net):	
Property Taxes.....	193,709
Sales Taxes.....	140,856
Federal Grants.....	216,204
State Government.....	70,106
Others.....	42,747
	4,455,049
Capital Assets (Note 8):	
Land and Construction in Progress.....	6,054,454
Other Capital Assets, (Net of Depreciation).....	11,975,086
Total Capital Assets.....	18,029,540
Total Assets	22,484,589
 LIABILITIES:	
Bank Overdraft.....	126,008
Accounts Payable and Accrued Expense.....	5,429,055
Bonds Payable.....	1,025,000
Accrued Interests.....	293,827
Due to Governmental Activities.....	373,770
Claims & Judgments.....	104,400
Deferred Revenue.....	1,237,171
Long-Term Liabilities (Note 10):	
Due within One Year.....	1,223,433
Due in More than One Year.....	20,991,083
Total Liabilities	30,803,747
 NET ASSETS	
Invested in Capital Assets, Net of Related Debt.....	15,864,540
Restricted for:	
Debt Service Fund.....	1,739,890
Other Purposes.....	2,541,809
Unrestricted (Deficit).....	(28,465,397)
Total Net Assets (Deficit)	\$ (8,319,158)

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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:					
General Government.....	\$ (6,153,409)	\$ -	\$ -	\$ -	\$ (6,153,409)
Public Safety.....	(1,690,023)	-	-	-	(1,690,023)
Public Works.....	(5,234,174)	120,481	5,064	-	(5,108,629)
Culture and Recreation.....	(1,103,321)	25,000	-	-	(1,078,321)
Human Services and Welfare.....	(3,358,852)	2,570	789,758	-	(2,566,524)
Urban Development.....	(735,606)	-	290,084	1,720,067	1,274,545
Education.....	(149,750)	-	148,733	-	(1,017)
Interest on Long-Term Debt.....	(592,696)	-	-	-	(592,696)
Total Governmental Activities....	<u>\$(19,017,831)</u>	<u>\$ 148,051</u>	<u>\$ 1,233,639</u>	<u>\$ 1,720,067</u>	<u>(15,916,074)</u>

General Revenues:

Taxes:

Property Taxes.....	2,310,048
Property Taxes, levied for Debt Services.....	1,189,828
Sales Taxes.....	853,449
Sales Taxes, levied for Debt Services.....	597,298
Volume of Business Taxes.....	1,632,387
Licenses, Permits and Other Local Taxes.....	1,618,494
Intergovernmental.....	5,610,898
Rent.....	23,515
Miscellaneous.....	347,177
Total General Revenues.....	14,183,094

CHANGE IN NET ASSETS.....	(1,732,980)
Net Assets - Beginning of Year.....	(6,586,178)
NET ASSETS - END OF YEAR.....	<u>\$ (8,319,158)</u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
BALANCE SHEET - GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

	General Fund	State Assignment Fund	Debt Service Fund	Other Governmental Funds	Total Funds
ASSETS:					
Cash and Investments.....	\$ -	\$ -	\$ -	\$ 98,209	\$ 98,209
Cash with Fiscal Agent.....	44,250	-	2,981,155	667,813	3,693,218
Receivables:					
Property Taxes.....	175,222	-	18,487	-	193,709
Sales Tax.....	81,781	-	59,075	-	140,856
Federal Grants.....	-	-	-	216,204	216,204
State Government.....	-	-	-	70,106	70,106
Due from Other Funds.....	188,634	1,751,740	-	192,772	2,133,146
Others.....	-	-	-	42,747	42,747
Total Assets.....	\$ 489,887	\$ 1,751,740	\$ 3,058,717	\$ 1,287,851	\$ 6,588,195
LIABILITIES AND FUND BALANCES:					
Liabilities:					
Bank Overdraft.....	\$ 126,008	\$ -	\$ -	\$ -	\$ 126,008
Accounts Payable & Accrued Expense Liabilities.....	5,294,126	-	-	134,929	5,429,055
Bonds Payable.....	-	-	1,025,000	-	1,025,000
Accrued Interests.....	-	-	293,827	-	293,827
Due to Governmental Units.....	373,770	-	-	-	373,770
Due to Other Funds.....	1,944,512	-	-	188,634	2,133,146
Claims & Judgments.....	104,400	-	-	-	104,400
Deferred Revenue:					
Volume of Business Tax.....	1,018,702	-	-	-	1,018,702
Property Taxes.....	175,222	-	-	-	175,222
Federal Grants.....	-	-	-	218,469	218,469
Total Liabilities.....	9,036,740	-	1,318,827	542,032	10,897,599
Fund Balances:					
Restricted.....	44,250	1,751,740	1,739,890	745,819	4,281,699
Unassigned.....	(8,591,103)	-	-	-	(8,591,103)
Total Fund Balances.....	(8,546,853)	1,751,740	1,739,890	745,819	(4,309,404)
TOTAL LIABILITIES AND FUND BALANCES.....	\$ 489,887	\$ 1,751,740	\$ 3,058,717	\$ 1,287,851	\$ 6,588,195

See accompanying notes to basic financial statements.

