

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

**MUNICIPIO DE SAN GERMAN
AUDITORÍA 2011-2012
30 DE JUNIO DE 2012**



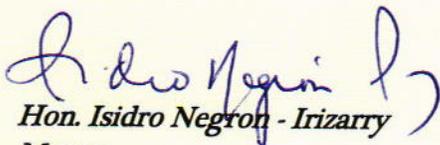
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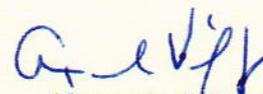
**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN**

***BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY
INFORMATION AND INDEPENDENT
AUDITOR'S REPORT
(WITH ADDITIONAL REPORTS REQUIRED
UNDER THE OMB CIRCULAR A-133)***

***AS OF AND FOR THE FISCAL YEAR ENDED
JUNE 30, 2012***




***Hon. Isidro Negron - Irizarry
Mayor***


***Alexandra Vélez-Lugo, CPA
Finance Director***

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

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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, 2012, 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, 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, 2012, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

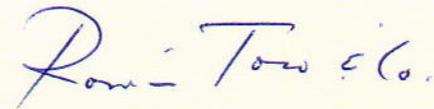
In accordance with *Government Auditing Standards*, we have also issued our report dated March 21, 2013, on our consideration of the Municipality of San Germán, Puerto Rico's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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 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)

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 15 and 53 through 55 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of San Germán, Puerto Rico's financial statements as a whole. The financial data schedule is presented for purpose of additional analysis and is not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget *Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*, and also is not a required part of the financial statements. The financial data schedule and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.



ROMAN TORO & CO., CPA, C.S.P.
LICENSE #35 - IN FORCE

Yauco, Puerto Rico
March 21, 2013

Stamp #E46245 was affixed to
the original of this report



MANAGEMENT'S DISCUSSION AND ANALYSIS

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

As management of the Municipality of San Germán ("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, 2012. 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 2012 by \$42,118,755 (net assets).
- Unrestricted net deficit amounted to \$2,303,610 in comparison with a net deficit of \$3,009,502 on fiscal year 2011, an improvement of 177%.
- Revenues increased by 4% and expenses increased 11% in comparison with fiscal year 2011.
- Net change in net assets amounted to a deficit of \$2,290,534, an increase in deficit of \$2,061,752 with respect to prior fiscal 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, 2012, a net change (increase) of \$3,912,195 in the fund balances of the Municipality's governmental funds resulted in a reported combined ending fund balances of \$10,005,945. Approximately (3%) of the total combined fund balances is unrestricted (committed and unassigned).
- For the fiscal year 2012, the General Fund reported an excess of revenues and other financing sources over expenditures and other financing uses of \$563,160. The unassigned fund balance deficit amounts to \$1,491,962, or 81% increase over 2011 year.

General Financial Highlights

- The investment in capital assets as of June 30, 2012 was \$48,740,306 (net of depreciation).
- Long term debt increased to \$20,299,215
- On a budgetary basis, actual expenditures and other financing uses exceeded actual revenue and other financing uses after readjustment of prior year fund balance by \$561,850.

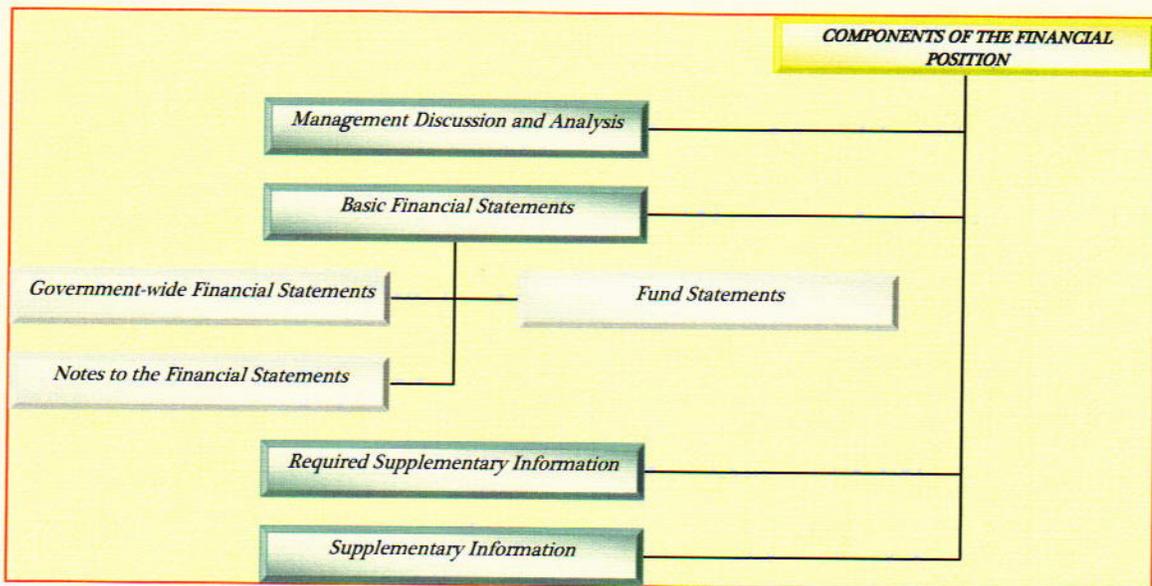
**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

OVERVIEW OF THE FINANCIAL STATEMENTS

The Municipality's basic financial statements comprise four components: (1) management's discussion and analysis (presented here), (2) basic financial statements, and (3) required supplementary information and (4) other 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'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

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'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

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, 2012 and 2011:

TABLE 1

<i>Summary Statement of Net Assets As of June 30,</i>		
	Governmental Activities	
	2012	2011 (as restated)
Assets		
Current and other assets	\$ 18,110,076	\$ 14,066,443
Capital assets	48,740,306	50,596,389
Total assets	\$ 66,850,382	\$ 64,662,832
Liabilities		
Current and other liabilities	\$ 4,432,412	\$ 4,701,374
Long term liabilities	20,299,215	15,552,172
Total liabilities	24,731,627	20,253,546
Net assets		
Invested in capital assets, net of related debt	35,489,707	40,451,372
Restricted	8,932,658	6,967,417
Unrestricted (deficit)	(2,303,610)	(3,009,502)
Total net assets	\$ 42,118,755	\$ 44,409,287

Net assets (assets over liabilities) may serve over time as an indicator of a government's financial position. Net change in net assets amounted to a deficit of \$2,290,534, an increase in deficit of \$2,061,752 with respect to prior fiscal year's net change.

The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g. land, construction in progress, 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'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

As of June 30 2012, the Municipality presented an unrestricted net assets deficit of \$2,303,610. This deficit primarily arises from long term obligations such as compensated absences and a payable to PREPA 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, they are reported as part of the unrestricted net assets section.

Changes in net assets

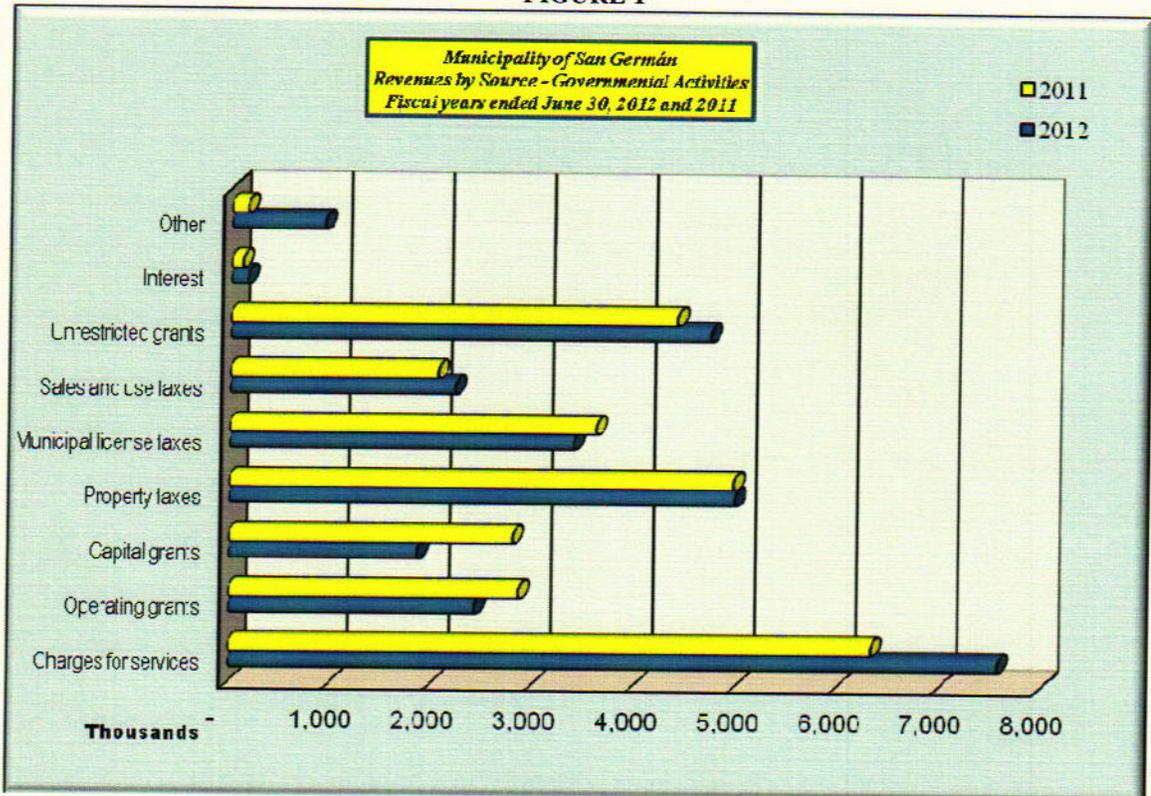
The following table summarizes the changes in net assets for the years ended June 30, 2012 and 2011:

TABLE 2

<i>Summary of Changes in Net Assets As of June 30,</i>		
	Governmental Activities	
	2012	2011 (as restated)
Program revenues:		
Fees, fines and charges for services	\$ 7,572,374	\$ 6,325,088
Operating grants and contributions	2,424,242	2,852,850
Capital grants and contributions	1,861,758	2,792,857
General revenues:		
Property taxes	4,979,469	4,964,373
Municipal license taxes	3,387,703	3,607,937
Sales and use taxes	2,218,124	2,049,431
Grants and contributions not restricted to specific programs	4,726,583	4,398,238
Interest	164,474	111,211
Other and gain on sale and disposition of assets	925,025	160,617
Total revenues	28,259,752	27,262,602
Expenses:		
General government	5,753,318	7,717,295
Public safety	1,553,118	1,575,486
Public works	16,933,179	10,106,706
Sanitation	290,916	2,325,947
Health	786,763	786,763
Welfare	3,500,538	3,086,753
Culture and recreation	544,342	603,021
Education	534,637	813,082
Interest on long term debt	653,473	476,328
Total expenses	30,550,284	27,491,382
Change in net assets	(2,290,532)	(228,780)
Net assets, at beginning of year	44,409,287	44,638,067
Net assets, at end of year	\$ 42,118,755	\$ 44,409,287

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2012**

FIGURE 1



Approximately 27% of the Municipality's revenues came from fees and charges for services, 18% from property taxes, 17% from unrestricted grants and 12% from municipal license taxes. Program revenues of the Municipality covered 39% of total expenses.

