

**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES**  
**AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL**  
**AREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE SAN GERMAN**  
**AUDITORIA 2006-2007**  
**30 DE JUNIO DE 2007**

UNIDAD DEL COMISIONARIO  
DE LA OFICINA DE  
CORREOS

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UNIDAD DE CORREO



**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

***FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT***

***FISCAL YEAR ENDED JUNE 30, 2007***



***Hon. Isidro Negrón - Irizarry***  
***Mayor***

***Mrs. Eli Eida Ortiz***  
***Finance Director***

5/24/07  
EJK

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT  
FISCAL YEAR ENDED JUNE 30, 2007**

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## INDEPENDENT AUDITOR'S REPORT

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

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of **Municipality of San Germán, Puerto Rico**, as of and for the year ended June 30, 2007, which collectively comprise the Municipality of San Germán, Puerto Rico's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Municipality of San Germán, Puerto Rico's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of San Germán, Puerto Rico, as of June 30, 2007, and the respective changes in financial position, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 30, 2007, on our consideration of the Municipality of San Germán, Puerto Rico's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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

The management's discussion and analysis and budgetary comparison information on pages 3 through 13 and 50 through 52, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of San Germán, Puerto Rico's basic financial statements. The accompanying financial data schedule is presented for purposes of additional analysis as required by US Department of Housing and Urban Development, Real Estate Assessment Center and is not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audit of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of Municipality of San Germán, Puerto Rico. The financial schedule data and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

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

Yauco, Puerto Rico  
November 30, 2007

Stamp #2263773 was affixed  
to the original of this report.

**MANAGEMENT DISCUSSION AND ANALYSIS**

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF SAN GERMAN**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
**YEAR ENDED JUNE 30, 2007**

As management of the Municipality of San German ("the Municipality"), we offer readers of the Municipality's financial statements this narrative overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2007. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our basic financial statements presented in this report.

**FINANCIAL HIGHLIGHTS**

**Highlights for Government-wide Financial Statements**

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

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2007 by \$33,503,652 (net assets).
- Revenues (including special items) increased by 4% and expenses increased 2% in comparison with year 2006.
- Net change in net assets amounted to \$1,909,030, an increase of 50% with respect to prior year's net change.

**Highlights for Fund Financial Statements**

Detailed information about the Municipality's most significant funds is found in the funds financial statements, which use the current financial resources measurement focus and modified accrual basis of accounting:

- At June 30, 2007, a net change of \$1,685,475 in the fund balances of the Municipality's governmental funds resulted in a reported combined ending fund balances of \$7,236,316. Approximately 18% of the total combined fund balances is unreserved.
- The General Fund reported an excess of revenues and other financing sources over expenditures and other financing uses of \$708,087 and an unreserved fund balance of \$1,317,275. Unreserved fund balance increased 120% from prior year.

**General Financial Highlights**

- The investment in capital assets as of June 30, 2007 was \$38,944,673 (net of depreciation).
- Long term debt decreased to \$14,380,065.
- On a budgetary basis, actual revenues and other financing sources exceeded actual expenditures by \$182,324.

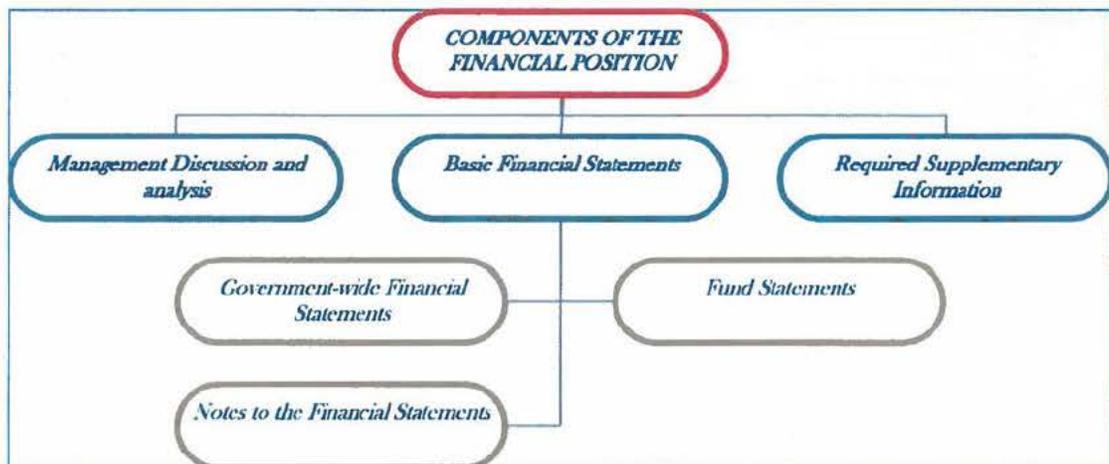
**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**YEAR ENDED JUNE 30, 2007**

**OVERVIEW OF THE FINANCIAL STATEMENTS**

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



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

**Basic Financial Statements**

- ***Government-Wide Financial Statements***

The government-wide statements report information about the Municipality as a whole using accounting methods similar to those used by private-sector businesses. They are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. The first government-wide statement – the statement of net assets – presents information on all of the Municipality's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in the Municipality's net assets are an indicator of whether its financial health is improving or deteriorating. Other non-financial factors such as the condition of the Municipality's capital assets may need to be considered to assess the overall health of the Municipality. The second statement – the statement of activities – presents information showing how the net assets changed during the year. All of the current year's revenues and expenses are taken into account in the statement of activities regardless of when cash is received or paid.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**YEAR ENDED JUNE 30, 2007**

The government-wide statements reports as governmental activities the Municipality's basic services such as public works, sanitation, public safety, culture and recreation, health, welfare, education and general administration. These activities are primarily financed through property taxes, other local taxes and intergovernmental revenues. Included in the governmental activities are the governmental funds.

- ***Fund Financial Statements***

The fund financial statements provide more detailed information about the Municipality's most significant funds. Funds are accounting devices that the Municipality uses to keep track of specific sources of funding and spending for particular purposes. Some funds are required by Federal and Commonwealth regulations, as well by bond covenants.

The Municipality's basic services are included in governmental funds, which are used to account for essentially the same functions reported as governmental activities in the government-wide statements. However, unlike the government-wide statements, the governmental funds are prepared using the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under this approach the financial statements focus on near-term inflows and outflows of external resources, as well on balances of expendable resources available at year end. Consequently, the governmental fund statements provide a detailed short-term view that helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, additional information is provided on a subsequent page that explains the relationship (or differences) between the government-wide and fund statements.

The governmental fund statements focus on major funds. The Municipality's major funds are the general fund (which accounts for the main operating activities of the Municipality) and funds that complies with a minimum criterion (percentage of the assets, liabilities, revenues or expenditures). Funds that do not comply with this criterion are grouped and presented in a single column as other governmental funds.

- ***Notes to the financial statements***

The basic financial statements also include notes to explain information in the financial statements and provide more detailed data.

**Required supplementary information**

The statements and notes are followed by the required supplementary information that contains the budgetary comparison schedule for the General Fund.

**Supplementary information**

The supplementary information includes a financial data schedule containing financial information of the Section 8 Housing Choice Voucher Program administered by the Municipality.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**YEAR ENDED JUNE 30, 2007**

**FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE**

**Net Assets**

The following table presents a summary of the Statements of Net Assets as of June 30, 2007 and 2006:

**TABLE 1**

<i>Summary Statement of Net Assets As of June 30,</i>		
	<b>Governmental Activities</b>	
	<b>2007</b>	<b>2006</b>
<b>Assets</b>		
Current and other assets	\$ 14,044,669	\$ 12,144,106
Capital assets	38,944,673	39,980,502
<b>Total assets</b>	<b>\$ 52,989,342</b>	<b>\$ 52,124,608</b>
<b>Liabilities</b>		
Current and other liabilities	\$ 5,105,625	\$ 4,726,083
Long term liabilities	14,380,065	15,803,902
<b>Total liabilities</b>	<b>19,485,690</b>	<b>20,529,985</b>
<b>Net assets</b>		
Invested in capital assets, net of related debt	29,865,361	30,515,207
Restricted	5,342,128	4,053,686
Unrestricted (deficit)	(1,703,837)	(2,974,270)
<b>Total net assets</b>	<b>\$ 33,503,652</b>	<b>\$ 31,594,623</b>

Net assets (assets over liabilities) may serve over time as a useful indicator of a government's financial position. Net assets for the year increased 6% with respect to prior year.

The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure); less accumulated depreciation and less any related outstanding debt used to acquire those assets. The Municipality uses these assets to provide services to its citizens and consequently, these assets are not available for future spending. The resources needed to repay the debt related to these capital assets must be provided from other sources, because capital assets are not generally liquidated for the purpose of retiring debt.

Restricted net assets represent resources that are subject to external restrictions on how they may be used. Unrestricted net assets are the part of the net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**YEAR ENDED JUNE 30, 2007**

As of June 30 2007, the Municipality presented an unrestricted net assets deficit. This deficit primarily arises from long term obligations such as compensated absences and debts to CRIM for which the Municipality did not provide funding in previous budgets. Historically, such obligations have been budgeted on a "pay as you go" basis without providing funding for their future liquidation. In addition, operational loans and certain general obligation bonds do not have a related capital asset to be reported as invested in capital assets, net of related debt section of net assets. Therefore, are reported as part of the unrestricted net assets section.

**Changes in net assets**

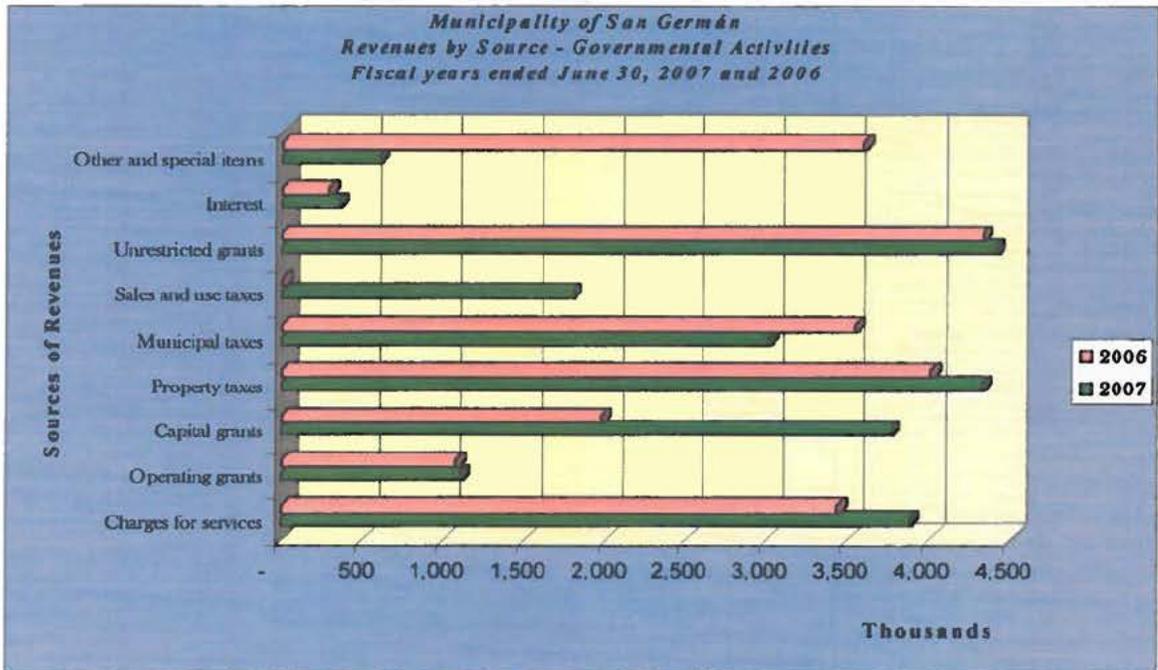
The following table summarizes the changes in net assets for the years ended June 30, 2007 and 2006:

**TABLE 2**

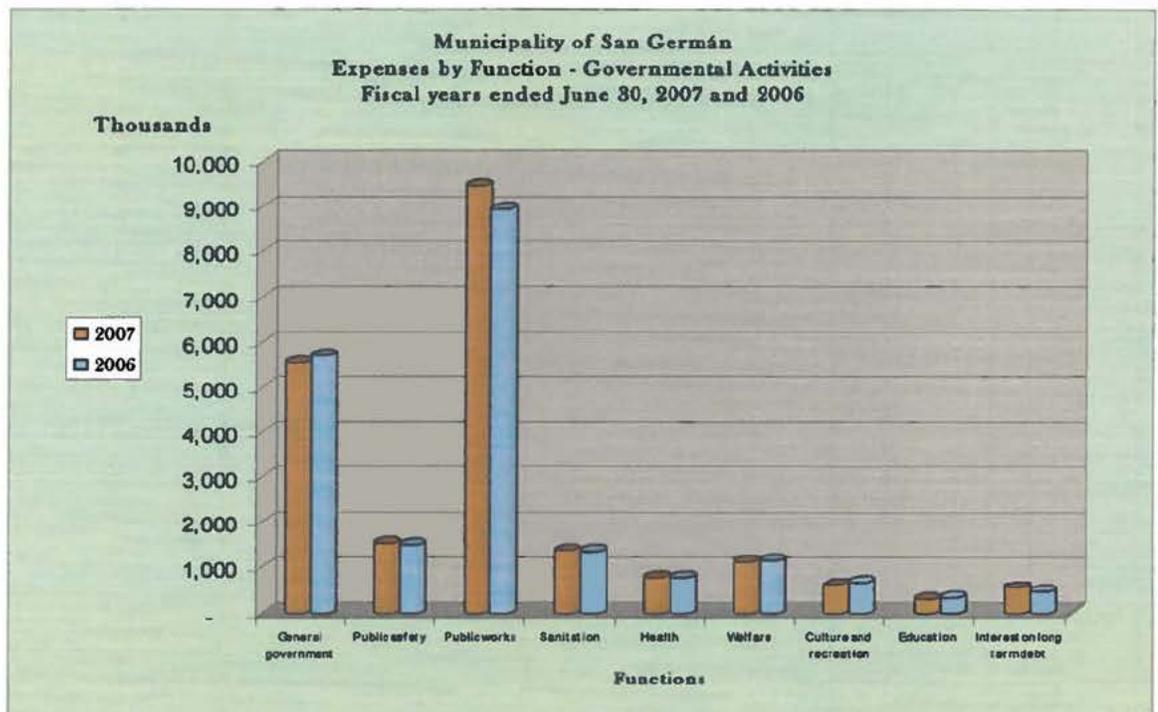
<i>Summary of Changes in Net Assets As of June 30,</i>		
	<b>Governmental Activities</b>	
	<b>2007</b>	<b>2006</b>
<b>Program revenues:</b>		
Fees, fines and charges for services	\$ 3,875,878	\$ 3,434,865
Operating grants and contributions	1,096,001	1,076,642
Capital grants and contributions	3,758,620	1,970,107
<b>General revenues:</b>		
Property taxes	4,319,042	4,007,234
Municipal license taxes	3,007,838	3,540,471
Sales and use taxes	1,784,337	-
Grants and contributions not restricted to specific programs	4,400,150	4,323,349
Interest	345,550	285,721
Other	443,149	443,271
Net gain (loss) on sale and disposition of capital assets	156,135	-
<b>Total revenues</b>	<b>23,186,700</b>	<b>19,081,660</b>
<b>Expenses:</b>		
General government	5,535,290	5,703,017
Public safety	1,523,056	1,511,702
Public works	9,466,752	8,938,940
Sanitation	1,378,811	1,360,311
Health	786,763	786,763
Welfare	1,112,948	1,164,797
Culture and recreation	622,628	678,945
Education	294,568	344,853
Interest on long term debt	556,854	471,614
<b>Total expenses</b>	<b>21,277,670</b>	<b>20,960,942</b>
<b>Special items</b>	<b>-</b>	<b>3,151,933</b>
<b>Change in net assets</b>	<b>1,909,030</b>	<b>1,272,651</b>
<b>Net assets—beginning of year, as restated</b>	<b>31,594,622</b>	<b>30,321,972</b>
<b>Net assets—end of year</b>	<b>\$ 33,503,652</b>	<b>\$ 31,594,623</b>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
MANAGEMENT DISCUSSION AND ANALYSIS  
YEAR ENDED JUNE 30, 2007**

**FIGURE 1**



**FIGURE 2**



**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**YEAR ENDED JUNE 30, 2007**

Approximately 17% of the Municipality's revenues came from fees and charges for services, 19% from property taxes, 19% from unrestricted grants, 16% from capital grants and 13% from municipal license tax. The Municipality's expenses cover a range of services. The largest expenses are public works and sanitation representing approximately 51%, and general government with 26%.

With respect to prior year, revenues (including special items) reported a net increase of approximately 4%. This net increase is primarily the result of: (1) a 13 % increase in fees and charges for services mostly due to an increase in construction permits and in the compensation provided by the Puerto Rico Electric Power Authority (PREPA); (2) a 91% increase in capital grants due to the recognition of the moneys received from the \$575,000,000 in 2006 Series A Public Improvements Bonds issued by the Commonwealth Government; (3) the recognition of the new revenue source sales and use taxes which amounted to \$1,784,337 for the fiscal year; (4) a 15% decrease in municipal license taxes (mainly due to a significant decrease in the business volume reported by one of the Municipality's major corporate taxpayers); (5) and an 100% decrease in the special items caption due to the recognition in last year's financial statements of the transfer to the Municipality by the P.R. Department of Transportation and Public Works of a public parking building with a construction cost of \$3,151,933.