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

	General Fund	State Assignment Fund	Debt Service Fund	Other Governmental Funds	Total Funds
REVENUES					
Property Taxes.....	\$ 2,151,886	\$ -	\$ 1,189,828	\$ -	\$ 3,341,714
Volume of Business Taxes.....	1,632,387	-	-	-	1,632,387
Sales Taxes.....	853,449	-	597,298	-	1,450,747
Charges for Services.....	120,481	-	-	27,570	148,051
Federal Assistances.....	-	-	-	2,464,389	2,464,389
Intergovernmental.....	5,610,898	130,000	-	359,317	6,100,215
Licenses and Permits.....	1,618,494	-	-	-	1,618,494
Rent.....	23,513	-	-	-	23,513
Miscellaneous.....	347,177	-	-	-	347,177
Total Revenues.....	12,358,285	130,000	1,787,126	2,851,276	17,126,687
EXPENDITURES					
Current:					
General Government.....	6,408,854	-	-	53,184	6,462,038
Public Safety.....	1,644,728	-	-	282,829	1,927,557
Public Works.....	4,829,346	-	-	-	4,829,346
Culture and Recreation.....	1,067,983	-	-	-	1,067,983
Human Services and Welfare.....	1,397,065	-	-	863,888	2,260,953
Urban Development.....	-	59,762	-	1,949,833	2,009,595
Education.....	-	-	-	149,750	149,750
Debt Service:					
Principal.....	-	-	1,283,750	-	1,283,750
Interest.....	-	-	592,697	-	592,697
Total Expenditures.....	15,347,976	59,762	1,876,447	3,299,484	20,583,669
Excess (deficiency) of revenues over (under) expenditures	(2,989,691)	70,238	(89,321)	(448,208)	(3,456,982)
OTHER FINANCING SOURCES (USES)					
Proceed From Issuance of Bonds.....	1,685,000	-	-	295,000	1,980,000
Transfers - In.....	25,028	-	307,713	-	332,741
Transfers - Out.....	(307,713)	-	-	(25,028)	(332,741)
Total Other Financing Sources and (Uses).....	1,402,315	-	307,713	269,972	1,980,000
Net Change in Fund Balances.....	(1,587,376)	70,238	218,392	(178,236)	(1,476,982)
Fund Balance - Beginning as Restated.....	(6,959,477)	1,681,502	1,521,498	924,055	(2,832,422)
FUND BALANCES- ENDING.....	\$ (8,546,853)	\$ 1,751,740	\$ 1,739,890	\$ 745,819	\$ (4,309,404)

02/09/2013

See accompanying notes to basic financial statements.

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

Total Fund Balances – Governmental Funds \$ (4,309,404)

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:

Capital Assets.....	\$26,128,865	
Accumulated Depreciation.....	<u>(8,099,325)</u>	
 Total Capital Assets.....		 18,029,540

Some of the Municipality’s revenues will be collected after year end, but are not available soon enough to pay for the current period’s expenditures and therefore, are deferred in the funds:

Municipal Revenue Collection Center		175,222
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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	13,530,000	
Compensated Absences	1,167,537	
Property Tax Debt – Law 42.....	974,140	
Property Tax Debt – Law 146	192,331	
Claims & Judgments	1,040,121	
Debt Agreement- State Retirement System Administration	64,485	
Debt Agreement- State Department of Labor.....	74,452	
State Health Insurance Administration	1,097,858	
Landfill Closure and Post-Closures Costs.....	<u>4,073,592</u>	
 Total Long-Term Liabilities.....		 <u>(22,214,516)</u>

Total Net Assets of Governmental Activities..... \$ (8,319,158)

See accompanying Notes to Basic Financial Statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES (CONTINUE)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

Net Change in Fund Balances – Total Governmental Funds \$ (1,476,982)

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.....	\$ 1,628,350	
Depreciation Expense.....	<u>(716,817)</u>	
Excess of Capital Outlay over Depreciation Expense.....		911,533

Revenues in the statement of activities that not provide current financial resources are not reported as revenue in the funds 175,222

Revenues in the statement of revenues that correspond to prior year resources are recorded as revenues in the statement of activities (17,060)

Debt proceeds provide current financial resources to governmental funds, but issuing debt increases long- term liabilities in the Statement of Net Assets. In the current period, these amounts are:

General obligation bond.....		(1,980,000)
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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. 1,283,750

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.....	(7,460)	
Decrease in Property Tax Debt – Law 42.....	23,150	
Decrease in Property Tax Debt – Law 146.....	9,615	
Decrease in LIMS Repayment Plan.....	22,040	
Decrease in Claims & Judgments.....	368,541	
Decrease in Debt Agreement- State Retirement System Administration.....		126,981
Increase in Debt Agreement- State Department of Labor.....	(74,452)	
Increase in State Health Insurance Administration.....	<u>(1,097,858)</u>	
Total Additional Expenditures.....		<u>629,443</u>

Change in Net Assets of Governmental Activities (Page 11)..... \$ (1,732,980)

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Salinas, Puerto Rico (Municipality) is a local governmental with full legislative, fiscal and administrative power to operate as a governmental under Law No. 81 of August 30, 1991, as amended, known as the *Autonomous Municipality Act of the Commonwealth of Puerto Rico (Law No. 81)*.

The Municipality's governmental system consists of executive and legislative branches. The Constitution of the Commonwealth of Puerto Rico (the "Commonwealth") provides for the separation of powers of the executive, legislative and judicial branches. A Mayor, elected every four years by the citizens, exercises the executive power of the Municipality. The legislative power is exercised by the Municipal Legislature, which is also elected every four years. 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. On July 1, 2002, 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 new 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 SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

As previously mentioned, on July 1, 2002, 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.

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. The specific evaluations of the criteria applicable to the Municipality indicate that none 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.

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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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

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.
- ❖ Landfill closure and post-closure costs are recorded as expenditure during the estimated life of the landfill. The amount of these costs during fiscal year 2011-2012 has been reported only in the government-wide financial statements.
- ❖ Claims and judgments are recorded as expenditure when incurred. The amount of claims and judgments 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 SALINAS
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 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 Statement of Activities is focused on both the gross and net costs per functional category. The statement reduces gross expenses (including depreciation) by related program revenues, operating and capital grants. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

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 previous financial reporting model. Emphasis here is on the major funds in the governmental category. Non-major funds are summarized into a single column.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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)

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 new 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:

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.

State Assignment Fund – This is the fund used to account for all the transactions of the State Assignment by Legislature Resolutions. The primarily objectives of this assignments is the development of projects on communities, not-for-profit organizations and indirect assignment to persons of low and moderate income.