With respect to prior year, revenues reported a net increase of approximately 4%. This net increase is primarily the result of: (1) a 20% increase in charges for services due to increase of \$587,953 in construction permits as a result of aggressive collection actions and an increase of \$1,151,278 in compensation in lieu of tax from PREPA; (2) a 48% increase in interest revenue due mainly from interest income from \$3,000,000 loan, (3) a 7% increase unrestricted grants due to increase in revenues for municipal equalization fund received from the Commonwealth of Puerto Rico; (4) increase in other revenues which includes collection of construction permits as a result of investigations and a gain on sale on disposition of capital assets due to an expropriation of a Municipality's parcel of land from the P.R. Highways and Transportation Authority

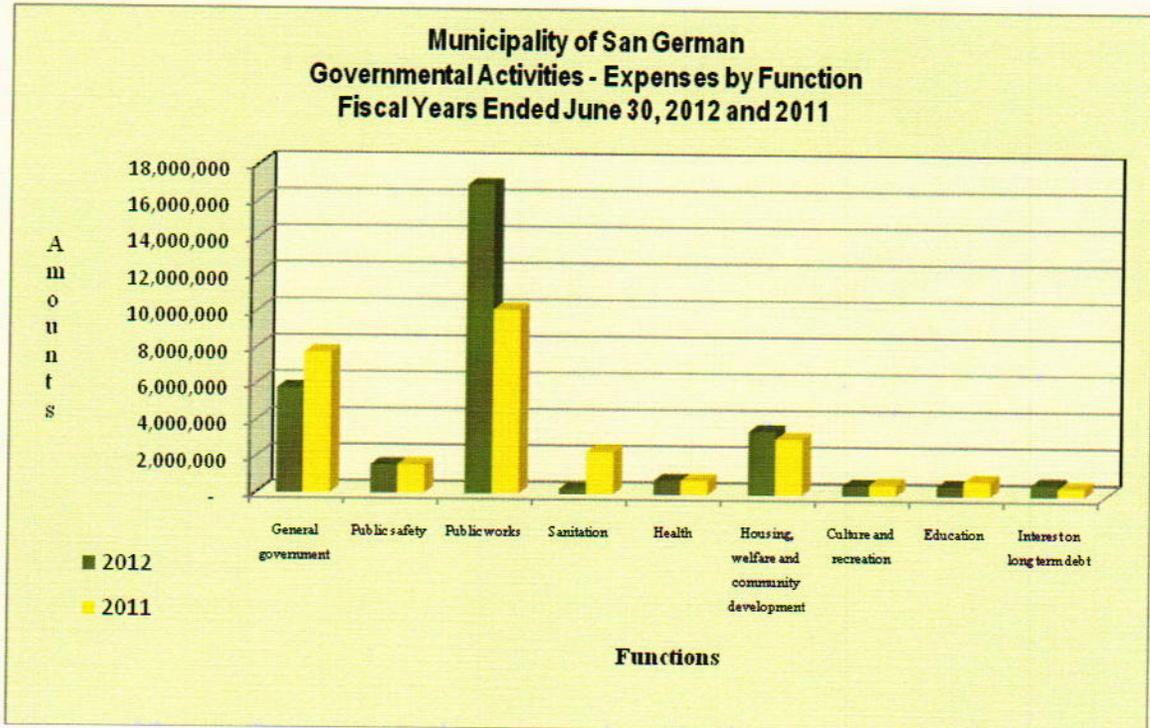
These increases were partially offset by decreases in capital and operating grants of 33% and 15% respectively due to the closing of certain federal grants financed with ARRA funds.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

FIGURE 2



The largest expenses are public works with 55%, general government representing approximately 19% and welfare 11%. Expenses increased 11% in comparison with the 2011 year. This net increase is a combination of an increase of 68% in public works, 37% in interest on long term debt along with a decrease in 87% in sanitation and 34% in education. Increase in public works arises from the recognition of a transfer of an infrastructure project to PRASA (\$3,818,543) and the recognition in this function of solid waste disposition costs and salaries, recorded as part of sanitation function in 2011 year. Increase in interest costs is due to additional bonds and notes issued during fiscal period. The decrease in education is due to a reduction of expenses from ARRA Early Head Start Grant.

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):

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

TABLE 3

<i>Net Cost of Municipality's Governmental Activities Fiscal years ended June 30,</i>				
Functions/Programs	Total Cost of Services		Net Cost of Services	
	2012	2011 (as restated)	2012	2011 (as restated)
General government	\$ 5,753,318	\$ 7,717,295	\$ (3,534,832)	\$ (5,621,161)
Public safety	1,553,118	1,575,486	(1,553,118)	(1,487,908)
Public works	16,933,179	10,106,706	(10,427,590)	(3,791,578)
Sanitation	290,916	2,325,947	(290,916)	(2,325,947)
Health	786,763	786,763	(786,763)	(786,763)
Housing, welfare and community development	3,500,538	3,086,753	(1,035,141)	315,008
Culture and Recreation	544,342	603,021	(484,523)	(540,572)
Education	534,637	813,082	74,446	(805,337)
Interest on Long Term Debt	653,473	476,328	(653,473)	(476,328)
	<u>\$ 30,550,284</u>	<u>\$ 27,491,382</u>	<u>\$ (18,691,910)</u>	<u>\$ (15,520,586)</u>

Some of the cost of governmental activities was paid by those who directly benefited from the programs (\$7,572,374) and other governments and organizations that subsidized certain programs with grants and contributions (\$4,286,000). The remaining was financed with general revenues.

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, unassigned 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, 2012, the governmental funds reported combined ending fund balances of \$10,005,945, a net increase of \$3,912,195 in comparison with the prior year. This increase was caused primarily by a net change in the Surf and Fun Water Park Fund of \$2,947,885 and \$1,052,032 in the other governmental funds due mainly to the net proceeds of long term debt issuance. Of the total combined fund balances, -3% constitutes unrestricted fund balance. The remainder of fund balance is restricted or nonspendable to indicate that is not available for new spending. Unassigned fund balance represents -18% of total fund balance.

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

The general fund is the operating fund of the Municipality. The fund balance of the general fund represents approximately 8% of total ending fund balances. The amount of \$746,171 of the fund balance of the general fund is nonspendable and represents advances provided to other funds, which are expected to be recovered after the next fiscal year. Committed portion of the unrestricted fund balance of the general fund is distributed as follows:

General public works and sanitation	\$ 18,846
Culture and recreation	11,320
Housing, Welfare and Community Development	47,005
Education	12,195
Capital outlays	1,396,277
General Government and other purposes	20,225

For the year ended June 30, 2012, the fund balance of the general fund increased by \$563,160 when compared with the prior year. There was a 6% net increase in revenues due to increases in (1) construction permits revenues, as a result of aggressive collection actions; (2) increase in compensation in lieu of tax from PREPA; (3) increase in municipal equalization fund received from the Commonwealth of Puerto Rico. In addition, the general fund recorded the transfer of \$1,473,466 from the debt service fund and related to excess amounts in CAE and Municipal Redemption Fund (IVU) which were recorded in a special fund as part of the general fund.

There was only a net increase of 8% in the general fund expenditures due to increases in (1) public works due the increase electric power utilities expense and to the recognition in this function of solid waste disposition costs and salaries, recorded as part of sanitation function in 2011 year; (2) capital outlays financed with excess funds transferred from the debt service fund discussed above.

GENERAL FUND BUDGETARY HIGHLIGHTS

The general fund original budget for the fiscal period 2011-2012 presented an increase of 7% 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 \$557,029 mainly in property tax and rent and charges for services functions. The budgetary comparison schedule disclosed a net negative variance of \$1,359,710 with respect to budgeted revenues mainly in unrealized municipal license taxes and charges for services revenues.

A positive variance of \$797,861 between revised budget and actual expenditures was due mainly to a net decrease of \$697,528 in public works with less actual expenditures that budget in electric power utility and solid waste disposition costs.

The budgetary comparison schedule - general fund present a fund balance readjustment of \$118,150. This represents a readjustment of current year budget with prior year's budgetary surpluses, approved by the Municipal Legislature. Actual expenditures and other financing uses exceeded actual revenue and other financing uses after readjustment of prior year fund balance by \$561,850.

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets

At the end of the fiscal year, the Municipality has invested \$48,740,306 (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 4% from the prior year.

TABLE 4

<i>Capital Assets, net As of June 30,</i>		
	Governmental Activities	
	2012	2011 (as restated)
Non-depreciable assets:		
Land	\$ 8,214,353	\$ 7,488,992
Construction in progress	2,301,960	6,179,046
Depreciable assets:		
Buildings and Buildings Improvements	24,374,918	24,036,531
Equipment	3,621,377	3,544,086
Roads	5,487,819	4,429,483
Bridges	4,739,879	4,918,251
Total	\$ 48,740,306	\$ 50,596,389

The Municipality's major capital projects in construction as of June 30, 2012 are:

1. "San German Surf and Fun Water Park," with \$1,205,291 costs incurred as of year-end. Costs incurred in prior years for a total amount of \$1,115,291 of Villa Paraíso ward and related to land improvements and other infrastructure were transferred to this project, which will be financed through general and special obligation bonds and notes.
2. "Sabana Eneas Baseball Park," with \$701,808 costs incurred as of year-end. Project is currently financed through Commonwealth's agencies grants and long-term debt issuance.

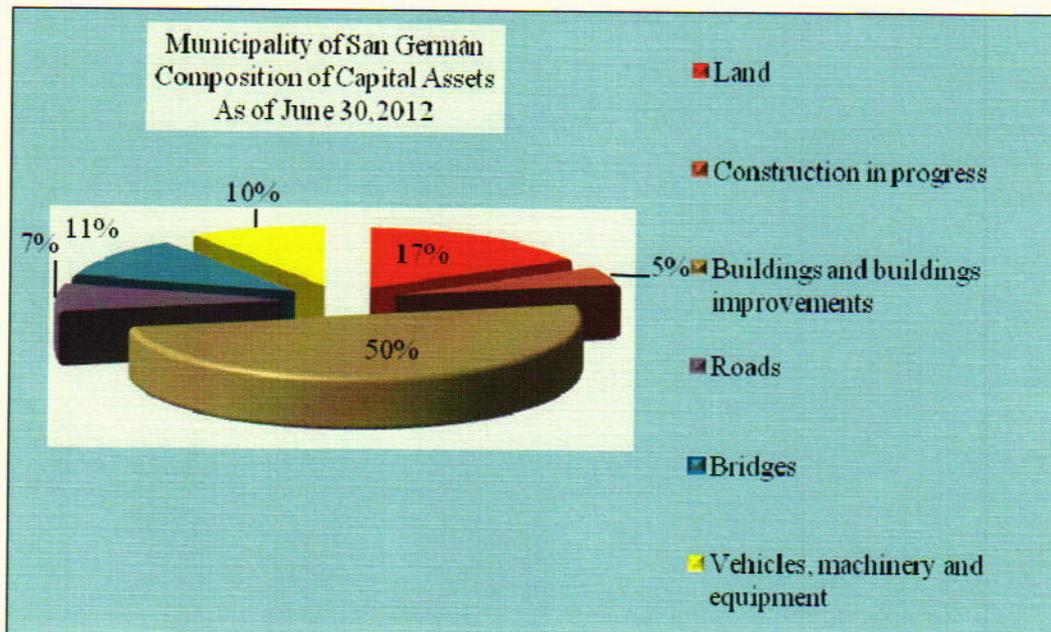
During the year the Municipality completed the improvements to the Early Head Start building for a total cost of \$347,740.

