OC-DA-123

mar. 17 (Rev.)
OC-17-19

Estado Libre Asociado de Puerto Rico
**OFICINA DEL CONTRALOR**
San Juan, Puerto Rico

**Certificación de Cumplimiento con la *Ley 273-2003*, según enmendada; y de Notificación de Envío de Cartas de Recomendaciones (*Management Letters*), Informes de Auditoría, Estados Financieros Auditados y Otros**[1]

Yo, Isidro Negrón Irizarry (nombre del funcionario principal) Funcionario Principal de Municipio de San Germán (nombre de la entidad)

4064 (número de entidad) certifico a la Oficina del Contralor de Puerto Rico (Oficina) que relacionado con el año fiscal terminado al 30 de junio de 2016 :

1. Recibimos fondos públicos por $6,244,904.00 .
2. Efectuamos desembolsos de fondos federales por $5,365,151.00 . No aplica ☐.
3. Tenemos la obligación de cumplir con ☐ la *Ley 273-2003, Ley de Normas Contractuales sobre Independencia en las Auditorías Externas de Entidades Gubernamentales*[2], según enmendada, y con ☒ el *Single Audit Act*. En cumplimiento de estos:

   a. El 31 de marzo de 2016 formalizamos el contrato número 2017-000001 para realizar la auditoría de los ☒ Estados Financieros y/o el ☐ *Single Audit Report*.

   b. El 29 de marzo de 2016 recibimos el *Informe de Auditoria* del 30 de junio de 2016 de los auditores externos.

   c. El 29 de marzo de 2017 los auditores externos comparecieron para presentar el informe final y comunicar los hallazgos y las recomendaciones.

[1] La entidad deberá remitir a esta Oficina, en formato **PDF** y no más tarde del 31 de mayo siguiente al año fiscal auditado, el *Formulario OC-DA-123* firmado por el funcionario principal, con los documentos que se especifican en el Apartado 3-e y f del mismo. Esto, a través de la aplicación *Certificaciones Anuales de la Oficina del Contralor*. La aplicación está disponible en la sección de Contraloría Digital en nuestra página en Internet: www.ocpr.gov.pr.

[2] En el Artículo 1 de la *Ley 273-2003* se establece que, para propósitos de dicha *Ley*, la frase "cualquier entidad de gobierno" incluye todos los organismos, con facultad de contratar, de las ramas Ejecutiva, Legislativa y Judicial tales como: departamentos, dependencias, municipios, corporaciones públicas y sus subsidiarias, afiliadas o cualesquiera entidades gubernamentales que tengan personalidad jurídica propia.

d. Relacionado con las cartas finales de recomendaciones (*Management Letters*):

☒ El 26 de mayo de 2017 recibimos las cartas finales de recomendaciones (*Management Letters*) emitidas por los auditores externos el 26 de mayo de 2017. El archivo electrónico, en formato **PDF**, de las mismas fue remitido a su Oficina el ____ de _____ de _____.

☐ Los auditores externos no emitieron las cartas finales de recomendaciones (*Management Letters*).

e. Se incluye el archivo electrónico, en formato PDF, de los siguientes documentos e informes:

☐ Informes de auditorías emitidos en forma final

☒ Estados financieros auditados

☐ Informes de Control Interno sobre Cumplimiento y la Opinión sobre Cumplimiento

☒ *Single Audit Report*

☒ Copia del *Form SF-SAC, Data Collection Form for Reporting on Audits of States, Local Governments, and Non-Profit Organizations*, y del recibo de envío al *Federal Audit Clearinghouse.*

☐ Otros (especifique): _____

f. Relacionado con el *Informe Especial Sobre el Cumplimiento de las Recomendaciones Contenidas en los Informes de Auditoría de la Oficina del Contralor de Puerto Rico y la Corrección de las Situaciones Comentadas en sus Informes Previos (Informe Especial)*:

☒ Se incluye el archivo electrónico, en formato **PDF**, del *Informe Especial* emitido por los auditores externos el 26 de mayo de 2017.

☐ No aplica, ya que no tenemos recomendaciones pendientes de cumplimentar relacionadas con

los informes publicados al 28 de febrero del año fiscal auditado.

4. ☐ No tenemos la obligación por ley, reglamento o acuerdo financiero, de contratar auditores externos para realizar la auditoría de los estados financieros del año fiscal terminado al ____ de _____ de _____.

En San Germán, Puerto Rico, hoy 30 de mayo de 2017.

Estado Libre Asociado de Puerto Rico
**OFICINA DEL CONTRALOR**
San Juan, Puerto Rico

Firma del Funcionario Principal

FORM SF-SAC 06/02/2016 U.S. Dept. of Comm. - Econ and Stat Admin. - U.S. Census Bureau

OMB No. 0348-0057: Approval Expires 06/30/2019 ACTING AS COLLECTING AGENT FOR OFFICE OF MANAGEMENT AND BUDGET

**Data Collection Form for Reporting on**

**Audits of States, Local Governments, Indian Tribes, Institutions of Higher Education and Nonprofit**

**For Fiscal Periods Beginning on or after December 26, 2014**

**PART I: GENERAL INFORMATION** **REPORTID: 720449 VERSION:2**

| | |
|---|---|
| **1. Fiscal Period End Date**<br>6/30/2016 | **2. Type of Uniform Guidance Audit**<br>Single Audit |
| **3. Audit Period Covered**<br>Annual | |
| **4. Auditee Identification Numbers**<br>a. Auditee Employer Identification Number (EIN)<br>66-0433531<br>b. Are multiple EINS covered in this report?<br>No | d. Auditee Data Universal Numbering System (DUNS) Number<br>13-144-8151<br>e. Are multiple DUNS covered in this report?<br>No |
| **5. Auditee Information** | **6. Primary Auditor Information** |
| a. Auditee name<br>MUNICIPALITY OF SAN GERMAN, PUERTO RICO | a. Audit Firm/Organization Name<br>ROMAN TORO & CO., CSP |
| b. Auditee address *(Number and street)*<br>PO BOX 85 | b. Audit Firm/Organization EIN<br>66-0567952 |
| | c. Audit Firm/Organization address *(Number and street)*<br>PO BOX 3043 |
| Auditee City<br>SAN GERMAN | Audit Firm/Organization City<br>YAUCO |
| Auditee State<br>PR | Audit Firm/Organization State<br>PR |
| Auditee ZIP Code<br>00683-0085 | Audit Firm/Organization ZIP Code<br>00698-3043 |
| c. Auditee Contact Name<br>WANDA RODRIGUEZ | d. Primary Auditor Contact Name<br>MARCOS MELENDEZ |
| Auditee Contact Title<br>FINANCE DIRECTOR | Primary Auditor Contact Title<br>AUDIT MANAGER |
| d. Auditee Contact Telephone<br>(787)892-3500 | e. Primary Auditor Contact Telephone<br>(787)856-6220 |
| e. Auditee Contact E-mail<br>WIRODRIGUEZ@MUNICIPIODESANGERMAN.C | f. Primary Auditor Contact E-mail<br>CPAMARCOSMELENDEZ@CPAROMANTORO.COM |
| | 7. Was a secondary auditor used?<br>No |

# COMMONWEALTH OF PUERTO RICO
# MUNICIPALITY OF SAN GERMAN

**BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY INFORMATION AND INDEPENDENT AUDITORS' REPORT**

**(WITH ADDITIONAL REPORTS REQUIRED UNDER THE UNIFORM GUIDANCE)**

**FOR THE FISCAL YEAR ENDED JUNE 30, 2016**

Hon. Isidro Negron-Irizarry
*Mayor*

Wanda I. Rodriguez-Rivera
*Finance Department Director*

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMÁN**

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ROMAN TORO & CO., PSC
Certified Public Accountants
Honesty - Integrity - Experience

Members of:
American Institute of Certified Public Accountants
and PR Society of Certified Public Accountants
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Fax (787) 856-6233

# INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and Member of the
Municipal Legislature
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 the Municipality of San Germán, Puerto Rico, as of June 30, 2016, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements as listed in the table of contents.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

**Summary of Opinions**

| Opinion Unit | Type of Opinion |
|---|---|
| Governmental Activities | Qualified |
| General Fund | Unmodified |
| Head Start Fund | Unmodified |
| Debt Service Fund | Unmodified |
| Loans Fund | Unmodified |
| Capital Improvements Funds | Unmodified |
| Other Governmental Funds | Unmodified |

**Basis for Qualified Opinion on Governmental Activities and Note Disclosure Regarding Pension Plan**

As discussed in Note N the Employee's Retirement System of the Commonwealth of Puerto Rico (ERS) has not issued audited financial statements as of and for the fiscal year ended June 30, 2015 nor has provided to the Municipality the required information to record transactions related to ***GASB Statement No. 68*** as of and for the fiscal year ended June 30, 2016. Amounts reported in the government-wide financial statements as deferred outflows of resources, deferred inflows of resources and net pension liability are the same amounts reported in the 2015 financial statements which were derived from the application of the proportional share included in the unaudited financial statements, notes and required supplementary information of the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico, cost-sharing multiple-employer pension plan for the fiscal year ended June 30, 2015. Accordingly, the Municipality did not record the current pension expense, changes in deferred outflows/inflows of resources and net pension liability, and additional disclosures required by ***GASB Statement No. 68*** and required supplementary information have been omitted. Accounting principles generally accepted in the United States of America require that the financial statement items discussed in this paragraph be determined and recorded in the financial statements on an annual basis. The amounts by which this departure would affect liabilities, deferred outflow of resources, deferred inflow of resources, net position, and expenses has not been determined.

**Qualified Opinion**

In our opinion, except for the possible effects of the matter discussed in the "Basis for Qualified Opinion on Governmental Activities and Note Disclosure Regarding Pension Plan" paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities of the **Municipality**, as of June 30, 2016, and the respective changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Unmodified Opinions**

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the Municipality of San Germán, Puerto Rico, as of June 30, 2016, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Emphasis-of-Matter**

*Contingency regarding Commonwealth of Puerto Rico's Going Concern*

As discussed in Notes 21 and 22, the Commonwealth of Puerto Rico and its component units currently face severe fiscal, economic, and liquidity situations, including accumulated net position and fund balance deficits, lack of access to financing, and difficulties in honoring its obligations as they become due. The Municipality is dependent on the Commonwealth for certain resources and services, while one of its component units, the Government Development Bank, provides custody of certain deposits and provides financing to the Municipality. The Commonwealth and its component units are currently under the supervision of a Federal Oversight Board, and have issued a general fiscal plan approved by the Board in order to remediate their situation. The financial statements do not include any adjustments that might result from the outcome of these uncertainties. Our opinion is not modified with respect to these matters.

**Other Matters**

*Required Supplementary Information Omitted*

The Municipality has omitted the Schedule of the Municipality' Proportionate Share of the Net Pension Liability, and the Schedule of Municipality's Contributions to the Employee's Pension Plan, information that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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 the financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. Our opinion on the basic financial statements is not affected by the information omitted.

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, and budgetary comparison information, on pages 4-15, and pages 67-69 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. We were unable to apply certain limited procedures to the required supplementary information related to employees' retirement systems information applicable to **Municipality**, in accordance with auditing standards generally accepted in the United States of America. We do not express an opinion or provide any assurance on the information.

*Other information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The financial data schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and also is not a required part of the basic financial statements. The financial data schedules and the schedule of expenditures of federal awards are the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic 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 basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America.

In our opinion, the financial data schedule and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic financial statements as a whole.

**Other Reporting Required by Government Auditing Standards**

In accordance with Government Auditing Standards, we have also issued our report dated March 29, 2017, 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 in considering Municipality of San Germán, Puerto Rico's internal control over financial reporting and compliance.

Román Toro & Co.

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

Yauco, Puerto Rico
March 29, 2017

Stamp #E256556 was affixed to
the original report

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMÁN**
**MANAGEMENT'S DISCUSSION AND ANALYSIS**
**YEAR ENDED JUNE 30, 2016**

The following Management's Discussion and Analysis is a required supplement to the Municipality of San Germán's (the "Municipality") financial statements. It describes and analyzes the financial position of the Municipality, providing an overview of the Municipality's activities for the year ended June 30, 2016. We encourage readers to consider the information we present here in conjunction with the information presented in the Municipality's financial statements and notes, which follow this section.

## *FINANCIAL HIGHLIGHTS*

- On a government-wide basis, total liabilities and deferred inflows of the Municipality (primary government) exceeded its total assets and deferred outflows of resources at the close of fiscal year 2016 by $(5,651,224) (net position). Of this amount, $(51,747,562) represents the unrestricted net deficit. This unrestricted deficit is the result of the implementation of GASB Statement No. 68 "Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27" and GASB Statement No. 71 "Pension Transition for Contributions Made Subsequent to the Measurement Date" in prior year 2015.
- With respect to 2015 the Municipality's governmental activities revenues increased 2% and expenses decreased 4%. Business-type activities revenues and expenses of $3,437,176 and $3,698,395 respectively represents the first year of operations for this activity. Net position, including business-type activity, decreased $1,083,363 in 2016.
- A negative net change in the fund balances of the Municipality's governmental funds of $206,589 in fiscal year 2016 resulted ending fund balances of $6,207,027 decreasing 3% with respect to 2015 year.
- For the fiscal year 2016, the General Fund reported an excess of expenditures and other financing uses over revenues and other financing sources of $685,706. The unassigned fund balance deficit amounts to $2,527,917 or 30% decrease in deficit when compared with year 2015.
- The investment in capital assets as of June 30, 2016 was $72,971,975 (net of depreciation).
- Long-term debt (total primary government) decreased to $88,124,078 a decrease of 3% with respect to 2015 year.
- On a budgetary basis, actual expenditures and other financing uses exceeded actual revenues and other financing sources by $(980,893).

## *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.

| | | |
|---|---|---|
| *COMPONENTS OF THE FINANCIAL POSITION* | *Management Discussion and Analysis* | |
| | *Basic Financial Statements* | *Government-wide (full accrual)*<br>*Governmental and Business-type activities* |
| | | *Fund*<br>*Governmental (modified accual)*<br>*Proprietary (full accrual)*<br>*Notes to Basic Financial Statements* |
| | *Required Supplementary Information* | |
| | *Other Supplementary Information* | |

**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 position presents all of the reporting entity's non-fiduciary assets, deferred outflows, liabilities and deferred inflows, with the difference reported as net position. Over time, increases or decreases in the Municipality's net position 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 position 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. The government-wide statements are divided into two categories:

*Governmental Activities:* Most of the Municipality's basic services such as public works and sanitation, public safety, culture and recreation, housing, welfare, and community development, education and general administration, are reported here. These activities are primarily financed through property taxes, other local taxes and intergovernmental revenues. Included in the governmental activities are the governmental funds.

*Business-type Activities:* Business-type activities charges fees to customers to finance the costs of their activities. The activities of *San Germán Municipal Enterprise, Inc.* (the only business-type activity) are included here.

- ***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 as by bond covenants. The Municipality has two kinds of funds: governmental and proprietary funds.

*Governmental funds:* 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 as on balances of spendable 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.

*Proprietary funds:* Services for which the Municipality charges customers a fee are generally reported as proprietary funds. These funds, like the government-wide statements, provide both long-term and short-term financial information and are accounted for using the economic resources measurement focus and accrual basis of accounting. The Municipality's proprietary funds consist of an enterprise fund, the same as business-type activities. The municipality reports the activities of *San Germán Municipal Enterprise, Inc.* as an enterprise fund.

The governmental and proprietary fund statements focus on major funds. The Municipality's major governmental and enterprise funds are funds that comply with a minimum criterion that is, a percentage of the assets and deferred outflows; liabilities and deferred inflows; revenues or expenditures or based on the Municipality's official's criteria if the fund is particularly important to financial statement users. Funds that do not comply with this criterion are grouped and presented in a single column as other governmental funds or other nonmajor enterprise 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, the schedule of Municipality's proportionate share of net pension liability and the schedule of Municipality's contributions.