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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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

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. Fund types are as follows:

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

Special Revenue Fund– This is the fund used to account for revenues derived from local funds, state grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality’s ordinances or state statutes.

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.

Capital Projects Fund – This is the fund used to account for financial resources used for the acquisition or construction of major capital facilities. The uses and limitations of each capital projects fund are specified by Municipality’s ordinances or state statutes.

E. FUND BALANCES

In the current year, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB 54). The fund balances are reported in five categories: 1) Nonspendable, 2) Restricted, 3) Committed, 4) Assigned and 5) Unassigned.

- ❖ **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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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)

- ❖ **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.

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

E. Budgetary Control

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, 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 Finance Director to implement grant budgets as the grant applications are accepted by the Municipality; and (3) to the Finance 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

E. Budgetary Control (Continued)

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;
5. If a budget is not adopted prior to the end of 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

E. Budgetary Control (Continued)

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.

F. Cash, Cash Equivalent and Investment

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

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.

G. 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.

H. 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

I. 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 \$500 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
Machinery and equipment	3 to 5

J. 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.

K. 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 SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

K. 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>
<u>\$1,160,077</u>	<u>\$7,460</u>	<u>\$ -</u>	<u>\$1,167,537</u>	<u>\$175,122</u>	<u>\$992,415</u>

L. 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.

M. Interfund Transactions

Interfund transactions are reflected as loans, reimbursements or transfers. Loans are reported as receivables and payables as appropriate and are eliminated in the statement of net assets. 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. 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 SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

O. 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.

P. 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.

Q. 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.

R. 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 \$192,877. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$247,127 for workers compensation insurance covering all municipal employees.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

S. Future Adoption of Accounting Pronouncements

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

- ❖ GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*. This Statement is effective for periods beginning 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, 2012;
- ❖ 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;

The Authority's management has concluded that the future adoption of these GASB Statements will not have a significant impact on the Authority's basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

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 risk that applies to the Municipality is the custodial risk.

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.

The Municipality's bank balances in commercial banks of \$98,209 in the Other Governmental Funds were fully collateralized at June 30, 2012.

The deposits at GDB of \$44,250 in the General Fund, the \$2,981,155 in the Debt Service Fund, and the \$667,813 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 SALINAS
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 amounting to \$175,222 in the General Fund represents the final liquidation of the property taxes of the fiscal year 2011-2012, not collected by the Municipality at June 30, 2012. In addition, property taxes receivable in Debt Service Fund in the amount of \$18,487 represents the amount due of property taxes 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 \$81,781 in the General Fund and \$59,075 in the Debt Service Fund represents the amounts due by the taxpayers at June 30, 2012.

C. Federal Grants Receivable

Federal grants receivable in the 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:

<u>Description</u>	<u>Amount</u>
Community Development Block Grant – State Program	\$102,719
Child Care Development Block Grant	31,213
Energy Efficiency and Conservation Block Grant	50,544
Homelessness Prevention and Rapid Re- housing Program	<u>31,728</u>
Total	<u>\$216,204</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 3 – RECEIVABLES (CONTINUED)

D. State Government Receivables

State government receivables in other governmental funds represent expenditures incurred not yet reimbursed by the state agencies. Following is a detail of the state government receivables:

<u>Governmental Entity</u>	<u>Amount</u>
Department of Labor and Human Resources – Law 52	<u>\$70,106</u>
Total	<u>\$70,106</u>

E. Due From Other Funds

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

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed	\$ 188,634
State Assignment Fund	General Fund	Reimbursable expenditures	1,751,740
Other Governmental Funds	General Fund	Reimbursable expenditures	83,952
Other Governmental Funds	General Fund	Cash pool in the same bank account and reimbursable expenditures	<u>108,820</u>
Total			<u>\$2,133,146</u>

F. Other Receivables

Other receivables in Other Governmental Funds, for the amount of \$42,747, represent Section 8 Housing Choice Vouchers receivables at June 30, 2012, resulting from fraud recoveries.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 4 – CAPITAL ASSETS

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. 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):

Governmental Activities	Balance July 1, 2011	Additions	Retirements / Reclassifications	Balance June 30, 2012
Capital asset, not being depreciated:				
Land	\$ 5,893,658	\$ -	\$ -	\$ 5,893,658
Construction in progress	<u>1,473,422</u>	<u>-</u>	<u>(1,312,626)</u>	<u>160,796</u>
Total capital assets not being depreciated	<u>7,367,080</u>	<u>-</u>	<u>(1,312,626)</u>	<u>6,054,454</u>
Capital assets, being depreciated:				
Buildings	8,441,000	200,544	1,258,249	9,899,793
Infrastructure	5,102,310	1,144,977	54,377	6,301,664
Machinery and equipment	1,263,089	-	-	1,263,089
Motor vehicles	<u>2,327,036</u>	<u>282,829</u>	<u>-</u>	<u>2,609,865</u>
Total capital assets being depreciated	<u>17,133,435</u>	<u>1,628,350</u>	<u>1,312,626</u>	<u>20,074,411</u>
Less accumulated depreciation for:				
Buildings	(2,864,356)	(225,379)	-	(3,089,735)
Infrastructure	(1,147,780)	(385,407)	-	(1,533,187)
Machinery and equipment	(1,112,972)	(32,914)	-	(1,145,886)
Motor vehicles	<u>(2,257,400)</u>	<u>(73,117)</u>	<u>-</u>	<u>(2,330,517)</u>
Total accumulated depreciation	<u>(7,382,508)</u>	<u>(716,817)</u>	<u>-</u>	<u>(8,099,325)</u>
Total capital assets being depreciated, net	<u>9,750,927</u>	<u>911,533</u>	<u>1,312,626</u>	<u>11,975,086</u>
Governmental activities capital assets, net	<u>\$ 17,118,007</u>	<u>\$ 911,533</u>	<u>\$ -</u>	<u>\$18,029,540</u>

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

Governmental activities	Amount
General government	\$ 159,783
Urban development	71,532
Public Safety	45,295
Public Works	404,828
Culture and Recreation	35,338
Human services and welfare	<u>41</u>
Total depreciation expenses	<u>\$ 716,817</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 4 – CAPITAL ASSETS (CONTINUED)

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.