Total capital assets balance reported a net decrease of \$1,856,083. The Municipality entered into agreements with agencies and instrumentalities of the Commonwealth to perform the construction of certain infrastructure projects to be ultimately used by those agencies and instrumentalities in their operations. These capital projects (including land acquired) are funded by the Municipality through grants and/or loans and included as part of the Municipality's capital assets until construction is completed and conditions for transfers to the ultimate beneficiaries are met. At that time, they are recorded as an expense in the statement of activities. During the fiscal year 2011-2012 the Municipality transferred to the Puerto Rico Electric Power Authority (PREPA) an infrastructure project amounting \$3,818,543 after conditions for transfers were met, including an inspection from PREPA's officials.

**COMMONWEALTH OF PUERTO RICO
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MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2012**

Finally, the Municipality acquired equipment amounting to \$613,067, composed mainly of vehicles for \$237,042 of which \$25,000 were donated. The Municipality disposed equipment amounting \$513,723.

Capital assets composition as of June 30, 2012 follows:



More detailed information about the capital assets is presented in Note G to the financial statements.

Long-term debt

At year-end, the Municipality maintains an outstanding balance of \$14,552,000 in general and special bonds and notes, an increase of 45% with respect to prior year. The following is a summary of the Municipality's outstanding debt as of June 30, 2012 and 2011:

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

TABLE 5

<i>Outstanding Long-term Debts As of June 30,</i>		
	Governmental Activities	
	2012	2011
General and special obligation bonds and notes	\$ 14,552,000	\$ 10,033,568
General obligation bond anticipation note	435,968	368,402
Note payable to CRIM – LIMS	-	35,135
Note payable to CRIM – prior years delinquent accounts	96,452	101,275
Compensated absences	3,458,781	3,574,507
Christmas Bonus	312,223	313,742
Claims and judgments	196,377	213,446
Payable to CRIM – property tax advances	-	49,526
Note payable to P.R. Department of Labor	43,367	64,465
Payable to PREPA	1,204,047	798,106
Total	\$ 20,299,215	\$ 15,552,172

During the year 2011-2012 the Municipality entered into loan agreements with the Governmental Development Bank of P.R. ("GDB") which provides for the issuance of general and special obligation bonds and note for the following: \$3,000,000 and \$1,310,000 for the water park construction, \$810,000 for building improvements and \$505,000 for equipment acquisition. In addition, the increase in amount payable to the Puerto Rico Electric Power Authority (PREPA) is the result of an excess of the annual energy charges incurred by the Municipality over the contribution in lieu of taxes ("CELI") for the fiscal year 2010-2011, which was recorded both as a long term debt and a receivable from the agency. More detailed information about the Municipality's long-term liabilities is presented in Note I 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 2011-2012 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 15.2%, which compares with the Commonwealth rate of 13.9%.

The Municipality applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2012-2013 are \$18,984,934, an increase of approximately 7% with respect to prior year estimates. Budgeted expenditures are expected to be reduced accordingly to the decrease 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.

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

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, 2012**

Assets	Governmental Activities
Cash and cash equivalents	\$ 1,838,005
Receivables (net of allowance for uncollectibles) (note C):	
Municipal license taxes	32,160
Sales and use taxes	144,129
Rents and construction permits	1,001,117
Other	21,292
Due From (note D):	
Commonwealth Government	1,929,518
Federal Government	242,474
Restricted Assets:	
Cash and cash equivalents	3,154,546
Cash with fiscal agents	9,687,579
Deferred bond issuance costs, net of accumulated amortization of \$48,748	59,256
Capital assets (note G):	
Land and construction in progress	10,516,313
Other capital assets, net	38,223,993
Total capital assets, net	<u>48,740,306</u>
Total assets	<u>\$ 66,850,382</u>
Liabilities	
Accounts payable and accrued liabilities	\$ 1,924,236
Interest payable	312,747
Due to:	
Commonwealth Government (note D)	177,216
Federal Government	43,698
Deferred revenues	1,974,515
Long term liabilities (note I):	
Due within one year	2,690,884
Due in more than one year	17,608,331
Total liabilities	<u>24,731,627</u>
Net assets	
Invested in capital assets, net of related debt	35,489,707
Restricted for:	
Capital projects	3,704,595
Debt service	3,503,828
Other specified purposes	1,724,235
Unrestricted (deficit)	<u>(2,303,610)</u>
Total net assets	<u>\$ 42,118,755</u>

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, 2012**

<u>Functions</u>	<u>Expenses</u>	<u>Program Revenues</u>			<u>Net (Expenses) Revenues and Changes in Net Assets</u>
		<u>Fees, Fines and Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>	
Governmental activities:					
General government	\$ 5,753,318	\$ 1,954,300	\$ 264,186	\$ -	\$ (3,534,832)
Public safety	1,553,118	-	-	-	(1,553,118)
Public works	16,933,179	4,581,684	62,147	1,861,758	(10,427,590)
Sanitation	290,916	-	-	-	(290,916)
Health	786,763	-	-	-	(786,763)
Welfare	3,500,538	1,036,390	1,429,007	-	(1,035,141)
Culture and recreation	544,342	-	59,819	-	(484,523)
Education	534,637	-	609,083	-	74,446
Interest on long-term debt	653,473	-	-	-	(653,473)
Total government activities	<u>\$ 30,550,284</u>	<u>\$ 7,572,374</u>	<u>\$ 2,424,242</u>	<u>\$ 1,861,758</u>	<u>(18,691,910)</u>
General Revenues:					
Taxes:					
					4,979,469
					3,387,703
					2,218,124
					4,726,583
					164,474
					434,921
					490,104
					<u>16,401,378</u>
					(2,290,532)
					<u>44,409,287</u>
					<u>\$ 42,118,755</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, 2012

	Major Funds				Total Governmental Funds
	General	Debt Service	Surf and Fun Water Park	Other Governmental Funds	
Cash and cash equivalents	\$ 1,838,005	\$ -	\$ -	\$ -	\$ 1,838,005
Receivables (net of allowance for uncollectibles):					
Municipal license taxes	32,160	-	-	-	32,160
Sales and use taxes	144,129	-	-	-	144,129
Rents and construction permits	973,960	-	-	27,157	1,001,117
Other	-	-	14,774	6,518	21,292
Due from:					
Commonwealth Government	1,482,381	60,102	-	387,035	1,929,518
Federal Government	-	-	-	242,474	242,474
Other funds (note E)	945,823	-	35,352	72,457	1,053,632
Advances to other funds (note E)	746,171	-	-	-	746,171
Restricted Assets:					
Cash and cash equivalents	-	-	-	3,154,546	3,154,546
Cash with fiscal agents	-	3,700,144	2,900,969	3,086,466	9,687,579
	<u>\$ 6,162,629</u>	<u>\$ 3,760,246</u>	<u>\$ 2,951,095</u>	<u>\$ 6,976,653</u>	<u>\$ 19,850,623</u>
Liabilities and fund balances					
Liabilities:					
Accounts payable and accrued liabilities	\$ 992,035	\$ -	\$ -	\$ 932,201	\$ 1,924,236
Matured bonds and interest payable	-	1,156,123	-	-	1,156,123
Due to:					
Commonwealth Government	168,853	8,363	-	-	177,216
Federal Government	-	-	-	43,698	43,698
Other funds (note E)	107,809	-	3,210	942,613	1,053,632
Advances from other funds (note E)	-	-	-	746,171	746,171
Deferred revenues (note H)	4,133,855	-	-	609,747	4,743,602
Total liabilities	<u>5,402,552</u>	<u>1,164,486</u>	<u>3,210</u>	<u>3,274,430</u>	<u>9,844,678</u>
Fund balances:					
Nonspendable	746,171	-	-	-	746,171
Restricted	-	2,595,760	2,947,885	4,031,088	9,574,732
Committed	1,505,868	-	-	-	1,505,868
Unassigned	(1,491,962)	-	-	(328,865)	(1,820,826)
Total fund balances	<u>760,077</u>	<u>2,595,760</u>	<u>2,947,885</u>	<u>3,702,223</u>	<u>10,005,945</u>
Total liabilities and fund balances	<u>\$ 6,162,629</u>	<u>\$ 3,760,246</u>	<u>\$ 2,951,095</u>	<u>\$ 6,976,653</u>	<u>\$ 19,850,623</u>

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

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

**RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET ASSETS
JUNE 30, 2012**

Total governmental fund balances:		\$ 10,005,945
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:		48,740,306
Other assets used in governmental activities are not financial resources and, therefore, are not reported in the funds:		
Deferred charges-bond issue costs		59,256
Other assets are not available to pay for current period expenditures and, therefore, are deferred in the funds:		
Receivables:		
CRIM - Intergovernmental (General Fund)	\$ 104,096	
Municipal license taxes	11,167	
Construction permits	186,579	
Rent - properties	44,060	
Rent - land lots	613,761	
P.R. Department of Family Law No. 105	16,459	
P.R. Department of Labor- Law No. 52 and No. 82	89,900	
P.R. Department of Treasury - Christmas bonus reimbursement	145,018	
P.R. Electric Power Authority (PREPA)	1,204,048	
P.R. Office of Ombudsman for the Elderly	5,171	
P.R. Permanent Improvement Funds-Law 2212	41,492	
OCAM - Public Order Code	40,039	
OCAM - Public Order Code	224,543	
Federal Grants - CDBG	19,625	
Federal Grants - Public Housing Capital Fund	393	
Federal Grants - ESG	4,001	
Federal Grant - State and Community Highway Safety	18,735	2,769,087
Interest liabilities are not due and payable in the current period and, therefore, are not reported in the funds:		(136,624)
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	(13,572,000)	
Compensated absences	(3,458,781)	
Claims and judgments	(196,377)	
Note payable to CRIM - delinquent accounts	(96,452)	
Payable to PREPA	(1,204,047)	
Christmas bonus	(312,223)	
Note payable to P.R. Department of Labor and Human Resources	(43,367)	
General obligation bond anticipation note	(435,968)	(19,319,215)
Net assets of governmental activities		<u>\$ 42,118,755</u>

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, 2012

	Major Funds			Other Governmental Funds	Total Governmental Funds
	General	Debt Service	Surf and Fun Water Park		
Revenues:					
Taxes:					
Property taxes (note J)	\$ 2,940,114	\$ 1,990,978	\$ -	\$ -	\$ 4,931,092
Municipal license taxes	3,480,466	-	-	-	3,480,466
Sales and use taxes	1,788,090	430,034	-	-	2,218,124
Intergovernmental:					
Commonwealth Government (note K)	4,727,288	-	-	992,688	5,719,976
Federal Government	-	-	-	3,255,507	3,255,507
Rental income and charges for services	5,916,833	-	-	1,133,240	7,050,073
Fines and forfeitures	17,727	-	-	-	17,727
Interest	94,727	3,736	50,127	15,884	164,474
Other	251,831	-	-	202,007	453,838
Total Revenues	19,217,076	2,424,748	50,127	5,599,326	27,291,277
Expenditures:					
Current:					
General government	5,834,982	-	-	226,005	6,060,987
Public safety	1,429,968	-	-	31,655	1,461,623
Public works	9,085,751	-	-	942,018	10,027,769
Sanitation	215,682	-	-	11,239	226,921
Health	786,763	-	-	-	786,763
Welfare	626,849	-	-	2,839,629	3,466,478
Culture and recreation	488,007	-	-	43,076	531,083
Education	7,982	-	-	526,295	534,277
Capital outlays	572,798	-	90,000	3,244,640	3,907,438
Debt service:					
Principal	-	1,148,000	-	-	1,148,000
Interest	-	454,164	-	-	454,164
Bond issuance costs	-	-	12,242	13,723	25,965
Total expenditures	19,048,782	1,602,164	102,242	7,878,280	28,631,468
Excess (deficiency) of revenues over expenditures	168,294	822,584	(52,115)	(2,278,954)	(1,340,191)
Other financing sources (uses):					
Proceeds from long term debt issuance	-	-	3,000,000	2,625,000	5,625,000
Proceeds from bond anticipation note issuance	-	-	-	67,566	67,566
Proceeds from disposition of capital assets	-	-	-	602,350	602,350
Payment of long-term debt - PREPA	(1,042,530)	-	-	-	(1,042,530)
Transfers - in	1,615,363	-	-	177,967	1,793,330
Transfers - (out)	(177,967)	(1,473,466)	-	(141,897)	(1,793,330)
Total other financing sources (uses)	394,866	(1,473,466)	3,000,000	3,330,986	5,252,386
Net change in fund balances (deficit)	563,160	(650,882)	2,947,885	1,052,032	3,912,195
Fund balance at beginning of year - as restated (note P)	196,917	3,246,642	-	2,650,191	6,093,750
Fund balance at end of year	760,077	\$ 2,595,760	\$ 2,947,885	\$ 3,702,223	\$ 10,005,945