**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.

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

**Net Position** - the following **TABLE 1** presents a summary of the Statements of Net Position as of June 30, 2016 and 2015:

**TABLE 1**

| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
|---|---|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| **Assets** | | | | | | |
| Current and other assets | $ 13,559,310 | $ 18,644,929 | $ 317,604 | $ - | $ 13,876,914 | $ 18,644,929 |
| Total capital assets, net | 72,971,975 | 74,137,934 | - | - | 72,971,975 | 74,137,934 |
| **Total assets** | 86,531,285 | 92,782,863 | 317,604 | - | 86,848,889 | 92,782,863 |
| Deferred outflows of resources | 2,781,626 | 2,781,626 | - | - | 2,781,626 | 2,781,626 |
| **Liabilities** | | | | | | |
| Current and other liabilities | 4,305,178 | 6,520,730 | 588,068 | - | 4,893,246 | 6,520,730 |
| Long-term liabilities: | 88,124,078 | 91,072,514 | - | - | 88,124,078 | 91,072,514 |
| **Total liabilities** | 92,429,256 | 97,593,244 | - | - | 93,017,324 | 97,593,244 |
| Deferred inflows of resources | 2,264,416 | 2,529,862 | - | - | 2,264,416 | 2,529,862 |
| **Net position** | | | | | | |
| Net investment in capital assets | 38,929,009 | 39,868,401 | - | - | 38,929,009 | 39,868,401 |
| Restricted | 7,167,329 | 7,587,326 | - | - | 7,167,329 | 7,587,326 |
| Unrestricted | (51,477,097) | (52,014,343) | (270,464) | - | (51,747,562) | (52,014,343) |
| **Total net position** | $ (5,380,760) | $ (4,558,616) | $ (270,464) | $ - | $ (5,651,224) | $ (4,558,616) |

Net position (difference of non-fiduciary assets, deferred outflows versus liabilities and deferred inflows) serve as a useful indicator of a government's financial position. Over time, increases or decreases in the Municipality's net position is one indicator of whether its financial health is improving or deteriorating. At June 30, 2016, total liabilities and deferred inflows exceeded total assets and deferred outflows of resources by $(5,651,224), a total for the entire primary government.

Of this amount, $(51,747,562) represents an unrestricted net deficit position. This unrestricted deficit is the part of net position that can be used to finance day-to-day governmental operations without constraints established by debt covenants, enabling legislation or other legal requirements. This deficit primarily arises from the implementation of ***GASB Statement No. 68*** *"Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27"* and ***GASB Statement No. 71*** *"Pension Transition for Contributions Made Subsequent to the Measurement Date"* in prior fiscal year 2015. Restricted net position represents resources that are subject to external restrictions on how they may be used.

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

The Municipality (total primary government) reported a negative change in net position of $1,083,363, an improvement of 59% with respect of prior year negative change in net position reported in fiscal period 2015 of $2,624,603. This improvement resulted from the net effect of an increase in 2% in revenues and a 4% decrease in expenses.

**Changes in net position** - the following **TABLE 2** summarizes the changes in net position for the years ended June 30, 2016 and 2015:

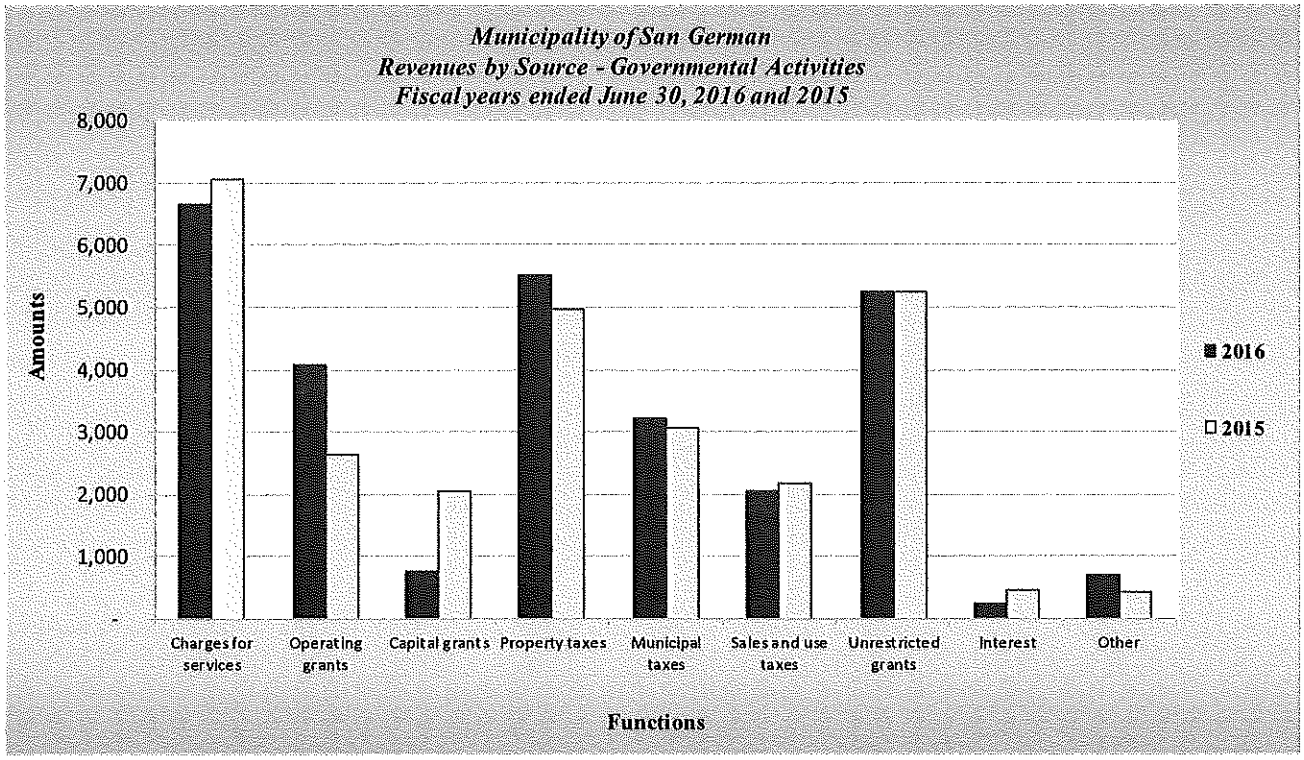
**TABLE 2**

| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
|---|---|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| **Program revenues:** | | | | | | |
| Fees, fines and charges for services | $ 6,666,821 | $ 7,060,055 | $ 3,437,176 | $ - | $ 10,103,997 | $ 7,060,055 |
| Operating grants and contributions | 4,067,637 | 2,631,421 | - | - | 4,067,637 | 2,631,421 |
| Capital grants and contributions | 771,788 | 2,046,746 | - | - | 771,788 | 2,046,746 |
| **General revenues:** | | - | | | - | - |
| Property taxes | 5,531,133 | 4,972,871 | - | - | 5,531,133 | 4,972,871 |
| Municipal license taxes | 3,221,667 | 3,060,867 | - | - | 3,221,667 | 3,060,867 |
| Sales and use taxes | 2,063,596 | 2,166,681 | - | - | 2,063,596 | 2,166,681 |
| Grants and contributions not restricted to specific programs | 5,246,482 | 5,254,139 | - | - | 5,246,482 | 5,254,139 |
| Interest and other | 928,750 | 866,990 | - | - | 928,750 | 866,990 |
| **Total revenues** | 28,497,874 | 28,059,770 | 3,437,176 | - | 31,935,050 | 28,059,770 |

| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
|---|---|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| **Expenses:** | | | | | | |
| General government | 6,162,411 | 9,711,730 | 3,698,395 | - | 9,860,806 | 9,711,730 |
| Public safety | 1,772,879 | 1,803,563 | - | - | 1,772,879 | 1,803,563 |
| Public works | 12,165,503 | 11,746,292 | - | - | 12,165,503 | 11,746,292 |
| Sanitation | 80,795 | 304,289 | - | - | 80,795 | 304,289 |
| Health | 786,763 | 786,763 | - | - | 786,763 | 786,763 |
| Welfare | 3,619,783 | 2,810,360 | - | - | 3,619,783 | 2,810,360 |
| Culture and recreation | 696,496 | 616,460 | - | - | 696,496 | 616,460 |
| Education | 2,067,844 | 1,467,040 | - | - | 2,067,844 | 1,467,040 |
| Interest on long-term debt | 1,967,544 | 1,437,876 | - | - | 1,967,544 | 1,437,876 |
| **Total expenses** | 29,320,018 | 30,684,373 | 3,698,395 | - | 33,018,413 | 30,684,373 |
| **Change in net position** | (822,144) | (2,624,603) | (261,219) | - | (1,083,362) | (2,624,603) |
| Net position at beginning of year, | (4,558,616) | (1,934,013) | (9,245) | - | (4,567,862) | (1,934,013) |
| **Net position at end of year** | $ (5,380,760) | $ (4,558,616) | $ (270,464) | $ - | $ (5,651,224) | $ (4,558,616) |

The following **Figure 1** illustrates the revenue comparison between 2016 and 2015:

**Figure 1**



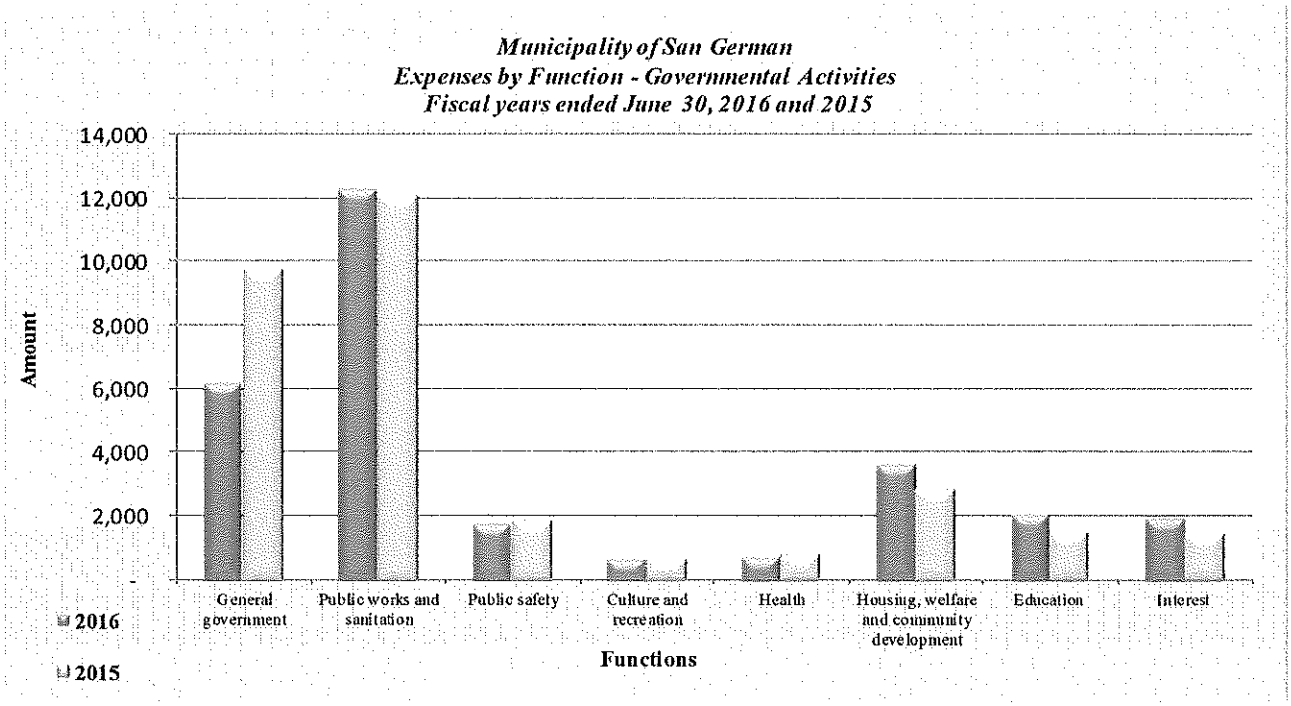
**Revenues, governmental activities** - Approximately 23% of the Municipality's revenues came from fees and charges for services, 19% from property taxes, 18% from unrestricted grants, 14% from operating grants, and 11% from municipal license taxes.

With respect to prior year, revenues reported a net increase of approximately 2%. This net increase is primarily the result of: (1) an increase of 55% in operating grants due an increase of over $800,000 in the funding for the Early Head Start and the Head Start expansion programs, and (2) increases of 11% and 5% in property taxes and municipal license taxes revenues respectively. These increases were partially offset with decreases in capital grants for approximately 66%, due to significant decrease in funding received from the State Government, and 50% in interest revenues.

**Revenues, business-type activities** – revenues of the business-type activity of *San Germán Municipal Enterprise, Inc.("SGME")* consists mainly from entrance fees and sales of food and beverage and general merchandise to the general public attending to the waterpark administered by SGME. The waterpark started formal operations in July, 2015.

The following **Figure 2** illustrates the expenses comparison between 2016 and 2015:

**Figure 2**




**Expenses, governmental activities** - The largest expenses are public works with 42%, general government with 21% and housing, welfare and community development with 12% of total expenses. Expenses decreased by 4% in comparison with the 2015 year. The most significant decrease is identified in the general government function because of the increased control over general expenses due to previous year's recurrent operating losses. This significant decrease was partially offset by (1) a 41% increase in education expenses, caused mostly by the increase in the Early Head Start program expenses due to expansion funds received and expended during the year; (2) a 37% increase in interest expense, due to increased debt payments incurred in recent years to finance the construction of the water park.; and (3) an increase of 29% in housing, welfare and community development function due to increased expenses related to services provided in the elderly care centers, and by non-recurring repairs performed over Rossy and El Recreo public housing units.

**Expenses, business-type activities** – Most expenses of business-type activity of SGME consists of salaries and fringe benefits, utilities, advertising, merchandise for sale, repairs and maintenance and other operational expenses, as well as certain nonoperating expenses. SGME started formal operations in July, 2015.

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 direct expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. The following **TABLE 3** discloses 2016 and 2015 expenses net of program revenue and the general revenues available to finance remaining costs:

**TABLE 3**

| *Net Cost of Municipality's Governmental activities For the years ended June 30,* | Net Costs of Services | |
|---|---|---|
| | 2016 | 2015 |
| **Governmental activities:** | | |
| General government | $ (4,734,676) | $ (8,804,576) |
| Public safety | (1,679,704) | (1,712,869) |
| Public works | (7,712,258) | (4,553,577) |
| Sanitation | (80,795) | (304,289) |
| Health | (786,763) | (786,763) |
| Welfare | (404,870) | (785,472) |
| Culture and recreation | (696,496) | (616,460) |
| Education | 249,335 | 55,731 |
| Interest on long-term debt | (1,967,544) | (1,437,876) |
| **Total expenses, net of program revenues** | (17,813,772) | (18,946,151) |
| **General revenues:** | | |
| Taxes | 10,816,396 | 10,200,419 |
| Grants and contributions not restricted to specific programs | 5,246,482 | 5,254,139 |
| Interest and other | 225,285 | 451,677 |
| Other | 703,465 | 415,313 |
| **Total general revenues** | 16,991,628 | 16,321,548 |
| **Change in net position** | $ (822,144) | $ (2,624,603) |

Some of the costs of governmental activities were paid by those who directly benefited from the programs ($6,666,821) and other governments and organizations that subsidized certain programs with grants and contributions ($4,839,425). The remaining costs were financed with general revenues. Like in the previous year, the net cost of services ($17,813,772) was not covered by other general revenues.

Expenses for the business-type activity were not covered by the charges for services by $261,219.

## *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 as they represent the portion of fund balance which has not yet been limited to use for a particular purpose by either an external party.