NOTE 5 – BANK OVERDRAFT

The bank overdraft of \$126,008 in the General Fund was the result of the adjusted cash balances at June 30, 2012, of the Municipality's current account, payroll account and other miscellaneous 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	\$4,145,643	\$1,148,483	\$5,294,126
Other Governmental Funds	<u>134,929</u>	<u>-</u>	<u>134,929</u>
Total	<u>\$4,280,572</u>	<u>\$1,148,483</u>	<u>\$5,429,055</u>

NOTE 7 – DUE TO OTHER GOVERNMENTAL UNITS

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

Governmental Agency	Amount
Puerto Rico Aqueduct and Sewer Authority	\$ 370,636
General Service Administration	<u>3,134</u>
Total	<u>\$ 373,770</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 8 – CLAIM AND JUDGMENTS

Liabilities of \$104,400 reported in the General Fund represent the balance owed for debt agreements and claims and judgments at June 30, 2012, as described in Note 19.

NOTE 9 – DEFERRED REVENUES

- A. Volume of business tax** – The deferred revenues of \$1,018,702 in the General Fund relates to the volume of business tax collected in fiscal year 2010-2011 that will be earned in fiscal year 2011-2012. The deferred revenues of \$175,222 relates to the 2011-2012 property tax final liquidation.
- B. Federal Grants** – The deferred revenues presented in Other Governmental Funds represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

Program Description	Amount
Community Services Block Grant	\$ 7,400
Public Assistance Grants	176,769
American Recovery and Re- investment Act Grant	26,734
Brownfield Grants	<u>7,566</u>
Total	<u>\$ 218,469</u>

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	\$ 12,833,750	\$ 1,980,000	\$ (1,283,750)	\$ 13,530,000	\$ 900,000
Property Tax Debt – Law 42	997,290	-	(23,150)	974,140	24,605
Compensated absences	1,160,077	7,460	-	1,167,537	175,122
LIMS Repayment Plan	22,040	-	(22,040)	-	-
Property Tax Debt – Law 146	201,946	-	(9,615)	192,331	9,616
Claims and Judgments	1,408,662	-	(368,541)	1,040,121	-
Estimated landfill closure and post-closure care cost	4,073,592	-	-	4,073,592	-
State Insurance Health Administration	-	1,097,858	-	1,097,858	-
Debt Agreement- State Department of Labor	-	74,452	-	74,452	49,605
Debt Agreement- State Retirement System	<u>191,466</u>	<u>136,476</u>	<u>(263,457)</u>	<u>64,485</u>	<u>64,485</u>
Total	<u>\$ 20,888,823</u>	<u>\$ 3,296,246</u>	<u>\$ (1,970,553)</u>	<u>\$ 22,214,516</u>	<u>\$ 1,223,433</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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
\$2,240,000, Series 1997, for operational purposes, payable in semi-annual installments ranging from \$55,000 to \$200,000, excluding interests from 6.00% to 8.00%, through July 1, 2017	\$ 870,000
\$1,495,000, Series 2002, for public improvement, payable in annual installments ranging from \$20,000 to \$115,000, excluding interests from 4.50% to 5.31% through January 1, 2027	1,160,000
\$1,710,000, Series 2004, for operational purposes, payable in semi-annual installments ranging from \$30,000 to \$125,000, excluding interests at 6.00%, through July 1, 2028	1,355,000
\$2,300,000, Series 1993, for operational purposes, payable in semi-annual installments ranging from \$15,000 to \$60,000, excluding interests from 4.375% to 8.75%, through October 1, 2012	60,000
\$385,000, Series 2004, for operation purposes, payable in semi-annual installments ranging from \$5,000 to \$30,000, excluding interests from 5.00% to 7.50%, through July 1, 2028	310,000
\$805,000, Series 2004, for operational, payable in semi-annual installments ranging from \$15,000 to \$65,000, excluding interests from 5.00% to 6.00%, through July 1, 2028	640,000
\$755,000, Series 2006, for purchase of equipment, payable in annual installments ranging from \$90,000 to \$130,000 excluding interests from 6.60% to 7.25%, through July 1, 2013	130,000
\$1,005,000, Series 2007, for operation purposes, payable in annual installments ranging from \$50,000 to \$120,000, excluding interests from 6.60% to 7.00%, through July 1, 2018	605,000
\$725,000, Series 2009, for operation purposes, payable in annual installments ranging from \$45,000 to \$100,000, excluding interests from 2.43% to 7.50%, through July 1, 2018	500,000

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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 (CONTINUED)

DESCRIPTION	AMOUNT
\$645,000, Series 2010, for purchase of building, payable in semi annual-installments ranging from \$10,000 to \$55,000, excluding interests from 4.75% to 7.50%, through July 1, 2034	615,000
\$1,635,000, Series 2010, for operation purposes, payable in semi-annual installments ranging from \$45,000 to \$160,000, excluding interests from 5.00% to 7.50%, through July 1, 2027	1,485,000
\$390,000, Series 2010, for operation purposes, payable in semi-annual installments ranging from \$40,000 to \$70,000, excluding interests from 6.00% to 7.50%, through July 1, 2016	250,000
\$3,760,000, Series 2011, for operation purposes, payable in semi-annual installments ranging from \$50,000 to \$290,000, excluding interests from 6.00% to 7.50%, through July 1, 2016	3,650,000
\$295,000, Series 2012, for purchase of vehicles, payable in semi-annual installments ranging from \$35,000 to \$50,000, excluding interests from 6.00% to 7.50%, through July 1, 2018	260,000
\$905,000, Series 2012, for operation purposes, payable in semi-annual installments ranging from \$15,000 to \$80,000, excluding interests from 6.00% to 7.50%, through July 1, 2036	890,000
\$780,000, Series 2012, for operation purposes, payable in semi-annual installments ranging from \$30,000 to \$85,000, excluding interests from 6.00% to 7.50%, through July 1, 2026	<u>750,000</u>
Total General Obligations – Bonds	<u>\$ 13,530,000</u>