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

**COMMONWELATH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN**

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
IN FUND BALANCES (DEFICIT) - GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FISCAL YEAR ENDED JUNE 30, 2012**

Net change in fund balances - total governmental funds		\$ 3,912,195
Amounts reported for governmental activities in the Statement of Activities are different because:		
Governmental funds reports capital assets outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense:		
Expenditures for capital assets:	\$ 3,907,438	
Less: current year depreciation	<u>(1,883,953)</u>	2,023,485
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:		
		(172,247)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the funds:		
CRIM - Property taxes (General Fund)	104,096	
Construction permits	186,579	
P.R. Department of Treasury - Law No. 52	21,304	
P.R. Department of Treasury - Christmas bonus reimbursement	145,018	
P.R. Electric Power Authority (PREPA)	965,648	
P.R. Office of Ombudsman for the Elderly	5,171	
P.R. Permanent Improvement Funds-Law 2212	41,492	
OCAM - Public Order Code (current year)	40,039	
OCAM - Public Order Code	790	
Federal Grants - Public Housing Capital Fund	393	
Federal Grants - CDBG	19,625	
Federal Grants - HPG	4,001	
Federal Grant - State and Community Highway Safety	18,735	
Donated capital assets	<u>111,222</u>	1,664,113
Revenues reported in funds which are not reported as revenues in the Statement of Activities:		
CRIM - Property taxes (General Fund) (prior year)	(55,719)	
Rent	(13,548)	
Municipal license tax (net change)	(92,762)	
P.R. Electric Power Authority (PREPA) (prior year)	(559,706)	
Construction permits	(20,200)	
Rent- land lots	(84,446)	
P.R. Department of Treasury - Christmas bonus reimbursement (prior year)	(145,723)	
P.R. Department of Treasury - Law No. 52	(28,350)	
Federal Grants - CDBG	(24,371)	
Federal Grants - HOPWA	(10,305)	
Federal Grants - EEC - ARRA	(4,022)	
Federal Grants - ESG	(4,001)	
Federal Grants - HPG	(10,595)	
Federal Grant - State and Community Highway Safety	(66,117)	
Federal Grants - Public Housing Capital Fund (prior year)	<u>(32,613)</u>	(1,152,478)
Expenditures reported in funds which are not reported as expenses in the Statement of Activities:		
Matured bonds principal payments (net change)		42,000
Proceeds from general obligation bonds is an other financing source in the governmental funds, but increase long-term liabilities in the Statement of Net Assets:		
		(5,625,000)
Proceeds from other long term debt is an other financing source in the governmental funds, but increase long-term liabilities in the Statement of Net Assets:		
		(67,566)
Repayment of long-term debt consumes the current financial resources of governmental funds, but has no effect on net assets of governmental activities:		
General obligation bonds and notes	1,106,568	
Other long term liabilities	<u>1,551,524</u>	2,658,092
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:		
Bond issuance costs	25,965	
Amortization of bond issuance costs	<u>(6,411)</u>	19,554
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:		
Transfer of capital asset to PREPA	(3,818,543)	
Claims and judgments	(47,931)	
Accrued interest (net change)	(61,568)	
Compensated absences	(216,167)	
P.R. Electric Power Authority (PREPA)	<u>(1,448,471)</u>	(5,592,680)
Change in net assets of governmental activities		<u>\$ (2,290,532)</u>

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

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

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of San Germán (“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

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 the Management's 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's Discussion and Analysis

This consists of a narrative introduction and analytical overview of the Municipality's financial activities. This analysis is similar to the 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

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 non-exchange 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-driven 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

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, liabilities, revenues or expenditures or based on the Municipality's official's criteria, if the fund is particularly important to financial statement users (for Commonwealth Legislature Resolutions and Permanent Capital Improvement Funds).

The Municipality reports the following major governmental funds:

General Fund: This is the operating fund of the Municipality and is used to account for and report all financial resources not accounted for and reported in another fund.

Debt Service Fund: This fund is used to account for and report financial resources that are restricted, committed, or assigned to expenditures for principal and interest.

Surf and Fun Water Fund: This fund is used to account for and report financial resources that are restricted, committed, or assigned for the construction of a water park.

The governmental funds reported in the fund financial statements 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.

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.

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

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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 in the governmental funds statements deferred revenues 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 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, a 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.

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.

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

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

3. *Deposits and investments*

Cash and cash equivalents consist of cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition. Nonnegotiable certificates of deposits with original maturity of more than three months are considered time deposits as required by current standards. 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 (including Commonwealth Legislature Resolutions) are restricted since their use is limited by applicable agreements or required by law.

The laws and regulations of the Commonwealth of Puerto Rico authorize the Municipality to invest only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by the Governmental Development Bank for Puerto Rico ("GDB").

4. *Restricted assets*

Restricted assets are liquid assets which have third-party limitations on their use. Cash and cash equivalents related to Commonwealth and Federal grants (including Commonwealth Legislature Resolutions) 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 and sales 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 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.

5. *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 and sales tax revenues of current fiscal year collected by the CRIM (property tax) and the Puerto Rico Department of Treasury (sales tax) on the subsequent fiscal year.

6. *Interfund receivables and payables*

Activity among 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 among funds are reported as "due from/to other funds".

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

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

7. 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.

8. 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.

9. Capital assets

Capital assets reported in the governmental activities in the Statements of Net Assets include property, plant, equipment and infrastructure, (e.g., roads, bridges, sidewalks, and similar items). The Municipality defines capital assets (except for infrastructure assets) as assets that have an individual cost of \$100 or more and have a useful life of one or more years. Infrastructure assets are capitalized based on a percentage of the estimated useful life. The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

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.

All capital assets, other than land and construction in progress, 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 a prominent event or change in circumstances affecting the asset. Current standards provide guidance for accounting and reporting for impairment and for insurance recoveries.

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

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

10. 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.

11. 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.

12. Fund balances and Net Assets

GASB Statement No. 54 Fund Balance Reporting and Governmental Fund Type Definitions ("GASB No. 54") establish accounting and reporting standards for all governments that report governmental funds. It also establishes criteria for classifying fund balances into specifically defined classifications and clarifies definitions for governmental fund types. These classifications comprise a hierarchy based primarily on the extent to which the Municipality is bound to observe constraints upon the use of the resources reported. As a result of the implementation certain special funds were reclassified from special revenue and capital project funds to the general fund. The classifications are as follows:

Nonspendable: Amounts that cannot be spent because are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN
NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

- Restricted: Amounts constrained by external parties (creditors, grantors, contributors, or laws and regulations of other governments), imposed by law through constitutional provisions or by enabling legislation. Enabling legislation authorizes the Municipality to assess, levy, charge or otherwise mandate payment or resources (from external resource providers) and includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation. Legally enforceability means that the Municipality can be compelled by an external party such as citizens, public interest groups, or the judiciary to use resources created by enabling legislation only for the purposes specified by the legislation.
- Committed: Amounts that can be used only for the specific purposes imposed through formal action (ordinance or resolution) by consent of both the Mayor and the Municipal Legislature, the highest level of decision-making authority for the Municipality. Those committed amounts cannot be used for any other purposes unless the highest level of decision-making authority for the Municipality removes or changes the specified use by taking the same type of action (ordinance or resolution) it employed to commit those amounts. Formal action to commits fund balance to a specific purpose should occur prior to the end of the fiscal year, but the amount, if any, which will be subject to the constraint, may be determined in the subsequent period.
- Assigned: Amounts intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed. Intent can be expressed by the Mayor or the Finance Director, the official to which the Mayor has also delegated the authority to assign amounts. With the exception of the general fund, this is the residual fund balance of the classification of all governmental funds with positive fund balances. Action taken to assign fund balance may be made after year-end.
- Unassigned: Is the residual classification for the general fund and includes all spendable amounts not restricted, committed or assigned. The general fund is the only fund that reports a positive unassigned fund balance amount. For all other governmental funds the unassigned classification is used only to report a deficit balance resulting for the overspending for specific purposes for which amounts had been restricted, committed or assigned.

The Municipality applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned and unassigned) amounts are available. Similarly, within unrestricted fund balance, committed amounts are reduced first followed by assigned and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used.

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

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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

Invested in capital assets, net of related debt:	Consist 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:	Represent 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.
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.

13. *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.

14. *Risk financing*

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

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

NOTES TO FINANCIAL STATEMENTS

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

15. 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.

16. Future adoption of accounting pronouncements Financial Statements June 30, 2012

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>
60 Accounting and Financial Reporting for Service Concession Arrangements	June 30, 2013
61 The Financial Reporting Entity; Omnibus-an amendment of GASB Statement No. 14 and No. 34	June 30, 2013
62 Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements	June 30, 2013
63 Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position	June 30, 2013
65 Items Previously Reported as Assets and Liabilities	June 30, 2014
66 Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62	June 30, 2014
67 Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25	June 30, 2014
68 Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27	June 30, 2015

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

NOTE B- 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 of deposits in commercial banks amounting to \$3,718,556 was covered by federal depository insurance or by collateral held by the Secretary of Treasury of Puerto Rico in the Municipality's name. 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 \$3,916,713.

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, 2012 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, 2012 follows:

<u>Description</u>	<u>Amount</u>
Total municipal license tax receivable:	\$ 577,019
Less: allowance for uncollectibles	(544,859)
	<u>\$ 32,160</u>

As required by current standards, \$32,160 of the \$11,165 net balance is recorded as deferred revenue since there were not collected within the availability period.

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 in advance, which totals \$1,825,128 is recorded as deferred revenue as of June 30.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN
NOTES TO FINANCIAL STATEMENTS

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. On July 29, 2007 the Commonwealth Legislature approved Act No. 80 (“Act 80”) which amend Act No. 117 of July 4, 2006 to impose 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% is collected by the Municipalities and the remaining .5% of the 1.5% is collected by the Puerto Rico Department of Treasury (PRDT). Act 80 also provides for restrictions on the use of the sales tax, which is required be invested in solid waste and recycling programs, capital improvements and health and public safety costs. Amount collected by the PRDT (the remaining .5% of the 1.5%) is deposited in accounts or special funds in the Governmental Development Bank for 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 a Municipal Ordinance to conform to dispositions of Act 80.

Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the Municipality. The tax is due the 10th day of each month based on tax collected in the preceding month. Municipal sales and use tax receivable of \$144,129 represents the tax collected on June by individuals, organizations and entities but reported and paid to the Municipality on or before July 10, net of uncollectible accounts; \$19,018 and \$60,102 represents amounts of “Municipal Development Fund” and “Municipal Redemption Fund” respectively represents the tax collected on June by individuals, organizations and entities but paid by the PRDT subsequent to June 30.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN
NOTES TO FINANCIAL STATEMENTS**

NOTE C – RECEIVABLES - Continued

3. Rents and construction permits

A detail of rents and construction permits' receivable as of June 30, 2012 follows:

<u>Description</u>	<u>Amount</u>
Rent-land lots	\$ 767,689
Rent-properties	231,789
Construction permits	224,732
Other	33,043
	<u>1,257,253</u>
Less: allowance for uncollectibles	(256,133)
	<u>\$ 1,001,120</u>

Of the total amount of \$1,001,120 the Municipality recorded \$844,401 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, 2012 follows:

	<u>Commonwealth Government</u>	<u>Federal Government</u>
<u>Major fund - General fund:</u>		
P.R. Electric Power Authority (PREPA)	\$ 1,204,048	\$ -
P.R. Department of Treasury – Christmas bonus reimbursement	145,018	-
Municipal Revenue Collection Center (CRIM) – intergovernmental subsidy (general fund)	104,096	-
P.R. Department of Treasury – sales and use taxes – Municipal Development fund	19,018	-
Solid Waste Authority	10,200	-
<u>Major fund – Debt service fund:</u>		
P.R. Department of Treasury – sales and use taxes-Municipal Redemption Fund	60,102	-
<u>Other governmental funds:</u>		
P.R. Department of Labor – Laws No. 52, No. 105, No. 82	106,358	-
P.R. Department of Treasury – Law No. 2212	41,492	-
P.R. Office of the Ombudsman for the Elderly (OPEA)	14,638	-
U.S. Department of Housing and Urban Development – CDBG	-	149,981
P.R. Public Housing Administration (PRPHA) – Low Rent and Capital Fund Programs	-	33,334
P.R. Department of Health – HOPWA	-	11,211
U.S. Department of Health and Human Services – Early Head Start	-	15,114
Others	224,548	32,833
	<u>\$ 1,929,518</u>	<u>\$ 242,473</u>

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

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

NOTES TO FINANCIAL STATEMENTS

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

2. *Amounts due to governmental entities as of June 30, 2012 follows:*

<u>Description</u>	<u>Commonwealth Government</u>
<u>General Fund:</u>	
P.R. Employees Retirement System (ERS)	\$ 98,207
P.R. Department of Labor – unemployment	18,137
P.R. Aqueduct and Sewer Authority (PRASA)	25,698
P.R. State Insurance Fund (FSE)	8,218
Others	18,593
<u>Major fund – Debt service fund:</u>	
Municipal Revenue Collection Center (CRIM) – property taxes	8,363
	<u>\$ 177,216</u>

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:	<u>Major fund:</u>	
	Surf & Water Park	\$ 3,210
	<u>Other governmental funds:</u>	
	Law No. 52	105,460
	Public and Indian Housing	34,577
	Improvements to Villa Auxerre	
	Basketball Court (EMP \$1,585,000)	95,678
	Early Head Start	27,363
	CDBG	26,551
	HOPWA	20,160
	Public Order Code	223,032
	DTOP	134,958
	Others	274,834
		<u>945,823</u>
Surf & Water Park:	<u>Major fund:</u>	
	General Fund	<u>35,352</u>
Other governmental funds:	<u>Major fund:</u>	
\$1,695,000 Bond issuance	General Fund	\$ 20,873
\$2,100,000 Bond issuance	General Fund	5,546
\$1,310,000 Bond issuance	General Fund	7,607
Early Head Start	General Fund	2,259
AFI	General Fund	36,172
		<u>72,457</u>
TOTAL		<u>\$ 1,053,632</u>

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

NOTES TO FINANCIAL STATEMENTS

NOTE E - INTERFUND TRANSACTIONS - Continued

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:

Receivable Fund	Payable Fund	Amount
General Fund	<u>Other governmental funds:</u>	
	P.R. Department of Transportation	\$ 463,552
	\$3,500,000 Loan Fund	51,141
	\$1,695,000 Loan Fund	19,391
	Special Communities Fund	25,061
	Rural Development Fund	30,994
	Others	156,032
		<u>\$ 746,171</u>

3. Transfers in (out):

Transfers among individual funds were made for operational purposes. Transfers include (1) interest earned on restricted cash with fiscal agent in the debt service fund and operating and capital improvement loans in other governmental funds which are transferred to the general fund (2) interest in Commonwealth Legislature Resolutions funds which is transferred to the general fund and, (3) principal and interest payments of long-term debt transferred from the general fund to the debt service fund.

NOTE F- FUND BALANCE

1. Fund balance classifications

The governmental fund balance classifications and amounts at June 30, 2012 are shown in the following table:

	<u>General Fund</u>	<u>Debt Service</u>	<u>Surf and Fun Water Park</u>	<u>Other Governmental Funds</u>	<u>Total</u>
<u>Nonspendable:</u>					
Advances to other funds	\$ 746,171	\$ -	\$ -	\$ -	\$ 746,171
	<u>746,171</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>746,171</u>
<u>Restricted:</u>					
Public safety	-	-	-	-	-
Housing, Welfare and Community Development	-	-	-	1,004,105	1,004,105
Debt Service	-	2,595,760	-	-	2,595,760
Capital outlays	-	-	2,947,886	3,026,693	5,974,578
General Government and other purposes	-	-	-	290	290
	<u>-</u>	<u>2,595,760</u>	<u>2,947,886</u>	<u>4,031,088</u>	<u>9,574,733</u>

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

NOTES TO FINANCIAL STATEMENTS

NOTE F- FUND BALANCE - Continued

	General Fund	Debt Service	Surf & Water Park	Other Governmental Funds	Total
<u>Committed:</u>					
General public works and sanitation	18,846	-	-	-	18,846
Culture and recreation	11,320	-	-	-	11,320
Housing, Welfare and Community Development	47,005	-	-	-	47,005
Education	12,195	-	-	-	12,195
Capital outlays	1,396,277	-	-	-	1,396,277
General Government and other purposes	20,225	-	-	-	20,225
	<u>1,505,868</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,505,868</u>
<u>Unassigned</u>	<u>(1,491,962)</u>	<u>-</u>	<u>-</u>	<u>(328,865)</u>	<u>(1,820,827)</u>
	<u>\$ 760,077</u>	<u>\$ 2,595,760</u>	<u>\$ 2,947,885</u>	<u>\$ 3,702,223</u>	<u>\$ 10,005,945</u>

2. Fund balance deficits

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

Funds	Fund balance - unassigned amount
Law No. 52	\$ 82,705
CDBG	49,778
Law No. 2212 Fund	41,492
Traffic Safety Commission	37,715
City Hall Storm Shutter- "FEMA"	21,316
EPA Brownfields Fund	19,167
Law No. 105	16,577
HSG- Homeland Security	8,184
Others	51,931
	<u>\$ 328,865</u>

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

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

NOTES TO FINANCIAL STATEMENTS

NOTE G - CAPITAL ASSETS

Capital assets and depreciation activity as of and for the year ended June 30, 2012 is as follows:

	<u>Beginning balance July 1, 2011 (as restated)</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending balance June 30, 2012</u>
<u>Governmental activities:</u>				
Capital assets, not being depreciated:				
Land	\$ 7,488,992	\$ 789,811	\$ 64,450	\$ 8,214,353
Construction in progress	6,179,046	920,152	4,797,238	2,301,960
Total capital assets not being depreciated:	13,668,038	1,709,963	4,861,688	10,516,313
Capital assets, being depreciated:				
Buildings and improvements	32,826,730	1,161,375	-	33,988,105
Equipment	10,390,735	587,067	513,723	10,464,079
Roads	13,443,487	1,538,952	179,194	14,803,245
Bridges	7,192,256	-	-	7,192,256
Total capital assets being depreciated	63,853,208	3,287,394	692,917	66,447,685
Less accumulated depreciation for:				
Buildings and improvements	8,790,199	822,988	-	9,613,187
Equipment	6,846,649	416,234	420,181	6,842,702
Roads	9,014,004	466,359	164,937	9,315,426
Bridges	2,274,005	178,372	-	2,452,377
Total accumulated depreciation	26,924,857	1,883,953	585,118	28,223,692
Total capital assets being depreciated, net	36,928,351	1,403,441	107,799	38,223,993
Governmental activities capital assets, net	<u>\$ 50,596,389</u>	<u>\$ 3,113,404</u>	<u>\$ 4,969,487</u>	<u>\$ 48,740,306</u>

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

Governmental activities:

General government	\$ 69,124
Public safety	64,759
Public works	1,652,344
Sanitation	63,995
Culture and recreation	13,258
Welfare	20,473
Total depreciation expense, governmental activities	<u>\$ 1,883,953</u>

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

NOTES TO FINANCIAL STATEMENTS

The Municipality entered into agreements with agencies and instrumentalities of the Commonwealth to perform the construction of certain infrastructure projects to be ultimately used by those agencies and instrumentalities in their operations. These capital projects (including land acquired) are funded by the Municipality through grants and/or loans and included as part of the Municipality's capital assets until construction is completed and conditions for transfers to the ultimate beneficiaries are met. At that time, they are recorded as an expense in the statement of activities.

During the fiscal year 2011-2012 the Municipality transferred to the Puerto Rico Electric Power Authority (PREPA) an infrastructure project amounting \$3,818,543 after conditions for transfers were met, including an inspection from PREPA's officials. Total project cost transferred was recorded as public works expense in the statement of activities.

NOTE H - DEFERRED REVENUES – GOVERNMENTAL FUNDS

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

	General fund	Other Governmental Funds
<u>Major fund - General fund:</u>		
Municipal license taxes – cash received in advance	\$ 1,825,128	\$ -
Municipal license taxes – receivable	11,165	-
Rents and construction permits	844,401	-
P.R. Electric Power Authority (PREPA)	1,204,047	-
P.R. Department of Treasury – Christmas bonus reimbursement	145,018	-
Municipal Revenue Collection Center (CRIM) – property taxes	104,096	-
<u>Other governmental funds:</u>		
P.R. Department of Labor – Law No. 52, 82 and 105	-	106,358
P.R. Traffic Safety Commission	-	18,785
Rural Development – Guama Sanitary Sewer System	-	101,659
P.R. Department of Treasury – Law No. 2212	-	41,492
U.S. Department of Housing and Urban Development – CDBG	-	59,665
U.S. Department of Housing and Urban Development – ARRA - Homeless Prevention and Rapid Re-Housing	-	11,157
Others	-	270,631
	\$ 4,133,855	\$ 609,747

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

NOTES TO FINANCIAL STATEMENTS

NOTE I – 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, 2012:

	<u>Balance at July 1, 2011</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at June 30, 2012</u>	<u>Due within one year</u>
General, Special Obligations Bonds and Notes	\$ 10,033,568	\$ 5,625,000	\$ 1,106,568	\$ 14,552,000	\$ 1,111,000
General obligation bond anticipation note	368,402	67,566	-	435,968	-
Note payable to CRIM-LIMS	35,135	-	35,135	-	-
Note payable to CRIM-financing of delinquent accounts	101,275	-	4,823	96,452	4,823
Note payable to P.R. Department of Labor	64,465	-	21,098	43,367	21,098
Compensated absences	3,574,507	216,167	331,893	3,458,781	324,139
Christmas Bonus	313,742	312,223	313,742	312,223	312,223
Claims and judgments	213,446	47,931	65,000	196,377	196,377
Payable to PREPA	798,106	1,448,471	1,042,530	1,204,047	721,224
Payable to CRIM-property tax advances	49,526	-	49,526	-	-
	<u>\$ 15,552,172</u>	<u>\$ 7,717,358</u>	<u>\$ 2,970,315</u>	<u>\$ 20,299,215</u>	<u>\$ 2,690,884</u>

2. General and special obligation bonds and notes payable

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2012 amount to \$14,552,000. All these bonds are serviced by the Governmental Development Bank for Puerto Rico (GDB) maturing at various dates. As required by law, the Commonwealth Government is obligated to collect property taxes for payment of principal and interest on bonds and notes. In addition, .2% of the .5% municipal sales and use tax collected by the P.R. Department of Treasury is deposited in a "Municipal Redemption Fund" to finance loans to Municipalities subject to restrictions imposed by law.