For the fiscal year ended June 30, 2016, the governmental funds reported combined ending fund balances of $6,207,027, a net decrease of 3% in comparison with the prior year. This decrease was caused primarily by a net change in the Surf and Fun Water Park Fund and Other Governmental Funds of $ $655,882 and $963,400 respectively (decreases) due mainly to the use in current year of prior years' proceeds of long term debt and grants. These decreases were partially offset by increases of $726,987 and $685,706 in the debt service and General Fund respectively. Of the total combined fund balances, a net deficit of $2,909,362 (or -47%) constitutes unrestricted and unassigned fund balance. The remainder of the fund balances is restricted to indicate that it is not available for new spending. Following is a summary of the financial analysis of the Municipality's major funds:

- ***General Fund***

  The general fund is the operating fund of the Municipality. The fund balance (deficit) of the general fund represents approximately -32% of total ending fund balances. Of the total fund balance, $529,032 is reported as non-spendable and represents advances provided to other funds, which are expected to be recovered after the next fiscal year. Unassigned fund balance (deficit) decreased 30% with respect to the prior year.

  For the year ended June 30, 2016, the fund balance of the general fund increased by $685,706 in comparison with the prior year. There was a 7% net increase in revenues due to 18% and 9% increases in municipal license taxes and sales and use taxes respectively. The Municipality reported a net decrease of 5% in the general fund expenditures due to strict expenditure controls in order to avoid increases in the operational deficit.

- ***Debt Service Fund***

  The debt service fund had an increase in fund balance during the current year of $726,987 to bring the year end fund balance to $3,324,423 which represents 54% of total fund balances. The increase results from an increase of $725,137 in property tax revenues and an increase of $1,131,966 in debt service principal and interest expenditures. The fund reported net other financing sources of $201,550 of which $1,114,905 represents a transfer to the general fund of excess funds of the CAE and IVU Municipal Redemption Funds and $1,316,455 represents a transfer from the general fund to finance the payment of the operational loans. The excess of funds may be transferred to the Municipality's general fund as authorized by Municipal regulations.

- ***Surf and Fun Water Park***

  This fund report revenue sources mostly from loans provided for the construction and future operation of a water park and from interest revenue. During the 2016 the fund balance decreased to $1,028,840. This decrease was mostly affected by $547,920 in capital outlays expenditures. These expenditures were partially offset by $18,773 of interest generated by the restricted cash in GDB.

**Proprietary funds.** The Municipality's proprietary funds provide the same type of information found in the government-wide statements but in more detail. The net position of SGME at the end of the fiscal year amounted to a deficit of $270,464. Revenues of the Municipal Enterprise consists mainly from charges for services – admission fees and sales of food and general merchandise. Expenses consist of salaries and fringe benefits, utilities, advertising, cost of sales, repairs and maintenance and other operating expenses, as well as some nonoperating expenses. SGME started formal operations in July, 2015.

## *GENERAL FUND BUDGETARY HIGHLIGHTS*

The Municipal budget is prepared for the General Fund following the requirements of the Autonomous Municipal Law of 1991, as amended. In order to demonstrate compliance with budget regulations and accounting standards, the Municipality presents a budgetary comparison schedule of the general fund as a required supplementary information. This schedule is prepared under a budgetary basis of accounting, which is different from accounting principles generally accepted in the United States of America ("US GAAP"). Revenues are generally recorded when cash is received and expenditures are generally recorded when the related expenditure is incurred or encumbered. The general fund original budget for the fiscal year 2015-2016 presented a decrease of $722,099 with respect to the prior year original budget. Actual revenues were less than expected final budgetary revenues by $1,808,512 (net). The Municipality also reported a positive variance of $825,790 between revised budgeted appropriations and actual expenditures. Actual expenditures exceeded actual revenues by $980,893 (including the transfer-out of $1,316,893 of which $1,114,905 is for debt service).

## *CAPITAL ASSET AND DEBT ADMINISTRATION*

**Capital assets -** At the end of the fiscal year, the Municipality has invested $72,971,975 (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 2% from the prior year. The following **TABLE 4** discloses the capital assets balances as of June 30, 2016:

**TABLE 4**

| *Capital Assets, net As of June 30,* | Governmental Activities | |
|---|---|---|
| | **2016** | **2015** |
| **Nondepreciable assets:** | | |
| Land | $ 8,214,356 | $ 8,214,356 |
| Construction in progress | 1,823,251 | 1,496,066 |
| **Depreciable assets (net):** | | |
| Buildings and buildings improveme | 48,436,231 | 50,176,757 |
| Equipment | 3,654,975 | 3,430,390 |
| Roads | 6,639,412 | 6,451,142 |
| Bridges | 4,203,750 | 4,369,223 |
| **Total:** | $ 72,971,975 | $ 74,137,934 |

The Municipality's major capital projects that were still in construction and the related construction in progress cost as of June 30, 2016 are as follows:

- Sabana Eneas Baseball Park," with $831,830 costs incurred as of year-end. Project is currently financed through Commonwealth's agencies grants and long-term debt issuance.
- The remodeling of the Santiago R. Palmer Convention Center, with $281,264 costs incurred as of year-end. Project is currently financed through Commonwealth's grants.
- Improvements to storm drainage system and infrastructure in the "Rosario Peñon" community with $119,263 costs incurred as of year-end. This construction is being financed with state grants.

- Additional improvements to the "water park" with $136,716 of costs incurred as of year-end. Project is being financed with long-term debt issuance.
- Improvements to "Poblado Rosario", Santa Maria and El Recreo residential communities' basketball courts, with combined costs of $190,376 incurred as of year-end. Projects are currently financed through Federal grants and long-term debt issuance.

Finally, the Municipality acquired equipment amounting to $311,940, composed mainly of vehicles for $88,826, air conditioning units with their electrical installation for $50,495, an amusement park module for $34,800, and a great variety of modules and office equipment.

The Municipality's fiscal year 2015-2016 capital budget calls for a significant amount of projects including the continued improvements to the Surf and Fun Water Park; the continuance of the construction of the Sabana Eneas baseball park, with an estimated total cost of $1,120,000; and the completion to the improvements to various sports and recreational areas.

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

**Long-term debt -** At year-end, the Municipality had $36,463,000 in general and special bonds and notes. Long-term debt decreased 3% to $88,124,078 with respect to 2015. This change primarily arises from the payment of the general, special obligations bonds and notes during the year, by the payment of the payable to PREPA, and a significant decrease in the debt from property tax advances. These decreases were partially offset by the new PRASA debt refinance accounted at June 30, 2016. The Municipality entered into an agreement with the PRASA to refinance current and old debt with the agency for a total amount of $538,524. Finally, the ERS has not issued audited financial statements as of and for the fiscal year ended June 30, 2015 nor has provided to the Municipality the required information to record transactions related to ***GASB Statement No. 68*** as of and for the fiscal year ended June 30, 2016. Amounts reported in the government-wide financial statements as net pension liability is the same amount reported in the 2015 financial statements. The following is a summary of the Municipality's outstanding debt as of June 30, 2016 and 2015:

**TABLE 5**

***Outstanding Long-term debt***
***Fiscal years ended June 30,***

| | Governmental Activities | |
|---|---|---|
| | **2016** | **2015** |
| General and special obligation bonds and notes | $ 36,463,000 | $ 37,471,000 |
| Payable to CRIM: | | |
| Financing of delinquent accounts | 77,154 | 81,976 |
| Property tax advances | 192,004 | 718,879 |
| Compensated absences | 3,645,131 | 3,641,726 |
| Christmas bonus payable | 350,898 | 364,417 |
| Claims and judgments | 25,000 | - |
| Payable To PREPA | - | 1,988,304 |
| Debt to be refinanced (PRASA) | 538,524 | - |
| COFIM - sales tax advances | 42,862 | 16,707 |
| Net pension liability | 46,789,505 | 46,789,505 |
| **Total:** | $ 88,124,078 | $ 91,072,514 |

More detailed information about the Municipality's long-term liabilities is presented in Note G to the financial statements.

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

The Commonwealth of Puerto Rico and its instrumentalities are currently facing a severe fiscal and liquidity crisis. Continued operational deficits and lack of access to capital markets have resulted in delays in the repayment of loans outstanding by the Commonwealth and its instrumentalities with GDB. This in turn have affected the GDB's liquidity position and the ability to repay its obligations. Although GDB took a number of liquidity enhancing and conservation measures, they were not sufficient to maintain GDB's operations in the ordinary course. The risks and uncertainties facing GDB, the Commonwealth and its instrumentalities and other factors described in the most recent GDB's audited financial statements have led management to conclude that there is a substantial doubt as to the ability of GDB to continue as a going concern. Pursuant to the moratorium Acts and several executive orders issued by the former and actual Commonwealth's Governors, the certain Commonwealth's entities, including GDB, were declared in a state of emergency. Regarding GDB, the Commonwealth implemented a regulatory framework governing its's operations and liquidity by prohibiting loan disbursements and establishing a procedure with respect to withdrawals, payments and transfer requests with respect of funds held on deposits by the Commonwealth and its instrumentalities, including the Municipalities. The withdrawal, payment and transfer of funds held on deposit at GDB are restricted to those reasonable and necessary to ensure the provision of essential services.

As part of the requirements of PL 114-187 known as the *Puerto Rico Oversight, Management and Economic Stability Act* ("PROMESA"), on February 21, 2017 and February 28, 2017 GDB, other Commonwealth entities as well as the Commonwealth itself submitted drafts of it fiscal plans to the *Financial Oversight and Management Board for Puerto Rico* ("the Board") for evaluation and approval. The Commonwealth's fiscal plan was approved by the Board on March 13, 2017. The final plans and future role of the other governmental entities, including GDB, is uncertain since the drafts are still under evaluation by the Board. The Commonwealth's approved fiscal plan discusses important reforms that may have a significant impact on the municipalities' finances as follows:

- **Modernization the property tax regime** - proposed measures will gradually eliminate the Commonwealth's $350MM subsidy to the municipalities and provide municipalities with a modernized property tax regime in order to fill the gap. The Commonwealth expects that the new system will produce a total of $426 million in revenues, at least $350 million to the municipalities and approximately $76 million to the central government

- **Retirement plans reform** - the Plan includes a comprehensive reform of the retirement plans including switch to pay-as-you-go model to cover remaining defined benefit obligations, segregate prospective employee contributions into new and separated defined contribution plans, facilitate enrollment in social security for qualifying participants and improve investment alternatives offered to participants. As the municipalities role as a participating employer of ERS, some of these initiatives such as switching to a pay-as-you-go model and the enactment of a new and separated defined contribution plan may have a significant impact in the municipalities fiscal operations.

- **Health reform** - the Plan includes a reform of the Governmental Health Insurance Plan ("Plan Mi Salud"). At present, the municipalities contribute to the Puerto Rico Health Insurance Administration ("ASES") to fund Plan Mi Salud through budgetary appropriations for direct health services in areas covered by the government health plan. The final impact of the health care reform on the Municipality's financial position or operations cannot be determined.

The Municipality's officials considered certain factors when establishing the fiscal year's 2016-2017 budget. One of these factors is the economy. Among economic areas considered are the estimates for the growth or decline in population, personal income, housing statistics and unemployment rates. The Municipality's unemployment rate at the end of fiscal year 2016 stands at 14.1%, and the Commonwealth rate stands at 10.8%.

For year 2016-2017 the Municipality applied a conservative approach in the development of budget estimates. Amounts available for appropriations in the General Fund are $19,045,122 representing an increase of approximately 3% with respect to prior year estimates. If these estimates are realized, the Municipality's budgetary general fund balance is expected to increase modestly by the close of the 2016-2017 fiscal year. In addition to the general fund estimated budget the Municipality plans to submit to the Federal and Commonwealth government fund proposals for welfare and community development as well as permanent capital improvements and public works.

## *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 Germán, Puerto Rico 00683.

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**STATEMENT OF NET POSITION**
**JUNE 30, 2016**

| | Primary Government | | |
|---|---|---|---|
| | Governmental Activities | Business-type Activities | Total |
| **ASSETS** | | | |
| Cash and cash equivalents in commercial banks | $ - | $ 218,474 | $ 218,474 |
| Cash in governmental bank | 468,291 | - | 468,291 |
| Receivables (net of allowance for uncollectibles): | | | |
| Municipal license taxes | 184,137 | - | 184,137 |
| Rents and construction permits | 192,587 | - | 192,587 |
| Due From: | | | |
| Commonwealth Government | 289,970 | - | 289,970 |
| Federal Government | 165,066 | - | 165,066 |
| Prepaid expenses | - | 99,130 | 99,130 |
| Restricted Assets: | | | |
| Cash and cash equivalents with commercial banks | 4,086,953 | - | 4,086,953 |
| Cash with fiscal agents | 7,862,496 | - | 7,862,496 |
| Other assets | 309,812 | - | 309,812 |
| Capital assets: | | | |
| Land and construction in progress | 10,037,607 | - | 10,037,607 |
| Other capital assets, net | 62,934,368 | - | 62,934,368 |
| Total capital assets, net | 72,971,975 | - | 72,971,975 |
| **Total assets** | $ 86,531,285 | $ 317,604 | $ 86,848,889 |
| **DEFERRED OUTFLOWS OF RESOURCES** | | | |
| Deferred outflows related to pension | 2,781,626 | - | 2,781,626 |
| **Total deferred outflows of resources** | 2,781,626 | - | 2,781,626 |
| **LIABILITIES** | | | |
| Accounts payable and accrued liabilities | 2,988,488 | 588,068 | 3,576,556 |
| Interest payable | 978,789 | - | 978,789 |
| Due to: | | | |
| Commonwealth Government | 136,627 | - | 136,627 |
| Federal Government | 2,256 | - | 2,256 |
| Unearned revenues | 199,017 | - | 199,017 |
| Long term liabilities: | | | |
| Due within one year | 2,190,148 | - | 2,190,148 |
| Due in more than one year | 85,933,930 | - | 85,933,930 |
| **Total liabilities** | 92,429,256 | 588,068 | 93,017,324 |
| **DEFERRED INFLOW OF RESOURCES** | | | |
| Municipal license taxes received in advance | 1,889,987 | - | 1,889,987 |
| Deferred inflows related to pension | 374,429 | - | 374,429 |
| **Total deferred inflows of resources** | 2,264,416 | - | 2,264,416 |
| **NET POSITION** | | | |
| Net investment in capital assets | 38,929,009 | - | 38,929,009 |
| Restricted for: | | | |
| Capital projects | 2,889,032 | - | 2,889,032 |
| Debt service | 4,132,660 | - | 4,132,660 |
| Other specified purposes | 145,636 | - | 145,636 |
| Unrestricted (deficit) | (51,477,097) | (270,464) | (51,747,562) |
| **Total net position** | $ (5,380,760) | $ (270,464) | $ (5,651,224) |