B. BONDS AND NOTES AMORTIZATION

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

Year Ending June 30,	Principal payment	Interest payment	Total
2013	\$ 900,000	\$ 738,703	\$ 1,638,703
2014	765,000	856,335	1,621,335
2015	820,000	805,560	1,625,560
2016	885,000	751,193	1,636,193
2017	860,000	692,421	1,552,421
2018-2022	2,810,000	2,798,542	5,608,542
2023-2027	3,465,000	1,833,788	5,298,788
2028-2032	1,770,000	850,600	2,620,600
2033-2037	<u>1,255,000</u>	<u>200,625</u>	<u>1,455,625</u>
Total	<u>\$ 13,530,000</u>	<u>\$ 9,527,767</u>	<u>\$ 23,057,767</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 10 – GENERAL LONG-TERM DEBTS (CONTINUED)

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 \$974,140.

D. COMPENSATED ABSENCES

The government-wide statement of net assets includes \$1,167,537 of accrued sick leave benefits, and accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

E. PROPERTY TAX DEBT – LAW 146

On September 24, 2002, the CRIM, on behalf of the municipalities of Puerto Rico, entered into a financing agreement with GDB pursuant to the provisions of Law No. 146 of October 11, 2001. The purpose of this financing agreement was to extinguish in advance certain bonds payable issued by the Public Finance Corporation, a subsidiary of the GDB, which were originally issued to pay certain property tax receivables owned by the municipalities of Puerto Rico through 1996. The outstanding balance of the note payable to the CRIM at June 30, 2012 amounted to \$192,331.

F. CLAIMS AND JUDGMENTS

Liabilities of \$1,040,121 reported in the statement of net assets represent the balance owed for claims and judgments at June 30, 2012, as described in Note 18.

G. ESTIMATED LANDFILL CLOSURE AND POST-CLOSURE CARE COST

According to the regulations set forth by the U.S. Environment Protection Agency (EPA) in its "Solid Waste Disposal Facility Criteria", issued on October 9, 1991, the Municipality is required to place a final cover on the Municipality's landfill site when it stops accepting waste, and to perform certain maintenance and monitoring functions at the site for 30 years after closure. The Municipality has not performed a study in accordance with GASB No. 18, to verify the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. The Municipality's management has recognized a liability of \$4,073,592 in the accompanying GWFS using an estimate of the closing and post closing costs at June 30, 2012. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations. At June 30, 2012, the Municipality's landfill is still operating and its remaining estimated useful life is not determinable.

H. STATE INSURANCE HEALTH ADMINISTRATION

Liabilities of \$1,097,858 reported in the statement of net assets represent the balance owed for services provided by the State Insurance Health Administration to the Municipality and not paid at June 30, 2012.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 10 – GENERAL LONG-TERM DEBTS (CONTINUED)

I. 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 \$74,452.

J. STATE RETIREMENT SYSTEM ADMINISTRATION

The Municipality entered into a financing agreement with the State Retirement System Administration, for the payment of the special laws and accumulated interests. The balance at June 30, 2012 of this agreement was \$64,485.

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, 2012 was 8.53% (of which taxpayers pay 8.33% and 0.20% is reimbursed by the Department of Treasury); after June 30, 2012, the total personal property tax rate has been 8.53%.

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 10.33% (of which 10.03% is paid by taxpayers and 0.20% is also reimbursed by the Department of Treasury).

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 SALINAS
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 Salinas. 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 SALINAS
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 municipal sales and use tax of 1.5%. This municipal sales and use tax has in general the same tax base and limitations (except for unprocessed foods) as those provided by the Commonwealth's sales and use tax.

Section 6189 of the Puerto Rico Internal Revenue Code of 1994, as amended, authorizes the Municipalities in Puerto Rico to impose a sales and use tax to consumers. This tax must be imposed in conformity with the base, exemptions and limitations contained 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 SALINAS
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	Debt Service Fund	Debt retirement	\$ 307,713
	Other	To cover	
General Fund	Governmental Fund	operational costs	<u>25,028</u>
		Total	<u>\$ 332,741</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 SALINAS
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 SALINAS
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 June 30, 2012 was approximately \$384,920. 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 – 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. With respect to pending litigation, the Municipality has reported liabilities of \$104,400 in the General Fund for awarded unfavorable judgments, plus \$1,040,121 in the government wide statement of net assets in addition to the amount reported in the General Fund.

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. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
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 (Deficit)	General Fund	State Assignment Fund	Debt Service Fund	Other Governmental Fund	Total
Restricted for:					
General Government	\$ 44,250	\$ -	\$ -	\$ -	\$ 44,250
Public Safety	-	-	-	1,568	1,568
Public Works	-	-	-	24,237	24,237
Human Services and Welfare	-	-	-	105,008	105,008
Urban Development	-	1,751,740	-	612,574	2,364,314
Education	-	-	-	2,432	2,432
Debt Service	-	-	1,739,890	-	1,739,890
Unassigned	<u>(8,591,103)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(8,591,103)</u>
Total Fund Balance (Deficit)	<u>\$ (8,546,853)</u>	<u>\$ 1,751,740</u>	<u>\$ 1,739,890</u>	<u>\$ 745,819</u>	<u>\$ (4,309,404)</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	State Assignment Fund	Debt Service Fund	Other Governmental Fund	Total
Fund balance (Deficit), beginning	\$ (7,150,943)	\$ 1,681,502	\$ 1,521,498	\$ 924,055	\$ (3,023,888)
Reclassification of a debt agreement with the State Retirement System	<u>191,466</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>191,466</u>
Fund balance (Deficit), beginning as restated	<u>\$ (6,959,477)</u>	<u>\$ 1,681,502</u>	<u>\$ 1,521,498</u>	<u>\$ 924,055</u>	<u>\$ (2,832,422)</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 21 – GOING CONCERN

The accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. During the current and prior years the General Fund of the Municipality has suffered recurring excess of expenditures over revenues, which have lead to an accumulated deficit in the General Fund of \$8,546,853 at June 30, 2012. The long term solution for this situation is to bring the expenditures in line with revenues, which at this date; the Municipality has been unable to do.