Debt service funds has been established for the bonds and notes at GDB with the proceeds of those property and sales and use taxes ("IVU"), 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 special obligation notes of \$996,000 and \$505,000 and special obligation bond of \$810,000 are made through the Municipal Redemption Fund (IVU). Principal and interest payments of \$1,310,000 and \$3,000,000 Rental Bonds will be financed with project's revenues or Municipality's operating revenues.

A detail of the general and special obligation bonds and notes as of June 30, 2012 follows:

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

NOTES TO FINANCIAL STATEMENTS

NOTE I - LONG-TERM DEBT - Continued

	<u>Outstanding Amount</u>
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 6.13%	\$ 32,000
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% (6.28% at June 30, 2012)	1,180,000
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% (4.50% at June 30, 2012)	455,000
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% (4.50% at June 30, 2012)	80,000
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% (4.50% at June 30, 2012)	665,000
2003 general obligation bonds of \$320,000 due in annual installments ranging from \$9,000 to \$22,000 through January 1, 2030; bearing interest at 4.25%	282,000
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% (4.73% at June 30, 2012)	290,000
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%	2,548,000
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 5.33% (4.75% at June 30, 2012)	285,000
2008 special obligation bond of \$780,000 due in annual installments ranging from \$50,000 to \$105,000 through July 1, 2018; bearing interest at rates ranging from 1.53% to 7.50% (7.50% at June 30, 2012)	605,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN
NOTES TO FINANCIAL STATEMENTS**

NOTE I - LONG-TERM DEBT – Continued

	Outstanding Amount
2008 special obligation note of \$996,000 due in annual installments ranging from \$16,000 to \$86,000 through July 1, 2032; bearing interest at rates ranging from 1.53% to 7.50% (7.50% at June 30, 2012)	945,000
2010 general obligation bonds of \$1,585,000 due in annual installments ranging from \$25,000 to \$130,000 through July 1, 2035; bearing interest at rates ranging from 6% to 7.50% (6% at June 30, 2012)	1,560,000
2012 special obligation bonds of \$810,000 due in annual installments ranging from \$5,000 to \$95,000 through July 1, 2018; bearing interest at Prime plus 1.5% with a minimum of 6% (6% at June 30, 2012)	810,000
2012 rental bond of \$3,000,000 due in annual installments ranging from \$60,000 to \$265,000 through July 1, 2036; bearing interest at Prime plus 1.5% with a minimum of 6% (6% at June 30, 2012)	3,000,000
2012 special obligation notes of \$505,000 due in annual installments ranging from \$55,000 to \$95,000 through July 1, 2018; bearing interest at Prime plus 1.5% with a minimum of 6% (6% at June 30, 2012)	505,000
2012 rental bond of \$1,310,000 due in annual installments ranging from \$25,000 to \$109,000 through July 1, 2036; bearing interest at Prime plus 1.5% with a minimum of 6% (6% at June 30, 2012)	1,310,000
	\$ 14,552,000

The annual requirement to amortize general and special obligation bonds and notes as of June 30, 2012 follows:

June 30,	Principal	Interest
2013	\$ 1,111,000	\$ 831,868
2014	854,000	832,700
2015	696,000	788,087
2016	796,000	736,275
2017	501,000	704,014
2018-2022	2,393,000	3,005,058
2023-2025	2,759,000	2,280,262
2028-2032	2,963,000	1,327,532
2033-2037	2,479,000	360,970
Totals	\$ 14,552,000	\$ 10,866,766

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

NOTES TO FINANCIAL STATEMENTS

NOTE I - LONG-TERM DEBT - Continued

3. Other long-term liabilities

**Outstanding
Amount**

General obligation bond anticipation notes – The Municipality has issued \$435,968 in general obligation bond anticipation notes to Rural Development (“RD”). They are part of a total note of \$457,000 to be issued to finance the construction of a sanitary sewer system financed by RD. The notes bears interest at 2.3750% and are due the date of the final payment issued by RD to the Municipality, but not exceeding 10 years from the date of the notes. The Municipality intends to refinance these notes on a long term basis through a \$457,000 general obligation bond issuance approved by the Municipal Legislature and the Governmental Development Bank for Puerto Rico, payable from sales and used taxes deposited in the Municipal Redemption Fund. Issuance will occur after the construction project is finished.

\$ 435,968

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 five years and variable for the next twenty-five 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 five 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 five years any collection from those delinquent accounts was credited to the loan principal. After the five year period the loan outstanding balance was restructured for a twenty-five years period. Debt service requirements in future years are as follows:

96,452

<u>June 30</u>	<u>Principal</u>	<u>Interest</u>
2013	\$ 4,823	\$ 5,999
2014	4,823	5,699
2015	4,823	5,399
2016	4,823	5,099
2017	4,823	4,799
2018-2022	24,113	19,498
2023-2027	24,113	11,999
2028-2032	24,111	4,499
Totals	<u>\$ 96,452</u>	<u>\$ 62,991</u>

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

NOTES TO FINANCIAL STATEMENTS

NOTE I - LONG-TERM DEBT – Continued

	<u>Outstanding Amount</u>
<p>Note payable, Department of Labor – In December 22, 2010 the Municipality entered into a payment plan agreement to finance debt for unemployment benefits paid by the Commonwealth of Puerto Rico in behalf of the Municipality matured and outstanding at June 30, 2010. In April 5, 2011 the Municipality entered in an additional payment plan agreement to refinance the previous agreement and to cover additional debt for unemployment benefits of the current year. The Municipality made a down payment of \$16,000 and issued a \$75,788 non-interest bearing note (imputed interest of 7.62%) due on April 5, 2014. Amount will be totally repaid through withholdings from the property tax advances sent to the Municipality by the Municipal Revenue Collection Center.</p>	43,367
<p>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.</p>	3,458,781
<p>Christmas Bonus - represents the accrued portion corresponding to fiscal year 2012 of the Christmas bonus to be paid in December 2012.</p>	312,223
<p>Claims and judgments - represents the estimated loss of legal cases to be paid subsequent to June 30, 2012. The awarded amount, if any, will be paid with unrestricted funds.</p>	196,377
<p>Payable to PREPA - As required by Act No. 83 of May 2, 1941 the Puerto Rico Electric Power Authority ("PREPA") should annually pay to the Municipalities of Puerto Rico a contribution in lieu of tax ("CELI") based on certain requirements as specified by the mentioned Act. The amount of CELI obligation is used by the Municipalities to finance the annual electric utility expense payment to PREPA. For fiscal year 2011 the Municipality's annual energy charges amounted to \$2,714,126 but the CELI obligation amounted to \$1,265,655. The excess amount of \$1,448,471 was recorded as a payable and a receivable for the same amount and will be amortized over a three-year period. As of June 30, 2012 the outstanding amount of \$1,204,047 includes a balance of \$238,400 from fiscal year 2010 and is recognized by the Municipality as a receivable and a liability to PREPA. Debt service requirements in future years are as follows:</p>	1,204,047

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

NOTES TO FINANCIAL STATEMENTS

NOTE I - LONG-TERM DEBT – Continued

June 30	Principal
2013	\$ 721,224
2014	482,823
Totals	\$ 1,204,047

NOTE J - 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 1st and January 1st. Total tax rates in force as of June 30, 2012 are 7.03% for personal property and 9.03% for real property. The distribution of these rates follows:

Description	Personal Property	Real Property
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:	2.00%	2.50%
Total tax rate:	7.03%	9.53%
Discount granted by law to the taxpayers but reimbursed to the Municipality by the P.R. Treasury Department:	(.20%)	(.20%)
Total percent to be paid by taxpayers:	6.83%	9.33%

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.

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.

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

NOTES TO FINANCIAL STATEMENTS

NOTE J - PROPERTY TAXES - Continued

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. This amount is recorded as long term debt. The Municipality has a net receivable of \$104,096 resulting from the final settlement of fiscal year 2012.

On June 16, 2011 the Commonwealth's Legislature approved Act No. 94 which established an incentive plan (amnesty) for the payment of property tax debts. The Act, applicable to fiscal years 2010-2011 and before, provided participants a 100% waiver on interest and penalties and a 50% waiver over principal debt in excess of 10 years. Funds will be collected by the CRIM and remitted to the Municipalities. During the year 2011-2012 amnesty collections of \$207,256 and \$66,851 were recorded in the general fund and debt service fund respectively.

NOTE K - INTERGOVERNMENTAL REVENUES

Intergovernmental revenues in the General Fund are comprised of Christmas bonus reimbursement of \$254,813 and revenues for municipal equalization fund of \$4,472,475 received from the Commonwealth of Puerto Rico. Amount recorded in other governmental funds consists of Federal and Commonwealth governmental grants.

NOTE L - 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 and 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.

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.

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

NOTES TO FINANCIAL STATEMENTS

NOTE L – RETIREMENT PLAN - Continued

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 the 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.

Disability pensions are not been granted under the new program. The employer contributions (10.275% 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 10.275% 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>
2012	\$ 193,703	\$ 304,632
2011	\$ 185,126	\$ 278,995
2010	\$ 205,386	\$ 284,535

NOTE M – POSTEMPLOYMENT BENEFITS

In addition to the pension benefits described in Note L, 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 2012, costs related to these post employment benefits amounted to \$195,089. These benefits are recorded as expenditures in the general fund.

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

NOTES TO FINANCIAL STATEMENTS

NOTE N - 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 to \$133,012. Management believes that the summary of the future minimum rental commitments under non-cancelable equipment leases with terms exceeding one year is not significant.

2. Construction

The Municipality has commitments at June 30, 2012 of \$1,565,633 for construction, improvements or renovation of certain municipal facilities.

3. Encumbrances

As of June 30, 2012 the Municipality has encumbrances outstanding totaling \$296,848 which represent the estimated amount of expenditures required to complete contracts, purchase orders and other commitments in process of completion at fiscal year-end. As required by current standards, outstanding encumbrances as of June 30, 2012 are reported as unassigned amounts in the general fund. Purpose classification follows:

Purpose	General Fund- unassigned fund balance
General public works and sanitation	\$ 166,935
Culture and recreation	5,465
Public Safety	329
Welfare	5,948
General government and other purposes	118,171
	\$ 296,848

Fund balance of major and other governmental funds (special revenue, capital project and debt service funds) is classified as restricted, some or all of which may be encumbered. Encumbrances of restricted fund balance are not reported separately from this classification because the encumbrance does not further restrict the purpose for which the resources may be used.