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, 2016**

| | | Program Revenues | | | Net (Expenses) Revenues and Changes in Net Position | | |
|---|---|---|---|---|---|---|---|
| | | | | | Primary Government | | |
| **Functions** | **Expenses** | **Fees, Fines and Charges for Services** | **Operating Grants and Contributions** | **Capital Grants and Contributions** | **Governmental Activities** | **Business-type Activities** | **Total** |
| **Governmental activities:** | | | | | | | |
| General government | $ 6,162,411 | $ 1,245,518 | $ 182,217 | $ - | $ (4,734,676) | $ - | $ (4,734,676) |
| Public safety | 1,772,879 | - | 93,175 | - | (1,679,704) | - | (1,679,704) |
| Public works | 12,165,503 | 3,672,881 | 8,576 | 771,788 | (7,712,258) | - | (7,712,258) |
| Sanitation | 80,795 | - | - | - | (80,795) | - | (80,795) |
| Health | 786,763 | - | - | - | (786,763) | - | (786,763) |
| Welfare | 3,619,783 | 1,748,423 | 1,466,490 | - | (404,870) | - | (404,870) |
| Culture and recreation | 696,496 | - | - | - | (696,496) | - | (696,496) |
| Education | 2,067,844 | - | 2,317,179 | - | 249,335 | - | 249,335 |
| Interest on long-term debt | 1,967,544 | - | - | - | (1,967,544) | - | (1,967,544) |
| Total government activities | $ 29,320,018 | $ 6,666,821 | $ 4,067,637 | $ 771,788 | (17,813,772) | - | (17,813,772) |
| **Business-type activities:** | | | | | | | |
| San German Municipal Enterprise, Inc. | 3,698,395 | 3,437,176 | - | - | - | (261,219) | (261,219) |
| **Total business-type activities** | 3,698,395 | 3,437,176 | - | - | - | (261,219) | (261,219) |
| **Total primary government** | $ 33,018,413 | $ 10,103,997 | $ 4,067,637 | $ 771,788 | (17,813,772) | (261,219) | (18,074,990) |
| **General Revenues:** | | | | | | | |
| Taxes: | | | | | | | |
| Property taxes | | | | | 5,531,133 | - | 5,531,133 |
| Municipal license taxes | | | | | 3,221,667 | - | 3,221,667 |
| Sales and use taxes | | | | | 2,063,596 | - | 2,063,596 |
| Grants and contributions not restricted to specific programs | | | | | 5,246,482 | - | 5,246,482 |
| Interest | | | | | 225,285 | - | 225,285 |
| Other | | | | | 703,465 | - | 703,465 |
| Total general revenues | | | | | 16,991,628 | - | 16,991,628 |
| **Change in net position** | | | | | (822,144) | (261,219) | (1,083,363) |
| **Net position at beginning of fiscal year** | | | | | (4,558,616) | (9,245) | (4,567,862) |
| **Net position at end of fiscal year** | | | | | $ (5,380,760) | $ (270,464) | $ (5,651,224) |

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, 2016**

| | Major Funds | | | | |
|---|---|---|---|---|---|
| | General | Debt Service | Surf and Fun Water Park | Other Governmental Funds | Total Governmental Funds |
| **Assets** | | | | | |
| Cash in governmental bank | $ 468,291 | $ - | $ - | $ - | $ 468,291 |
| Receivables (net of allowance for uncollectibles): | | | | | |
| Municipal license taxes | 184,137 | - | - | - | 184,137 |
| Rents, construction permits and others | 180,402 | - | - | 12,186 | 192,587 |
| Due from: | | | | | |
| Commonwealth Government | 81,491 | 162,573 | - | 45,906 | 289,970 |
| Federal Government | - | - | - | 165,066 | 165,066 |
| Other funds | 417,618 | - | - | 27,205 | 444,824 |
| Advances to other funds | 529,032 | - | - | - | 529,032 |
| Restricted Assets: | | | | | |
| Cash and cash equivalents with commercial banks | - | - | 32,478 | 4,054,475 | 4,086,953 |
| Cash in governmental bank | - | 4,948,877 | 1,058,845 | 1,854,774 | 7,862,496 |
| Other assets | 309,812 | - | - | - | 309,812 |
| **Total assets** | $ 2,170,782 | $ 5,111,449 | $ 1,091,323 | $ 6,159,612 | $ 14,533,166 |
| **Liabilities, Deferred Inflows of Resources and Fund Balances (deficit)** | | | | | |
| **Liabilities:** | | | | | |
| Accounts payable and accrued liabilities | $ 1,812,873 | $ - | $ 62,483 | $ 1,113,132 | $ 2,988,488 |
| Matured bonds and interest payable | - | 1,714,691 | - | - | 1,714,691 |
| Due to: | | | | | |
| Commonwealth Government | 136,627 | - | - | - | 136,627 |
| Federal Government | - | - | - | 2,256 | 2,256 |
| Other funds | 27,205 | - | - | 417,618 | 444,824 |
| Advances from other funds | - | - | - | 529,032 | 529,032 |
| Unearned revenues | - | - | - | 199,017 | 199,017 |
| **Total liabilities** | 1,976,705 | 1,714,691 | 62,483 | 2,261,056 | 6,014,935 |
| **Deferred inflows of resources** | | | | | |
| Municipal license taxes received in advance | 1,889,987 | - | - | - | 1,889,987 |
| Unavailable revenues: | | | | | |
| Commonwealth Government Funds | 81,491 | 72,335 | - | 45,907 | 199,732 |
| Other | 221,485 | - | - | - | 221,485 |
| **Total deferred inflows of resources** | 2,192,962 | 72,335 | - | 45,907 | 2,311,203 |
| **Fund balances (deficit):** | | | | | |
| Nonspendable | 529,032 | - | - | - | 529,032 |
| Restricted | - | 3,324,423 | 1,028,840 | 4,234,094 | 8,587,358 |
| Unassigned | (2,527,917) | - | - | (381,445) | (2,909,362) |
| **Total fund balances (deficit)** | (1,998,885) | 3,324,423 | 1,028,840 | 3,852,649 | 6,207,027 |
| **Total liabilities, deferred inflows of resources and fund balances (deficit)** | $ 2,170,782 | $ 5,111,449 | $ 1,091,323 | $ 6,159,612 | $ 14,533,166 |

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

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS**
**TO THE STATEMENT OF NET POSITION**
**JUNE 30, 2016**

| | | |
|---|---|---|
| **Total governmental fund balances:** | | **$ 6,207,027** |
| Amounts reported for governmental activities in the Statement of Net Position are different because: | | |
| Capital assets used in governmental activities are not current financial resources and, therefore, are not reported in the governmental funds balance sheet | | 72,971,975 |
| Other assets are not available to pay current-period expenditures and, therefore, are reported as deferred inflows of resources in the funds: | | |
| Receivables, due from Commonwealth and Federal Government: | | |
| Municipal license taxes | $ 116,913 | |
| Construction permits | 24,190 | |
| Rent - properties | 34,224 | |
| Rent - land lots | 46,158 | |
| CRIM - Property taxes (Debt Service Fund) | 72,335 | |
| P.R. Department of Labor- Law No. 52 | 45,907 | |
| P.R. Department of Treasury - Christmas bonus reimbursement | 81,491 | 421,218 |
| Deferred outflows of resources related to pensions not recognized in the governmental funds balance sheet: | | 2,781,626 |
| Interest liabilities are not due and payable in the current period and, therefore, are not reported in the funds: | | (59,098) |
| 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 | (35,668,000) | |
| Compensated absences | (3,645,130) | |
| Claims and judgments | (25,000) | |
| Note payable to CRIM - delinquent accounts | (77,154) | |
| Payable to AAA | (538,524) | |
| Christmas bonus | (350,899) | |
| Payable to CRIM- Property taxes advances | (192,004) | |
| Net pension liability | (46,789,505) | |
| Payable to COFIM- Sales taxes advances | (42,863) | (87,329,079) |
| Deferred inflows of resources related to pensions not recognized in the governmental funds balance sheet: | | (374,429) |
| **Net position of governmental activities** | | **$ (5,380,759)** |

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, 2016

| | Major Funds | | | | |
|---|---|---|---|---|---|
| | General | Debt Service | Surf and Fun Water Park | Other Governmental Funds | Total Governmental Funds |
| **Revenues:** | | | | | |
| Taxes: | | | | | |
| Property taxes | $ 2,774,029 | $ 2,928,774 | $ - | $ - | $ 5,702,803 |
| Municipal license taxes | 3,360,481 | - | - | - | 3,360,481 |
| Sales and use taxes | 1,752,637 | 444,941 | - | - | 2,197,578 |
| Intergovernmental: | | | | | |
| Commonwealth Government | 5,249,621 | - | - | 995,284 | 6,244,904 |
| Federal Government | - | - | - | 3,890,192 | 3,890,192 |
| Rental income and charges for services | 6,784,761 | - | - | 1,837,513 | 8,622,274 |
| Fines and forfeitures | 8,334 | - | - | - | 8,334 |
| Interest | 103,090 | 19,629 | 18,773 | 83,794 | 225,285 |
| Other | 122,740 | - | - | 37,053 | 159,793 |
| **Total Revenues** | 20,155,692 | 3,393,344 | 18,773 | 6,843,836 | 30,411,644 |
| **Expenditures:** | | | | | |
| Current: | | | | | |
| General government | 8,180,380 | - | 85,799 | 77,543 | 8,343,723 |
| Public safety | 1,359,882 | - | - | 331,237 | 1,691,119 |
| Public works and sanitation | 8,572,027 | - | - | 1,274,112 | 9,846,138 |
| Health | 786,763 | - | - | - | 786,763 |
| Welfare | 525,253 | - | - | 3,057,576 | 3,582,828 |
| Culture and recreation | 590,967 | - | 77,442 | 11,347 | 679,756 |
| Education | 9,256 | - | - | 2,058,589 | 2,067,844 |
| Capital outlays | 2,594 | - | 547,920 | 918,612 | 1,469,126 |
| Debt service: | | | | | |
| Principal | - | 925,000 | - | - | 925,000 |
| Interest | - | 1,942,906 | 6,625 | 78,220 | 2,027,752 |
| **Total expenditures** | 20,027,122 | 2,867,906 | 717,786 | 7,807,236 | 31,420,050 |
| **Excess (deficiency) of revenues over expenditures** | 128,570 | 525,437 | (699,013) | (963,400) | (1,008,406) |
| **Other financing sources (uses):** | | | | | |
| Note payable issuance - P.R. Water and Sewer Authority | 538,524 | - | | - | 538,524 |
| Payment of debt - COFIM | (16,708) | - | | - | (16,708) |
| Transfers - in | 1,394,905 | 1,316,455 | 43,131 | - | 2,754,491 |
| Transfers - (out) | (1,359,585) | (1,114,905) | - | - | (2,474,491) |
| **Total other financing sources (uses)** | 557,136 | 201,550 | 43,131 | - | 801,817 |
| **Net change in fund balances (deficit)** | 685,706 | 726,987 | (655,882) | (963,400) | (206,589) |
| **Fund balance at beginning of fiscal year** | (2,684,592) | 2,597,436 | 1,684,722 | 4,816,049 | 6,413,616 |
| **Fund balance at end of fiscal year** | $ (1,998,885) | $ 3,324,423 | $ 1,028,840 | $ 3,852,649 | $ 6,207,027 |

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 FUND BALANCES (DEFICIT) - GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES**
**FISCAL YEAR ENDED JUNE 30, 2016**

| | | |
|---|---|---|
| **Net change in fund balances (deficit) - total governmental funds:** | | **$ (206,589)** |
| 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: | $ 1,469,126 | |
| Less: current year depreciation | (2,622,785) | (1,153,659) |
| 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: | | (12,300) |
| Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the funds: | | |
| Municipal license tax (net change) | 116,912 | |
| CRIM - Property taxes (Debt Fund) | 72,335 | |
| Construction permits | 24,190 | |
| Rent (net change) | 25,355 | |
| P.R. Department of Treasury - Law No. 52 | 45,907 | |
| P.R. Department of Treasury - Christmas bonus reimbursement | 81,491 | 366,190 |
| Revenues reported in funds which are not reported as revenues in the Statement of Activities: | | |
| CRIM - Property taxes (Debt Service Fund) (prior year) | (206,018) | |
| Rent | (3,916) | |
| Sales and use taxes (Debt Service Fund) (prior year) | (55,439) | |
| Sales and use taxes (General Fund) (prior year) | (35,680) | |
| Municipal license tax (net change) | (255,726) | |
| P.R. Electric Power Authority (PREPA) (prior year) | (1,988,305) | |
| Rent- land lots | (21,110) | |
| P.R. Department of Treasury - Christmas bonus reimbursement (prior year) | (84,630) | |
| P.R. Department of Treasury - Law No. 52 | (91,958) | (2,742,782) |
| Expenditures reported in funds which are not reported as expenses in the Statement of Activities: | | |
| Matured bonds principal payments (net change) | | (23,000) |
| Repayment of long-term debt consumes the current financial resources of governmental funds, but has no effect on net position of governmental activities: | | |
| General obligation bonds and notes | 1,008,000 | |
| Other long term liabilities | 3,306,411 | 4,314,411 |
| 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: | | |
| Claims and judgments | (25,000) | |
| Accrued interest (net change) | 1,560 | |
| Compensated absences | (370,703) | |
| Christmas bonus | (350,899) | |
| P.R. Acueduct & Sewer Authority (AAA) | (538,524) | |
| Property tax advances | (37,987) | |
| Sales tax advances | (42,863) | (1,364,416) |
| **Change in net position of governmental activities** | | **$ (822,144)** |

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

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

**STATEMENT OF NET POSITION - PROPRIETARY FUND**

**JUNE 30, 2016**

| | Business-type Activities - Enterprise Fund San German Municipal Enterprise, Inc. |
|---|---|
| **Assets** | |
| Current assets: | |
| Cash | $ 218,474 |
| Prepaid expenses | 99,130 |
| **Total Current Assets** | 317,604 |
| **Total assets** | 317,604 |
| **Liabilities and net position** | |
| **Liabilities** | |
| Current liabilities: | |
| Accounts payable trade | 250,506 |
| Accounts payable other | 39,185 |
| Accrued liabilities | 239,545 |
| Note payable | 58,832 |
| **Total current liabilities** | 588,068 |
| **Total liabilities** | 588,068 |
| **Net position** | |
| Unrestricted (deficit) | (270,464) |
| **Total net position** | $ (270,464) |

**The accompanying notes are an integral part of this statement.**

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

**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION -**

**PROPRIETARY FUND**
**FISCAL YEAR ENDED JUNE 30, 2016**

| | Business-type Activities - Enterprise Fund<br>San German Municipal Enterprise, Inc. |
|---|---|
| **Operating revenues** | |
| Fees and charges for services | $ 3,437,176 |
| **Total operating revenues** | 3,437,176 |
| **Operating expenses** | |
| Salaries and fringe benefits | 1,315,133 |
| Utilities | 316,651 |
| Advertising | 499,804 |
| Merchandise for sale | 315,324 |
| Insurance | 239,991 |
| Profesional services | 225,839 |
| Supplies | 115,101 |
| Repairs and maintenance | 247,652 |
| Other | 137,454 |
| | 3,412,949 |
| **Operating income** | 24,227 |
| **Nonoperating revenues (expenses)** | |
| Transfers from (to) other funds | (280,000) |
| Interest expense | (6,502) |
| Interest income | 1,056 |
| **Total nonoperating expenses, net** | (285,446) |
| **Change in net position** | (261,219) |
| **Net position at beginning of year** | (9,245) |
| **Net position at end of year** | $ (270,464) |

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**STATEMENT OF CASH FLOWS -**
**PROPRIETARY FUND**
**FISCAL YEAR ENDED JUNE 30, 2016**

| | Business-type Activities - Enterprise Fund San German Municipal Enterprise, Inc. |
|---|---|
| **Cash flows from operating activities:** | |
| Receipts from fees and charges for services | $ 3,389,534 |
| Other receipts | 47,980 |
| Payments to suppliers and service providers | (1,619,299) |
| Payments to employees for salaries and benefits | (1,314,342) |
| **Net cash provided by operating activities** | 503,873 |
| **Cash flows from noncapital financing activities:** | |
| Transfers to the Municipality | (280,000) |
| Principal payment on note payable | (25,907) |
| Interest paid | (6,502) |
| **Net cash used in noncapital and financing activities** | (312,409) |
| **CASH FLOW FROM INVESTING ACTIVITIES** | |
| Interest | 1,056 |
| Net cash provided by investing activities | 1,056 |
| **Net increase in cash** | 192,520 |
| **Cash at beginning of year** | 25,954 |
| **Cash at end of year** | $ 218,474 |
| **Reconciliation of operating income (loss) to net cash provided by (used in) operating activities** | |
| Operating income | $ 24,227 |
| Adjustments to reconcile change in net position to net cash provided by operating activities: | |
| Increase (decrease) in: | |
| Insurance paid | (42,637) |
| Accounts payable trade | 217,611 |
| Accounts payable other | 36,881 |
| Accrued liabilities | 239,545 |
| Insurance amortization | 28,246 |
| Total Adjustments | 479,646 |
| **Net cash provided by operating activities** | $ 503,873 |

**The accompanying notes are an integral part of this statement.**

## 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 Germán (the primary government) and component units, if any. A primary government is any state government or general purpose local government (a municipality). All funds, organizations, institutions, agencies, departments, and offices that are not legally separate are, for financial reporting purposes, part of a primary government. If an organization is part of a primary government, its financial data should be included with the financial data of the primary government. Component units are legally separate organizations for which the primary government is financially accountable or organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. A component unit may be a governmental organization, a nonprofit corporation or a for-profit corporation.