Among the actions that management is considering are; an implementation of a cost reduction plan, implementation of increased collection effort over accounts receivable, possible long term financing agreement with the Government Development Bank and monitoring the execution of the property tax, volume of business tax and sales and use tax.

The financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the possible inability of the Municipality to continue as a going concern.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
BUDGETARY COMPARISON SCHEDULE- GENERAL FUND
(SEE NOTES TO BUDGETARY COMPARISON SCHEDULE)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>Budgeted Amounts</u>		Actual Amounts	Variance with
	Original	Final	(Budgetary	Final Budget
			Basis) (See Note 1)	Positive
				(Negative)
RESOURCES (INFLOWS):				
Property Taxes	\$ 2,151,886	\$ 2,151,886	\$ 2,151,886	\$ -
Sales Taxes	1,004,000	1,004,000	853,449	(150,551)
Volume of Business Taxes	988,000	988,000	1,632,387	644,387
Intergovernmental Revenues	5,686,872	5,686,872	5,610,898	(75,974)
Licenses and Permits	4,189,125	4,189,125	1,618,494	(2,570,631)
Rent	100,000	100,000	23,513	(76,487)
Charges for Services	95,000	95,000	120,481	25,481
Miscellaneous	<u>600,000</u>	<u>600,000</u>	<u>347,177</u>	<u>(312,823)</u>
Total Resources (Inflows)	<u>14,874,883</u>	<u>14,874,883</u>	<u>12,358,285</u>	<u>(2,516,598)</u>
CHARGES TO APPROPRIATIONS (OUTFLOWS)				
Current:				
General Government	5,198,891	5,473,465	5,200,185	273,280
Public Safety	1,942,520	1,771,281	1,644,728	126,553
Public Works	4,519,214	4,542,832	4,829,346	(286,514)
Culture and Recreation	1,189,129	1,127,323	1,067,983	59,340
Human Services and Welfare	1,804,929	1,739,782	1,397,065	342,717
Transfer to Other Funds	<u>220,200</u>	<u>220,200</u>	<u>307,713</u>	<u>(87,513)</u>
Total changes to appropriations	<u>14,874,883</u>	<u>14,874,883</u>	<u>14,447,020</u>	<u>427,863</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (2,088,735)</u>	<u>\$ (2,088,735)</u>

See accompanying Notes to Required Supplementary Information

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO BUDGETARY COMPARISON SCHEDULE- GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

NOTE A – EXPLANATION OF DIFFERENCES BETWEEN BUDGETARY INFLOWS AND OUTFLOWS AND GAAP REVENUES AND EXPENDITURES

	<u>GENERAL FUND</u>
Sources/inflows of resources:	
Actual amounts (budgetary basis)“available for appropriation” from the budgetary comparison schedule	\$ 12,358,285
Differences-budget to GAAP:	
Prior and current adjustments to revenues	_____ -
Total revenues as reported on the Statement of Governmental Fund Revenues, Expenditures and Changes in Fund Balances	<u>\$ 12,358,285</u>
Uses/outflows of resources:	
Actual amounts (budgetary basis)“total charges to appropriations” from the budgetary comparison schedule (Page 45)	\$ 14,447,020
Differences-budget to GAAP:	
Prior year expenditures are not outflows of budgetary resources but are expenditures for financial reporting purposes	23,757
Transfers to other funds are outflows of budgetary resources, but are not expenditures for financial reporting purposes	(307,713)
Adjustment to expenditures	_____ 1,184,912
Total expenditures as reported on the Statement of Governmental Fund Revenues, Expenditures, and Changes in Fund Balances	<u>\$ 15,347,976</u>

NOTE B – 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO BUDGETARY COMPARISON SCHEDULE- GENERAL FUND (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

NOTE B – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY (CONTINUED)

B. BUDGETARY CONTROL (CONTINUED)

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 SALINAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2012**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2012**

<u>FEDERAL GRANTOR</u>	<u>FEDERAL CFDA NUMBER</u>	<u>FEDERAL EXPENDITURES</u>
<u>US Department of Housing and Urban Development</u>		
Passed through:		
Municipal Service Administration:		
Community Development Block Grant	14.228	\$1,505,665
Puerto Rico Department of Family:		
ARRA-Homeless Prevention and Rapid Re-Housing Program	14.257	187,721
Direct Program:		
Section 8- Housing Choice Vouchers	14.871	<u>470,446</u>
Total US Department of Housing and Urban Development		<u>2,163,832</u>
<u>US Department of Homeland and Security</u>		
Passed through:		
PR Office of Management and Budget (GAR) Public Assistance Grant	97.036	<u>14,251</u>
<u>US Department of Health and Human Services</u>		
Passed through:		
PR Department of Family: Child Care and Development Block Grant	93.575	<u>146,163</u>
<u>Environmental Protection Agency Office of Solid Waste and Emergency Response</u>		
Direct Program:		
Brownfield Petroleum Assessment	66.818	10,681
Brownfield Hazardous Substances Assessment	66.818	<u>13,454</u>
Total Environmental Protection Agency Office of Solid Waste and Emergency Responses		<u>24,135</u>
<u>US Department of ENERGY</u>		
Passed through:		
Puerto Rico Energy affairs administration: Energy Efficacy Conservation Block Grant	81.128	<u>141,843</u>
Total Federal Awards Expenditures		<u>\$2,490,224</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
JUNE 30, 2012

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of Municipality of Salinas and is prepared on the modified accrual basis of accounting. Accordingly, amounts presented in the accompanying schedule agree to amounts presented in the basic financial statements.