Expenses increased 2% in comparison with the 2006 year. The most significant increases occurred in public works and in interest on long-term debt, with 6% and 18%, respectively, which were offset by an 8% decrease in culture and recreation and a 15% decrease in education. As noted previously, the net increase in revenues and the minimal increase in expenses caused an increase of 50% in the net change in net assets with respect to the prior year's net change.

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

**TABLE 3**

*Net Cost of Municipality's Governmental Activities  
Fiscal years ended June 30,*

Functions/Programs	Total Cost of Services		Net Cost of Services	
	2007	2006	2007	2006
General government	\$ 5,535,290	\$ 5,703,017	\$ (3,497,596)	\$ (3,964,945)
Public safety	1,523,056	1,511,702	(1,382,843)	(1,372,710)
Public works	9,466,752	8,938,940	(3,529,001)	(5,023,722)
Sanitation	1,378,811	1,360,311	(1,378,811)	(1,360,311)
Health	786,763	786,763	(786,763)	(786,763)
Housing, welfare and community development	1,112,948	1,164,797	(662,948)	(539,480)
Culture and Recreation	622,628	678,945	(511,233)	(622,372)
Education	294,568	344,853	(241,122)	(337,411)
Other	556,854	471,614	(556,854)	(471,614)
	<u>\$ 21,277,670</u>	<u>\$ 20,960,942</u>	<u>\$ (12,547,171)</u>	<u>\$ (14,479,328)</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**YEAR ENDED JUNE 30, 2007**

The net cost of services was fully covered by other general revenues such as property and municipal license taxes among others.

**FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS**

**Governmental funds**

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a Municipality's net resources available at the end of a fiscal year. For the fiscal year ended June 30, 2007, the governmental funds reported combined ending fund balances of \$7,236,316, a net increase of \$1,685,476 in comparison with the prior year. This increase was caused primarily by a net change in the general fund of \$708,087; \$259,888 in the debt service fund; (\$778,991) in the \$1,695,000 bond issuance and \$1,544,135 in the permanent capital improvements funds. Of the total combined fund balances, \$1,317,275 (18%) constitutes unreserved fund balance. The remainder of fund balance is reserved to indicate that is not available for new spending.

The general fund is the operating fund of the Municipality. For the year ended June 30, 2007, the fund balance of the general fund increased by \$708,087 when compared with the prior year. The principal components of the net increase of \$1,622,254 in revenues are: an increase of \$456,562 in rental income and charges for services (mainly due to construction permits and the compensation provided by PREPA); a decrease of \$548,863 in municipal license taxes, a \$103,540 increase in intergovernmental revenues; a \$146,710 decrease in other revenues; and the recognition of the new revenue source sales and use taxes, which amounted to \$1,784,337 for the fiscal year 2006-2007. The net decrease in expenditures of \$3,066 is mainly due to an increase of \$257,686 in general government, and decreases in public works, \$80,967; culture and recreation, \$61,616; education, \$41,904; welfare, \$38,751; and sanitation, \$21,095, mainly due to a reduction in salaries and fringe benefits expenditures of these functions.

**GENERAL FUND BUDGETARY HIGHLIGHTS**

The general fund original budget for the fiscal period 2006-2007 presented an increase of 4% with respect to prior year budget. Amendments to the original budget are approved by the Municipal Legislature. During the fiscal year budget revenues were increased by \$170,411 due to additional collections of charges for services, mainly due to an increase in the estimate of the compensation provided by PREPA. Budget expenditures were increased by \$230,500. Actual revenues were more than the revised budgeted revenues by \$270,011 (net). The most significant positive variances were in property taxes (\$363,504) and municipal license taxes (\$293,118), which were offset by a negative variance of \$515,290 in rental income and charges for services due mainly to a negative variance of \$683,091 in construction permits fees.

A negative variance of (\$91,934) between revised budget and actual expenditures was due mainly to a net decrease of \$20,252 in general government, and a net increase of (\$120,195) in public works expenditures due mainly to utility charges in excess of budget. Actual revenues exceeded actual expenditures by \$182,324.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**YEAR ENDED JUNE 30, 2007**

**CAPITAL ASSET AND DEBT ADMINISTRATION**

**Capital assets**

At the end of the fiscal year, the Municipality has invested \$38,944,673 (net of accumulated depreciation) in a broad range of capital assets, including buildings, parks, roads, bridges, land and equipment. This amount represents a net decrease of approximately 3% over the prior year.

**TABLE 4**

<i>Capital Assets, net As of June 30,</i>			
	<b>Governmental Activities</b>		
	<b>2007</b>	<b>2006</b>	
<b>Non-depreciable assets:</b>			
Land	\$ 5,946,956	\$ 5,943,873	
Construction in progress	2,298,233	5,353,042	
<b>Depreciable assets:</b>			
Buildings and Buildings Improvements	16,546,444	14,056,487	
Equipment	4,016,782	3,673,708	
Roads	4,786,159	5,556,058	
Bridges	5,350,099	5,397,334	
<b>Total</b>	<b>\$ 38,944,673</b>	<b>\$ 39,980,502</b>	

The Municipality's major capital projects that were still in construction as of June 30, 2007 are as follows:

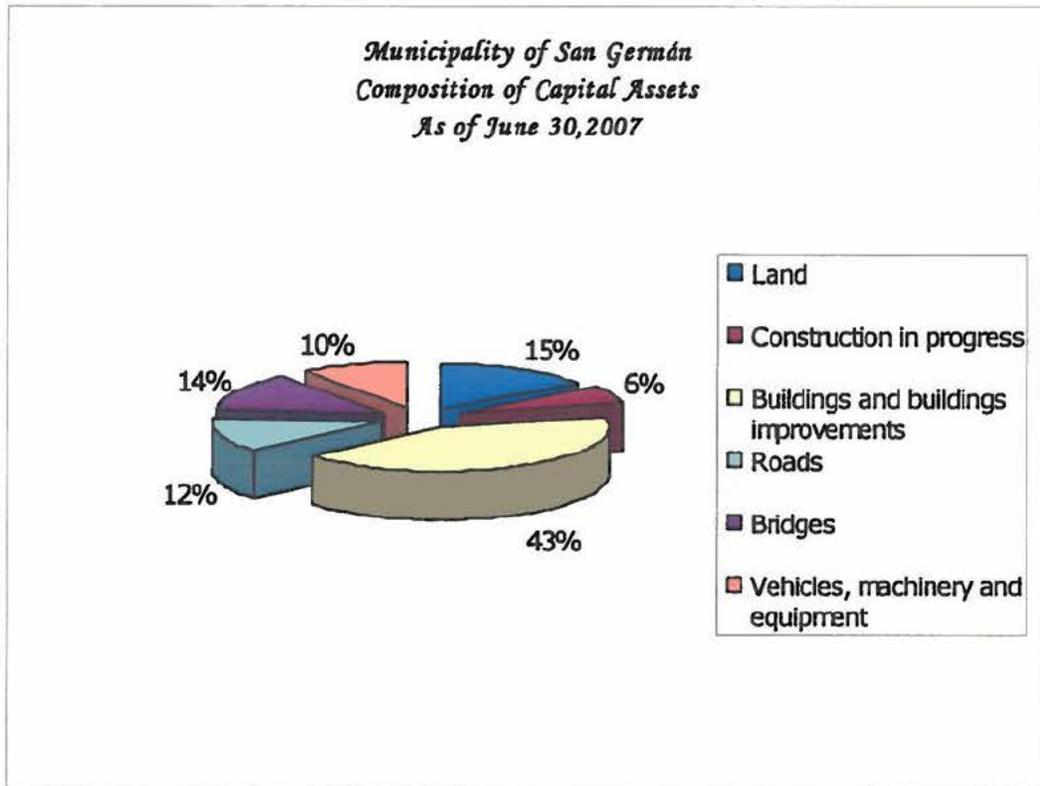
- Construction of a Recreational Center for the Elderly
- Construction of a sanitary sewer system
- Various roads and bridges improvements

These projects will be financed through Federal and Commonwealth grants, funds from the Commonwealth Legislature, general obligation bonds and Municipal funds.

In addition, the Municipality acquired equipment amounting to \$980,935, mainly vehicles and heavy equipment.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
MANAGEMENT DISCUSSION AND ANALYSIS  
YEAR ENDED JUNE 30, 2007**

Capital assets composition as of June 30, 2007 follows:



More detailed information about the Municipality's capital assets is presented in Note F to the financial statements.

**Long term debt**

At year-end, the Municipality maintains an outstanding balance of \$14,380,065 in general and special bonds and notes, a decrease of 9% with respect to prior year. The following is a summary of the Municipality's outstanding debt as of June 30, 2007 and 2006:

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**MANAGEMENT DISCUSSION AND ANALYSIS  
YEAR ENDED JUNE 30, 2007**

**TABLE 5**

<i>Outstanding Long-term Debt As of June 30,</i>			
	<b>Governmental Activities</b>		
	<b>2007</b>	<b>2006</b>	
General and special obligation bonds and notes	\$ 10,115,568	\$ 11,294,272	
Note payable to CRIM – LIMS	282,099	335,306	
Note payable to CRIM – prior years delinquent accounts	120,567	178,083	
Compensated absences	3,180,043	3,185,801	
Christmas Bonus	303,481	322,414	
Claims and judgments	-	58,327	
Payable to CRIM – property tax advances	65,402	429,699	
Bond anticipation loan	100,000	-	
Note payable to PRASA	30,650	-	
Note payable to ERS	182,255	-	
<b>Total</b>	<b>\$ 14,380,065</b>	<b>\$ 15,803,902</b>	

The general and special obligation bonds and notes decreased by \$1,178,704. During the year, a new bond anticipation note was issued in the amount of \$100,000 for the construction of a sanitary sewer system. The Municipality issued notes payable to the P.R. Aqueduct and Sewer Authority (PRASA) and to the P.R. Employee Retirement System Administration (ERS) in the amounts of \$46,260 and \$182,255, respectively. More detailed information about the Municipality's long term liabilities is presented in Note H to the financial statements.

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGET**

The Municipality's selected and appointed officials considered many factors when setting the fiscal year 2007-2008 budget. One of these factors is the economy. Among economic areas considered are the population growth estimates, personal income, housing statistics and unemployment rates. The Municipality's unemployment rate now stands at 13.7%, which compares with the Commonwealth rate of 12.0%. Another important factor that may affect the 2007-2008 budget is the implementation of the new Act No. 80 which imposes certain restrictions on the use of the resources obtained from the sales and use taxes collected.

The Municipality applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2007-2008 are \$15,957,013, an increase of approximately 4% with respect to prior year estimates. Budgeted expenditures are expected to rise accordingly to the increase of budgeted revenues. In addition to the estimated budget for the general fund, the Municipality has submitted Federal and Commonwealth funds proposals for welfare as well as for capital improvements and public works funds.

**CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, and creditors with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability for the money it receives. If you have questions about this report or need additional information, contact the Municipality's Director of Finance at P.O. Box 85, San German, Puerto Rico 00683.

**BASIC FINANCIAL STATEMENTS**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**STATEMENT OF NET ASSETS  
JUNE 30, 2007**

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<b>Assets</b>		<b>Governmental Activities</b>
Cash and cash equivalents		\$ 3,883,372
Receivables (net of allowance for uncollectibles) (note C)		
Municipal license taxes		642,791
Sales and use taxes		193,554
Rents and construction permits		114,774
Due from:		
Commonwealth Government		1,086,893
Federal Government		211,764
Restricted Assets:		
Cash and cash equivalents		3,877,163
Cash with fiscal agents		3,977,877
Deferred charges		45,088
Capital assets: (note F)		
Land and construction in progress		8,245,189
Other capital assets, net		<u>30,699,484</u>
Total capital assets, net		38,944,673
Other assets		<u>11,393</u>
<b>Total assets</b>		<b><u>\$52,989,342</u></b>

Continue

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**STATEMENT OF NET ASSETS, Continued  
JUNE 30, 2007**

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<b>Liabilities</b>	
Accounts payable and accrued liabilities	\$ 1,460,722
Interest payable	265,720
Due to:	
Commonwealth Government	125,246
Deferred revenues	3,253,937
Long term liabilities (note H)	
Due within one year	1,562,551
Due in more than one year	<u>12,817,514</u>
<b>Total liabilities</b>	<b><u>\$19,485,690</u></b>
 <b>Net assets</b>	
Invested in capital assets, net of related debt	29,865,361
Restricted for:	
Capital projects	1,784,006
Debt service	2,136,242
Other specified purposes	1,421,880
Unrestricted (deficit)	<u>(1,703,837)</u>
<b>Total net assets</b>	<b><u>\$33,503,652</u></b>

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**STATEMENT OF ACTIVITIES  
FISCAL YEAR ENDED JUNE 30, 2007**

ROMAN TORO & CO., CSP Certified Public Accountants and Business Consultants  
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Functions	Expenses	Program Revenues			Net (Expenses) Revenues and Change in Net Assets
		Fees, Fines and Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
<b>Governmental activities:</b>					
General government	\$ 5,535,290	\$1,696,747	\$ 340,947	-	\$( 3,497,596)
Public safety	1,523,056	-	140,213	-	( 1,382,843)
Public works	9,466,752	2,179,131	-	3,758,620	( 3,529,001)
Sanitation	1,378,811	-	-	-	( 1,378,811)
Health	786,763	-	-	-	( 786,763)
Welfare	1,112,948	-	450,000	-	( 662,948)
Culture and recreation	622,628	-	111,395	-	( 511,233)
Education	294,568	-	53,446	-	( 241,122)
Interest on long-term debt	<u>556,854</u>	-	-	-	<u>( 556,854)</u>
<b>Total government activities</b>	<b><u>\$21,277,670</u></b>	<b><u>\$3,875,878</u></b>	<b><u>\$1,096,001</u></b>	<b><u>\$3,758,620</u></b>	<b><u>\$(12,547,171)</u></b>
		<b>General Revenues:</b>			
		Taxes:			
		Property taxes			\$ 4,319,042
		Municipal license taxes			3,007,838
		Sales and use taxes			1,784,337
		Grants and contributions not restricted to specific programs			4,400,150
		Interest			345,550
		Other			443,149
		Net gain (loss) on sale and disposition of capital assets			<u>156,135</u>
		Total general revenues			<u>14,456,201</u>
		Change in net assets			1,909,030
		Net assets, beginning of year			<u>31,594,622</u>
		Net assets, end of year			<u>\$33,503,652</u>

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**BALANCE SHEET – GOVERNMENTAL FUNDS  
JUNE 30, 2007**

	Major funds					Other Governmental Funds	Total Governmental Funds
	General	Debt Service	Commonwealth Legislative Resolutions	\$1,695,000 Bond Issuance	Permanent Capital Improvements		
<b>Assets</b>							
Cash and cash equivalents	\$3,883,372	-	-	-	-	-	3,883,372
Receivables (net of allowance for uncollectibles)							
Municipal license taxes	642,791	-	-	-	-	-	642,791
Sales and use taxes	193,554	-	-	-	-	-	193,554
Rents and construction permits	106,703	-	-	-	-	8,071	114,774
Due from:							
Commonwealth Government	651,785	146,536	-	-	-	288,572	1,086,893
Federal Government	-	-	-	-	-	211,764	211,764
Other funds (Note E)	699,591	-	40,000	-	-	2,003	741,594
Advances to other funds (Note E)	135,786	-	-	-	-	-	135,786
Restricted Assets							
Cash and cash equivalents	-	-	1,603,738	-	1,584,135	689,290	3,877,163
Cash with fiscal agents	-	2,254,027	9,742	788,689	-	925,419	3,977,877
<b>Total assets</b>	<b>\$6,313,582</b>	<b>\$2,400,563</b>	<b>\$1,653,480</b>	<b>\$788,689</b>	<b>\$1,584,135</b>	<b>\$2,125,119</b>	<b>\$14,865,568</b>
<b>Liabilities and fund balances</b>							
<b>Liabilities:</b>							
Accounts payable and accrued liabilities	\$372,341	-	\$17,987	\$507,018	-	\$563,376	\$ 1,460,722
Matured bonds and interest payable	-	812,356	-	-	-	-	812,356
Due to:							
Commonwealth Government	125,246	-	-	-	-	-	125,246
Other funds (Note E)	-	-	16,092	12,634	40,000	672,868	741,594
Advances from other funds (Note E)	-	-	-	31,716	-	104,070	135,786
Deferred revenues (Note G)	3,945,540	115,917	-	-	-	292,091	4,353,548
<b>Total liabilities</b>	<b>4,443,127</b>	<b>928,273</b>	<b>34,079</b>	<b>551,368</b>	<b>40,000</b>	<b>1,632,405</b>	<b>\$ 7,629,252</b>
<b>Fund balances:</b>							
Reserved for:							
Encumbrances	\$417,394	-	-	-	-	-	\$ 417,394
Debt Service	-	1,472,290	-	-	-	-	1,472,290
Capital projects	-	-	451,988	-	1,544,135	428,598	2,424,721
Other specified purposes	-	-	1,167,413	237,321	-	64,116	1,468,850
Advances	135,786	-	-	-	-	-	135,786
Unreserved	1,317,275	-	-	-	-	-	1,317,275
<b>Total fund balances</b>	<b>1,870,455</b>	<b>1,472,290</b>	<b>1,619,401</b>	<b>237,321</b>	<b>1,544,135</b>	<b>492,714</b>	<b>7,236,316</b>
<b>Total liabilities and fund balances</b>	<b>\$6,313,582</b>	<b>\$2,400,563</b>	<b>\$1,653,480</b>	<b>\$788,689</b>	<b>\$1,584,135</b>	<b>\$2,125,119</b>	<b>\$14,865,568</b>