The following circumstances set forth a primary government's financial accountability for a legally separate organization:

- The primary government appoints a voting majority of the entity's governing body, and either:
  - A financial benefit/ burden exists between the primary government and the entity or
  - The primary government can impose its will on the entity.

  The entity is fiscally dependent on the primary government and there is a financial benefit/burden between the primary government and the entity.

- In addition, as described above, it would be necessary to include other organizations as a component unit if the exclusion would cause the primary government's financial statements to be misleading or incomplete. Organizations that are legally separate, tax-exempt entities and that meet all of the following criteria should be *discretely* presented as component units:

  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.

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

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.

Professional judgment should be applied in determining whether the relationship between a primary government and other organizations for which the primary government is not financially accountable and that do not meet the above criteria is such that exclusion of the organization would render the financial statements of the reporting entity 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 and (b) *discrete* presentation of the component unit's financial data. When a component unit functions as an integral part of the primary government, its data is *blended* with those of the primary government ("*blended component units*"). That is, the component unit's funds are treated just as though they were funds of the primary government with one exception: the general fund. Component units should be reported as *blended* if meets any of the following criteria:

a. The component unit's governing body is substantively the same as the governing body of the primary government and there is either:

   - A financial benefit/ burden exists between the primary government and the entity or
   - Management of the primary government has operational responsibility for the component unit.

b. The component unit provides services entirely, or almost entirely, to the primary government or otherwise exclusively, or almost exclusively, benefits the primary government.

c. The component unit's debt is expected to be paid by the primary government.

Otherwise, the component unit should be presented as *discrete*. Those component units does not function as an integral part of the primary government and its data is presented discretely (separately) from the data of the primary government ("*discretely component units*"). As discussed earlier, other legally separate, tax-exempt organizations that meet the applicable criteria should be included as *discretely component units.*

Based on the above criteria the following component unit, while legally separated from the Municipality, meet the blending criteria to be reported as part of the primary government financial statements:

**"San Germán Municipal Enterprise, Inc." ("SGME")** – is a domestic for-profit municipal enterprise organized pursuant Article 2.004 (u) of the Autonomous Municipalities Act No. 81 of 1991 as amended. It was created through the Municipal Legislature Ordinance No. 31 Series 2011-2012 to operate the "San Germán Surf N' Fun Water Park" ("the Waterpark"). As required by law, it is governed by a Board of Directors composed of five (5) members (all Municipal officer's members of the executive branch) appointed by the Mayor (except for the Finance Director whose membership is compulsory). The Waterpark started operations and services to the general public on July, 2015. The Municipality appoints a voting majority of SGME's board of directors, has the ability to impose its will on the organization and provide significant financial support to finance its operating expenses. The Municipality owns the major capital assets that SGME use to operate the Waterpark including land, machinery and equipment and has issued all related long-term debt used to finance those capital assets. Furthermore, the Municipality is legally entitled to the SGME resources. Twenty-five percent (25%) of the SGME's profits shall be maintained and used for operational expansion or additional jobs creation and the remaining 75% shall be transferred to the Municipality.

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

The financial statements of SGME are blended into the Municipality's financial statements as an enterprise fund since (1) the governing body of SGME is in substance the same of the Municipality and (2) the significant financial support the Municipality provides to SGME to finance its operating expenses.

SGME issued separate compiled financial statements as of and for the year ended June 30, 2016 which can be obtained directly by contacting it administrative office at P.O. Box 85 San Germán, P.R. 00683.

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.

**Government-wide statements**

The government-wide statements consist of a Statement of Net Position and a Statement of Activities. These statements are prepared using the economic resources measurement focus, which refers to the reporting of all of the net position available to the governmental unit for the purpose of providing goods and services to the public. 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 Position presents all of the reporting entity's non-fiduciary assets, deferred outflows, liabilities and deferred inflows, with the difference reported as net position. 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 direct expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. Direct expenses are those that are clearly identifiable with a specific function. As a policy, indirect expenses are not allocated in the Statement of Activities. 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.

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

Likewise, general revenues include all taxes. Property taxes are considered imposed non-exchange transactions since are based on assessments imposed by the Municipality that are not based on exchange transactions. Property taxes are recognized as revenues in the year for which the taxes are levied. Municipal license taxes and sales and use taxes are considered derived tax revenues since are taxes imposed by the Municipality based on exchange transactions. Municipal license taxes are recorded as revenues in the period the Municipality has an enforceable legal claim and time requirements are met; sales and use taxes are recognized as revenues in the period when the underlying exchange has occurred. Revenues on both operating and capital grants are recognized when all eligibility requirements (including time requirements) imposed by the provider have been met. For certain expenditure-driven grants, revenue is recognized after allowable expenditures are incurred.

The Municipality reports a liability for unearned revenues in the government-wide statements. Unearned revenues arise when (1) resources received in advance of an exchange transaction, (2) resources received in advance in relation to a derived tax revenue, and (3) resources received in advance related to voluntary non-exchange transactions when eligibility requirements other than time requirements have not been met (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, after related exchange transactions occur or applicable eligibility requirements are met the liability for unearned revenues is removed from the statement of net position and the revenue is recognized.

The government-wide statements are divided into two categories:

*Governmental Activities:* Most of the Municipality's basic services are reported here including: public works and sanitation, public safety, culture and recreation, housing, welfare, and community development, 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.

*Business-type Activities:* Business-type activities charges fees to customers to finance the costs of their activities. The activities of SGME (the only business-type activity) are included here.

### 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, deferred outflows, liabilities, deferred inflows, 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. The fund financial statements provide more detailed information about the Municipality's most significant funds.

The Municipality has two kinds of funds, governmental and proprietary funds, as follows:

*Governmental Funds* - 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 and deferred outflows; liabilities and deferred inflows; revenues or expenditures or based on the Municipality's official's criteria if the fund is particularly important to financial statement users.

## NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

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. This fund accounts for the resources of three individual funds including "Fondo 10 - CAE Redemption Fund" (a special surtax redemption fund established at GDB which accounts for the 2% of property taxes collected by the CRIM); "Fondo 11 - CRIM Fund" (resources transferred from the Municipality's general fund to the CRIM for payment of debt issued for operational purposes) and the "Fondo 12 - IVU Municipal Redemption Fund" (.2% of the .5% from sales and use taxes deposited in the Municipal Administration fund of GDB to finance loans to Municipalities).

**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 Municipality also reports nonmajor governmental funds in a single column, which includes the following:

**Special Revenue Funds:** This fund is used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specific purposes other than debt service or capital projects. The core revenue source of the fund must represent a substantial portion of the fund's total inflows. The limitation on spending (specific purpose) may be imposed by external parties (creditors, grantors, contributors, other governments), by constitutional provisions, by enabling legislation or by action taken by the government's own highest level of decision-making authority.

**Capital Project Funds:** This fund is used to account for and report financial resources that are restricted, committed or assigned to expenditures for capital outlays, including the acquisition or construction of capital facilities and other capital projects. Typically the fund is not used for routine or minor capital outlays (equipment, vehicles, furniture, among others) which are reported instead in the fund from which financial resources were expended. Rather, the fund is used primarily for major projects and acquisitions financed with borrowed or contributed resources. The use of a capital project fund frequently is required by debt covenants, grant contracts, law or regulation.

The governmental 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 the taxes are levied; municipal license taxes, recognized in the period the Municipality has an enforceable legal claim and time requirements are met; and sales and use taxes, recognized when the underlying exchange has occurred, 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),

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

before any amounts are paid to the Municipality. Revenue is, therefore, recognized as expenditures are incurred to the extent available. In the other cases, monies are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. In these cases, revenues are recognized as the time of receipt or earlier if the susceptible to accrual criteria is met. Licenses and permits, charges for services, rent, fines and miscellaneous revenues are generally recorded as revenues when received or are recognized earlier if the susceptible to accrual criteria is met.

The Municipality reports a liability for unearned revenues in the governmental funds statements. Unearned revenues arise when (1) resources received in advance of an exchange transaction, (2) resources received in advance in relation to a derived tax revenue, and (3) resources received in advance related to voluntary non-exchange transactions when eligibility requirements other than time requirements have not been met (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, after related exchange transactions occur or applicable eligibility requirements are met the liability for unearned revenues is removed from the balance sheet and the revenue is recognized.

Expenditures are generally recognized when the related liability is incurred as under accrual basis of accounting. 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) and (2) vested compensated absences, claims and judgments and special termination benefits which are recorded as expenditures only to the extent that they are expected to be liquidated with expendable financial resources (in the government-wide statements the expense and related accrual liability for long-term portions of debt must be included).

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

*Proprietary funds* - Proprietary fund financial statements are accounted for using the economic resources measurement focus and the accrual basis of accounting, as the business-type activities in the government-wide financial statements. Under this method of accounting, revenues are recorded when earned, independently when are collected, and expenses are recorded when incurred, independently when are paid. Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the proprietary funds are charges to customers for services. Operating expenses for the funds include the cost of operations and maintenance, administration and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. The proprietary fund statements include a Statement of Net Position, a Statement of Revenues, Expenditures and Changes in Net Position and a Statement of Cash Flows.

The Municipality's proprietary funds consist of one enterprise fund. Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent is that the cost of providing goods and services be financed or recovered primarily through user charges. Major Enterprise funds are determined based on a minimum criterion, that is, a percentage of the assets, liabilities, revenues or expenses or based on the Municipality's official's criteria if the fund is particularly important to financial statement users.

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

The Municipality reports the following major enterprise fund:

**San Germán Municipal Enterprise, Inc. Fund:** This fund, a blended component unit, was created as a Municipal Enterprise to provide an entertainment and tourism alternative for the general public. The organization finance its operations from charges from services and sales to the general public.

**NOTES TO BASIC FINANCIAL STATEMENTS**

The NOTES TO BASIC FINANCIAL STATEMENTS provide information that is essential to a user's understanding of the basic financial statements.

**Required Supplementary Information:**

Consists of the Budgetary Comparison Schedule – General Fund, the Schedule of Municipality's Proportionate Share of Net Pension Liability and the Schedule of Municipality's Contributions, as required by GASB.

3. ***Cash deposits and investments (unrestricted and restricted)***

**Governmental activities** - The Municipality invest its available cash in checking bank accounts and certificates of deposits. 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 equivalents consist of nonnegotiable certificates of deposits 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 and are recorded at cost.

Unrestricted cash in governmental bank consists of nonnegotiable certificates of deposits with original maturity of more than three months held at the Governmental Development Bank for Puerto Rico ("GDB").

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 in governmental bank in the debt service fund consists of the undisbursed balance of some of the property and sales and use tax collections retained by the CRIM and 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, held at GDB. Restricted cash in governmental bank of other governmental funds represent the undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account at GDB.

**Business-type activities** - Cash includes cash on hand and cash in bank accounts.

4. ***Restricted assets***

**Governmental activities** - 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.

## NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

### 5. *Receivables and due from governmental entities*

**Governmental activities** - 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 and use tax) on the subsequent fiscal year.

### 6. *Interfund transactions*

The Municipality reports inter-fund transactions as follows:

| | |
|---|---|
| **Inter-fund loans:** | Represent legally advances that are representative of lending/borrowing arrangements from one fund to other fund to finance payroll, payroll taxes and other expenditures. The current portion of such transactions are referred as to either "due from/to other funds" and the noncurrent portion as "advances to/from other funds". Amounts not expected to be collected within a reasonable period of time are reduced to the estimated realizable value and amounts not expected to be repaid are reported as "transfer-out" from the lender fund and "transfer-in" in the borrower fund. |
| **Inter-fund transfers:** | Represent legally flows of assets without equivalent flows of assets in return and without a requirement for repayment. These are reported as "transfers-out" (other financing uses) in the fund that issue the transfers and as "transfers-in" (other financing sources) in the fund receiving the transfers. |
| **Inter-fund reimbursements:** | Represent repayment from a fund responsible for particular expenditures or expenses to the fund that initially finance them. |

### 7. *Inventories*

**Governmental activities** - 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 Position, as management believes is not significant.

### 8. *Capital assets*

**Governmental activities** - Capital assets reported in the governmental activities in the Statements of Net Position 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 measured at acquisition value at the date of donation. Acquisition value is the price that would be paid to acquire an asset with equivalent service capacity in an orderly market transaction at the acquisition date.

## NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

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

| Description | Years |
|---|---|
| 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.

### 9. *Long-term obligations*

**Governmental activities** - Long-term debt and other long-term obligations, which are reported as liabilities in the governmental activities column in the Statement of Net Position, consist of general and special obligation bonds, liabilities for compensated absences, claims and judgments, and long-term liabilities to other governmental entities. Related bond issuance costs, whenever rise, are reported as current outflows of resources in the Statement of Activities, 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.

### 10. *Compensated absences*

**Governmental activities** - 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.

## NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

### *11. Claims and judgments*

The liability and expense amounts for claims and judgments are recorded in the government-wide statements as incurred or when a loss is probable and the amount can be reasonably estimated. Amounts are recorded as liabilities and expenditures in the general fund when they mature (generally, when payment is due).

### *12. Accounting for pension costs*

The Municipality accounts for pension costs in accordance with the requirements of ***GASB Statement No. 68*** *"Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27"* as a participant employer of the retirement plans administered by the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). Accordingly, pension costs are reported based on its proportional share of the collective net pension liability, pension expense and deferred outflows/inflows of resources reported by the Plan.

For purposes of measuring, (1) the net pension liability, (2) deferred outflows of resources related to pensions, (3) deferred inflows of resources related to pensions, (4) pension expense, (5) information about the pension plan's fiduciary net position and (6) additions to/deductions from the plan's fiduciary net position all have been determined on the same basis as they are reported by the Plan. For this purpose, plan member contributions are recognized in the period in which the contributions are due. The Municipality's employer contributions are recognized when due and when the Municipality has a legal requirement to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of Plan. Investments are reported at fair value. In the governmental fund statements pension expense is equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

### *13. Deferred outflows / inflows of resources*

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. In the statement of net position deferred outflows / inflows of resources arise as a result of the following:

a. The implementation of GASB Statement No. 68 "Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27" and GASB Statement No. 71 "Pension Transition for Contributions Made Subsequent to the Measurement Date - an amendment of GASB Statement No. 68"

b. Municipal license taxes ("patentes en suspenso") and voluntary non-exchange transactions (grants) received in advance before time requirements are met are recorded as deferred inflows of resources. The deferred inflow of resources is recognized as inflow of resources (revenues) in the period when time requirements are met.

In the governmental funds balance sheet deferred inflows of resources arise as a result of the following:

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

a. Recognition of unavailable revenue as a result of the application of the modified accrual basis of accounting. The governmental funds report unavailable revenue from one source: unavailable intergovernmental revenues. These amounts are recognized as an inflow of resources (revenue) in the period that the amounts become available.

b. Municipal license taxes ("patentes en suspenso") and voluntary non-exchange transactions (grants) received in advance before time requirements are met are recorded as deferred inflows of resources. The deferred inflow of resources is recognized as inflow of resources (revenues) in the period when time requirements are met.