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

Carlos R. Diaz Negrón

Certified Public Accountant

MEMBER:

American Institute of Certified Public Accountants
Puerto Rico Society of Certified Public Accountants

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

**To The Honorable Mayor And
Municipal Legislative Body
Municipality of Salinas
Salinas, Puerto Rico**

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Municipality of Salinas, Puerto Rico, as of and for the year ended June 30, 2012, which collectively comprise the Municipality of Salinas, Puerto Rico's basic financial statements and have issued our report thereon dated January 9, 2013. We did not express an opinion on the governmental-wide financial statements because we were unable to obtain a discussion or evaluation from the Municipality's outside legal council of the pending or threatened litigations described on Note 18 and to obtain sufficient and competent evidential matter related to capital assets and estimated land field closure post closure core cost liability.

Except as discussed in the preceding 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.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses and therefore, there can be no assurance that all 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.

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING (CONTINUED)

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the differences described in the accompanying schedule of findings and questioned cost to be material weakness. Findings 1-12 through 4-12.

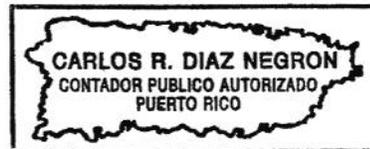
Compliance and Other Matters

As part of obtaining reasonable assurance about whether Municipality of Salinas, Puerto Rico's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial 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 Governmental Auditing Standards and which are described in the accompanying schedule of findings and questioned cost as items 01-12 to 4-12.

This report is intended solely for the information and use of management, City Council, others within the entity, 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.

January 9, 2013
Aguas Buenas, Puerto Rico

License No. 1339
Expire December 1, 2013



The stamp No. **E40867** of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

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

Carlos R. Diaz Negrón

Certified Public Accountant

MEMBER:

American Institute of Certified Public Accountants

Puerto Rico Society of Certified Public Accountants

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

**To The Honorable Mayor And
Municipal Legislative Body
Municipality Of Salinas
Salinas, Puerto Rico**

Compliance

We have audited the compliance of **Municipality of Salinas, Puerto Rico**, with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2012. Municipalities of Salinas, Puerto Rico's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Municipality of Salinas, Puerto Rico's management. Our responsibility is to express an opinion on Municipality of Salinas, Puerto Rico's compliance based on our audit.

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

As described in item 5-12 in the accompanying schedule of findings and questioned costs, Municipality of Salinas did not comply with requirements regarding Davis Bacon Act that are applicable to its Energy efficiency Conservation Block Grant ARRA Fund. Compliance with such requirements is necessary, in our opinion, for Municipality of Salinas to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, Municipality of Salinas complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE (CONTINUED)

Internal Control Over Compliance

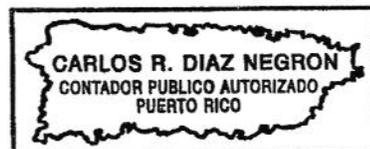
Management of Municipality of Salinas, Puerto Rico, is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Municipality of Salinas, Puerto Rico's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance 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 of Salinas, Puerto Rico'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 consider to be material weaknesses.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as item 5-12 to be material weaknesses.

Municipality of Salinas, Puerto Rico's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Municipality of Salinas, Puerto Rico's responses and, accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of management, City Council, others within the entity, 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.



January 9, 2013
Aguas Buenas, Puerto Rico

License No. 1339
Expire December 1, 2013

The stamp No. **E40868** of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2012**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2012**

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued

- Governmental – wide financial statements
- Governmental – fund financial statements

Disclaimer
Unqualified

Internal control over financial reporting:

- Material weakness identified?
- Significant deficiency identified that is not considered to be material weaknesses?

X yes ___ no
___ yes X no

Noncompliance material to financial statement noted?

X yes ___ no

Federal Awards

Internal control over major programs:

- Material weakness identified?
- Significant deficiency identified that is not considered to be material weaknesses?

X yes ___ no
___ yes X no

Type of auditor's report issued on compliance for major programs

Qualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133

X yes ___ no

Identification of major programs:

CFA Number(s)

Name of Federal Program

14.228

Community Development Block Grant

81.128

Energy Effective Conservation Block Grant

Dollar threshold used to distinguish between type A and type B programs:

\$300,000

Audit qualified as low-risk audited?

___ yes X no

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS

Finding No. 1-12 - Accounting Records and Financial Statements

Requirement:

Accounting Records and Financial Statements

Category:

Internal Control

Condition:

During our examination of the accounting cycle, we noted that the Municipality has not established an accounting system that generates accurate accounting information for the preparation of the financial statements in conformity with generally accepted accounting principles. The 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, encumbrances, capital assets transactions, accounts receivables, accounts payable and long term-debts. These worksheets are used for the preparation of the financial statements.

Also, we noted the following conditions during our evaluation of the accounting cycle:

- a. 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 do not provide for a self balancing set of accounts for each fund operated by the Municipality. Both systems have significant differences at June 30, 2012, principally those arising of significant amounts of checks issued manually from the General Fund bank account and the special revenue funds bank accounts.
- b. Both accounting systems, does not help management to distinguish between expenditures incurred and encumbrances, does not provide reliable financial information of transactions related with capital assets, accounts receivables, accounts payable and long-term debts.
- c. No adequate year-end closing entries procedures are made to account for all transactions affecting all funds.