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS  
TO THE STATEMENT OF NET ASSETS  
JUNE 30, 2007**

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<b>Total governmental fund balances:</b>		<b>\$ 7,236,316</b>
Amounts reported for the 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:		38,944,673
Other assets used in governmental activities are not financial resources and therefore are not reported in the funds:		
Deferred charges-bond issue costs	\$ 45,088	
Other assets	<u>11,393</u>	56,481
Other assets are not available to pay for current period expenditures and therefore are deferred in the funds:		
Receivables:		
CRIM – Property taxes (General Fund)	187,234	
Municipal license taxes	16,230	
Rent	17,320	
Other	80,895	
P.R. Department of Treasury – Christmas bonus reimbursement	140,957	
CRIM – Property taxes (Debt Service Fund)	115,917	
OCAM – Public Order Code	325,014	
Federal Grants – CDBG	2,746	
P.R. Department of Treasury – Law. No. 52	<u>213,298</u>	1,099,611
Interest liabilities are not due and payable in the current period and therefore, are not reported in the funds:		(88,364)
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds:		
General and special obligation bonds and notes	(9,480,568)	
Compensated absences	(3,180,043)	
Note payable to PRASA	( 30,650)	
Note payable to CRIM – delinquent accounts	( 120,567)	
Note payable to CRIM – LIMS	( 282,099)	
Payable to CRIM – Property taxes advances	( 65,402)	
Christmas bonus	( 303,481)	
General obligation bond anticipation note	( 100,000)	
Note payable to ERS	<u>( 182,255)</u>	<u>(13,745,065)</u>
<b>Net assets of governmental activities</b>		<b><u>\$33,503,652</u></b>

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES  
IN FUND BALANCES - GOVERNMENTAL FUNDS  
FISCAL YEAR ENDED JUNE 30, 2007**

	Major funds						Total Governmental Funds
	General	Debt Service	Commonwealth Legislative Resolutions	\$1,695,000 Bond Issuance	Permanent Capital Improvements	Other Governmental Funds	
<b>Revenues:</b>							
<b>Taxes:</b>							
Property taxes (Note I)	\$ 2,691,098	\$1,546,856	-	-	-	-	\$ 4,237,954
Municipal license taxes	2,991,608	-	-	-	-	-	2,991,608
Sales and use taxes	1,784,337	-	-	-	-	-	1,784,337
<b>Intergovernmental:</b>							
Commonwealth Government (Note J)	4,420,400	-	45,476	-	1,600,000	1,674,347	7,740,223
Federal Government	-	-	-	-	-	1,493,752	1,493,752
Rental income and changes for services	3,789,182	-	-	-	-	36,647	3,825,829
Fines and forfeitures	36,387	-	-	-	-	-	36,387
Interest	237,265	78,733	291	-	20,135	9,126	345,550
Other	82,901	-	-	-	-	113,241	196,142
<b>Total Revenues</b>	<u>16,033,178</u>	<u>1,625,589</u>	<u>45,767</u>	<u>-</u>	<u>1,620,135</u>	<u>3,327,113</u>	<u>22,651,782</u>
<b>Expenditures:</b>							
<b>Current:</b>							
General government	\$ 5,174,928	-	2	\$ 27,083	-	\$ 385,415	\$ 5,587,428
Public safety	1,349,019	-	-	-	-	54,663	1,403,682
Public works	5,772,108	-	151,621	-	76,000	1,534,954	7,534,683
Sanitation h Government	1,308,097	-	-	-	-	3,315	1,311,412
Health	786,763	-	-	-	-	-	786,763
Welfare	420,305	-	9,666	-	-	664,401	1,094,372
Culture and recreation	550,485	-	-	-	-	56,220	606,705
Education	283,162	-	2,472	-	-	8,934	294,568
Capital outlays	37,772	-	53,287	751,908	-	531,238	1,374,205
<b>Debt service:</b>							
Principal	-	829,704	-	-	-	-	829,704
Interest	-	455,053	-	-	-	-	455,053
<b>Total expenditures</b>	<u>15,682,639</u>	<u>1,284,757</u>	<u>217,048</u>	<u>778,991</u>	<u>76,000</u>	<u>3,239,140</u>	<u>\$21,278,575</u>
<b>Excess (deficiency) of revenues over expenditures</b>	350,539	340,832	(171,281)	(778,991)	1,544,135	87,973	1,373,207

Continue

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES  
IN FUND BALANCES - GOVERNMENTAL FUNDS, Continued  
FISCAL YEAR ENDED JUNE 30, 2007**

	Major funds						Total Governmental Funds
	General	Debt Service	Commonwealth Legislative Resolutions	\$1,695,000 Bond Issuance	Permanent Capital Improvements	Other Governmental Funds	
<b>Other financing sources (uses):</b>							
Proceeds from general obligation bond anticipation note	-	-	-	-	-	\$100,000	\$ 100,000
Payment of water and sewer utility charges	( 46,260)	-	-	-	-	-	( 46,260)
Payment of increase in retirement plan benefits under special Laws	(182,255)	-	-	-	-	-	(182,255)
Proceeds from note payable – PRASA	47,725	-	-	-	-	-	47,725
Proceeds from note payable – P.R. Employees Retirement System	198,355	-	-	-	-	-	198,355
Discount on note payable – PRASA	( 1,466)	-	-	-	-	-	( 1,466)
Discount on note payable – P.R. Employees Retirement System	( 16,100)	-	-	-	-	-	( 16,100)
Proceeds from sale of capital assets	212,269	-	-	-	-	-	212,269
Transfers - in	145,280	-	-	-	-	14	145,294
Transfers - (out)	-	(80,944)	( 14)	-	-	(64,336)	(145,294)
<b>Total Other Financing sources (uses)</b>	<u>357,548</u>	<u>(80,944)</u>	<u>( 14)</u>	<u>-</u>	<u>-</u>	<u>35,678</u>	<u>312,268</u>
<b>Net change in fund balances</b>	708,087	259,888	(171,295)	(778,991)	1,544,135	123,651	1,685,475
<b>Fund balance at beginning of year</b>	<u>1,162,368</u>	<u>1,212,402</u>	<u>1,790,696</u>	<u>1,016,312</u>	<u>-</u>	<u>369,063</u>	<u>5,550,841</u>
<b>Fund balances at end of year</b>	<u>\$1,870,455</u>	<u>\$1,472,290</u>	<u>\$1,619,401</u>	<u>\$ 237,321</u>	<u>\$1,544,135</u>	<u>\$492,714</u>	<u>\$7,236,316</u>

*OK/10/24/07*

The accompanying notes are an integral part of these financial statements.

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES  
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE  
STATEMENT OF ACTIVITIES  
FISCAL YEAR ENDED JUNE 30, 2007**

<b>Net change in fund balances – total governmental funds</b>		<b>\$1,685,475</b>
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 as depreciation expense. This is the amount by which depreciation (\$2,265,734) exceed capital outlays (\$1,374,204) in the current year:		(891,530)
Governmental funds only report the proceeds received in the disposal of assets. In the Statement of Activities, a gain or loss is reported for each disposal. Thus, the change in net assets differs from the change in fund balance by the cost of the disposed asset:		( 56,133)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the funds:	\$187,234	
CRIM – Property taxes (General Fund)	17,320	
Rent	16,230	
Municipal license taxes	54,919	
Others	213,298	
P.R. Department of Treasury – Law No. 52	140,957	
P.R. Department of Treasury – Christmas bonus reimbursement	115,917	
CRIM – Property taxes (Debt service Fund) (current)	163,588	
OCAM – Public Order Code	2,746	
Federal Grants – CDBG	<u>122,580</u>	1,034,789
Revenues reported in funds which are not reported as revenues in the Statement of Activities:		
CRIM – Property taxes (Debt Service Fund) (prior year)	(222,063)	
Construction permits	( 18,297)	
Rent	( 24,669)	
Other	( 13,676)	
P.R. Department of Treasury – Law No. 52	( 89,748)	
OCAM – Public Order Code	( 17,432)	
Federal Grants – CDBG	( 9,219)	
Federal Grants – EDA	( 99,694)	
P.R. Department of Treasury – Christmas bonus reimbursement (prior year)	<u>(161,207)</u>	(656,005)
Expenditures reported in funds which are not reported as expenses in the Statement of Activities:		
Matured bonds principal payments (net change)	(347,500)	
Expenditures for other assets	11,393	(336,107)
Proceeds from long term debt is an other financing source in the governmental funds, but increase long-term liabilities in the Statement of Net Assets:		(328,515)
Repayment of long-term debt consumes the current financial resources of governmental funds, but has not effect on net assets of governmental activities:		
General obligation bonds and notes	1,177,204	
Other long term liabilities	<u>1,103,649</u>	2,280,853

Continue

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES  
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE  
STATEMENT OF ACTIVITIES, Continued  
FISCAL YEAR ENDED JUNE 30, 2007**

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Governmental funds report the effect of bond issuance costs as expenditure when debt is first issued, whereas these amounts are deferred and amortized in the Statement of Activities. This amount is the net effect of these differences:

Amortization of bond issuance costs		( 5,420)
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 the governmental funds:		
Accrued interest (net change)	( 66,237)	
Compensated absences	(226,520)	
Christmas bonus	(303,481)	
Other assets retirements	<u>(222,139)</u>	<u>(818,377)</u>
<b>Change in net assets of governmental activities</b>		<b><u>\$1,909,030</u></b>

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The Municipality of San German ("the Municipality") was founded in 1573. The Municipality is governed by the executive and the legislative branch elected for a four year term during the general elections in Puerto Rico. The Mayor is the executive officer and the legislative branch consists of fourteen (14) members of the Municipal Legislature. The Municipality engages in a comprehensive range of services to the community such as: general government administration, public works, health, environmental control, education, public security, welfare, housing, community development and culture and recreation activities.

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

**1. *Financial reporting entity***

The financial reporting entity included in this report consists of the financial statements of the Municipality of San German (primary government). To fairly present the financial position and the results of operations of the financial reporting entity, management must determine whether its reporting entity consists of only the legal entity known as the primary government or one or more organizations called component units. The inclusion of a potential component unit in the primary government's reporting entity depends on whether the primary government is financially accountable for the potential component unit or on whether the nature and significance of the relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. There are two methods of presentation of the component unit in the financial statements: (a) blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances and (b) discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

The basic criteria for deciding financial accountability are any one of the following:

- a. Fiscal dependency of the potential component unit on the primary government, or
- b. The primary government appoints a voting majority of the potential component unit's governing body and,
  - 1) The primary government can impose its will on the potential component unit and/or,
  - 2) A financial benefit/ burden exist between the primary government and the potential component unit.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

In addition, a legally separate, tax-exempt organization should be discretely presented as a component unit of a reporting entity if *all* of the following criteria are met:

- a. The economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents.
- b. The primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization.
- c. The economic resources received or held by an *individual organization* that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

Other organizations should be evaluated as potential component units if they are closely related to, or financially integrated with, the primary government. Professional judgment is applied in determining whether the relationship between a primary government and other organizations for which the primary government is not accountable and that do not meet these criteria is such that exclusion of the organization would render the financial statements of the reporting entity misleading or incomplete.

Based on the above criteria there are no potential component units which should be included as part of the financial statements.

**2. *Basis of presentation, measurement focus and basis of accounting***

The financial report of the Municipality consists of a management discussion and analysis (MD&A), basic financial statements, notes to the financial statements and required supplementary information other than the MD&A. Following is a summary presentation of each, including the measurement focus and basis of accounting. Measurement focus is a term used to describe *which* transactions are recorded within the various financial statements. Basis of accounting refers to *when* transactions are recorded regardless of the measurement focus:

**Management Discussion and Analysis**

This consists of a narrative introduction and analytical overview of the Municipality's financial activities. This analysis is similar to analysis the private sector provides in their annual reports.

**Basic financial statements**

Basic financial statements include both government-wide and fund financial statements. Both levels of statements categorize primary activities as governmental type, which are primarily supported by taxes and intergovernmental revenues.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

**Government-wide statements**

The government-wide statements consist of a Statement of Net Assets and a Statement of Activities. These statements are prepared using the economic resources measurement focus, which concentrates on an entity or fund's net assets. All transactions and events that affect the total economic resources (net assets) during the period are reported. The statements are reported on the accrual basis of accounting. Revenues are recognized in the period earned and expenses recognized in the period in which the associated liability is incurred. Fiduciary activities, if any, whose resources are not available to finance government programs, are excluded from the government-wide statements. The effect of inter-fund activities is eliminated.

The Statement of Net Assets incorporates all capital (long lived) assets and receivables as well as long term debt and obligations. The Statement of Activities reports revenues and expenses in a format that focus on the net cost of each function of the Municipality. Both the gross and net cost of the function, which is otherwise being supported by the general government revenues, is compared to the revenues generated directly by the function. This Statement reduces gross expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. Program revenues must be directly associated with the function.

The types of transactions included as program revenues are: charges for services, fees, licenses and permits; operating grants which include operating-specific and discretionary (either operating or capital) grants; and capital grants which are capital-specific grants. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes. Property taxes (imposed nonexchange transactions) are recognized as revenues in the year for which they are levied and municipal license taxes and sales and use taxes (derived tax revenues) when the underlying exchange has occurred. Revenues on both operating and capital grants are recognized when all eligibility requirements (which include time requirements) imposed by the provider have been met. For certain expenditure-driven grants revenue is recognized after allowable expenditures are incurred. As a policy, indirect expenses in the Statement of Activities are not allocated. The Municipality first uses restricted assets for expenses incurred for which both restricted and unrestricted assets are available.

The Municipality reports deferred revenues in the government wide statements. Deferred revenues arise when resources are received before the Municipality has a legal claim to them or before applicable eligibility requirements are met (in case of certain federal expenditure-driver grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed and the revenue is recognized.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989 generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The Municipality has elected not to follow subsequent statements and interpretations issued by the FASB after November 30, 1989.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

**Fund Statements**

The financial transactions of the Municipality are recorded in individual funds, each of which are considered an independent fiscal entity. Each fund is accounted for by providing a separate set of self balancing accounts that comprise its assets, liabilities, reserves, fund equity, revenues and expenditures. Funds are segregated according to their intended purpose which helps management in demonstrating compliance with legal, financial and contractual provisions. Governmental Funds are those through which most governmental functions of the Municipality are financed. The governmental fund statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances with one column for the general fund, one for each major fund and one column combining all non-major governmental funds. Major funds are determined based on a minimum criterion, that is, a percentage of the assets. A fund is considered major if it is the primarily operating fund of the Municipality or if total assets, liabilities, revenues, or expenditures/expenses of that individual governmental fund are at least 10 percent of the corresponding total for all fund of that category or type.

The Municipality reports the following major governmental funds:

**General Fund:** This is the operating fund of the Municipality and accounts for all financial resources, except those required to be accounted for in another fund.

**Debt Service Fund:** Debt Service Fund is used to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest.

**Commonwealth Legislature Resolutions Fund:** The Commonwealth Legislative Resolutions Fund is used to account for grants from the Commonwealth's Legislature.

**\$1,695,000 Bond Issuance Fund:** The \$1,695,000 bond issuance fund is used to account for the acquisition of equipment.

**Permanent Capital Improvements Fund:** The Permanent Improvement fund is used to account for the moneys received from the \$575,000,000 in 2006 Series A Public Improvement Bonds issued by Commonwealth Government. The financial resources received by this fund are used for the restoration of the downtown area and the construction of an educational park.

Governmental funds are accounted for using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method of accounting, revenues are recognized when they are susceptible to accrual (i.e. both measurable and available). Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Municipality considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

Revenues susceptible to accrual include property taxes (recognized as revenues in the year for which they are levied), municipal license taxes and sales and use taxes (recognized when the underlying exchange has occurred and time requirements are met) and interest. In applying the susceptible to accrual concept to intergovernmental revenues, revenues are recognized when all eligibility requirements (including time requirements) imposed by the provider have been met and revenue becomes available. There are, however, essentially two types of these revenues. In the first case, on expenditure-driven grants, monies must be expended on the specific project or purpose (eligibility requirement), before any amounts are paid to the Municipality. Revenue is, therefore, recognized as expenditures are incurred to the extent available. In the other cases, monies are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. In these cases revenues are recognized as the time of receipt or earlier if the susceptible to accrual criteria is met. Licenses and permits, charges for services, rent, fines and miscellaneous revenues are generally recorded as revenues when received or are recognized earlier if the susceptible to accrual criteria is met.

The Municipality reports deferred revenues in the governmental funds statements which arise when potential revenue does not meet both measurable and available criteria for recognition in the current period (in the government-wide statements revenue is recognized as soon as it is earned regardless of its availability). Deferred revenues also arise when resources are received before the Municipality has a legal claim to them or before applicable eligibility requirements are met (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the revenue recognition criteria is met, or when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed from the combined balance sheet and the revenue is recognized.