### *14. Net Position*

In the government-wide statements, assets plus deferred outflows of resources less liabilities and deferred inflows of resources equal net position, and should be displayed in three components: net investment in capital assets, restricted, and unrestricted, as follows:

**Net investment in capital assets:** Consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of bonds, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. The portion of the debt or deferred inflows of resources attributable to the unspent debt proceeds is not included in the calculation of net investment in capital assets. Instead, the portion of the debt or deferred inflows of resources is included in the same net position component (restricted or unrestricted) as the unspent amount.

**Restricted net position:** The restricted component of net position consists of restricted assets (subject to restrictions beyond the Municipality's control) reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported Restrictions are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or imposed by the law through constitutional provisions or enabling legislation.

**Unrestricted net position:** Unrestricted net position is the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position. Unrestricted net position is 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.

### *15. Net Position flow assumption*

Sometimes the government will fund outlays for a particular purpose from both restricted (restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

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

### *16. Fund Balances*

The GASB Statement No. 54 Fund Balance Reporting and Governmental Fund Type Definitions ("GASB No. 54") establishes 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. 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.

**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 pursuant to constraints imposed through formal action (ordinance or resolution) by consent of the government's highest level of decision-making authority, which in the case of the Municipality is the Mayor and the Municipal Legislature. Those committed amounts cannot be used for any other purposes unless the Mayor and the Municipal Legislature 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 that are constrained by the Municipality's intent to be used for specific purposes, but are neither restricted nor committed. In distinction to committed balances, the authority for making an assignment is not required to be the government's highest level of decision-making authority, (both the Mayor and the Municipal Legislature). It is the Municipality's policy that intent can be expressed by the Mayor, the Finance Director (the official to which the Mayor has also delegated the authority to assign amounts) or by any other official or body to which the Mayor delegates. Furthermore, the nature of the actions necessary to remove or modify an assignment is not as prescriptive as it is with committed fund balances. 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.

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

### *17. Fund Balance flow assumptions*

Sometimes the government will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

### *18. Risk financing*

The Municipality carries insurance coverage for professional, public responsibility, property and theft, auto and fidelity bond losses. In addition, the Municipality also obtains medical insurance for its employees. Pursuant to Act No. 63 of June 21, 2010 the municipalities of Puerto Rico procure and manage, at their own discretion, all insurance policies, including those related to the health plans provided to the municipal employees. The total cost of the annual insurance premiums is paid in full and recorded as expense by the Municipality during the fiscal year.

The Municipality obtains workers compensation insurance though the State Insurance Fund Corporation, a component unit of the Commonwealth of Puerto Rico. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. The annual cost of insurance is allocated to the Municipality and amounts are retained from monthly advances of property tax and municipal equalization fund sent to the Municipality by the CRIM.

The Municipality carries insurance coverage for death and bodily injuries caused by automobile accidents. This insurance is obtained through the Automobile Accidents Compensation Administration, a component unit of the Commonwealth of Puerto Rico. The annual premium is paid per licensed motor vehicle.

The Municipality obtains unemployment compensation, non-occupational disability, and drivers' insurance coverage for its employees through various insurance programs administered by the Puerto Rico Department of Labor and Human Resources ("PRDOL"). These insurance programs cover workers against unemployment and provide supplementary insurance coverage for temporary disability or death because of work or employment-related accidents or because of illness suffered as a consequence of their employment. Unemployment compensation, non-occupational disability and drivers' insurance premiums are paid directly to the PRDOL on a cost reimbursement basis. Settled cases have not exceeded insurance coverage for any of the past three years.

### *19. 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.

## NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

*20. **Adoption of new accounting pronouncements***

Effective July 1, 2015 the Municipality adopted the provisions of ***GASB Statement No. 72*** *"Fair Value Measurement and Application"*; ***GASB Statement No. 73*** *"Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68"*; ***GASB Statement No. 76*** *"The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments"* and ***GASB Statement No. 82*** *"Pension Issues-an amendment of GASB Statements No. 67, No. 68 and No. 73"*.

***GASB Statement No. 72*** *"Fair Value Measurement and Application"*. This Statement addresses accounting and financial reporting issues related to fair value measurements. It also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. This Statement generally requires investments to be measured at fair value. An investment is defined as a security or other asset that (a) a government holds primarily for the purpose of income or profit and (b) has a present service capacity based solely on its ability to generate cash or to be sold to generate cash. This Statement requires a government to use valuation techniques that are appropriate under the circumstances and for which sufficient data are available to measure fair value. The techniques should be consistent with one or more of the following approaches: the market approach, the cost approach, or the income approach. While a majority of ***Statement No. 72*** applies to assets, the standard also applies to liabilities required to be measured at fair value. This Statement establishes a hierarchy of inputs to valuation techniques used to measure fair value.

That hierarchy has three levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are inputs—other than quoted prices—included within Level 1 that are observable for the asset or liability, either directly or indirectly. Finally, Level 3 inputs are unobservable inputs, such as management's assumption of the default rate among underlying mortgages of a mortgage-backed security. ***Statement No. 72*** requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques.

The Municipality has implemented ***Statement No. 72*** effective July 1, 2015 but adoption of the statement does not have a significant impact on the financial statement amounts and related disclosures. The Municipality invested available cash in nonnegotiable certificates of deposits which are valued at cost, in accordance with ***Statement No. 31, paragraph 8***. The Municipality does not maintain real property that meets the definition of investment. Accordingly, these capital assets, since are not considered investments, are not carried at fair value, but rather at cost. In addition, upon implementation of ***Statement No. 72*** donated capital assets are measured at acquisition value. Acquisition value is the price that would be paid to acquire an asset with equivalent service capacity in an orderly market transaction at the acquisition date. Donated capital assets were previously reported at estimated fair value at the time of acquisition, in accordance with ***Statement No. 34***.

***GASB Statement No. 73*** *"Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68"*. The objective of this Statement is to improve the usefulness of information about pensions included in the general purpose external financial reports of state and local governments for making decisions and assessing accountability. This Statement establishes requirements for defined benefit pensions that are not within the scope of ***Statement No. 68***, *"Accounting and Financial Reporting for Pensions,"* as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of ***Statement no. 68***. The Statement also amends certain provisions of ***Statement No. 67***, *"Financial Reporting for Pension Plans"*, and ***Statement No. 68*** for pension plans and pensions that are within their respective scopes.

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

The Municipality has implemented ***Statement No. 73*** effective July 1, 2015 but adoption of the statement does not have a significant impact on the financial statement amounts and related disclosures.

***GASB Statement No. 76*** *"The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments"*. The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of generally accepted accounting principles (GAAP). The "GAAP hierarchy" consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. This Statement supersedes ***Statement No. 55***, *"The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments"*.

The Municipality has implemented ***Statement No. 76*** effective July 1, 2015.

***GASB Statement No. 82*** *"Pension Issues-an amendment of GASB Statements No. 67, No. 68 and No. 73"*. The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, No. 68 and No. 73, Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

The Municipality has implemented paragraph 6 of ***Statement No. 82*** effective July 1, 2015. The implementation of the Statement have an impact in the presentation of the presentation of payroll-related measures in required supplementary information required by ***Statement No. 68.***

### *21. Future adoption of accounting pronouncements*

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

***GASB Statement No. 74*** *"Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans"*. The objective of this Statement is to improve the usefulness of information about postemployment benefits other than pensions (other postemployment benefits or OPEB) included in the general purpose external financial reports of state and local governmental OPEB plans for making decisions and assessing accountability. This Statement replaces **Statements No. 43**, *"Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans"*, as amended, and **No. 57**, *"OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans"*. It also includes requirements for defined contribution OPEB plans that replace the requirements for those OPEB plans in **Statement No. 25**, *"Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans"*, as amended, **Statement No. 43**, and **Statement No. 50**, *"Pension Disclosures"*. The Statement establishes new accounting and financial reporting requirements for governments whose employees are provided with OPEB, as well as for certain non-employer governments that have a legal obligation to provide financial support for OPEB provided to the employees of other entities. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2016 (fiscal year ended June 30, 2017). Earlier application is encouraged.

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

***GASB Statement No. 75*** *"Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions".* The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement replaces the requirements of **Statements No. 45**, *"Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions"*, as amended, and **No. 57**, *"OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans"*, for OPEB. **Statement No. 74**, *"Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans"*, establishes new accounting and financial reporting requirements for OPEB plans. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2017 (fiscal year ended June 30, 2018). Earlier application is encouraged.

***GASB Statement No. 77*** *"Tax Abatement Disclosures".* Financial statement users need information about certain limitations on a government's ability to raise resources. This includes limitations on revenue-raising capacity resulting from government programs that use tax abatements to induce behavior by individuals and entities that is beneficial to the government or its citizens. Tax abatements are widely used by state and local governments, particularly to encourage economic development. For financial reporting purposes, this Statement defines a tax abatement as resulting from an agreement between a government and an individual or entity in which the government promises to forgo tax revenues and the individual or entity promises to subsequently take a specific action that contributes to economic development or otherwise benefits the government or its citizens. Although many governments offer tax abatements and provide information to the public about them, they do not always provide the information necessary to assess how tax abatements affect their financial position and results of operations, including their ability to raise resources in the future. This Statement requires disclosure of tax abatement information about (1) a reporting government's own tax abatement agreements and (2) those that are entered into by other governments and that reduce the reporting government's tax revenues. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2015 (fiscal year ended June 30, 2017). Earlier application is encouraged.

***GASB Statement No. 78*** *"Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans".* The objective of this Statement is to address a practice issue regarding the scope and applicability of **Statement No. 68**, *"Accounting and Financial Reporting for Pensions".* This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local governmental employers whose employees are provided with such pensions. This Statement amends the scope and applicability of Statement 68 to exclude pensions provided to employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan that (1) is not a state or local governmental pension plan, (2) is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees of employers that are not state or local governmental employers, and (3) has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pensions through the pension plan). This Statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary information for pensions that have the characteristics described above. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2015 (fiscal year ended June 30, 2017). Earlier application is encouraged.

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

***GASB Statement No. 79*** *"Certain External Investment Pools and Pool Participants"*. This Statement addresses accounting and financial reporting for certain external investment pools and pool participants. Specifically, it establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2015 (fiscal year ended June 30, 2017). Earlier application is encouraged.

***GASB Statement No. 80*** *"Blending Requirements for Certain Component Units—an amendment of GASB Statement No. 14"* The objective of this Statement is to improve financial reporting by clarifying the financial statement presentation requirements for certain component units. This Statement amends the blending requirements established in paragraph 53 of Statement No. 14, "The Financial Reporting Entity, as amended". This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of ***Statement No. 39***, *"Determining Whether Certain Organizations Are Component Units"*. The requirements of this Statement are effective for reporting periods beginning after June 15, 2016 (fiscal year ended June 30, 2017). Earlier application is encouraged.

***GASB Statement No. 81*** *"Irrevocable Split-Interest Agreements"* The objective of this Statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. The requirements of this Statement are effective for reporting periods beginning after December 15, 2016 (fiscal year ended June 30, 2018). Earlier application is encouraged.

***GASB Statement No. 83*** *"Certain Asset Retirement Obligations"* This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement. The requirements of this Statement are effective for reporting periods beginning after June 15, 2018 (fiscal year ended June 30, 2019). Earlier application is encouraged.

***GASB Statement No. 84*** *"Fiduciary Activities"* The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. Governments with activities meeting the criteria should present a statement of fiduciary net position and a statement of changes in fiduciary net position. This Statement describes four fiduciary funds that should be reported, if applicable: (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018 (fiscal year ended June 30, 2020). Earlier application is encouraged.

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

***GASB Statement No. 85*** *"Omnibus 2017"* The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). Specifically, this Statement addresses the following topics: (1) blending a component unit in circumstances in which the primary government is a business-type activity that reports in a single column for financial statement presentation, (2) reporting amounts previously reported as goodwill and "negative" goodwill, (3) classifying real estate held by insurance entities, (4) measuring certain money market investments and participating interest-earning investment contracts at amortized cost, (5) timing of the measurement of pension or OPEB liabilities and expenditures, (6) recognized in financial statements prepared using the current financial resources measurement focus, (7) recognizing on-behalf payments for pensions or OPEB in employer financial statements, (8) presenting payroll-related measures in required supplementary information for purposes of reporting by OPEB plans and employers that provide OPEB, (9) classifying employer-paid member contributions for OPEB, (10) simplifying certain aspects of the alternative measurement method for OPEB and (11) accounting and financial reporting for OPEB provided through certain multiple-employer defined benefit OPEB plans. The requirements of this Statement are effective for reporting periods beginning after June 30, 2017 (fiscal year ended June 30, 2018). Earlier application is encouraged.

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

## NOTE B – DEPOSITS

**Custodial credit risk – deposits**, 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:

1. ***Deposits in commercial banks***

Under Commonwealth of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of insurance provided by the Federal Deposit Insurance Corporation (FDIC). All securities pledged as collateral by the Municipality are held by agents designated by the Puerto Rico Secretary of Treasury but not in the Municipality's name. At year-end, the Municipality's bank balance of deposits in commercial banks amounting to $4,046,054 were covered by the FDIC and by pledged securities. Accordingly, custodial credit risk is considered low.

2. ***Deposits in governmental bank***

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 the Governmental Development Bank of Puerto Rico ("GDB"), a governmental bank, amounts to $7,078,723.

**Fiscal condition of the GDB**

The Commonwealth of Puerto Rico and its instrumentalities are currently facing a severe fiscal and liquidity crisis. Continued operational deficits and lack of access to capital markets have resulted in delays in the repayment of loans outstanding by the Commonwealth and its instrumentalities with GDB. This in turn have affected the GDB's liquidity position and the ability to repay its obligations. Although GDB took a number of liquidity enhancing and conservation measures, they were not sufficient to maintain GDB's operations in the ordinary course. The risks and uncertainties facing GDB, the Commonwealth and its instrumentalities and other factors described in the most recent GDB's

**NOTE B- DEPOSITS- Continued**

audited financial statements have led management to conclude that there is a substantial doubt as to the ability of GDB to continue as a going concern.

On April 6, 2016, the Commonwealth approved Act No. 21 of 2016 known as the Puerto Rico Emergency Moratorium and Financial Rehabilitation Act ("Act No. 21") (as amended) to declare a moratorium on debt service payments and to stay related creditor remedies for a temporary period for the Commonwealth and certain of its instrumentalities, including GDB. It allows the Commonwealth's Governor to take any and all actions that are reasonable and necessary to allow GDB to continue carrying out its operations. Act No. 21 was amended by Act No. 2 of January 18, 2017 to create under a separate Act the Puerto Rico Fiscal Agency and Financial Advisory Authority ("FAFAA") and by Act No. 5 of January 29, 2017 known as the Puerto Rico Financial Emergency and Fiscal Responsibility Act to expand the Act enforcement powers pursuant to the approval by the U.S. Government of PL 114-187 known as the Puerto Rico Oversight, Management and Economic Stability Act ("PROMESA").

Pursuant to the moratorium Acts and several executive orders issued by the former and actual Commonwealth's Governors, the certain Commonwealth's entities, including GDB, were declared in a state of emergency. Regarding GDB, the Commonwealth implemented a regulatory framework governing its's operations and liquidity by prohibiting loan disbursements and establishing a procedure with respect to withdrawals, payments and transfer requests with respect of funds held on deposits by the Commonwealth and its instrumentalities, including the Municipalities. The withdrawal, payment and transfer of funds held on deposit at GDB are restricted to those reasonable and necessary to ensure the provision of essential services and GDB is authorized to establish weekly limits on the aggregate amount of such disbursements. Specific procedures are to be followed by the Commonwealth instrumentalities and Municipalities to request the disbursement of its funds deposited in GDB. The executive orders also suspended payment of GDB debt obligations (other than certain interest obligations that are payment-in-kind), although GDB may request the Governor's authorization to pay interest on its bonds to the extent its liquidity permits. GDB has been unable to fully meet its principal debt service obligations in full since May 1, 2016, and does not currently expect to make additional debt service payments while the moratorium is in effect.