NOTE O - 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 that the 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.

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

NOTES TO FINANCIAL STATEMENTS

NOTE O – CONTINGENCIES - Continued

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. As a result of one legal case as of June 30, 2012 and not to be covered by insurance, the Municipality accrued an estimated loss of \$196,377 in the government-wide statements. 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.

NOTE P – RESTATEMENT OF FUND BALANCE AND NET ASSETS

The following table disclosed the net change in fund balances and net assets at beginning of year as previously reported in the financial statements. The beginning balances have been restated as follows:

<u>Description</u>	<u>Fund Balance Other Governmental Funds</u>	<u>Net Assets Government Wide Statements</u>
Fund balance / net assets, at beginning of year, as previously reported	\$ 2,317,804	\$ 44,442,338
Correction of error, overstatement of accrued liability related to a 10% withholding payable to a construction contractor	332,388	332,388
Correction of error, overstatement of amounts due from Commonwealth Government	-	(433,826)
Balance of construction in progress of an infrastructure asset not recorded in previous year	-	42,387
Balance of machinery and equipment not recorded in previous year	-	26,000
Fund balance / net assets, at end of year, as restated	<u>\$ 2,650,192</u>	<u>\$ 44,409,287</u>

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

NOTES TO FINANCIAL STATEMENTS

NOTE Q – SUBSEQUENT EVENTS

Subsequent to June 30, 2012 the Municipality entered into the following long-term obligations:

1. On October 8, 2012 the Municipality entered into a Loan Agreement (“the Agreement”) with the Governmental Development Bank of P.R. (“GDB”) for the acquisition of real property. The Agreement provides for the issuance of 2012 Municipal General Obligation Bonds (“GOB”) in the amount of \$865,000 with maturities of July 1 of each year through its maturity date July 1, 2037. The GOB will bear interest at 1.50% over prime rate (with a minimum of 6%) payable semiannually in January 1 and July 1 of each year. Principal and interest will be repaid from revenues of the Municipal Sinking Fund (CAE).
2. On November 27, 2012 the Municipality entered into a Note Purchase Agreement (“the Agreement”) with Banco Santander Puerto Rico to finance the construction of the recreational facility “San German Surf & Fun Water Park”. The Agreement provides for the issuance of 2012 Municipal General Obligation Note in the amount of \$8,305,000 and the issuance of 2012 Special Obligation Note of \$1,005,000 with maturities of July 1 of each year through its maturity date July 1, 2019. The Notes will bear interest at 3.25% over LIBOR payable semiannually in January 1 and July 1 of each year. Principal and interest on the \$8,305,000 Note will be repaid from revenues of the Municipal Sinking Fund (CAE). Principal and interest on the \$1,005,000 Note will be repaid from revenues of the Municipal Redemption Fund (IVU) and 50% of the Municipal Development Fund.
3. On December 7, 2012 the Municipality entered into a Loan Agreement (“the Agreement”) with the Governmental Development Bank of P.R. (“GDB”) for improvements to a recreational facility. The Agreement provides for the issuance of 2012 Municipal General Obligation Bonds (“GOB”) in the amount of \$230,000 with maturities of July 1 of each year through its maturity date July 1, 2022. The GOB will bear interest at 1.50% over prime rate (with a minimum of 6%) payable semiannually in January 1 and July 1 of each year. Principal and interest will be repaid from revenues of the Municipal Sinking Fund (CAE).
4. On December 7, 2012 the Municipality entered into a Loan Agreement (“the Agreement”) with the Governmental Development Bank of P.R. (“GDB”) for construction to a recreational facility. The Agreement provides for the issuance of 2012 Special General Obligation Bonds (“GOB”) in the amount of \$575,000 with maturities of July 1 of each year through its maturity date July 1, 2032. The GOB will bear interest at 1.50% over prime rate (with a minimum of 6%) payable semiannually in January 1 and July 1 of each year. Principal and interest will be repaid from revenues of the Municipal Redemption Fund (IVU) and 50% of the Municipal Development Fund.
5. On December 7, 2012 the Municipality entered into a Loan Agreement (“the Agreement”) with the Governmental Development Bank of P.R. (“GDB”) for construction to a recreational facility. The Agreement provides for the issuance of 2012 Special General Obligation Bonds (“GOB”) in the amount of \$305,000 with maturities of July 1 of each year through its maturity date July 1, 2032. The GOB will bear interest at 1.50% over prime rate (with a minimum of 6%) payable semiannually in January 1 and July 1 of each year. Principal and interest will be repaid from revenues of the Municipal Sinking Fund (CAE).

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

NOTES TO FINANCIAL STATEMENTS

NOTE Q – SUBSEQUENT EVENTS – Continued

6. On December 11, 2012 the Governmental Development Bank of P.R. (“GDB”) approved the request of a \$455,000 Loan for the acquisition of real property. The Loan will be due 25 years after the loan first disbursement with maturities of July 1 of each year. The Loan will bear interest at 1.50% over prime rate (with a minimum of 6%) payable semiannually in January 1 and July 1 of each year. Principal and interest will be repaid from revenues of the Municipal Sinking Fund (CAE).

REQUIRED SUPPLEMENTARY INFORMATION

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

**BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2012**

	Budgeted amounts		Actual amounts (Budgetary basis)	Variance with final budget Positive (Negative)
	Original	Final		
Revenues:				
Taxes:				
Property taxes	\$ 4,004,358	\$ 4,263,896	\$ 4,267,334	\$ 3,437
Municipal license taxes	3,881,448	3,881,448	3,264,979	(616,469)
Sales and use taxes	1,690,000	1,690,000	1,771,675	81,675
Intergovernmental	3,425,256	3,425,256	3,400,068	(25,188)
Rental income and charges for services	4,829,174	5,260,934	4,510,837	(750,097)
Fines and forfeitures	40,000	40,000	21,010	(18,990)
Interest	90,000	90,000	139,769	49,769
Other	409,769	275,500	191,653	(83,847)
Total Revenues	<u>18,370,005</u>	<u>18,927,034</u>	<u>17,567,324</u>	<u>(1,359,710)</u>
Expenditures:				
Current:				
General government	6,267,043	6,039,123	5,939,046	100,078
Public safety	1,513,641	1,418,448	1,418,448	-
Public works	8,336,367	9,090,411	8,392,882	697,528
Sanitation	278,851	215,682	215,682	-
Health	837,755	786,763	786,763	-
Welfare	621,132	597,337	597,306	31
Culture and recreation	515,216	463,200	462,977	223
Total expenditures	<u>18,370,005</u>	<u>18,610,964</u>	<u>17,813,103</u>	<u>797,861</u>
Excess (deficiency) of revenues over expenditures	-	316,070	(245,779)	(561,849)
Other financing sources (uses)				
Transfers - in		996	995	-
Transfers - out		(435,216)	(435,216)	-
Total other financing sources (uses)	<u>-</u>	<u>(434,220)</u>	<u>(434,220)</u>	<u>-</u>
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	-	(118,150)	(680,000)	(561,850)
Readjustment from prior year fund balance (note B)	-	118,150	118,150	-
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses after readjustment from prior year fund balance	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (561,850)</u>	<u>\$ (561,850)</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, 2012

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 assigned fund balance since they do not constitute expenditures or liabilities while on a budgetary basis encumbrances are recorded as expenditures of the 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

The budgetary comparison schedule - general fund present a fund balance readjustment of \$118,150. This represents a readjustment of current year budget with prior year's budgetary surpluses, approved by the Municipal Legislature.

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
June 30, 2012

NOTE C - BUDGET TO GAAP RECONCILIATION - Continued

Excess of revenues and other financing sources over expenditures and other financing uses (budgetary basis):	\$(561,850)
Budget to GAAP differences:	
Entity differences:	
Non-budgeted funds recorded as revenues for financial reporting purposes:	97,447
Non-budgeted funds recorded as expenditures for financial reporting:	(701,415)
Non budgeted transfers in:	1,935,282
Non budgeted transfers out:	(996)
Basis of accounting differences:	
Revenues recorded for financial reporting purposes but not in budgetary basis:	2,093,051
Revenues recorded in budgetary basis purposes but not in financial reporting:	(538,554)
Readjustment from prior year fund balance recorded for budgetary basis purposes but not in financial reporting:	(118,150)
Expenditures recorded in budgetary basis but not for financial reporting purposes:	227,839
Expenditures recorded for financial reporting purposes but not in budgetary basis:	(1,880,307)
Timing differences:	
Current year encumbrances recorded as expenditures for budgetary reporting purposes:	260,922
Prior year encumbrances recorded as expenditures for financial reporting purposes:	<u>(250,109)</u>
Net change in fund balance (GAAP basis):	<u>\$ 563,160</u>

SUPPLEMENTARY INFORMATION

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

**SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2012**

Line Item No.	Description	14.871 Housing Choice Vouchers
	Balance Sheet	
111	Cash - unrestricted	\$ 71,607
113	Cash - other restricted	\$ 38,218
100	Total cash	\$ 109,825
121	Accounts receivable - PHA projects	\$ 4,305
122	Accounts receivable - HUD other projects	\$ 224
125	Accounts receivable - miscellaneous	\$ 3,681
126.2	Allowance for doubtful accounts - other	\$ (1,265)
128	Fraud recovery	\$ 11,120
128.1	Allowance for doubtful accounts - fraud	\$ (4,235)
120	Total receivables, net of allowance for doubtful accounts	\$ 13,830
142	Prepaid expenses and other assets	\$ 1,639
150	Total Current Assets	\$ 125,294
164	Furniture, equipment and machinery - administration	\$ 47,809
166	Accumulated depreciation	\$ (37,735)
160	Total capital assets, net of accumulated depreciation	\$ 10,074
180	Total Non-current Assets	\$ 10,074
190	Total Assets	\$ 135,368
313	Accounts payable > 90 days past due	\$ 2,664
322	Accrued compensated absences - current portion	\$ 2,156
332	Accounts Payable - PHA Projects	\$ 6,603
310	Total Current Liabilities	\$ 11,423
353	Non-current liabilities - other	\$ 8,593
354	Accrued compensated absences - non current	\$ 19,290
350	Total Non-current Liabilities	\$ 27,883
300	Total Liabilities	\$ 39,306
508.1	Invested in Capital Assets, Net of Related Debt	\$ 10,074
511.1	Restricted Net Assets	\$ 36,510
512.1	Unrestricted Net Assets	\$ 49,478
513	Total Equity/Net Assets	\$ 96,062

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN

SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2012

Line Item No.	Description	14.871 Housing Choice Vouchers
Income Statement		
70600-010	Housing assistance payments	\$ 327,480
70600-020	Ongoing administrative fees earned	\$ 59,944
70600-031	FSS Coordinator	\$ 45,241
70600	HUD PHA operating grants	\$ 432,665
71400-010	Housing Assistance Payment	\$ 623
71400-020	Administrative Fee	\$ 623
71400	Fraud recovery	\$ 1,246
71500	Other revenue	\$ 38,845
700	Total Revenue	\$ 472,756
91100	Administrative salaries	\$ 25,828
91200	Auditing fees	\$ 2,950
91500	Employee benefit contributions- administrative	\$ 12,939
91600	Office expenses	\$ 3,894
91000	Total Operating - Administrative	\$ 45,611
92100	Tenant services - salaries	\$ 16,376
92300	Employee benefit contributions- tenant services	\$ 3,727
92400	Tenant services - other	\$ 30,161
96000	Total Tenant Services	\$ 50,264
96200	Other general expenses	\$ 2,943
96210	Compensated absences	\$ 9,146
96600	Bad debt - other	\$ 1,265
96000	Total Other General Expenses	\$ 13,354
96900	Total Operating Expenses	\$ 109,229
97000	Excess Revenue Over Operating Expenses	\$ 363,527
97300-050	All Other	\$ 352,037
97300	Housing assistance payments	\$ 352,037
97350	HAP Portability-in	\$ 34,240
97400	Depreciation expense	\$ 156