Expenditures are generally recognized when the related liability is incurred. Certain exceptions to this fundamental concept include the following: 1) payments of principal and interest on general long term debt, which are recorded as expenditures when due, except for principal and interest due on July 1 (in this case amounts are recorded as liabilities and expenditures on June 30 since amounts have been accumulated or transferred to the debt service fund before July 1 payments are made) 2) vested compensated absences, claims and judgments and special termination benefits which are recorded as expenditures only to the extent that they are expected to be liquidated with expendable financial resources (in the government-wide statements the expense and related accrual liability for long term portions of debt must be included).

Since the governmental fund statements are presented on a different measurement focus and basis of accounting than the government-wide statements, reconciliation is necessary to explain the adjustments needed to transform the fund financial statements into the government-wide statements. This reconciliation is part of the financial statements.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

**Notes to Financial Statements**

The notes to financial statements provide information that is essential to a user's understanding of the basic financial statements.

**Required Supplementary Information:**

Required supplementary information consists of the Budgetary Comparison Schedule – General Fund as required by GASB.

**3. *Cash, cash equivalents (unrestricted and restricted) and restricted cash with fiscal agents***

Cash and cash equivalents consists of cash on hand, demand deposits and short term investments with original maturities of three months or less from the date of acquisition. The Municipality follows the practice of pooling cash of all funds except for certain Commonwealth's grants, restricted funds generally held by outside custodians and federal grants. Available pooled cash balance beyond immediate needs is invested in certificates of deposits. Cash and cash equivalents related to Commonwealth and Federal grants are restricted since their use is limited by applicable agreements or required by law.

Restricted cash with fiscal agent in the debt service fund consists of the undisbursed balance of property tax collections retained by the Commonwealth of Puerto Rico which are restricted for the repayment of the Municipality's general and special obligation bonds and notes as established by law. Restricted cash with fiscal agent of the general and other governmental funds represent the undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the GDB or a federal government agency.

**4. *Receivables and due from governmental entities***

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions.

Amounts due from federal government represent amounts owed to the Municipality for the reimbursement of expenditures incurred pursuant to federally funded programs. Amounts reported in the debt service fund represent property tax revenue of current fiscal year collected by the CRIM on the first month (July) of subsequent fiscal year.

**5. *Interfund receivables and payables***

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due from/to other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due from/to other funds".

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS  
June 30, 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

6. *Inventories*

The Municipality purchases gasoline, oil and other expendable supplies held for consumption. The cost of those purchases is recorded as expenditure when incurred in the appropriate fund but the year-end inventory is not recorded in the Statement of Net Assets, as management believes is not significant.

7. *Deferred bond issuance costs*

Bond issuance costs are reported as deferred charges and amortized as required by current standards. Governmental fund types recognize bond issuance costs as expenditures during the current period. Those issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the appropriate fund.

8. *Capital assets*

Capital assets of the primary government, which include property, plant, equipment, and infrastructure, (e.g., roads, bridges, sidewalks, and similar items) are reported in the governmental activities column in the Statement of Net Assets. Capital assets are capitalized at historical cost or estimated historical cost if historical cost is not available. Donated assets are recorded as capital assets at their estimated fair market value at the date of donation. The Municipality maintains a threshold level of \$50 or more for capitalizing vehicles, machinery and equipment. Infrastructure assets are capitalized based on a percentage of the estimated useful life. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

All capital assets, other than land are depreciated using the straight-line method over the following useful lives:

<u>Description</u>	<u>Years</u>
Buildings	40
Improvements	10-20
Vehicles, machinery and equipment	5-10
Infrastructure	2-50

In accordance with current accounting standards capital assets are reviewed for impairment. Impairment occurs when there is a significant decline in asset service utility due to the occurrence of prominent event or change in circumstances affecting the asset. Current standards provide guidance for accounting and reporting for impairment and for insurance recovers.

9. *Long-term obligations*

Long-term debt and other long-term obligations, which are reported as liabilities in the governmental activities column in the Statement of Net Assets, consists of general and special obligation bonds, liabilities for compensated absences, claims and judgments, and long-term liabilities to other governmental entities.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

10. *Compensated absences*

The Municipality's employees accumulate vacation, sick leave and compensatory time based on continuous service. Compensated absences are recorded as a liability if (1) are earned on the basis of services already performed by employees, (2) it is probable that will be paid (in the form of paid time off, cash payments at termination or retirement, or some other means) and (3) are not contingent on a specific event (such as illness).

The compensated absences are accumulated on the basis of 2½ days per month of vacation and 1½ days per month of sick pay and compensatory time up to a maximum of 60 days of vacations and 90 days of sick leave. Upon separation from employment the accumulated vacations are liquidated up to the maximum number of days. Accumulated sick leave, which is accrued based on all vesting amounts for which payment is probable, is liquidated to employees with 10 years or more service up to the maximum number of days.

The accrual of compensated absences includes estimated payments that are related to payroll. The entire compensated absence liability is reported on the government-wide financial statements. For governmental fund financial statements, the current portion of unpaid compensated absences is the amount that is normally expected to be paid using expendable available financial resources. The non-current portion of the liability is not reported.

Pursuant to Law No. 152 of August 20, 1996 effective July 1, 1997 the Municipality is required to pay any excess of vacations and sick leave accumulated over 90 days as of December 31 of each year. Payments should be made on or before March 31 of the following year.

11. *Fund balances and Net Assets*

a. Fund balances:

In the fund financial statements, governmental funds report reserved and unreserved fund balances. Reservations of fund balance represent portions of the fund balance that are legally segregated for a specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:

Encumbrances:	Represent future expenditures under purchase orders and other commitments, which generally will become liabilities in future periods as the goods or services are received.
Debt Service:	Represents net assets available to finance future debt service payments.
Capital Projects:	Represent amounts to be used for future expenditures for capital projects under contracts and other commitments. These commitments generally will become liabilities in future periods as the projects are completed.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

Other specified purposes: Represent amounts to be used for future expenditures of Federal and Commonwealth's grants as well as funds reserved through enabling legislation passed by the government itself, to be used to finance activities other than construction or capital improvement commitments

Advances: Represents the non-current portion of interfund loans.

b. Net assets

In the government-wide statements net assets are segregated into three categories:

Invested in capital assets, net of related debt: Consists of capital asset balances net of accumulated depreciation and outstanding balances of any bonds, notes and other borrowings that are attributable to the acquisition, construction, or improvement of those assets. This category should not include cash that is restricted to capital asset acquisition or construction (unspent bond proceeds) and any unamortized debt issue costs.

Restricted net assets: Represents net assets (restricted assets net of related debt) that are subject to restrictions beyond the Municipality's control. These include restrictions that are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or restrictions imposed by the law through constitutional provisions or enabling legislation (including enabling legislation passed by the government itself).

Unrestricted net assets: Represent net assets that do not meet the definition of net assets Invested in capital assets, net of related debt or restricted. Unrestricted assets are often designated to indicate that management does not consider them to be available for general operations. These types of constraints are internal and management can remove or modify them. Designations are not reported on the face of the statement of net assets.

**12. Interfund transactions**

The Municipality reports certain transactions as transfers, which are legally required transfers that are reported when incurred as "Transfers-in" by the recipient fund and as "Transfers-out" by the disbursing fund.

**13. Risk financing**

The Puerto Rico Treasury Department (PRDT) acts as an agent, obtaining and determining the coverage for the municipalities of Puerto Rico. The coverage for the Municipality of San German consists of professional, public responsibility, property and theft, auto and fidelity bond coverage.

COMMONWEALTH OF PUERTO RICO  
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NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Insurance policies costs are allocated by PRDT among all the municipalities of Puerto Rico. Payment of the Municipality's insurance premiums is monthly deducted from advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM). Workers compensation insurance is also deducted from the monthly advances by the CRIM. Settled cases have not exceeded insurance coverage for any of the past three years.

14. *Use of estimates*

The preparation of the basic financial statements in accordance 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 disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

15. *Future adoption of accounting pronouncements*

The GASB has issued the following statements, which the Municipality has not yet adopted:

	<u>Statement</u>	<u>To be Adopted in Fiscal year ended,</u>
43	Financial Reporting for Post employment Benefits Plans Other Than Pension Plans	June 30, 2008
45	Accounting and Financial Reporting by Employers for Post employment Benefits Other Than Pensions	June 30, 2009
48	Sales and Pledges of Receivables and Future Revenues and Intra-entity Transfers of Assets and Future Revenues	June 30, 2008
49	Accounting and Financial Reporting for Pollution Remediation Obligations	June 30, 2009
50	Pension Disclosures – an amendment of GASB Statements No. 25 and No. 27	June 30, 2008
51	Accounting and Financial Reporting for Intangible Assets	June 30, 2010

The impact of these statements in the Municipality's basic financial statements has not yet been determined.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE B – CUSTODIAL CREDIT RISK - DEPOSITS**

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The Municipality maintains cash deposits in commercial and governmental banks located in Puerto Rico.

Under Commonwealth of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal deposit insurance. All securities pledged as collateral by the Municipality are held by the Secretary of Treasury of Puerto Rico in the Municipality's name. At year end the Municipality's bank balance in commercial banks amounts to \$8,025,947. Deposits in governmental banks (all of which are uninsured and uncollateralized), are exposed to custodial credit risk. At year end the Municipality's bank balance in governmental banks amounts to \$3,911,613.

**NOTE C – RECEIVABLES**

**1. *Municipal license taxes***

Municipal License taxes are assessed annually by the Municipality to all organizations or entities subject to the tax doing business in the Municipality's location except for entities totally or partially exempt pursuant to certain Commonwealth's statutes. This tax is based generally on volume of business or gross sales as shown in a tax return that should be submitted on or before April 15. During the Fiscal year ended June 30, 2007 the tax rates were as follows:

Financial business - 1.50% of gross revenues  
Other organizations - .50% of gross revenues

Municipal license tax receivable and corresponding deferred revenues as of June 30, 2007 follows:

<u>Description</u>	<u>Amount</u>
Total municipal license tax receivable:	\$937,823
Less: allowance for uncollectibles	<u>(295,032)</u>
	<u>\$642,791</u>

As required by current standards, the Municipality recognizes assets related to municipal license taxes when cash is received or in the period when the exchange transaction on which the government imposes the tax occurs. Management understands that as of tax return filling date an enforceable legal claim arises against the provider of resources. Therefore, an asset (receivable) is recognized as of June 30 for the balance on tax returns filed but not paid at that date.

The tax is due in two equal installments on July 1 and January 1 of each fiscal year. Resources are intended to finance the operations of the applicable fiscal year. At this moment the Municipality recognizes revenues on municipal license taxes. A discount of 5% is allowed when full payment is made on or before April 15. Since this time requirement, cash collected and the receivable balance on tax returns filed but not collected, which totals \$3,253,937 are recorded as deferred revenues as of June 30.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE C – RECEIVABLES - Continued

2. *Sales and use taxes*

On July 4, 2006 the Commonwealth Legislature approved Act No. 117 ("Act 117") which amends the Puerto Rico Internal Revenue Code of 1994 to provide, among other things, for a sales and use tax of 5.5% to be imposed by the Commonwealth Government. Act 117 also authorizes each municipal government to impose a 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 in Subtitle BB of the Code. The municipal sales and use 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 sales and use 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 on November 1, 2006 with Ordinance No. 36 Series 2006-2007, effective on November 15, 2006. Municipalities were authorized to implement a municipal sales and use tax of 1% starting on July 1, 2006 and the Municipality has already done so, as approved by the Municipal Legislature. 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 20<sup>th</sup> 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 part of the general fund of the Municipality and are used to finance costs related to waste disposal, recycling programs, maintenance of sports and cultural facilities, construction of welfare housing, educational facilities and maintenance and construction of roads and other infrastructure.

Municipal sales and use tax receivable of \$193,554 represents the tax collected on June by individuals, organizations and entities but reported and paid to the Municipality on or before July 20, net of uncollectible accounts.

3. *Rents and construction permits*

A detail of rents and construction permits' receivable as of June 30, 2007 follows:

<u>Description</u>	<u>Amount</u>
Rent-land lots	\$185,821
Rent-properties	130,071
Less: allowance for uncollectibles	<u>(201,118)</u>
	<u>\$114,774</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE C – RECEIVABLES - Continued**

Of the total amount of \$114,774 the Municipality recorded \$47,271 as deferred revenue in the governmental funds statements since they are not available as required by current standards.

**NOTE D - DUE FROM (TO) GOVERNMENTAL ENTITIES**

1. Amounts due from governmental entities as of June 30, 2007 follows:

<u>Description</u>	<u>Commonwealth Government</u>	<u>Federal Government</u>
Municipal Revenue Collection Center (CRIM) – property taxes (general fund)	\$ 187,234	\$ -
Municipal Revenue Collection Center (CRIM) – property taxes (debt service fund)	146,537	-
P.R. Department of Treasury – Christmas bonus reimbursement	140,957	-
Office of Commissioner of Municipal Affairs – Public Order Code	325,014	-
P.R. Department of Labor – Law No. 52	213,298	-
P.R. Department of Labor – Law No. 82	34,335	-
Others	39,518	16,608
Office of Commissioner of Municipal Affairs –CDBG	-	143,948
U.S. Department of Housing and Urban Development – CDBG	-	<u>51,208</u>
	<u>\$1,086,893</u>	<u>\$211,764</u>

See note G for detail of amounts due from Governmental Entities recorded as deferred revenue.

2. Amounts due to governmental entities as of June 30, 2007 follows:

<u>Description</u>	<u>Commonwealth Government</u>
Employees' Retirement System of the Government of P.R. (ERS)	\$ 86,475
P.R. Department of Labor – unemployment	14,325
P.R. Aqueduct and Sewer Authority (PRASA)	14,612
Others	<u>9,834</u>
	<u>\$125,246</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE E - INTERFUND TRANSACTIONS**

**1. Due from/to other funds:**

Amounts due from/to other funds represent advances to other funds for payroll and payroll taxes expenditures, as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General Fund	Other governmental funds:	
	Law No. 52 and 82	\$201,691
	DTOP	144,469
	OMEF	51,787
	Law No. 82	51,313
	\$2,100,000 Bond issuance	44,800
	CDBG	28,211
	Others	<u>177,320</u>
		<u>\$699,591</u>
Commonwealth Legislative Resolutions	Permanent Capital Improvements	<u>-</u> <u>\$ 40,000</u> <u>-</u>
Other governmental funds:		
Others	\$1,695,000 Bond issuance	<u>\$ 2,003</u>

**2. Advances to(from) other funds:**

Advances to (from) other funds represent long term advances to other funds by the general fund for payroll, payroll taxes and other expenditures, as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General Fund	Other governmental funds:	
	FEMA	\$ 29,171
	Special Communities	25,061
	Public Order Code	23,592
	\$3,500,000 Bond issuance	15,099
	Others	11,147
	\$1,695,000 Bond issuance	<u>31,716</u>
		<u>\$135,786</u>

**3. Transfers:**

Transfers between individual funds includes transfers to the general fund for interest earned on restricted cash with fiscal agents in the debt service fund and for equity balances on certain special funds transferred from other governmental funds.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE F - CAPITAL ASSETS**

Capital assets and depreciation activity as of and for the year ended June 30, 2007 is as follows:

	<u>Beginning balance July 1, 2006</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending balance June 30, 2007</u>
<b><u>Governmental activities:</u></b>				
Capital assets, not being depreciated:				
Land	\$ 5,943,873	\$ 48,000	\$ 44,917	\$ 5,946,956
Construction in progress	<u>5,353,042</u>	<u>389,478</u>	<u>3,444,287</u>	<u>2,298,233</u>
Total capital assets not being depreciated:	11,296,915	437,478	3,489,204	8,245,189
Capital assets, being depreciated:				
Buildings and improvements	19,688,951	3,049,487	-	22,738,438
Equipment	8,797,760	980,935	161,046	9,617,649
Roads	11,399,628	163,887	30,843	11,532,672
Bridges	<u>6,790,571</u>	<u>122,833</u>	<u>-</u>	<u>6,913,404</u>
Total capital assets being depreciated	46,676,910	4,317,142	191,889	50,802,163
Less accumulated depreciation for:				
Buildings and improvements	5,632,464	559,530	-	6,191,994
Equipment	5,124,052	603,802	126,987	5,600,867
Roads	5,843,570	932,334	29,391	6,746,513
Bridges	<u>1,393,237</u>	<u>170,068</u>	<u>-</u>	<u>1,563,305</u>
Total accumulated depreciation	17,993,323	2,265,734	156,378	20,102,679
Total capital assets being depreciated, net	<u>28,683,587</u>	<u>2,051,408</u>	<u>35,511</u>	<u>30,699,484</u>
Governmental activities capital assets, net	<u>\$39,980,502</u>	<u>\$2,488,886</u>	<u>\$3,524,715</u>	<u>\$38,944,673</u>

Depreciation expense was charged to functions/programs of the Municipality as follows:

**Governmental activities:**

General government	\$ 112,394
Public safety	119,374
Public works	1,932,069
Sanitation	67,398
Culture and recreation	15,923
Welfare	<u>18,576</u>
Total depreciation expense, governmental activities	<u>\$2,265,734</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE G - DEFERRED REVENUES**

Deferred revenues for amounts due from Commonwealth Government represent revenues not available as required by current standards and for amounts due from Federal Grants represent resources received before allowable expenditures are incurred or not available as required by current standards. A detail of these balances follows:

<u>Description</u>	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Other Governmental Funds</u>
Municipal license taxes	\$3,253,937	\$ -	\$ -
P.R. Department of Treasury – Christmas bonus reimbursement	140,957	-	-
Office of Commissioner of Municipal Affairs – Public Order Code	299,911	-	25,103
Rents and construction permits	47,271	-	-
Others	16,230	-	16,609
Municipal Revenue Collection Center (CRIM) – property taxes	187,234	115,917	-
P.R. Department of Labor – Law No. 52	-	-	213,298
P.R. Department of Labor – Law No. 82	-	-	34,335
U.S. Department of Housing and Urban Development – CDBG	-	-	2,746
	<u>\$3,945,540</u>	<u>\$115,917</u>	<u>\$292,091</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE H - LONG TERM DEBT**

**1. Summary of long-term debt activity**

The following summarizes activity in long-term debt for the fiscal year ended June 30, 2007:

	<u>Balance at July 1, 2006</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at June 30, 2007</u>	<u>Due within one year</u>
<b>Governmental activities:</b>					
<b>General and special obligation bonds and notes payable:</b>					
General obligation bonds	\$ 5,700,000	\$ -	\$ 232,000	\$ 5,468,000	\$ 250,000
Public improvement bonds	3,106,772	-	294,204	2,812,568	288,000
General obligation notes	2,430,000	-	595,000	1,835,000	275,000
Special obligation bonds	<u>57,500</u>	<u>-</u>	<u>57,500</u>	<u>-</u>	<u>-</u>
Total general and special obligation bonds and notes payable:	<u>11,294,272</u>	<u>-</u>	<u>1,178,704</u>	<u>10,115,568</u>	<u>813,000</u>
<b>Other long term liabilities:</b>					
General obligation bond anticipation note	-	100,000	-	100,000	-
Note payable to CRIM-LIMS	335,306	-	53,207	282,099	56,420
Note payable to CRIM-financing of delinquent accounts	178,083	-	57,516	120,567	4,823
Note payable to PRASA	-	46,260	15,610	30,650	30,650
Note payable to ERS	-	182,255	-	182,255	61,815
Compensated absences	3,185,801	226,520	232,278	3,180,043	226,960
Christmas Bonus	322,414	303,481	322,414	303,481	303,481
Claims and judgments	58,327	-	58,327	-	-
Payable to CRIM- property tax advances	<u>429,699</u>	<u>-</u>	<u>364,297</u>	<u>65,402</u>	<u>65,402</u>
Total other long term liabilities:	<u>4,509,630</u>	<u>858,516</u>	<u>1,103,649</u>	<u>4,264,497</u>	<u>749,551</u>
	<u>\$15,803,902</u>	<u>\$858,516</u>	<u>\$2,282,353</u>	<u>\$14,380,065</u>	<u>\$1,562,551</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE H - LONG TERM DEBT - Continued**

**2. General and special obligation bonds and notes payable**

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2007 amount to \$10,115,568. All these bonds and notes are serviced by the Governmental Development Bank of Puerto Rico (GDB) maturing at various dates. As required by law, the Commonwealth Government is obligated to levy and collect property taxes for payment of principal and interest on bonds and notes. A debt service fund has been established for the bonds and notes at GDB with the proceeds of those property taxes, whereby sufficient funds must be set aside in order to cover the projected debt service requirement, before any new bonds are issued. Principal and interest payments of long term debt issued for operational purposes are made through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM).

A detail of the general and special obligation bonds and notes as of June 30, 2007 follows:

	<b>Outstanding Amount</b>
1988 public improvement bonds of \$400,000 due in annual installments ranging from \$7,000 to \$32,000 through January 1, 2013; bearing interest at 6.125%	\$ 159,000
1989 public improvement bonds of \$765,000 due in annual installments ranging from \$16,000 to \$60,000 through January 1, 2011; bearing interest at 6.375%	216,341
1991 public improvement bonds of \$616,000 due in annual installments ranging from \$16,000 to \$45,000 through January 1, 2012; bearing interest at 5.00%	202,227
1996 public improvement bonds of \$3,500,000 due in annual installments ranging from \$70,000 to \$330,000 through July 1, 2015; bearing interest at rates ranging from 4.70% to 6.58% (6.05% at June 30, 2007)	2,235,000
2000 general obligation bonds of \$2,100,000 due in annual installments ranging from \$85,000 to \$235,000 through July 1, 2013; bearing interest at rates ranging from 2.70% to 7.81% (3.54% at June 30, 2007)	1,325,000
2002 general obligation bonds of \$130,000 due in annual installments ranging from \$5,000 to \$10,000 through July 1, 2026; bearing interest at rates ranging from 2.70% to 5.60% (3.54% at June 30, 2007)	105,000

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE H - LONG TERM DEBT - Continued**

2002 general obligation bonds of \$830,000 due in annual installments ranging from \$10,000 to \$75,000 through July 1, 2026; bearing interest at rates ranging from 2.70% to 5.60% (3.54% at June 30, 2007)	765,000
2004 general obligation bonds of \$355,000 due in annual installments ranging from \$5,000 to \$30,000 through July 1, 2028; bearing interest at rates ranging from 2.36% to 5.28% (4.17% at June 30, 2007)	340,000
2005 special obligation note of \$455,000 due in annual installments ranging from \$55,000 to \$75,000 through July 1, 2011; bearing interest at rates ranging from 3.27% to 4.62% (4.17% at June 30, 2007)	340,000
2006 general obligation bonds of \$3,000,000 due in annual installments ranging from \$67,000 to \$194,000 through January 1, 2031; bearing interest at 4.50%	2,933,000
2006 special obligation note of \$1,695,000 due in annual installments ranging from \$200,000 to \$285,000 through July 1, 2012; bearing interest at rates ranging from 4.23% to 5.32% (4.23% at June 30, 2007)	<u>1,495,000</u>
	<u><b>\$10,115,568</b></u>

The annual requirement to amortize general and special obligation bonds and notes as of June 30, 2007 follows:

June 30,	Principal	Interest	Total
2008	\$ 813,000	\$ 472,801	\$ 1,285,801
2009	873,000	431,014	1,304,014
2010	927,000	385,519	1,312,519
2011	979,341	336,398	1,315,739
2012	988,227	285,121	1,273,348
2013-2017	2,658,000	894,909	3,552,909
2018-2022	907,000	570,138	1,477,138
2023-2027	1,189,000	316,588	1,505,588
2028-2031	<u>781,000</u>	<u>68,646</u>	<u>849,646</u>
Totals	<u><b>\$10,115,568</b></u>	<u><b>\$3,761,134</b></u>	<u><b>\$13,876,702</b></u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE H - LONG TERM DEBT - Continued**

**3. Other long-term liabilities**

	<b>Outstanding Amount</b>
<p><b>General obligation bond anticipation note</b> – On July 7, 2006 the Municipality issued a \$100,000 general obligation bond anticipation note to Rural Development (“RD”). This represents the first note of a total note of \$320,000 to be issued to finance the construction of a sanitary sewer system financed by RD. The note bears interest at 4.25% and is due the date of the final payment by RD to the Municipality, but not exceeding 10 years from the date of the first note. Accrued interest on note as of June 30, 2007 of \$4,168 is recorded in the government wide statements. The municipality intends to refinance this note on a long term basis through a 2003 general obligation bond issuance of \$320,000 approved by the Governmental Development Bank of Puerto Rico on September 30, 2003. Issuance will occur after the construction project is finished.</p>	<b>\$100,000</b>
<p><b>Note payable to CRIM (LIMS)</b> – On July 3, 2001 the Municipality entered into a financing agreement with the CRIM in the amount of \$539,645 for the payment of the Municipality’s share of the cost of a management information system (LIMS) acquired by the CRIM for the management of taxpayer’s properties located in Puerto Rico. The note is payable in semiannual installments of \$36,188, including interest of 5.95% and is due on November 28, 2011. Amount is financed with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM). Debt service requirements in future years are as follows:</p>	<b>\$282,099</b>

<b>June 30</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2008	\$ 56,420	\$15,678	\$ 72,098
2009	59,827	12,254	72,081
2010	63,439	8,624	72,063
2011	67,270	4,774	72,044
2012	<u>35,143</u>	<u>872</u>	<u>36,015</u>
<b>Totals</b>	<b><u>\$282,099</u></b>	<b><u>\$42,202</u></b>	<b><u>\$324,301</u></b>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE H - LONG TERM DEBT - Continued**

**Note payable to CRIM (Financing of delinquent accounts)**– On March 26, 2002, the Municipality entered into a financing agreement with the CRIM in the amount of \$470,818, to finance delinquent property tax accounts sold to private investors, under the provision of Law No. 146 of October 11, 2001. The agreement is in the form of a non-revolving line of credit bearing interest of 6.5% for the first 5 years and variable for the next 25 years at 125 points over London Interbank Offered Rate (LIBOR) and is due on December 1, 2032. As described in Law No. 146, interest payments for the first 5 years were financed through .48% of the net increase of subsidy provided by the Commonwealth of Puerto Rico's general fund. Also, during the first 5 years any collection from those delinquent accounts was credited to the loan principal. After the 5 year period the loan outstanding balance was restructured for a 25 years period. Debt service requirements in future years are as follows:

\$120,567

<u>June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2008	\$ 4,823	\$ 7,499	\$ 12,322
2009	4,823	7,199	12,022
2010	4,823	6,899	11,722
2011	4,823	6,599	11,422
2012	4,823	6,299	11,122
2013-2017	24,113	26,931	51,044
2018-2022	24,113	19,498	43,611
2023-2027	24,113	11,999	36,112
2028-2032	<u>24,113</u>	<u>4,500</u>	<u>28,613</u>
Totals	<u>\$120,567</u>	<u>\$97,423</u>	<u>\$217,990</u>

**Note payable to Puerto Rico Aqueduct and Sewer Authority (PRASA)** – On March 27, 2007 the Municipality entered into a financing agreement with PRASA to refinance through a long term (non-interest) obligation a \$47,725 debt for water and sewer services as of February 28, 2007. The note has an imputed interest rate of 6.61% and was originally recorded at its present value of \$46,259, net of an unamortized discount of \$1,466 at inception. This note is payable in annual installments of \$3,500 (including interest) and due on March 27, 2008. At June 30, 2007 the outstanding balance, net of the unamortized discount of \$850, amounted to \$30,650 and will be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center (CRIM).

\$30,650

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE H - LONG TERM DEBT - Continued**

Note payable to Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). - On June 29, 2007 the Board of Trustees of the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) approved Resolution No. 2007-02 authorizing the ERS to establish payment plans with employers related to the application of certain "Special Laws" issued by the Commonwealth Government. Those Special Laws granted increases in pensions to retired employees of the Municipality. This obligation was recognized by the Municipality prior to June 30, 2007. On October 19, 2007 the Municipality refinanced this debt on a long term basis through a \$198,355 non-interest bearing note with the ERS. The note has an imputed interest rate is 6.48% and was recorded at its present value of \$182,255 net of an unamortized discount of \$16,100. The note is payable in annual installments of \$66,118 (including interest), is due on February 26, 2010 and will be repaid with unrestricted funds. Debt service requirements in future years are as follows:

\$182,255

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2008	\$ 61,815	\$ 4,303	\$ 66,118
2009	58,335	7,783	66,118
2010	<u>62,105</u>	<u>4,014</u>	<u>66,119</u>
Totals	<u>\$182,255</u>	<u>\$16,100</u>	<u>\$198,355</u>

**Compensated absences** - includes accrued vacations, sick leave benefits and other benefits with similar characteristics such as compensatory time, represents the Municipality's commitment to fund such costs from future operations. Amount is paid with unrestricted funds.

\$3,180,043

**Christmas Bonus** - represent the accrued portion corresponding to fiscal year 2006-2007 of the Christmas bonus to be paid in December 2007.

\$ 303,481

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE H - LONG TERM DEBT - Continued**

**Payable to CRIM, property tax advances** - represents the balance owed to CRIM at June 30, 2007 for excess of advances of property tax and other subsidies over final amount of property tax collections for the fiscal year 2005-2006. This amount will be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM).

\$65,402

**NOTE I - PROPERTY TAXES**

The Municipal Revenue Collection Center (CRIM) of the Commonwealth of Puerto Rico is responsible for the assessment, collection and distribution of real and personal property taxes. The tax on personal property is self-assessed by the taxpayer. The assessment is made on a return, which must be filed with the CRIM by May 15 of each year and is based on the current value at the date of the assessment. Real property is assessed by the CRIM. The tax is general assessed on January 1 on all taxable property located within the Municipality and is based on the current value existing in the year 1957. For personal property the tax is due with the return filed on or before May 15. Taxes on real property may be paid on two equal installments, July 1<sup>st</sup> and January 1<sup>st</sup>. Total tax rates in force as of June 30, 2007 are 7.03% for personal property and 9.03% for real property. The distribution of these rates follows:

<u>Description</u>	<u>Personal Property</u>	<u>Real Property</u>
Basic property tax rate, which is appropriated for general purposes and accounted in the Municipality's general fund:	4.00%	6.00%
Percent that belongs to the Commonwealth's debt service fund:	1.03%	1.03%
Percent that belongs to the Municipality's debt service fund:	<u>2.00%</u>	<u>2.00%</u>
Total tax rate:	7.03%	9.03%
Discount granted by law to the taxpayers but reimbursed to the Municipality by the P.R. Treasury Department:	<u>(.20%)</u>	<u>(.20%)</u>
Total percent to be paid by taxpayers:	<u>6.83%</u>	<u>8.83%</u>

Residential real property occupied by its owner is exempt by law from property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the Puerto Rico Department of Treasury assumes payment of the basic tax to the Municipality, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. Revenue related to exempt property is recorded in the General Fund. The Municipality grants a complete exemption from personal property taxes up to an assessment value of \$50,000 to retailers with annual net sales of less than \$150,000.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE I - PROPERTY TAXES - Continued**

The CRIM advances funds to the Municipality based on an estimate of special governmental subsidies and the property taxes to be levied and which are collected in subsequent periods. This distribution includes advances of property tax and amounts of municipal equalization fund from the Commonwealth government. The 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. The CRIM prepares a preliminary settlement not later than three months after fiscal year-end and a final settlement not later than six months after fiscal year-end. If actual collections exceed the advances a receivable from CRIM is recorded. However, if advances exceed actual collections, a payable to CRIM is recorded. For the fiscal year 2005-2006 the CRIM performed the final settlement and determined that that Municipality has a net debt of \$65,402. This amount is recorded as long term debt. For the fiscal year 2006-2007 a net receivable of \$187,234 was determined as a result of the preliminary settlement. This amount is recorded in the general fund as a receivable but also as deferred revenue since is not available as required by current standards.

**NOTE J - INTERGOVERNMENTAL REVENUES**

Intergovernmental revenues in the General Fund are comprised of Christmas bonus reimbursement of \$257,888 and revenues for municipal equalization fund of \$4,162,512 received from the Commonwealth of Puerto Rico. Amount recorded in other governmental funds consists of Federal and Commonwealth governmental grants.

**NOTE K - RETIREMENT PLAN**

**1. Plan description**

Regular employees of the Municipality contribute to a cost sharing multiple employer defined benefit retirement plan, administered by the Employee's Retirement System of the Government of Puerto Rico an its Instrumentalities (ERS). ERS covers all regular full time public employees working for the central government, the municipalities and certain public corporations not having their own retirement systems. The system provides retirement pensions, death and disability benefits.

Retirement benefits depend upon age at retirement and number of years of credited service. Disability retirement benefits are available to members of occupational and no occupational disabilities. Benefits vest after ten years of plan participation. The system was created under Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75% of the average compensation. ERS issues a publicly financial report that includes financial statements and required supplementary information of the Plan, which may be obtained from the ERS.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

**NOTE K - RETIREMENT PLAN - Continued**

Law No. 305 of September 24, 1999 amended the Act No. 447 of 1951 and was enacted with the purpose of establishing a new pension program (System 2000). The new pension program became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999 may elect either to stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000 will only be allowed to become members of the new program.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. There will be a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. Benefits at retirement age will not be guaranteed by the State government and will be subjected to the total accumulated balance of the savings account. The annuity will be based on a formula, which assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. If savings accounts balance is \$10,000 or less at time of retirement, the balance will be distributed by the System to the participant as a lump sum. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances.

Disability pensions are not been granted under the new program. The employer contributions (9.275% of the employee's salary) will be used to fund the current plan. Under System 2000 the retirement age is reduced from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

**2. Funding policy**

The Act 447, as amended, is the authority under which obligations to contribute to the Plan by the Plan members, employers and other contributing entities are established or may be amended. Plan members are required to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600 except for the Mayor or employee under a supplementation plan, which contributes 8.275% of gross salary. The Municipality is required to contribute 9.275% of gross salary.

The Municipality's actual contribution for the current and the previous three fiscal years, which is equal to the required contribution, follows:

<u>Fiscal year ended:</u>	<u>Law No. 447</u>	<u>System 2000</u>
2007	<u>\$233,799</u>	<u>\$217,278</u>
2006	<u>\$247,535</u>	<u>\$224,966</u>
2005	<u>\$237,368</u>	<u>\$201,431</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2007**

**NOTE L – POSTEMPLOYMENT BENEFITS**

In addition to the pension benefits described in Note K, the Municipality is required to cover annually the 3% increase in the retirement plan of its retired employees, as required by Commonwealth's laws. Also, the Municipality is required to finance costs related to the application of certain "Special Laws" issued by the Commonwealth Government. Those Special Laws granted increases in pensions and other benefits to retired employees of the Municipality such as medicines bonus, Christmas bonus and death benefits. For the fiscal year ended, costs related to these post employment benefits amounted to \$93,545. These benefits are recorded as expenditures when paid in the general fund.