As disclosed earlier, the Puerto Rico Fiscal Agency and Financial Advisory Authority ("FAFAA") was created pursuant Act No. 21 of 2016 and Act 2 of 2017 as an independent public corporation and governmental instrumentality with separate legal existence, fiscal and administrative autonomy, and independence from the Commonwealth. The FAFAA was created for the purpose of (1) act as fiscal agent, financial advisor and reporting agent of the Commonwealth and its public corporations, instrumentalities, commissions, authorities, municipalities and political subdivisions, (2) assist such entities in confronting the grave fiscal and economic emergency that the Commonwealth is currently experiencing and (3) perform oversight supervision of fiscal plans of applicable Commonwealth entities, including GDB, resulting from the requirements of PROMESA. All fiscal agency, financial advisory, and reporting functions of GDB were transferred to FAFAA.

**Management assessment on custodial credit risk on deposits in GDB**

Management has concluded that, based on the GDB fiscal condition and the limitations imposed by moratorium laws and executive orders as described above, the custodial credit risk on deposits in GDB is high.

**NOTE B- DEPOSITS- Continued**

**Evaluation of effect of contingent events on deposits in GDB**

The Municipality's management has carefully evaluated and taken into consideration the GDB's current fiscal condition, based on the facts described above. They determined that an uncertainty exists on whether the Municipality may or may not recover in the value of the investments in deposits in GDB. This uncertainty is caused by the lack of sufficient and accurate information about GDB's future outcome or any certain determination of GDB's or Commonwealth's authorities with regard to its investments in bank deposits of the municipalities and other Commonwealth's entities. At present, GDB has not issued its audited financial statements for the fiscal years 2015 and 2016. Furthermore, the final outcome of GDB's fiscal plan submitted to the Financial Oversight and Management Board for Puerto Rico ("the Board") for evaluation and approval, as well as its future role as a Commonwealth's governmental entity are uncertain.

The Commonwealth's intents to honor withdrawals and mitigate the possibility of unrecoverable amounts. As stated in the moratorium Acts and executive orders issued, although governmental entities, including municipalities, are currently suffering restrictions to access its funds deposited in GDB, such deposits are currently honored and will continue to be honored subject to GDB's adequate liquidity levels and compliance by governmental entities of request requirements of such moratorium Acts and executive orders. After year-end, the Municipality received certain amounts of cash deposits held at GDB subject to the limitation imposed by moratorium regulations including installment payments of certificates of deposits and escrow amounts of undisbursed proceeds of bonds and notes. GDB continued to pay principal and interest on general and special obligation bonds and notes.

Since is reasonably possible that the recoverability of deposits in GDB may be affected, the Municipality performed a detailed analysis of its deposits in GDB in order to determine if a proper estimate of an impairment in the value of the investments in deposits in GDB may be calculated and disclosed. The analysis consists of:

1) Determination of total deposits in GDB as of June 30, 2016, classified by funds and categories,
2) Recording additions and reductions of actual amounts of income, payments or withdrawals applicable to each category and fund,
3) Recording of adjustments related to future withdrawals or disposition of deposits based on management's past experience,
4) Calculation of a final net amount of deposits in GDB per fund and category as of March, 2017,
5) Determination of an amount or range of amounts of estimated impairment loss.

As a result of the analysis the Municipality determined the net amounts of deposits at GDB per fund and category as of March, 2017. Notwithstanding, the Municipality concluded that, from these net amounts of deposits, an amount of an impairment loss in the value of the net deposits in GDB cannot be reasonably estimated to be disclosed. There are no competent and accurate sources of information to determine if the total amount is impaired, to determine a percent of impairment or to determine a range of loss of impairment. The calculation of an estimate is affected by the lack of GDB's actualized financial data and the uncertainty related to the final outcome of the bank deposits by GDB.

These matters are ongoing and the Municipality cannot predict when and how will be its final outcome.

## 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 five (5) business days after April 15. During the Fiscal year ended June 30, 2016 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 inflows of resources as of June 30, 2016, follows:

| Description | Amount |
|---|---|
| Total municipal license tax receivable: | $ 1,052,833 |
| Less: allowance for uncollectibles | (868,696) |
| | **$ 184,137** |

Tax payment is due 15 days after each period due date or on July 15 and January 15 of the subsequent fiscal year. Tax revenue is recognized at that moment by the Municipality. A discount of 5% is allowed when full payment is made along with tax return submission on or before five (5) business days after April 15. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year in the amount of $1,889,987 are recorded as deferred inflows of resources.

### 2. *Rents and construction permits*

A detail of rents and construction permits' receivable as of June 30, 2016, follows:

| Description | Amount |
|---|---|
| Rent-land lots | $ 94,935 |
| Rent-properties | 855,452 |
| Construction permits | 24,190 |
| Other | 39,378 |
| | 1,013,955 |
| Less: allowance for uncollectibles | (821,371) |
| | **$ 192,584** |

Of the total amount of $192,584 the Municipality recorded $104,572 as deferred inflows of resources 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, 2016, follows:***

| | Commonwealth Government | Federal Government |
|---|---|---|
| **Major fund - General fund:** | | |
| P.R. Department of Treasury – Christmas bonus reimbursement | $ 81,491 | $ - |
| **Major fund – Debt service fund:** | | |
| Municipal Revenue Collection Center (CRIM) – property taxes (debt service fund) | 162,573 | - |
| **Other governmental funds:** | | |
| P.R. Department of Labor – Law No. 52 | 45,906 | - |
| U.S. Department of Health and Human Services – Early Head Start | - | 78,886 |
| P.R. Public Housing Authority- Public and Indian Housing | - | 62,102 |
| U.S. Department of Housing and Urban Development – CDBG | - | 24,078 |
| | **$ 289,970** | **$ 165,066** |

Certain amounts are recorded as deferred inflows of resources in the governmental funds statements since they are not available as required by current standards. See related note H.

2. ***Amounts due to governmental entities as of June 30, 2016, follows:***

| Description | Commonwealth Government |
|---|---|
| **General Fund:** | |
| P.R. Employees Retirement System (ERS) | $ 114,211 |
| P.R. Department of Labor – unemployment | 20,030 |
| Others | 2,386 |
| | **$ 136,627** |

## NOTE E - INTERFUND TRANSACTIONS

*1. Due from/to other funds*

| Receivable Fund | Payable Funds | Amount |
|---|---|---|
| General Fund | **Other Governmental Funds:** | |
| | Law No. 52 | $ 45,407 |
| | Public School Maintenance | 73,395 |
| | Programs for the Elderly | 30,633 |
| | Early Head Start | 37,742 |
| | Transit Safety Commission | 47,976 |
| | Fine Arts School | 55,130 |
| | Alzheimer Program | 12,387 |
| | Department of the Family | 29,762 |
| | Other | 85,186 |
| | | 417,618 |
| Other governmental Funds | **Major fund** | |
| $1,310,000 Bond Issuance | General Fund | 27,205 |
| | | **$ 444,823** |

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

| Receivable Fund | Payable Funds | Amount |
|---|---|---|
| General Fund | **Other Governmental Funds:** | |
| | P.R. Department of Transportation | $ 142,828 |
| | $3,500,000 Loan Fund | 51,141 |
| | $1,695,000 Loan Fund | 19,391 |
| | Improvements to Villa Auxerre Basketball Court ($1,585,000 bond issuance) | 53,291 |
| | Irregular Employees Special Fund | 60,186 |
| | Special Communities Fund | 25,061 |
| | Rural Development Fund | 60,419 |
| | Other | 116,715 |
| | | **$ 529,032** |

*3. Transfers in (out)*

Transfers among individual funds were made for operational purposes. Transfers include:

a. Internal subsidy of $43,131 from the General Fund to the Surf and Fun Water Park Governmental Fund to finance part of the construction of the water park.

b. Internal subsidy of $1,316,455 from the general fund to the debt service fund to finance the principal and interest payments of a special obligation and rent bonds.

c. Transfers from debt service fund to the general fund for excess funds on IVU Municipal Redemption Fund – sales and use taxes for $417,342 excess funds on CAE redemption fund property taxes for $696,061 and interest earned on restricted cash of $1,502.

## NOTE E - INTERFUND TRANSACTIONS - Continued

d. Transfer of $280,000 from the SGME enterprise fund to the general fund pursuant to provisions of the Municipal Law regarding municipal enterprises.

## NOTE F - CAPITAL ASSETS

Capital assets and depreciation activity as of and for the year ended June 30, 2016 is as follows:

| | Beginning balance July 1, 2015 | Increases | Decreases | Ending balance June 30, 2016 |
|---|---|---|---|---|
| **Governmental activities:** | | | | |
| Capital assets, not being depreciated: | | | | |
| Land | $ 8,214,356 | $ - | $ - | $ 8,214,356 |
| Construction in progress | 1,496,066 | 534,146 | 206,961 | 1,823,251 |
| Total capital assets not being depreciated: | 9,710,422 | 534,146 | 206,961 | 10,037,607 |
| Capital assets, being depreciated: | | | | |
| Buildings and improvements | 62,443,141 | 259,564 | 450,453 | 62,252,252 |
| Equipment | 11,469,730 | 762,393 | 54,447 | 12,177,676 |
| Roads | 16,495,491 | 556,949 | 60,549 | 16,991,891 |
| Bridges | 7,356,099 | 13,488 | - | 7,369,587 |
| Total capital assets being depreciated | 97,764,461 | 1,592,394 | 565,449 | 98,791,406 |
| Less accumulated depreciation for: | | | | |
| Buildings and improvements | 12,266,384 | 1,549,637 | - | 13,816,021 |
| Equipment | 8,039,340 | 525,508 | 42,147 | 8,522,701 |
| Roads | 10,044,349 | 368,679 | 60,549 | 10,352,479 |
| Bridges | 2,986,876 | 178,961 | - | 3,165,837 |
| Total accumulated depreciation | 33,336,949 | 2,622,785 | 102,696 | 35,857,038 |
| Total capital assets being depreciated, net | 64,427,512 | (1,030,391) | 462,753 | 62,934,368 |
| Governmental activities capital assets, net | **$ 74,137,934** | **$ (496,245)** | **$ 669,713** | **$ 72,971,975** |

## NOTE F - CAPITAL ASSETS - Continued

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

| Governmental activities: | Amount |
|---|---|
| General government | $ 87,271 |
| Public safety | 81,760 |
| Public works | 2,330,371 |
| Sanitation | 80,795 |
| Culture and recreation | 16,740 |
| Welfare | 25,848 |
| Total depreciation expense, governmental activities | **$ 2,622,785** |

## NOTE G – 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, 2016:

| | Balance at July 1, 2015 | Increases | Decreases | Balance at June 30, 2016 | Due within one year |
|---|---|---|---|---|---|
| General, Special Obligations Bonds and Notes | $ 37,471,000 | $ - | $ 1,008,000 | $ 36,463,000 | $ 932,000 |
| Note payable to CRIM- financing of delinquent accounts | 81,976 | - | 4,822 | 77,154 | 4,822 |
| Compensated absences | 3,641,726 | 370,704 | 367,299 | 3,645,131 | 432,844 |
| Christmas Bonus | 364,417 | 350,898 | 364,417 | 350,898 | 350,898 |
| Note payable - PRASA | - | 538,524 | - | 538,524 | 247,705 |
| Property tax advances | 718,879 | 37,987 | 564,862 | 192,004 | 154,017 |
| Claims and judgments | - | 25,000 | - | 25,000 | 25,000 |
| Payable to PREPA | 1,988,304 | - | 1,988,304 | - | - |
| COFIM – sales tax advances | 16,708 | 42,862 | 16,708 | 42,862 | 42,862 |
| Net pension liability | 46,789,505 | - | - | 46,789,505 | - |
| | **$ 91,072,515** | **$ 1,365,975** | **$ 4,314,412** | **$ 88,124,078** | **$ 2,190,148** |

**NOTE G – LONG-TERM DEBT - continued**

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

Pursuant to Act No. 64 of July 3, 1996 as amended, known as the Puerto Rico Municipal Financing Act of 1996 the Municipality is subject to a legal limitation on the total amount of indebtedness for general obligation bonds or notes, special obligation bonds, notes or instruments. The legal debt limitation of the Municipality for general obligation bonds or notes or notes in advance of general obligation bonds is equal to 10% of the total appraised value of the property located in the Municipality should be as said appraisal values are determined by the CRIM. For special obligation bonds, notes or instruments the Municipality is prevented to incur in additional obligations if the annual payment of principal and interest on said bonds, notes or instruments together with the annual payment of principal and interest of the outstanding ones at that time exceeds 10% of the average recurrent operating income of the Municipality of the 2 fiscal years immediately preceding the current fiscal year. These limitations are not applicable to obligations or loans whose source of repayment is the SUT Municipal Redemption Fund. Debt margin for these obligations are based on the Municipality's repayment capacity.

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2016 amount to $36,463,000. The Municipality levies an annual additional special ad valorem tax of 2% of the assessed value of personal and real property which is collected by the CRIM and deposited in the CAE Redemption Fund at GDB. In addition, .2% of the .5% municipal sales and use tax collected by the P.R. Department of Treasury is deposited in the "IVU Municipal Redemption Fund" at GDB. Debt service funds has been established for the bonds and notes at GDB with the proceeds of those property and sales and use taxes, whereby sufficient funds must be set aside in order to cover the projected debt service requirement, before any new bonds are issued. Principal and interest payments of special obligation notes of $996,000, $505,000, and $1,005,000 and special obligation refunding bonds of $1,386,000 are made through the Municipal Redemption Fund (IVU). Interest payments of $1,310,000 rental bond, $3,000,000 rental bond and $11,110,000 special obligation bond are primarily financed through withholdings from property tax advances sent to the Municipality by the Municipal Revenue Collection Center (CRIM). The remaining debt is paid through the CAE Redemption Fund.