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

**SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2012**

Line Item No.	Description	14.871 Housing Choice Vouchers
10000	Excess (Deficiency) of Revenue Over (Under) Expenses	\$ (22,906)
11030	Beginning equity	\$ 118,968
11770-001	Administrative Fee Equity - Beginning Balance	\$ 58,524
11170-010	Administrative Fee Revenue	\$ 59,944
11170-020	Hard to House Fee Revenue	\$ -
11170-021	FSS Coordinator Grant	\$ 45,241
11170-030	Audit Costs	\$ -
11170-040	Investment Income	\$ -
11170-045	Fraud Recovery Revenue	\$ 623
11170-050	Other Revenue	\$ 38,845
11170-051	Comment For Other Revenue	This amount corresponds to the administrative fees earned on the portability-in vouchers administered by the Municipality (\$5,025) plus the reimbursement received from the initial PHAs of the HAP rent payments made on behalf of the portability-in units during 11-12 (\$33,820).
11170-060	Total Admin Fee Revenues	\$ 144,653
11170-080	Total Operating Expenses	\$ 109,229
11170-090	Depreciation	\$ 156
11170-095	Housing Assistance Portability In	\$ 34,240
11170-100	Other Expenses	\$ -
11170-101	Comment For Other Expense	
11170-110	Total Expenses	\$ 143,625
11170-002	Net Administrative Fee	\$ 1,028
11170-003	Administrative Fee Equity - Ending Balance	\$ 59,552
11170	Administrative Fee Equity	\$ 59,552
11180-001	Housing Assistance Payments Equity - Beginning Balance	\$ 60,444
11180-010	Housing Assistance Payments Revenues	\$ 327,480
11180-015	Fraud Recovery Revenue	\$ 623
11180-020	Other Revenue	\$ -

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN

SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2012

Line Item No.	Description	14.871 Housing Choice Vouchers
11180-021	Comment For Other Revenue	
11180-025	Investment Income	\$ -
11180-030	Total HAP Revenues	\$ 328,103
11180-080	Housing Assistance Payments	\$ 352,037
11180-090	Other Expenses	\$ -
11180-091	Comment For Other Expense	
11180-100	Total Housing Assistance Payments Expenses	\$ 352,037
11180-002	Net Housing Assistance Payments	\$ (23,934)
11180-003	Housing Assistance Payments Equity - Ending Balance	\$ 36,510
11180	Housing Assistance Payments Equity	\$ 36,510
11190-210	Total ACC HCV Units	1,053
11190-220	Unfunded Units	-
11190-230	Other Adjustments	-
11190	Unit Months Available	1,053
11210	Unit Months Leased	1,045

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, 2012

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.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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, 2012

Federal Grantor/Pass Through Grantor/Program Title	Federal CFDA Number (note B)	Pass-Through Entity Identifying Number (note B)	Federal Expenditures (notes A and B)
<u>U.S. Department of Agriculture</u>			
Direct programs:			
Rural Housing Preservation Grants	10.433	N/A	\$ 10,091
Water and Waste Disposal Systems for Rural Communities	10.760	N/A	71,003
Passed-through program from:			
<u>P.R. Department of Education</u> Child and Adult Care Food Program	10.558	CCC-269	9,400
Subtotal U.S. Department of Agriculture			<u>90,494</u>
<u>U.S. Department of Housing and Urban Development</u>			
Direct programs:			
Community Development Block Grants / Entitlement Grants	14.218	N/A	1,110,850
Community Development Block Grants - Program Income	14.218	N/A	137,316
Shelter Plus Care	14.238	N/A	54,689
Section 8 Housing Choice Vouchers Program	14.871	N/A	432,665
Passed-through program from:			
<u>Office of Commissioner of Municipal Affairs:</u> Community Development Block Grant / State's Program (State-Administered Small Cities Program)	14.228	FD-57 AB-57, FC-57	226,061
<u>P.R. Department of Family:</u> Emergency Shelter Grants Program	14.231	S08DC720001, S09DC720001	29,229
ARRA - Homeless Prevention and Rapid Re-Housing Program Technical Assistance	14.262	S08DC720001	182,753
<u>P.R. Department of Health:</u> Housing Opportunities for Persons with AIDS (HOPWA)	14.241	2008-DS 0618	38,839
<u>P.R. Department of Housing - (Puerto Rico Public Housing Administration "PRPHA"):</u> Public and Indian Housing	14.850	RQ003091, RQ005145	911,410
Public Housing Capital Fund	14.872	RQ005008026	74,562
Subtotal U.S. Department of Housing and Urban Development			<u>3,198,374</u>
<u>U.S. Department of Justice</u>			
Passed-through program from:			
<u>P.R. Department of Justice:</u> ARRA - Eward Byrne Memorial Justice Assistance Grant (JAG) Program/ Grants to States and Territories	16.803	2009-SU-CSSAG-01	22,258
<u>U.S. Department of Transportation</u>			
Passed-through program from:			
<u>P.R. Traffic Safety Commission</u> State and Community Highway Safety	20.600	10-06-28, 10-03-76	25,591
<u>Environmental Protection Agency</u>			
Direct programs:			
Brownfields Assessment and Cleanup Cooperative Agreements	66.818	N/A	8,700
<u>U.S. Department of Energy</u>			
Direct programs:			
ARRA - Energy Efficiency and Conservation Block Grant Program (EECBG)	81.128	EEC10630	50,125
<u>U.S. Department of Health and Human Services</u>			
Direct programs:			
Head Start Cluster:			
Head Start	93.600	N/A	585,071
ARRA - Early Head Start	93.709	N/A	580,112
Total Head Start Cluster:			<u>1,165,183</u>
Passed-through programs from:			
<u>P.R. Office of the Ombudsman for the Elderly:</u> Special Programs for the Aging_ Title III, Part C_ Nutrition Services	93.045	N/AV	194,718
Subtotal U.S. Department of Health and Human Services:			<u>1,359,901</u>
<u>U.S. Department of Homeland Security</u>			
Passed-through programs from:			
<u>P.R. Governor's Office - Governor's Authorized Representative (GAR):</u> Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	125-99-125	4,000
Total Expenditures of Federal Awards			<u>\$ 4,759,443</u>

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, 2012

NOTE A – BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality under programs of the federal government for the year ended June 30, 2012. 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. Because the schedule presents only a selected portion of the operations of the Municipality, it is not intended to and does not present the financial position and changes in net assets of the Municipality.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported on the modified accrual basis of accounting, except for Section 8 Housing Choice Voucher Program (HCV). Such expenditures are recognized when the related liability is incurred following the cost principles contained in OMB Circular A-87 *Cost Principles for State, Local and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Expenditures for HCV Program are reported on a statutory basis as required by the U.S. Department of Housing and Urban Development. Such expenditures should equal the net ACC subsidy for the PHA's fiscal period.

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.

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 C – RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE BASIC FINANCIAL STATEMENTS

CFDA No. / Description	Other Governmental Funds
10.433	\$ 10,091
10.558	9,400
10.760	71,003
14.871	432,665
14.218	1,110,850
14.218 (Program Income)	137,316
14.238	54,689
14.228	226,061
14.231	29,229
ARRA – 14.262	182,753
14.241	38,839

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

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2012

NOTE C - RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE BASIC FINANCIAL STATEMENTS - Continued

<u>CFDA No. / Description</u>	<u>Other Governmental Funds</u>
14.850	911,410
14.872	74,562
16.803	22,258
20.600	25,591
66.818	8,700
ARRA -- 81.128	50,125
ARRA - 93.709	580,112
93.045	194,718
93.600	585,071
97.036	4,000
Total federal awards expenditures:	<u>4,759,443</u>
Additional amount recorded as expenditures under modified accrual basis for Section 8 HCV Program:	54,069
Total non-federal awards expenditures:	3,064,768
Total expenditures, fund statements:	<u>\$ 7,878,280</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 Member 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, 2012, which collectively comprise Municipality of San Germán, Puerto Rico's basic financial statements and have issued our report thereon dated March 21, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of Municipality of San Germán, Puerto Rico, is responsible for establishing and maintaining effective 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 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.

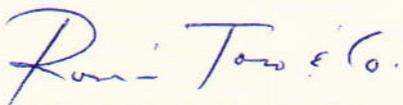
A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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 previously.

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 statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Governmental Auditing Standards*.

This report is intended solely for the information and use of management, 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., CPA, C.S.P.
LICENSE #35 - IN FORCE

Yauco, Puerto Rico
March 21, 2013

Stamp #E46246 was affixed to
the original of this report





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

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

Compliance

We have audited Municipality of San Germán, Puerto Rico's compliance, with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Municipality of San Germán, Puerto Rico's major federal programs for the year ended June 30, 2012. 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's management. Our responsibility is to express an opinion on Municipality of San Germán'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 compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

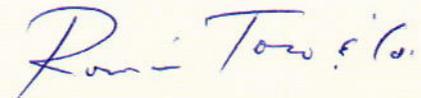
Internal Control Over Compliance

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 to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality of San Germán, Puerto Rico's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness* in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be *significant deficiencies* or *material weaknesses*. We did not identify any deficiencies in internal control over compliance that we consider to be a *material weakness*, as defined above.

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



ROMAN TORO & CO., CPA, C.S.P.
LICENSE #35 - IN FORCE

Yauco, Puerto Rico
March 21, 2013

Stamp #E46247 was affixed 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, 2012**

SECTION I – SUMMARY OF AUDITORS' RESULTS

Financial Statements

- Type of auditor's report issued: Unqualified Opinion Qualified Opinion
 Adverse Opinion Disclaimer Opinion
- Internal control over financial reporting:
- Significant control deficiency identified? Yes None reported
 - Material weakness (es) identified? Yes No
- Noncompliance material to financial statements noted? Yes No

Federal Awards

- Internal control over major programs:
- Significant control 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 Grants/ Entitlement
14.850	Public and Indian Housing
14.871	Section 8 Rental Housing Choice Vouchers
93.600	Early Head Start Program
93.709	ARRA - Early Head Start Program

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, 2012**

SECTION II – FINANCIAL STATEMENT FINDINGS

None.

SECTION III – FEDERAL AWARD FINDINGS AND 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, 2012**

Year	Finding Number	Finding	CFDA Number	Questioned Cost(s)	Comments
(1) Audit Findings that have been fully corrected or not noted during our audit:					
2011	2011-III-1	The Municipality submitted late certain required reports of its Head Start Program.	93.600	None.	The Municipality implemented changes to internal controls which corrected situation at June 30, 2012.
(2) Audit Findings not corrected or partially corrected:					
NONE.					
(3) Corrective action taken is significantly different from corrective action previously reported:					
NONE.					
(4) Audit findings are no longer valid:					
NONE.					
END OF SCHEDULE					