**NOTE M - COMMITMENTS**

**1. *Operating leases***

The Municipality leases office space and office equipment under operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same terms. Rental expenses amounted approximately \$69,411. Management believes that the summary of the future minimum rental commitments under noncancelable equipment leases with terms exceeding one year is not significant.

**2. *Construction***

The Municipality has commitments at June 30, 2007 of approximately \$1,750,857 for construction, improvements or renovation of certain municipal facilities

**NOTE N - CONTINGENCIES**

**1. *Federal and State grants***

Projects financed by Federal and State Grants are subject to audits by grantors and other governmental agencies in order to determine its expenditures to comply with the conditions of such grants. It is the Municipality's opinion that no additional material unrecorded liabilities will arise from audits previously performed or to perform.

**2. *Litigations***

The Municipality is, at present, a defendant in a number of legal matters that arise in the ordinary course of the Municipality's activities. There are cases whereby the Municipality is a defendant or codefendant that will be covered by insurance, certain cases whereby the legal counsel has not determined an outcome and other cases that will not be covered by insurance. However, it is the opinion of the Municipality and the legal counsels that based on their experience, such actions and the potential liabilities will not impair the Municipality financial position.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

**NOTE O – FUND BALANCE DEFICITS**

Certain special funds included as other governmental funds in the fund statements disclosed fund balance deficits as follows:

	<u>Amount</u>
Law No. 52	\$153,408
Law No. 82	\$ 29,874
Traffic Safety Commission	\$ 22,911
Elderly Affairs	\$ 14,447
INSEC	\$ 15,745
Homeland Security	\$ 88,216

The deficits results from the accrual of expenditures without accruing intergovernmental revenues. As required by current standards, the Municipality recorded intergovernmental revenues for grants on fund statements when all applicable eligibility requirements have been met and the resources are available.

**NOTE P– SUBSEQUENT EVENTS**

**1. Sales and use tax implementation**

On July 29, 2007 the Commonwealth Legislature approved Act No. 80 (“Act 80”) which imposed to all the Municipalities of Puerto Rico a uniform municipal sales and use tax of 1.5%. Effective August 1, 2007 1% of the 1.5% will be collected by the Municipalities and the remaining .5% of the 1.5% will be collected by the Puerto Rico Department of Treasury.

Act 80 also provides for restrictions on the use of the resources (including the .5 of 1.5% collected by the Commonwealth Government) to be invested in solid waste and recycling programs, capital improvements and health and public safety costs. Amount collected by the Commonwealth Government will be deposited in accounts or special funds in the Governmental Development Bank of Puerto Rico (“GDB”), subject to restrictions imposed and distributed as follows:

- .2% of the .5% will be deposited in a “Municipal Development Fund” to finance costs as restricted by the Act,
- .2% of the .5% will be deposited in a “Municipal Redemption Fund” to finance loans to Municipalities subject to restrictions imposed by the Act and,
- .1% of the .5% will be deposited in a “Municipal Improvement Fund” to finance capital improvement projects; these funds will be distributed based on legislation from the Commonwealth’s Legislature.

The Municipal Legislature approved Ordinance No. 15 Series 2007-2008 to amend Municipal Ordinance No. 36 Series 2006-2007 to conform to dispositions of Act 80.

**REQUIRED SUPPLEMENTARY INFORMATION**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**BUDGETARY COMPARISON SCHEDULE – GENERAL FUND  
FISCAL YEAR ENDED JUNE 30, 2007**

	Budgeted amounts		Actual amounts (Budgetary basis)	Variance with final budget Positive Negative
	Original	Final		
<b>Revenues:</b>				
<b>Taxes:</b>				
Property taxes	\$ 3,525,860	\$ 3,525,860	\$ 3,889,364	\$363,504
Municipal license taxes	2,747,365	2,747,365	3,040,483	293,118
Sales and use taxes	1,197,576	1,197,576	1,212,054	14,478
Intergovernmental	3,122,430	3,122,930	3,164,618	41,688
Rental income and charges for services	4,179,638	4,332,238	3,816,948	(515,290)
Fines and forfeitures	20,000	20,000	22,905	2,905
Interest	211,000	211,000	318,209	107,209
Other	317,567	334,878	297,277	( 37,601)
<b>Total Revenues</b>	<u>15,321,436</u>	<u>15,491,847</u>	<u>15,761,858</u>	<u>270,011</u>
<b>Expenditures</b>				
<b>Current</b>				
General government	5,268,918	5,166,587	5,146,338	20,249
Public safety	1,399,278	1,355,051	1,349,362	5,689
Public works	5,129,356	5,690,707	5,810,902	(120,195)
Sanitation	1,402,469	1,290,953	1,290,416	537
Health	786,764	786,764	786,763	1
Welfare	438,281	407,925	407,725	200
Culture and recreation	583,630	558,077	557,601	476
Education	312,740	295,872	294,763	1,109
<b>Total expenditures</b>	<u>15,321,436</u>	<u>15,551,936</u>	<u>15,643,870</u>	<u>( 91,934)</u>
<b>Excess (deficiency) of revenues over expenditures</b>	<u>-</u>	<u>(60,089)</u>	<u>117,988</u>	<u>178,077</u>
<b>Other financing sources (uses)</b>				
Transfers – in		60,089	64,336	4,247
<b>Total other financing sources (uses)</b>		<u>60,089</u>	<u>64,336</u>	<u>4,247</u>
<b>Excess of revenues and other financing sources over expenditures and other financing uses</b>		<u>-</u>	<u>\$ 182,324</u>	<u>\$182,324</u>

The accompanying notes to required supplemental information are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION -  
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND**

**June 30, 2007**

**NOTE A – BUDGET PROCESS AND BUDGETARY BASIS OF ACCOUNTING**

The Municipal budget is prepared for the General Fund following the requirements of the Autonomous Municipal Law of 1981, as amended. It is developed utilizing elements of performance-based program budgeting and zero-based budgeting and includes estimates of revenues and other sources for ensuing fiscal year under laws existing at the time the budget is prepared.

Budget amendments are approved by the Municipal Legislature. Certain budget transfers within the limitations and restrictions of the Municipal Law can be approved by the Mayor or by the Municipal Legislature. The budget comparison schedule provides information about the original budget, the amended budget and the actual results, under the budgetary basis of accounting.

The budgetary basis of accounting is different from GAAP. Revenues are generally recorded when cash is received and expenditures are generally recorded when the related expenditure is incurred or encumbered. The encumbrances (that is, purchase orders, contracts) are considered expenditures when a commitment is made. On a GAAP basis, encumbrances outstanding at year end are reported in the governmental funds statements as a reservation of fund balance since they do not constitute expenditures or liabilities while on a budgetary basis encumbrances are recorded as expenditures of current year. Encumbrance appropriations lapse one year after the end of the fiscal year. Unencumbered appropriations are lapsed at year end. The legal level of budgetary control (the level at which expenditures may not legally exceed appropriations) is at the function level.

The presentation of the budgetary data excludes other appropriations such as capital projects, debt service and special revenue funds because projects are funded on a multi-year nature, generally requiring several years to complete or effective budgetary control is alternatively achieved through general obligation bond indentures and legal and contractual grant agreement provisions.

**NOTE B - BUDGET READJUSTMENT**

During the year the approved operational budget was increased by \$ 1,226,840 from previous year excess fund balance. The purpose of this readjustment was to increase the amount assigned to certain expenditures in the general fund.

**NOTE C - BUDGET TO GAAP RECONCILIATION**

The accompanying budgetary comparison schedule presents comparisons of the original and final legally adopted budget with actual data on a budgetary basis. Since accounting principles applied for the purposes of developing data on a budgetary basis differ significantly from those used to present accounting principles generally accepted in the United States, the following budget to GAAP reconciliation is presented:

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION –  
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND, Continued  
JUNE 30, 2007

NOTE C – BUDGET TO GAAP RECONCILIATION – Continued

<b>Excess of revenues and other financing sources over expenditures and other financing uses (budgetary basis):</b>	<b>\$182,324</b>
<b>Budget to GAAP differences:</b>	
<b>Entity differences:</b>	
Non budgeted funds recorded as revenues for financial reporting purposes:	443,247
Non budgeted funds recorded as expenditures for financial reporting:	( 13,659)
<b>Basis of accounting differences:</b>	
Revenues recorded for financial reporting purposes but not in budgetary basis:	152,717
Revenues recorded in budgetary basis purposes but not in financial reporting	( 88,949)
Expenditures recorded for financial reporting purposes but not in budgetary basis	(158,415)
<b>Timing differences:</b>	
Current year encumbrances recorded as expenditures for budgetary reporting purposes:	417,395
Prior year encumbrances recorded as expenditures for financial reporting purposes:	<u>(226,573)</u>
<b>Net change in fund balance (GAAP basis):</b>	<b><u>\$708,087</u></b>

**SUPPLEMENTARY INFORMATION**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**SUPPLEMENTARY INFORMATION – FINANCIAL DATA SCHEDULE  
BALANCE SHEET INFORMATION  
JUNE 30, 2007**

<u>Line Item Number</u>	<b>ASSETS</b>	<b>Section 8 Housing Choice Vouchers <u>14,871</u></b>
	<b>Current Assets</b>	
	Cash:	
111	Cash – unrestricted	\$ 4,338
113	Cash – other restricted	<u>39,983</u>
100	<b>Total cash</b>	<u>44,321</u>
	Accounts and notes receivables	
121	Accounts receivable – PHA projects	6,180
125	Accounts receivable – miscellaneous	3,378
128	Fraud recovery	<u>6,278</u>
120	<b>Total receivables, net of allowance for doubtful accounts</b>	<u>15,836</u>
150	<b>Total Current Assets</b>	<u>60,157</u>
	<b>Noncurrent Assets</b>	
	Fixed assets	
164	Furniture, equipment & machinery – administration	46,825
166	Accumulated depreciation	<u>(29,672)</u>
160	<b>Total fixed assets, net of accumulated depreciation</b>	<u>17,153</u>
180	<b>Total Noncurrent Assets</b>	<u>17,153</u>
190	<b>TOTAL ASSETS</b>	<u>\$77,310</u>
	<b>LIABILITIES AND EQUITY LIABILITIES</b>	
	<b>Current Liabilities</b>	
322	Accrued compensated absences – current portion	\$ 2,247
345	Other current liabilities	6,473
347	Inter-program – due to	<u>7,570</u>
310	<b>Total Current Liabilities</b>	<u>16,290</u>
	<b>Noncurrent liabilities</b>	
353	Noncurrent liabilities – other	1,204
354	Accrued Compensated Absences – non current	<u>1,596</u>
350	<b>Total Noncurrent Liabilities</b>	<u>2,800</u>
300	<b>TOTAL LIABILITIES</b>	<u>19,090</u>
	<b>EQUITY</b>	
508.1	Invested in Capital Assets, Net of Related Debt	17,153
509	Restricted Net Assets	38,779
512.1	Unrestricted Net Assets	<u>2,288</u>
513	<b>TOTAL EQUITY/NET ASSETS</b>	<u>58,220</u>
600	<b>TOTAL LIABILITIES and EQUITY/NET ASSETS</b>	<u>\$77,310</u>

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**SUPPLEMENTARY INFORMATION – FINANCIAL DATA SCHEDULE  
STATEMENT OF REVENUES AND EXPENSES INFORMATION  
FISCAL YEAR ENDED JUNE 30, 2007**

<u>Line Item Number</u>		<u>Section 8 Housing Choice Vouchers 14,871</u>
	<b>REVENUES:</b>	
706	HUD PHA operating grants	\$363,051
711	Investment income – unrestricted	33
714	Fraud recovery	6,438
715	Other revenue	24,737
716	Gain or loss on the sale of fixed assets	<u>(161)</u>
700	<b>TOTAL REVENUES</b>	<u>394,098</u>
	<b>EXPENSES</b>	
	<b>Administrative</b>	
911	Administrative salaries	38,400
914	Compensated absences	1,891
915	Employee benefit contributions –administrative	14,345
916	Other operating – administrative	<u>14,463</u>
969	<b>TOTAL OPERATING EXPENSES</b>	<u>69,099</u>
970	<b>EXCESS OPERATING REVENUES OVER OPERATING EXPENSES</b>	324,999
973	Housing assistance payments	308,417
974	Depreciation expense	<u>6,922</u>
	Subtotal	<u>315,339</u>
900	<b>TOTAL EXPENSES</b>	<u>384,438</u>
1000	<b>EXCESS OF TOTAL REVENUE OVER (UNDER) TOTAL EXPENSES</b>	<u>\$ 9,660</u>
	<b>MEMO account information</b>	
1103	Beginning equity	68,707
1104	Prior period adjustments, equity transfers and correction of errors	(20,147)
1117	Administrative Fee Equity	19,441
1118	Housing Assistance Payments Equity	38,779
1120	Unit months available	1,008
1121	Number of units months leased	933

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO SUPPLEMENTARY INFORMATION  
FINANCIAL DATA SCHEDULE**

**June 30, 2007**

**NOTE A – BASIS OF PRESENTATION**

The accompanying financial data schedule (FDS) is a trial balance of the Section 8 Housing Choice Voucher Program, administered by the Municipality. The FDS was created in order to standardize the financial information reported by Public Housing Authorities (PHA) to the Real Estate Assessment Center (REAC), as required by the Uniform Financial Reporting Standards (UFRS). REAC is the US Department of Housing and Urban Development (HUD) national management center created to assess the condition of HUD owned and assisted properties. The UFRS are rules to implement requirements of 24 CFR, Part 5, Subpart H, for the electronic filing of financial information to HUD.

In accordance with the guidelines for reporting and attestation requirements of UFRS, the accompanying FDS is included as information supplementary to the financial statements. It was prepared using the accrual basis of accounting, as required by REAC regulations.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FISCAL YEAR ENDED JUNE 30, 2007**

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number (note B)	Pass-Through Entity Identifying Number (note C)	Federal Expenditures (note A)
<b><u>U.S. Department of Housing and Urban Development</u></b>			
Community Development Block Grant-Entitlement Grant	14.218	N/A	\$ 728,700
Passed through the Office of Commissioner of Municipal Affairs: Community Development Block Grant – State’s Program	14.228	AB-57, FC-57 FD-57	152,432
Section 8 Housing Choice Vouchers	14.871	N/A	<u>393,821</u>
Subtotal U.S. Department of Housing and Urban Development:			<u>1,274,953</u>
<b><u>U.S. Department of Justice</u></b>			
Passed through the P.R. Department of Justice: Edward Byrne Justice Assistance Grant	16.738	2005-DJ-EPMSG-01	49,893
<b><u>U.S. Department of Transportation – National Highway Traffic Safety Administration</u></b>			
Passed through the P.R. Department of Transportation – (Traffic Safety Commission): State and Community Highway Safety	20.600	03-03-76	23,296
<b><u>U.S. Department of Health and Human Services</u></b>			
Passed through the Puerto Rico Governor’s Office – (Office of Elderly Affairs): Special Program for the Aging Title III Part C-1 and C-2 Grants for Supportive Services and Seniors Centers	93.045	N/AV	77,212
Passed through the “Instituto de Servicios Comunales Inc. (INSEC)” Community Services Block Grant	93.569	CSBG 03-04-32	<u>31,754</u>
Subtotal U.S. Department of Health and Human Services:			<u>108,966</u>
<b><u>U.S. Department of Homeland Security</u></b>			
Passed through the Puerto Rico Governor’s Office – (Governor’s Authorized Representative-GAR): Disaster Grants – Public Assistance	97.036	125-99-125	69,626
Passed through the Puerto Rico Governor’s Office (Office of Public Safety Affairs): Homeland Security Grant Program (SHSP)	97.067	2005-GE-T5-4009	<u>84,750</u>
Subtotal U.S. Department of Homeland Security:			<u>154,376</u>
<b>Total Expenditures of Federal Awards</b>			<b><u>\$1,611,484</u></b>

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN**

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

June 30, 2007

**NOTE A – BASIS OF PRESENTATION**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Municipality and is presented on the modified accrual basis of accounting. Expenditures are recognized when the related liability is incurred. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, "Audits of States, Local Governments and Nonprofit Organizations". Therefore, some amounts presented in this schedule may differ from the amounts presented in, or used in the preparation of, the basic financial statements.

**NOTE B - FEDERAL CFDA NUMBER**

The Catalog of Federal Domestic Assistance (CFDA) Number is a program identification number. The first two digits identify the federal department or agency that administers the program and the last three numbers are assigned by numerical sequence.

**NOTE C – PASS-THROUGH ENTITY IDENTIFYING NUMBER**

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

**NOTE D – RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE BASIC FINANCIAL STATEMENTS**

Description	Other Governmental Funds
14.218	\$ 728,700
14.228	152,432
14.871	393,821
16.738	49,893
20.600	23,296
93.045	77,212
93.569	31,754
97.036	69,626
97.067	<u>84,750</u>
Total federal awards expenditures	1,611,484
Total nonfederal awards expenditures	<u>1,627,656</u>
Total expenditures, fund statements	<u>\$3,239,140</u>

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

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of **Municipality of San Germán, Puerto Rico**, as of and for the year ended June 30, 2007, which collectively comprise the Municipality of San Germán, Puerto Rico's basic financial statements and have issued our report thereon dated November 30, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Municipality of San Germán, Puerto Rico's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Municipality of San Germán, Puerto Rico's financial statements that is more than inconsequential will not be prevented or detected by the Municipality of San Germán, Puerto Rico's internal control.