This finding is repeated from prior years.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

Finding No. 1-12 - Accounting Records and Financial Statements (Continued)

Criteria:

Article 8.010(b) of State Act Number 81 — "*Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico*" of August 30, 1991, states that the Municipality must maintain its fund accounting in accordance with accounting principles generally accepted in the United States of America (GAAP). In addition, Article 8.010(c), states that uniform accounting system used by the Municipality must produce reliable reports and financial statements, provide complete information about the results of operations of the Municipality and include the necessary internal controls to account for all funds, capital assets and other assets.

Cause:

The Municipality did not establish effective internal control over the preparation of the financial statements and the transactions recorded on its accounting records.

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 accounting principles generally accepted in the United States of America (GAAP).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

Finding No. 2 -12 - Accounting Records — Property, Plant and Equipment

Requirement:

Accounting Records and Financial Statements

Category:

Internal Control / Compliance

Condition:

At June 30, 2012, the Municipality does not have an effective system to account for capital assets, principally the infrastructure assets. The Municipality does not have adequate internal controls and procedures to ensure that all capitalizable expenditures and dispositions are recorded in the capital assets subsidiary ledger. Also, the Municipality has not recorded depreciation expense for the infrastructure not reported in the subsidiary ledger. 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 has not performed periodical physical inventories of its capital assets during fiscal year 2011-12.

This finding is repeated from prior years.

Criteria:

Article 10.002 of State Law Number 81 — "*Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico*" of August 30, 1991, stated that Municipality should maintain updated property accounting records.

Cause:

The Municipality did not maintain an adequate control of the accountability of its capital assets.

Recommendation:

We recommend management and the Property Division of the Municipality to make an inventory of the capital assets and reconcile with the capital assets subsidiary ledger. In addition, the Municipality should implement adequate internal control procedures to improve the accountability of its infrastructure assets.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

Finding No. 3-12 - Municipal Solid Waste Landfill GASB 18

Requirement:

Accounting Records and Financial Statements

Category:

Internal Control / Compliance

The estimated liability and the related disclosure presented in the financial statement related to costs of closure and postclosure of the Municipal solid waste landfill is not based on actual engineering studies. Therefore, we were unable to obtain a reliable base on which those estimates were based. Management believes that the effect in the basic financial statements is not material. However, as years going by the accrual will be material and the amount must be based on reliable sources.

We recommend performing the engineering studies to determine the factors necessary to calculate the amount to be accrued for cost closure and postclosure care. These costs include the following:

- The cost of equipment expected to be installed and facilities expected to be constructed near or after the date the landfill stops accepting waste and during the postclosure period. Such equipment might include gas monitoring and collection systems, storm water management systems, and groundwater monitoring wells.
- The cost of final cover (i.e., capping) expected to be applied near or after the closure date.
- The cost of monitoring and maintaining the expected usable landfill area during the postclosure period.

The amount to be accrued each period should be determined using a depletion approach and should be based on the percentage of capacity used during the period.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

Finding No. 4-12 - General Fund's Accumulated Deficit

Category:

Compliance

Condition:

During our examination of the financial statements as of and for the fiscal year ended June 30, 2012, we noted that the General Fund has an accumulated deficit of \$8,546,853. Such accumulated deficit is caused by the cumulative results from many years in which expenditures have exceeded revenues.

Criteria:

Article 7.011(a) of State Law Number 81 — "*Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico*" of August 30, 1991 (as amendments as of January 2004), stated that for any accumulated deficit incurred in the General Fund at the end of any given fiscal year, the Municipality must reserve the necessary financial resources in the General Fund's operating budget of the immediately following fiscal year to cover such deficit.

Cause:

The Municipality, over the years, has suffered recurring excesses of expenditures over revenues, which have lead to the accumulated deficit in the General Fund. In addition, the Municipality has not established an adequate budget control.

Effect:

The Municipality will continue having liquidity problems and will continue affecting the Municipality's ability to finance current operations.

Recommendation:

We recommend management to improve the budget control process, implement a cost reduction plan, increase the collection efforts over the municipal license tax, the property taxes, sales and uses tax and finally evaluate possible long term financing agreement with the Government Development Bank.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012

SECTION III - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 5-12 – Davis Bacon Act

Federal Program

CFDA – 81.128 Energy Efficiency Conservation Block Grant (ARRA Funds)

Compliance requirement:

Davis – Bacon Act

Category:

Compliance/internal control

Condition:

As part of our audit procedures we tested 4 disbursements to test the compliance with the Davis-Bacon Act for Energy Conservation Block Grant (ARRA Funds). In 4 of the 4 disbursements amounting \$64,482 did not submit the payrolls to the Municipality for examination must comply with the requirements the David Bacon Act.

Criteria:

All laborers and mechanics employed by any contractors or subcontractors of the grantee during any construction in excess of \$2,000, alteration, or repair activity funded, in whole or in part, by the grant shall be paid wages at rates not less than the prevailing wages for similar construction activities in the locality, as determined by the Secretary of Labor, in accordance with Section 3141 through 3144, 3146 and 3147 of Title 40, United States Code (42 USC 17155 and ARRA, Section 1606).

Non-federal entities shall include in their construction contracts subject to the Davis-Bacon Act a requirement that the contractor or subcontractor comply with the requirements of the Davis-Bacon Act and the DOL regulations (29 CFR part 5, "Labor Standards Provisions Applicable to Contracts Governing Federally Financed and Assisted Construction"). This includes a requirement for the contractor or subcontractor to submit to the non-Federal entity weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance (certified payrolls) (29 CFR sections 5.5 and 5.6). This reporting is often done using Optional Form WH-347 which includes the required statement of compliance (OMB No. 1215-0149).

Effect:

The Municipality could be exposed to administrative action by the grantor.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SALINAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012**

SECTION III - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS (CONTINUED)

Finding No. 5-12 – Davis Bacon Act

Questioned cost:

\$64,482.24

Recommendation:

We recommend that the Municipality establishes and adequate internal control system to ascertain compliance with Davis-Bacon Act.