### **Internal Control Over Financial Reporting, Continued**

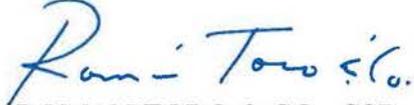
A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Municipality of San Germán, Puerto Rico's internal control.

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

### **Compliance and Other Matters**

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

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

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

Yauco, Puerto Rico  
November 30, 2007

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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**

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

**Compliance**

We have audited the compliance of **Municipality of San Germán, 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, 2007. Municipality of San Germán, 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 San Germán, Puerto Rico's management. Our responsibility is to express an opinion on Municipality of San Germán, 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 San Germán, 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 San Germán, Puerto Rico's compliance with those requirements.

In our opinion, Municipality of San Germán, Puerto Rico complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2007. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2007-2 and 2007-3.

### **Internal Control Over Compliance**

The management of Municipality of San Germán, 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 San Germán, Puerto Rico's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality of San Germán, Puerto Rico's internal control over compliance.

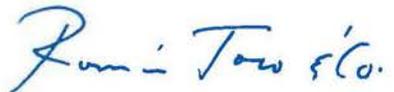
A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal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

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

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

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

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

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

Yauco, Puerto Rico  
November 30, 2007

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to the original of this report

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2007**

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**SECTION I – SUMMARY OF AUDITORS' RESULTS**

**Financial Statements**

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

**Internal control over financial reporting:**

• Control deficiency identified?  Yes  None reported  
 • Significant deficiency identified?  Yes  None reported  
 • Material weakness (es) identified?  Yes  No  
 Noncompliance material to financial statements noted?  Yes  No

**Federal Awards**

**Internal control over major programs:**

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

**Type of auditor's report issued on compliance for Major Programs:**

Unqualified Opinion  Qualified Opinion  
 Adverse Opinion  Disclaimer Opinion

**Any audit finding disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133?**

Yes  No

**Identification of Major Programs:**

CFDA Number	Name of Federal Program or Cluster
14.218	Community Development Block Grant – Entitlement Grants
14.871	Section 8 – Rental Housing Choice Vouchers

**Dollar threshold used to distinguish between Type A and Type B Programs:**

\$300,000

**Auditee qualified as low-risk auditee?**

Yes  No

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)  
FOR THE YEAR ENDED JUNE 30, 2007

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**SECTION II – FINANCIAL STATEMENTS FINDINGS**

**2007 -1**

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

**Condition:**

The Municipality made 6 out of 56 disbursements examined for the Section 8 program for which the Pre-Intervention Officer (employee who reviewed, signed, and approved the disbursement) performed the physical disbursement of checks, also as a task assigned to the Official Payer, resulting in a lack of separation of duties.

**Criteria:**

The Municipality's internal control system provides for separate functions for the disbursement process, each carried out by employees independent of each other, in order to improve monitoring, information and communication controls. The Pre-Intervention Officer is in charge of reviewing and approving all documentation supporting a disbursement before its release, whose work is then considered and relied upon by other employees, including the Finance Director. The Official Payer is only limited to preparing and disbursing the physical checks.

**Cause:**

This situation was an isolated item because the Official Payer was not available to prepare and release the checks on a certain date, and the Pre-Intervention Officer performed both the pre-intervention and official payment functions for disbursements prepared that day. This situation was not observed in our tests for other disbursements.

**Effect:**

The Municipality's internal control structure concerning proper monitoring of disbursements was affected by one employee performing two required functions of reviewing and approving, and preparing checks.

**Recommendation:**

The Municipality should ensure proper monitoring over transactions, specifically that the separation of duties controls not be affected. The Pre-Intervention Officer should not prepare and release the checks on documents he/she pre-audited. The Municipality should either assign additional personnel to assist the Pre-intervention area or the Official Payer, or should withhold payments until the functions are performed properly.

**Questioned Costs:** Not applicable.

**END OF SECTION**

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)  
FOR THE YEAR ENDED JUNE 30, 2007

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**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

**2007 -2**

Type of finding: Internal Controls Over Compliance of Major Program  
Situation: Control deficiency  
Federal Program: Section 8 Housing Choice Voucher Program (14.871)  
Compliance Requirements: Eligibility (E)  
Prior-Year(s) Audit Finding(s): None.

**Condition:**

During our audit, we discovered the following deficiencies in the documentation of reexaminations and the determination of tenant income and eligibility:

1. For one voucher examined, no annual reexamination was performed during the 2006-2007 fiscal year. The tenant was last reexamined on February 1, 2006. Subsequently, the tenant moved to a different housing unit but remained with the same voucher effective September 1, 2006. A HUD-50058 Family Report was prepared to report the change of unit and no other procedures were performed. However, the program's personnel mistakenly considered this change as a reexamination and did not perform the annual reexamination and income determination effective February 1, 2007 as of our audit date.
2. For another voucher, the program did not consider \$3,120 in tenant annual income during the reexamination on February 1, 2007, despite third-party evidence included in the participant's file.
3. The program did not obtain third-party evidence of potential tenant income regarding to child support income during the reexamination on March 1, 2007.

**Criteria:**

For the first situation, 24 CFR section 982.516 subtitle (a)(1) states that "the PHA must conduct a reexamination of family income and composition at least annually."

For the second and third situations, 24 CFR section 982.516 subtitle (a)(2) states that "the PHA must obtain and document in the tenant file third party verification of...(i) reported family annual income." Subtitle (e) of the same section states that "family income must include income of all family members;" while subtitle (f) adds that "the PHA must establish procedures that are appropriate and necessary to assure that income data provided by applicant or participant families is complete and accurate."

**Cause:**

The situations mentioned above were caused by inadequate monitoring procedures regarding the scheduling of reexaminations and the review of participant files before and after the scheduled reexamination date.

**Effect:**

The Municipality did not perform a reexamination as required by HUD regulations, and failed to consider income of tenants, thereby miscalculating the HAP payment owed to the owner.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)  
FOR THE YEAR ENDED JUNE 30, 2007**

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**2007 -2 Deficiencies in Tenant Reexaminations and Income Determinations  
(Continued)**

**Recommendation:**

The program's management should implement additional monitoring and reviewing procedures in order to ensure the program's personnel are adequately determining tenant income, including tracing evidence of income to the HUD-50058 Family Report and vice versa, and ensuring that all reexaminations are performed annually.

**Questioned Costs:** Not yet determined.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)  
FOR THE YEAR ENDED JUNE 30, 2007**

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**2007-3**

Type of finding: Internal control over major program  
Situation: Control deficiency  
Federal Program: Section 8 Housing Choice Vouchers  
Compliance Requirements: None.  
Prior-Year(s) Audit Finding(s): None.

**Condition:**

6 out of 56 disbursements examined for the Section 8 program had a lack of separation of duties relating to monitoring and check preparing functions of disbursements and expenditures. See Finding 2007-1.

**Criteria:**

The Municipality's internal control system provides for separate functions for the disbursement process relating to review and approval of documents and the preparation of checks, each carried out by employees independent of each other, in order to improve monitoring and information and communication controls.

**Cause:**

This situation was an isolated item because the Official Payer was not available to prepare and release the checks on a certain date, and the Pre-Intervention official performed both the Pre-Intervention and Official Payer functions for that day. This situation was not observed in our tests for other disbursements.

**Effect:**

The Municipality's internal control structure concerning proper monitoring of federal award expenditures was affected by one employee performing the two required functions of reviewing and approving and preparing checks.

**Recommendation:**

The Municipality should ensure proper monitoring over transactions, specifically that the separation of duties controls not be affected. The Pre-Intervention official Official Payer should not prepare and release the checks on documents he/she pre-audited. The Municipality should either assign additional personnel to assist the Pre-intervention Area or the Official Payer, or should withhold payments until the functions are performed properly.

**Questioned Costs:** None.

**END OF SECTION**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2007**

Year	Finding Number	Finding	Number	CFDA Questioned Cost(s)	Comments
------	----------------	---------	--------	-------------------------	----------

**(1) Audit Findings that have been fully corrected or not noted during our audit:**

2006	2006 III-1	Various deficiencies in compliance with Davis-Bacon Act, including vendor payrolls submitted without the required compliance statement, payrolls submitted tardy, and construction contracts for which certified payrolls were not received.	14.228 and 14.218	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.
2006	2006 III-2	The Municipality does not maintain a complete general ledger, with all grant receivables and payables, for the CDBG program.	14.228	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.
2005	2005 III-4	The Municipality does not maintain a complete general ledger, with all grant receivables and payables, for the CDBG program.	14.218	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.
2005	2005-III-6	Information in financial reports tested did not reconcile with the SBGP program's general ledger, including the budget accumulated balances and summary information.	14.228	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.
2004	2004-III-7	Missing and inaccurate financial reports of the SBGP program.	14.228	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.
2004	2004-III-8	The Municipality's general ledger for the SBGP program is incomplete and unbalanced. The amounts recorded in the manual general ledger system do not agree with the centralized accounting system.	14.228	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.
2004	2004 III-9	Conflict of interest in the performance of an inspection of a repaired housing unit of the SBGP program.	14.228	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.
2004	2004 III-10	Deficiencies in follow-up inspections and monitoring of participants of the SBGP program.	14.228	None.	Situation was corrected by the Municipality. Awaiting grantor clearance.

**(2) Audit Findings not corrected or partially corrected:**

NONE.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF SAN GERMAN  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (Continued)  
FOR THE YEAR ENDED JUNE 30, 2007**

Year	Finding Number	Finding	Number	CFDA Questioned Cost(s)	Comments
------	----------------	---------	--------	-------------------------	----------

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

NONE.

**(4) Audit findings are no longer valid:**

2005	2005 III-1	The Municipality's general ledger for the Community Facilities Loans and Grants is incomplete and unbalanced. The amounts recorded in the manual general ledger system do not agree with the centralized accounting system.	10.766	None.	Project was completed. Situation was corrected by the Municipality. Awaiting grantor clearance.
2004	2004 III-1	The Municipality did not provide evidence that contractor's weekly payrolls were being reviewed for constructions of the Community Facilities Loans and Grants.	10.766	None.	Project was completed. Awaiting grantor clearance.
2004	2004-III-2	The Municipality's general ledger for the Community Facilities Loans and Grants is incomplete and unbalanced. The amounts recorded in the manual general ledger system do not agree with the centralized accounting system.	10.766	None.	Project was completed. Awaiting grantor clearance.
2004	2004-III-3	Excess cash in bank for an unreasonable amount of time for the Grants for Public Works and Economic Development program.	11.300	None.	Project was completed. Awaiting grantor clearance.
2004	2004-III-4	The Municipality did not provide evidence that contractor's weekly payrolls were being reviewed for constructions of the Grants for Public Works and Economic Development program. No clauses regarding this were included in the construction contract. Deficiencies in the documentation of weekly certified payrolls received from the contractor.	11.300	None.	Project was completed. Situation was corrected by the Municipality. Awaiting grantor clearance.
2004	2004 III-5	Missing and inaccurate financial reports of the Grants for Public Works and Economic Development program.	11.300	None.	Project was completed. Situation was corrected by the Municipality. Awaiting grantor clearance.
2004	2004 III-6	The Municipality's general ledger for the Grants for Public Works and Economic Development program is incomplete and unbalanced. The amounts recorded in the manual general ledger system do not agree with the centralized accounting system. Incompatible duties assigned to the accountant.	11.300	None.	Project was completed. Incompatible duties situation was corrected by the Municipality. Awaiting grantor clearance.

**END OF SCHEDULE**

MUNICIPIO AUTÓNOMO DE SAN GERMÁN  
DEPARTAMENTO DE FINANZAS

APARTADO 85

SAN GERMÁN, PR 00683

TEL. (787) 892-3500

FAX: (787) 892-1060



20 de diciembre de 2007

Lcdo. Angel M. Castillo  
Comisionado  
OCAM  
PO Box 70167  
San Juan, PR 00936-8167

Estimado Sr. Castillo:

Reciba un cordial saludo de parte de todos los que laboramos en la administración municipal de San Germán.

Le acompaño copia de los estados financieros del Municipio de San Germán para el año que finalizó el 30 de junio de 2007 y el Data Collection Form.

Sin otro particular, quedo.

Cordialmente,

Eli Eida Ortiz Feliciano  
Directora de Finanzas

mip



Estado Libre Asociado de Puerto Rico  
Municipio Autónomo de San Germán

Oficina del Alcalde



RECIBIDO  
UNIDAD DE CORREO  
08 JAN -8 PM 3:41

08 JAN 10 PM 3:20

DIVISION DE PLANEAMIENTO  
E INTERVENCION  
OCAM

Hon. Isidro Negrón Irizarry  
Alcalde

November 30, 2007

Román Toro & Co., CSP  
Certified Public Accountants  
PO Box 3043  
Yauco PR 00698-3043

We are providing this letter in connection with your audit of the financial statements of **Municipality of San German, Puerto Rico as of June 30, 2007** and for the year then ended for the purpose of expressing an opinion as to whether the financial statements present fairly, in all material respects, the financial position of the governmental activities, each mayor fund, and the aggregate remaining fund information of the Municipality of San German, Puerto Rico and the respective changes in financial position thereof in conformity with U.S. generally accepted accounting principles. We confirm that we are responsible for the fair presentation of the previously mentioned financial statements in conformity with U.S. generally accepted accounting principles. We are also responsible for adopting sound accounting policies, establishing and maintaining internal control, and preventing and detecting fraud.

We confirm, to the best of our knowledge and belief, as of November 30, 2007, the following representations made to you during your audit.

1. The financial statements referred to above are fairly presented in conformity with U.S. generally accepted accounting principles and include all properly classified funds and other financial information of the primary government and all component units required by generally accepted accounting principles to be included in the financial reporting entity.
2. We have made available to you all—
  - a. Financial records and related data and all audit or relevant monitoring reports, if any, received from funding sources.
  - b. Minutes of the meetings of Municipal Assembly or summaries of actions of recent meetings for which minutes have not yet been prepared.



"Construyendo un  
Nuevo San Germán"

3. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.
4. There are no material transactions that have not been properly recorded in the accounting records underlying the financial statements or the schedule of expenditures of federal awards.
5. We believe the effects of the uncorrected financial statement misstatements summarized in the attached schedule are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.
6. We acknowledge our responsibility to identify, measure, and assess the risks the Municipality of San German is exposed to. We confirm that we have established, maintained, operated and demonstrated an appropriate framework of internal controls to cover all our operational, technical, financial, compliance, and administrative activities.
7. We have maintained proper accounts and records of all the transactions and affairs of the Municipality of San German and have adequate procedures to ensure all moneys received are properly brought to account, all payments are correctly made and properly authorized, and that adequate control is maintained over public property and other property of or in the custody of the Municipality of San German and over the incurring of liabilities by the Municipality of San German.
8. We acknowledge our responsibility for the design and implementation of programs and controls to prevent and detect fraud.
9. We have no knowledge of any fraud or suspected fraud affecting the entity involving—
  - a. Management
  - b. Employees who have significant roles in internal control, or
  - c. Others where the fraud could have a material effect on the financial statements.
10. We have no knowledge of any allegations of fraud or suspected fraud affecting the entity received in communications from employees, former employees, analysts, regulators, short sellers, or others.

11. The Municipality of San German, Puerto Rico has no plans or intentions that may materially affect the carrying value or classification of assets, liabilities, or equity.
12. The following, if any, have been properly recorded or disclosed in the financial statements:
  - a. Related party transactions, including revenues, expenditures/expenses, loans, transfers, leasing arrangements, and guarantees, and amounts receivable from or payable to related parties.
  - b. Guarantees, whether written or oral, under which the Municipality of San German is contingently liable.
  - c. Other oral transactions that could be material to the financial statements.
  - d. All accounting estimates that could be material to the financial statements, including the key factors and significant assumptions underlying those estimates and measurements. We believe the estimates and measurements are reasonable in the circumstances, consistently applied, and adequately disclosed.
13. We are responsible for compliance with the laws, regulations, and provisions of contracts and grant agreements applicable to us, including tax or debt limits and debt contracts; and we have identified and disclosed to you all laws, regulations and provisions of contracts and grant agreements that we believe have a direct and material effect on the determination of financial statement amounts, or other financial data significant to the audit objectives, including legal and contractual provisions for reporting specific activities in separate funds.
14. There are no—
  - a. Violations or possible violations of budget ordinances, laws and regulations (including those pertaining to adopting, approving, and amending budgets), provisions of contracts and grant agreements, tax or debt limits, and any related debt covenants whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency, or for reporting noncompliance.

- b. Unasserted claims or assessments that our lawyer has advised us are probable of assertion and must be disclosed in accordance with Financial Accounting Standards Board (FASB) Statement No. 5, *Accounting for Contingencies*.
  - c. Other liabilities or gain or loss contingencies that are required to be accrued or disclosed by FASB Statement No. 5.
  - d. Reservations or designation of fund equity those were not properly authorized and approved.
15. As part of your audit, you assisted along with our consultant firm in the preparation of the draft financial statements and related notes, and schedule of expenditures of federal awards. We have designated a competent management-level individual to oversee your services and have made all management decisions and performed all management functions. We have reviewed, approved, and accepted responsibility for those financial statements, the related notes and schedule of expenditures of federal awards.
16. The Municipality of San German, Puerto Rico, has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor has any asset been pledged as collateral.
17. The Municipality of San German, Puerto Rico has complied with all respects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
18. The financial statements properly classify all funds and activities.
19. All funds that meet the quantitative criteria GASB Statement Nos. 34 and 37 for presentation as major are identified and presented as such and all other funds that are presented as major are particularly important to financial statement users.
20. Net balance components (invested in capital assets, net of related debt; restricted and unrestricted) and fund balance reserves and designations are properly classified and, if applicable, approved.
21. Revenues are appropriately classified in the statement of activities within program revenues, general revenues, contributions to term or permanent endowments, or contributions to permanent fund principal.

22. Receivables recorded in the financial statements represent valid claims against debtors for transactions arising on or before the balance sheet date and have been appropriately reduced to their estimated net realizable value.
23. Interfund, internal, and intra-entity activity and balances have been appropriately classified and reported.
24. Capital assets, including infrastructure assets, are properly capitalized, reported, and, if applicable, depreciated. Capital assets have been evaluated for impairment as a result of significant and unexpected decline in service utility, with adjustments, if necessary, properly recorded.
25. Required supplementary information (RSI) is measured and presented within prescribed guidelines.
26. With respect to federal award programs:
  - a. We are responsible for complying and have complied with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.
  - b. We have, in accordance with OMB Circular A-133, identified in the schedule of expenditures of federal awards, expenditures made during the audit period for all awards provided by federal agencies in the form of grants, federal cost-reimbursement contracts, loans, loan guarantees, property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, and other assistance.
  - c. We are responsible for complying with, and have complied in all material aspects, the requirements of laws, regulations, and the provisions of contracts and grant agreements related to each of our federal programs and have identified and disclosed to you the requirements of laws, regulations, and the provisions of contracts and grant agreements that are considered to have a direct and material effect on each major federal program.

- d. We are responsible for establishing and maintaining effective internal control over compliance requirements applicable to federal programs that provide reasonable assurance that we are managing our federal awards in compliance with laws, regulations, and the provisions of contracts and grant agreements that could have a material effect on our federal programs. We believe the internal control system is adequate and is functioning as intended. Also, no changes have been made in internal control over compliance or other factors to the date of this letter that might significantly affect internal control, including any corrective action taken with regard to reportable conditions reported in the schedule of findings and questioned costs.
- e. We have made available to you all contracts and grant agreements (including amendments, if any) and any other correspondence with federal agencies or pass-through entities relating to each major federal program.
- f. We have received no requests from a federal agency to audit one or more specific programs as a major program.
- g. We have complied, in all material respects, with the compliance requirements, including when applicable, those set forth in the *OMB Circular A-133 Compliance Supplement*, relating to federal awards and have identified and disclosed to you all amounts questioned and any known noncompliance with the requirements of federal awards, including those resulting from other audits or program reviews.
- h. Amounts claimed or used for matching were determined in accordance with relevant guidelines in *OMB Circular A-87, Cost Principles for State, Local, and Tribal Governments*, and *OMB's Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*.
- i. We have disclosed to you our interpretation of compliance requirements that may have varying interpretations.
- j. We have made available to you all documentation related to the compliance requirements, including information related to federal program financial reports and claims for advances and reimbursements.

- k. Federal program financial reports and claims for advances and reimbursements are supported by the books and records from which the financial statements have been prepared.
- l. We have charged costs to federal awards in accordance with applicable cost principles.
- m. The copies of federal program financial reports provided you are true copies of the reports submitted, or electronically transmitted, to the respective federal agency or pass-through entity, as applicable.
- n. We have monitored sub recipients to determine that they have expended pass-through assistance in accordance with applicable laws and regulations and have met the requirements of OMB Circular A-133.
- o. We have taken appropriate action, including issuing management decisions, on a timely basis after receipt of sub recipients' auditor's reports that identified noncompliance with laws, regulations, or the provisions of contracts or grant agreements to ensure that sub recipients have taken the appropriate and timely corrective action on findings.
- p. We have considered the results of sub recipient audits and have made any necessary adjustments to our books and records.
- q. We are responsible for and have accurately prepared the summary schedule of prior audit findings to include all findings required to be included by OMB Circular A-133 and we have provided you with all information on the status of the follow-up on prior audit findings by federal awarding agencies and pass-through entities, including all management decisions.
- r. We are responsible for and have accurately prepared the auditee section of the Data Collection Form as required by OMB Circular A-133, and we are responsible for preparing and implementing a corrective action plan for each audit finding.
- s. We have disclosed to you all contracts or other agreements with our service organizations, and we have disclosed to you all communications from the service organizations relating to noncompliance at the service organizations.

Román Toro & Co., CSP  
November 30, 2007  
Page 8

To the best of our knowledge and belief, no events, including instances of noncompliance, have occurred subsequent to the balance sheet date and through the date of this letter that would require adjustment to or disclosure in the aforementioned financial statements or in the schedule of findings and questioned costs.

  
Hon. Isidro Negron Irizarry  
Mayor

  
Eli Eida Ortiz Feliciano  
Finance Director

  
Luis E. Padovani Padilla  
Federal Funds Department Director

FORM SF-SAC (5-2004)

U.S. DEPT. OF COMM. - Econ. and Stat. Admin. - U.S. CENSUS BUREAU ACTING AS COLLECTING AGENT FOR OFFICE OF MANAGEMENT AND BUDGET

### Data Collection Form for Reporting on AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS for Fiscal Year Ending Dates in 2004, 2005, or 2006

Complete this form, as required by OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations."

RETURN TO

Federal Audit Clearinghouse 1201 E. 10th Street Jeffersonville, IN 47132

#### PART I

#### GENERAL INFORMATION (To be completed by auditee, except for Items 4 and 7)

1. Fiscal period ending date for this submission

Month Day Year  
06 / 30 / 2007

Fiscal Period End Dates Must Be in 2004, 2005, or 2006

2. Type of Circular A-133 audit

1  Single audit 2  Program-specific audit

3. Audit period covered

1  Annual 2  Biennial 3  Other -  Months

4. FEDERAL GOVERNMENT USE ONLY

Date received by Federal clearinghouse

#### 5. Auditee Identification Numbers

a. Primary Employer Identification Number (EIN)

66 - 0433531

b. Are multiple EINs covered in this report? 1  Yes 2  No

c. If Part I, Item 5b = "Yes," complete Part I, Item 5c on the continuation sheet on Page 4.

d. Data Universal Numbering System (DUNS) Number

-  -

e. Are multiple DUNS covered in this report? 1  Yes 2  No

f. If Part I, Item 5e = "Yes," complete Part I, Item 5f on the continuation sheet on Page 4.

#### 6. AUDITEE INFORMATION

a. Auditee name

MUNICIPALITY OF SAN GERMAN

b. Auditee address (Number and street)

PO BOX 85

City

SAN GERMAN

State

ZIP + 4 Code

PR

00683 - 0085

c. Auditee contact

Name

HON. ISIDRO NEGRON IRIZARRY

Title

MAYOR

d. Auditee contact telephone

(787) 892 - 3500

e. Auditee contact FAX

(787) 892 - 1114

f. Auditee contact E-mail

g. AUDITEE CERTIFICATION STATEMENT - This is to certify that, to the best of my knowledge and belief, the auditee has: (1) engaged an auditor to perform an audit in accordance with the provisions of OMB Circular A-133 for the period described in Part I, Items 1 and 3; (2) the auditor has completed such audit and presented a signed audit report which states that the audit was conducted in accordance with the provisions of the Circular; and, (3) the information included in Parts I, II, and III of this data collection form is accurate and complete. I declare that the foregoing is true and correct.

Signature of certifying official Date  
Month Day Year

Printed Name of certifying official

MAYOR

Printed Title of certifying official

#### 7. AUDITOR INFORMATION (To be completed by auditor)

a. Auditor name

ROMAN TORO & CO., CSP

b. Auditor address (Number and street)

PO BOX 3043

City

YAUCO

State

ZIP + 4 Code

PR

00698 - 3043

c. Auditor contact

Name

CPA JOSE D. ROMAN

Title

PARTNER

d. Auditor contact telephone

(787) 856 - 6220

e. Auditor contact FAX

(787) 856 - 6233

f. Auditor contact E-mail

CPAJOSEDRT@AOL.COM

g. AUDITOR STATEMENT - The data elements and information included in this form are limited to those prescribed by OMB Circular A-133. The information included in Parts II and III of the form, except for Part III, Items 7, 8, and 9a-9f, was transferred from the auditor's report(s) for the period described in Part I, Items 1 and 3, and is not a substitute for such reports. The auditor has not performed any auditing procedures since the date of the auditor's report(s). A copy of the reporting package required by OMB Circular A-133, which includes the complete auditor's report(s), is available in its entirety from the auditee at the address provided in Part I of this form. As required by OMB Circular A-133, the information in Parts II and III of this form was entered in this form by the auditor based on information included in the reporting package. The auditor has not performed any additional auditing procedures in connection with the completion of this form.

Signature of auditor Date  
Month Day Year

Roman Toro & Co.

12 / 19 / 2007

**PART II**

**FINANCIAL STATEMENTS (To be completed by auditor)**

1. Type of audit report

Mark either:

1  Unqualified opinion **OR**

any combination of: 2  Qualified opinion 3  Adverse opinion 4  Disclaimer of opinion

2. Is a "going concern" explanatory paragraph included in the audit report?

1  Yes 2  No

3. Is a reportable condition disclosed?

1  Yes 2  No - SKIP to Item 5

4. Is any reportable condition reported as a material weakness?

1  Yes 2  No

5. Is a material noncompliance disclosed?

1  Yes 2  No

**PART III**

**FEDERAL PROGRAMS (To be completed by auditor)**

1. Does the auditor's report include a statement that the auditee's financial statements include departments, agencies, or other organizational units expending \$500,000 or more in Federal awards that have separate A-133 audits which are not included in this audit? (AICPA Audit Guide, Chapter 12)

1  Yes 2  No

2. What is the dollar threshold to distinguish Type A and Type B programs? (OMB Circular A-133 § .520(b))

\$ 300,000

3. Did the auditee qualify as a low-risk auditee? (§ .530)

1  Yes 2  No

4. Is a reportable condition disclosed for any major program? (§ .510(a)(1))

1  Yes 2  No - SKIP to Item 6

5. Is any reportable condition reported as a material weakness? (§ .510(a)(1))

1  Yes 2  No

6. Are any known questioned costs reported? (§ .510(a)(3) or (4))

1  Yes 2  No

7. Were Prior Audit Findings related to **direct** funding shown in the Summary Schedule of Prior Audit Findings? (§ .315(b))

1  Yes 2  No

8. Indicate which **Federal** agency(ies) have current year audit findings related to **direct** funding or prior audit findings shown in the Summary Schedule of Prior Audit Findings related to **direct** funding. (Mark (X) all that apply or None)

98  U.S. Agency for International Development

83  Federal Emergency Management Agency

43  National Aeronautics and Space Administration

96  Social Security Administration

10  Agriculture

39  General Services Administration

89  National Archives and Records Administration

19  U.S. Department of State

23  Appalachian Regional Commission

93  Health and Human Services

05  National Endowment for the Arts

20  Transportation

11  Commerce

97  Homeland Security

06  National Endowment for the Humanities

21  Treasury

94  Corporation for National and Community Service

14  Housing and Urban Development

06  National Endowment for the Humanities

82  United States Information Agency

12  Defense

03  Institute of Museum and Library Services

47  National Science Foundation

64  Veterans Affairs

84  Education

15  Interior

07  Office of National Drug Control Policy

00  None

81  Energy

16  Justice

09  Small Business Administration

Other - Specify:

66  Environmental Protection Agency

09  Legal Services Corporation

Each agency identified is required to receive a copy of the reporting package.

In addition, one copy each of the reporting package is required for:

- the Federal Audit Clearinghouse archives
- and, if not marked above, the Federal cognizant agency

Count total number of boxes marked above and submit this number of reporting packages

FORM SF-SAC (5-2004)

**PART III FEDERAL PROGRAMS - Continued**

9. FEDERAL AWARDS EXPENDED DURING FISCAL YEAR							10. AUDIT FINDINGS		
CFDA Number		Research and development	Name of Federal program	Amount expended	Direct award	Major program		Type(s) of compliance requirement(s) <sup>4</sup>	Audit finding reference number(s) <sup>5</sup>
Federal Agency Prefix <sup>1</sup>	Extension <sup>2</sup>					Major program	If yes, type of audit report <sup>3</sup>		
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(a)	(b)
1	4 .218	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	COMMUNITY DEVELOPMENT BLOCK GRANT ENTITLEMENT GRANT	\$ 728,700 .00	1 <input checked="" type="checkbox"/> Yes 2 <input type="checkbox"/> No	1 <input checked="" type="checkbox"/> Yes 2 <input type="checkbox"/> No	U	O	N/A
1	4 .871	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	SECTION 8 HOUSING CHOICE VOUCHERS	\$ 393,821 .00	1 <input checked="" type="checkbox"/> Yes 2 <input type="checkbox"/> No	1 <input checked="" type="checkbox"/> Yes 2 <input type="checkbox"/> No	U	EB	2007-21, 2007-3
1	4 .228	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	COMMUNITY DEVELOPMENT BLOCK GRANT STATES PROGRAM	\$ 152,432 .00	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No		O	N/A
1	6 .738	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	EDWARD BYRNE JUSTICE ASSISTANCE GRANT	\$ 49,893 .00	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No		O	N/A
2	0 .600	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	STATE AND COMMUNITY HIGHWAY SAFETY	\$ 23,296 .00	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No		O	N/A
9	3 .045	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	SPECIAL PROGRAM FOR THE AGING TITLE III PART C-1 AND C-2 GRANTS	\$ 77,212 .00	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No		O	N/A
9	3 .569	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	COMMUNITY SERVICE BLOCK GRANT	\$ 31,754 .00	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No		O	N/A
9	7 .036	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	DISASTER GRANTS-PUBLIC ASSISTANCE	\$ 69,626 .00	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No		O	N/A
9	7 .067	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	HOMELAND SECURITY GRANT PROGRAM (SHSP)	\$ 84,750 .00	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input checked="" type="checkbox"/> No		O	N/A
		1 <input type="checkbox"/> Yes 2 <input type="checkbox"/> No		\$ .00	1 <input type="checkbox"/> Yes 2 <input type="checkbox"/> No	1 <input type="checkbox"/> Yes 2 <input type="checkbox"/> No			
<b>TOTAL FEDERAL AWARDS EXPENDED</b> →				\$ 1,611,484 .00	IF ADDITIONAL LINES ARE NEEDED, PLEASE PHOTOCOPY THIS PAGE, ATTACH ADDITIONAL PAGES TO THE FORM, AND SEE INSTRUCTIONS				

<sup>1</sup> See Appendix 1 of instructions for valid Federal Agency two-digit prefixes.

<sup>2</sup> Or other identifying number when the Catalog of Federal Domestic Assistance (CFDA) number is not available. (See Instructions)

<sup>3</sup> If major program is marked "Yes," enter only one letter (U = Unqualified opinion, Q = Qualified opinion, A = Adverse opinion, D = Disclaimer of opinion) corresponding to the type of audit report in the adjacent box. If major program is marked "No," leave the type of audit report box blank.

<sup>4</sup> Enter the letter(s) of all type(s) of compliance requirement(s) that apply to audit findings (i.e., noncompliance, reportable conditions (including material weaknesses), questioned costs, fraud, and other items reported under § 510(a)) reported for each Federal program.

- |                                    |  |  |                                 |
|------------------------------------|--|--|---------------------------------|
| A. Activities allowed or unallowed | E. Eligibility                             | I. Procurement and suspension and debarment            | L. Reporting                    |
| B. Allowable costs/cost principles | F. Equipment and real property management  | J. Program income                                      | M. Subrecipient monitoring      |
| C. Cash management                 | G. Matching, level of effort, earmarking   | K. Real property acquisition and relocation assistance | N. Special tests and provisions |
| D. Davis - Bacon Act               | H. Period of availability of Federal funds |  | O. None                         |
| <sup>5</sup> N/A for NONE          |  |  | P. Other                        |

**PART I**      **Item 5 Continuation Sheet**

c. List the multiple Employer Identification Numbers (EINs) covered in this report.										f. List the multiple DUNS covered in the report.													
1	N	/	A			21	-			41	-			1	N	/	A			21	-		
2						22	-			42	-			2						22	-		
3						23	-			43	-			3						23	-		
4						24	-			44	-			4						24	-		
5						25	-			45	-			5						25	-		
6						26	-			46	-			6						26	-		
7						27	-			47	-			7						27	-		
8						28	-			48	-			8						28	-		
9						29	-			49	-			9						29	-		
10						30	-			50	-			10						30	-		
11						31	-			51	-			11						31	-		
12						32	-			52	-			12						32	-		
13						33	-			53	-			13						33	-		
14						34	-			54	-			14						34	-		
15						35	-			55	-			15						35	-		
16						36	-			56	-			16						36	-		
17						37	-			57	-			17						37	-		
18						38	-			58	-			18						38	-		
19						39	-			59	-			19						39	-		
20						40	-			60	-			20						40	-		

IF ADDITIONAL LINES ARE NEEDED, PLEASE PHOTOCOPY THIS PAGE, ATTACH ADDITIONAL PAGES TO THE FORM, AND SEE INSTRUCTIONS.