A detail of the general and special obligation bonds and notes as of June 30, 2016, follows:

| | Outstanding Amount |
|---|---|
| 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% (4.91% at June 30, 2016) | $ 60,000 |
| 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% (4.91% at June 30, 2016) | 555,000 |
| 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% | 236,000 |
| 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 5.31% (4.62% at June 30, 2016) | 250,000 |

## NOTE G – LONG-TERM DEBT- Continued

| | Outstanding Amount |
|---|---|
| 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% | 2,172,000 |
| 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 1.48% to 7.50% (1.88% at June 30, 2016) | 295,000 |
| 2008 special obligation bond of $996,000 due in annual installments ranging from $16,000 to $86,000 through July 1, 2032; bearing interest at rates ranging from 1.48% to 7.50% (1.88% at June 30, 2016) | 858,000 |
| 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% (7.5% at June 30, 2016) | 2,940,000 |
| 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, 2016) | 255,000 |
| 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, 2016) | 1,310,000 |
| 2012 general obligation note of $8,305,000 due in annual installments ranging from $115,000 to $695,000 through July 1, 2037; bearing interest at rates ranging from 3.40% to 7.50% (3.49% at June 30, 2016) | 7,925,000 |
| 2012 special obligation note of $1,005,000 due in annual installments ranging from $10,000 to $85,000 through July 1, 2037; bearing interest at rates ranging from 3.40% to 7.50% (3.72% at June 30, 2016) | 975,000 |
| 2013 general obligation refunding bond of $3,402,000 due in annual installments ranging from $45,000 to $287,000 through July 1, 2037; bearing interest at rates ranging from 3.42% to 7.50% (4.22% at June 30, 2016) | 3,252,000 |
| 2013 special obligation refunding bond of $1,386,000 due in annual installments ranging from $20,000 to $121,000 through July 1, 2037; bearing interest at rates ranging from 3.92% to 7.50% (4.22% at June 30, 2016) | 1,321,000 |
| 2013 special obligation bond of $11,110,000 due in annual installments ranging from $195,000 to $960,000 through July, 1, 2038; bearing interest rate at 6% | 11,110,000 |
| 2015 general obligation bond of $457,000 due in annual installments ranging from $18,000 to $29,000 through July, 1, 2035; bearing interest rate at 2.37% | 439,000 |
| 2015 general obligation bond of $2,545,000 due in annual installments ranging from $35,000 to $220,000 through July 1, 2039: bearing interest at rates ranging from 7% to 8% (7% at June 30, 2016) | 2,510,000 |
| | **$ 36,463,000** |

**NOTE G – LONG-TERM DEBT- Continued**

The annual requirements to amortize general and special obligation bonds and notes as of June 30, 2016, are as follow:

| June 30, | Principal | Interest |
|---|---|---|
| 2017 | $ 932,000 | $ 2,002,242 |
| 2018 | 1,041,800 | 2,143,283 |
| 2019 | 1,116,800 | 2,295,559 |
| 2020 | 977,800 | 2,227,064 |
| 2021 | 1,057,800 | 2,161,295 |
| 2022-2026 | 6,392,800 | 9,648,427 |
| 2027-2031 | 8,535,000 | 7,199,305 |
| 2032-2036 | 10,277,000 | 3,988,465 |
| 2037-2040 | 6,132,000 | 570,050 |
| Totals | **$ 36,463,000** | **$ 32,235,690** |

3. ***Other long-term liabilities***

| | Outstanding Amount |
|---|---|
| **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 $470,818, to finance delinquent property tax accounts sold to private investors, under the provision of Law No. 146 of October 11, 2001. The agreement is in the form of a non-revolving line of credit bearing interest of 6.5% for the first five years and variable for the next twenty-five years at 125 points over London Interbank Offered Rate (LIBOR) and is due on December 1, 2032. As described in Law No. 146, interest payments for the first five years were financed through .48% of the net increase of subsidy provided by the Commonwealth of Puerto Rico's general fund. Also, during the first five years any collection from those delinquent accounts was credited to the loan principal. After the five year period the loan outstanding balance was restructured for a twenty-five years period. Debt service requirements in future years are as follows: | **$ 77,154** |

| June 30 | Principal | Interest |
|---|---|---|
| 2017 | $ 4,822 | $ 1,932 |
| 2018 | 4,822 | 1,812 |
| 2019 | 4,822 | 1,690 |
| 2020 | 4,822 | 1,572 |
| 2021 | 4,822 | 1,449 |
| 2022-2026 | 24,110 | 4,434 |
| 2027-2031 | 24,110 | 2,415 |
| 2032 | 4,824 | 121 |
| **Totals** | **$ 77,154** | **$ 15,425** |

## NOTE G - LONG-TERM DEBT – Continued

| | Outstanding Amount |
|---|---|
| **Compensated absences** - includes accrued vacations, sick leave benefits and other benefits with similar characteristics such as compensatory time; represents the Municipality's commitment to fund such costs from future operations. Amount is paid with unrestricted funds. | **3,645,131** |
| **Christmas Bonus** - represents the accrued portion corresponding to fiscal year 2016 of the Christmas bonus to be paid in December 2016. | **350,898** |
| **Note payable to PRASA** – subsequent to June 30, 2016 the Municipality entered into an agreement with the Puerto Rico Aqueduct and Sewer Authority ("PRASA") to refinance on a long-term basis a matured water utility debt recorded in the general fund. The note requires a down payment of $107,705 due on or before August 31, 2016 and 30 monthly payments of $10,819 due on March, 2019. | **538,524** |
| **Payable to CRIM, property tax advances** – represents the amount reported by CRIM of the settlement of excess of advances over actual collections of property taxes applicable to fiscal years 2014 and 2015. (See related note K) | **192,004** |
| **Claims and judgments** - represents the estimated loss of legal cases to be paid subsequent to June 30, 2016. The awarded amount, if any, will be paid with unrestricted funds. | **25,000** |
| **Payable to COFIM** - represents the excess of COFIM advances over the actual sales and use tax collected for the municipality for the fiscal year. (see related note L) | **42,862** |
| **Net pension liability** – represents the proportional share of the collective pension liability of all employers for benefits provided through the pension plan as of June 30, 2015 (See related note N) | **46,789,505** |

## NOTE H - DEFERRED INFLOW OF RESOURCES

*1. Government wide and governmental funds:*

Municipal license taxes ("patentes en suspenso") are due on July 1 and January 1 of the subsequent fiscal year. Taxes may be paid in advance to the due dates. These taxes paid in advance are recorded as revenues or inflows of resources in the following fiscal period. Due to this time requirement, the amount paid in advance of $1,889,987 is recognized as deferred inflows of resources as of June 30, 2016.

## NOTE H - DEFERRED INFLOW OF RESOURCES – Continued

2. ***Governmental funds – unavailable revenues:***

As required by current standards, revenues and other governmental fund financial resources should be recognized in the accounting period in which they become both measurable and available. When an asset is recorded in governmental fund's financial statements but the revenue is not available, the Municipality should report a deferred inflow of resources until such time as the revenue becomes available. A detail of these balances follows:

| | Commonwealth Government | Other |
|---|---|---|
| **Major fund - General fund:** | | |
| Municipal license taxes – receivable | $ - | $ 116,912 |
| Rents and construction permits | - | 104,573 |
| P.R. Department of Treasury – Christmas bonus reimbursement | 81,491 | - |
| **Debt Service fund:** | | |
| Municipal Revenue Collection Center (CRIM) – property taxes | 72,335 | - |
| **Other governmental funds:** | | |
| P.R. Department of Labor – Law No. 52 | 45,906 | - |
| | **$ 199,732** | **$ 221,485** |

## NOTE I - FUND BALANCE

1. ***Fund balance classifications***

The governmental fund balance classifications and amounts at June 30, 2016 are shown in the following table:

| | General Fund | Debt Service | Surf and Fun Water Park | Other Governmental Funds | Total |
|---|---|---|---|---|---|
| **Nonspendable:** | | | | | |
| Advances to other funds | $ 529,032 | $ - | $ - | $ - | $ 529,032 |
| | 529,032 | - | - | - | 529,032 |
| **Restricted:** | | | | | |
| General public works and sanitation | - | - | - | 2,169 | 2,169 |
| Public safety | - | - | - | 21,719 | 21,719 |
| Housing, Welfare and Community Development | | - | - | 121,748 | 121,748 |
| Debt Service | - | 3,324,423 | - | - | 3,324,423 |
| Capital outlays | - | - | 1,028,840 | 4,088,458 | 5,117,298 |
| | - | 3,324,423 | 1,028,840 | 4,234,094 | 8,587,357 |
| **Unassigned** | (2,527,917) | - | - | (381,445) | (2,909,362) |
| | **$ (1,998,885)** | **$ 3,324,423** | **$ 1,028,840** | **$ 3,852,649** | **$ 6,207,027** |

## NOTE I - FUND BALANCE- Continued

*2. Fund balance deficits*

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

| Funds | Amount |
|---|---|
| **Other Governmental Funds:** | |
| Special Program for the Aging | $ 181,431 |
| Permanent Improvements Fund (Law No.43 and 2212) | $ 79,385 |
| Alzheimer Proposal Fund | $ 44,506 |
| Emergency Shelter | $ 3,009 |
| Law 52 | $ 44,670 |
| $305,000 Bond issuance fund | $ 27,169 |
| Others | $ 4,774 |

These deficits result from the recognition of deferred inflows of resources for unavailable revenues. As required by current standards, the Municipality recorded intergovernmental revenues for reimbursement (expenditure-driven) grants on fund statements when all applicable eligibility requirements have been met and the resources are available. Any amount not covered by the corresponding award will be covered with future budgetary appropriations of the general fund, if necessary.

## NOTE J - NET INVESTMENT IN CAPITAL ASSETS

The net investment in capital assets component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. The portion of the debt attributable to significant unspent proceeds should not be included in the calculation. The amount of net investment in capital assets as of June 30, 2016, is comprised of the following:

| Description | Amount |
|---|---|
| Capital assets, net of accumulated depreciation | $ 72,971,980 |
| Outstanding balance on capital related debt | (36,463,000) |
| Unspent capital related debt proceeds | 2,420,029 |
| | **$ 38,929,009** |

## NOTE K - 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, 2016, are 7.78% for personal property and 10.28% for real property. The distribution of these rates follows:

**NOTE K - PROPERTY TAXES - Continued**

| Description | Personal Property | Real Property |
|---|---|---|
| Basic property tax rate, which is appropriated for general purposes and accounted in the Municipality's general fund **("Basic Tax")**: | 4.00% | 6.00% |
| Percent that belongs to the Commonwealth's debt service fund **("Special Tax")**: | 1.03% | 1.03% |
| Percent that belongs to the Municipality's debt service fund **("CAE Tax")**: | 2.75% | 3.25% |
| Total tax rate: | 7.78% | 10.28% |
| 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:** | **7.58%** | **10.08%** |

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.

Collections from the Basic Tax, the Special Tax and the CAE Tax described above, plus 35% of net revenues from the lottery system and 2.5% of net internal revenues from the Commonwealth's General Fund corresponding to the municipalities are deposited in a trust fund known as the Municipal Matching Fund, where GDB serves as trustee and a private bank serves as the custodian. From the Municipal Matching Fund, the collections that correspond to the Special Tax are transferred to the Commonwealth General Obligation Redemption Fund and those that correspond to the CAE Tax and any other revenues that are needed to service general obligations are transferred to the Municipal Public Debt Redemption Fund. Remaining amounts in the Municipal Matching Fund are eventually distributed among the municipalities following specific rules and formulas set forth by law.

The *Municipal Public Debt Redemption Fund* is a trust fund in which GDB serves as trustee and a private bank serves as the custodian. It was established for the deposit of any CAE Tax it collects on behalf of the municipalities. Pursuant to the Trust Deed, the *Municipal Public Debt Redemption Fund* is composed of two Sub-Funds: (1) the GDB Sub-Fund and (2) the MFA/Private Sector Sub-Fund. In the GDB Sub-Fund, CRIM is required to deposit on a monthly basis CAE Tax revenues necessary to meet annual debt service on bonds, notes and loans issued by GDB. In the MFA/Private Sector Sub-Fund, the CRIM is required to deposit on a monthly basis CAE Tax revenues necessary to meet annual debt service on bonds, notes and loans issued or bought by the Municipal Finance Agency ("MFA"), the federal government or private banks. The GDB Sub-Fund remains at GDB and the MFA/Private Sector Sub-Fund is held by a private bank trust division. The CRIM established that there are excess CAE Tax funds deposited in GDB and accordingly, since April 2016 is not depositing CAE Tax revenues in the GDB Sub-Fund.

Once a reserve equivalent to twelve months of debt service on all outstanding general obligations is funded, any surplus in the *Municipal Public Debt Redemption Fund* is placed at the disposal of the Municipality. Upon request, once in a year these surplus funds, known as "excess CAE funds" are distributed net of withdrawal for payment of debts to governmental agencies, if any, to the Municipality. Generally, these funds are transferred to the Municipality's general fund. Instead, GDB informed the Municipality that these excess funds are subject to the withdrawal restrictions imposed by the Commonwealth's moratorium Acts and executive orders. In accordance with these restrictions, GDB invested the excess CAE funds in nonnegotiable certificates of deposits held by GDB in the Municipality's name.

**NOTE K - PROPERTY TAXES - Continued**

The final transfer to the Municipality of funds held on deposit at GDB are restricted to those reasonable and necessary to ensure the provision of essential services, as determined by the Commonwealth. The Municipality recorded these excess CAE funds as transfers-out in the debt service fund and as transfers-in the general fund.

The CRIM advances funds to the Municipality based on an estimate of special governmental subsidies and the property taxes to be levied and which are collected in subsequent periods. This distribution includes advances of property tax and amounts of municipal equalization fund from the Commonwealth government. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. The CRIM prepares a preliminary settlement not later than three months after fiscal year-end and a final settlement not later than 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. A payable of $192,004 resulting from the final settlement of fiscal years 2013-2014 and 2014-2015 was recorded as other long term debt in the government-wide financial statements since it will not be paid with current available resources.

**NOTE L – SALES AND USE TAXES**

As imposed by Commonwealth and Municipal laws and regulations, the citizens of Puerto Rico are subject to a sales and use tax ("SUT") on a broad range of goods and services. The total tax is imposed at a combined 11.5% rate of which 10.5% belongs to the Commonwealth (collection process administered through the Puerto Rico Department of Treasury) and 1% for the municipalities (collection process administered through the Municipal Finance Corporation – "COFIM").

The Municipal SUT is due the 20th day of each month based on tax collected in the preceding month. Merchants at the Municipality of San Germán may render their tax return and payment directly to the Municipality as certain municipalities decided to collect the tax after being certified as such by COFIM. These certified collecting municipalities may accept filings and payments through their Municipal Collections Officer. This information should be transmitted on a daily basis by the collecting Municipalities to the COFIM data base. In addition, merchants can render their tax return and payment through COFIM's web site or through a bank institution.

Effective on February 1, 2014 the Commonwealth approved Act No. 18 and Act No. 19 to provide for the restructuring and creation of financing structures from sales and use tax sources to guarantee and pay municipal long term debt issuances. As a result of these legislations the municipalities of Puerto Rico may improve its credit capacity along with maintaining sufficient resources for operations.

Act No. 18 known as the "Municipal Administration Fund Law" improves the financing capacity of the Puerto Rico Sales Tax Financing Corporation ("COFINA"), a component unit of the Commonwealth and a related entity of GDB and creates a special fund called "Municipal Administration Fund" ("FAM") under custody of GDB. The FAM permits the Municipalities to guarantee and pay long term debt and provide funds for its general operations. The Act includes provisions for municipalities that do not want to be covered by the Act. Special rules apply for those municipalities. The Municipality of San Germán signed the agreement to be covered.

The FAM will be funded in all fiscal years with an amount attributable to the .5% of the Commonwealth's SUT for the current fiscal year once all required deposits by law have been made to COFINA from the 6% Commonwealth's SUT. The .5% is distributed as follows:

**NOTE L – SALES AND USE TAXES - Continued**

a. .2% deposited in the Municipal Development Fund to be distributed to the municipalities to finance operational costs,

b. .2% deposited in a Municipal Redemption Fund or may be deposited in the municipalities' general fund. The municipalities has the option to maintain funds in the Municipal Redemption Fund to increase its debt margin and,

c. .1% deposited in a Municipal Improvement Fund to finance capital improvement projects; these funds will be distributed based on legislation from the Commonwealth's Legislature.

To the extent the amount of Commonwealth SUT collections available for deposit into the FAM during any fiscal year is less than the amount attributable to 0.5% of the Commonwealth sales and use tax for such fiscal year, the Commonwealth's General Fund is required to cover any such shortfall.

Act No. 19 created the Municipal Finance Corporation ("COFIM") a public corporation and a component unit of GDB to issue bonds and use other financing mechanisms to pay or refinance all or a portion of the municipalities' debt obligations payable from the 1% municipal SUT. The Act includes provisions for municipalities that do not want to be covered by Act No. 18. Special rules apply for those municipalities. As discussed above the Municipality of San Germán signed the agreement to be covered by Act No. 18.

The first collections of the 1% municipal SUT are deposited into the COFIM's sinking fund until the greater of: .3% of the 1% municipal SUT or an Annual Rental Fee ("RFA"). The RFA for fiscal year 2015-2016 and thereafter will be 1.5% of the RFA of the preceding fiscal period, which at fiscal year 2014-2015 amounted to $65,541,281. The excess amount of 1% municipal SUT remaining after the required deposit to the COFIM's sinking fund (the "1% Municipal Transfer") is transferred to the general fund of municipalities or to the Municipal Redemption Fund as decided by the municipality. If at any moment the required deposits to the COFIM's sinking fund were not sufficient to pay principal and interest of any outstanding obligation, the deficiency will be covered by appropriations of the Commonwealth's general fund budget.

Until June 30, 2016 the Act provided for monthly cash advances from GDB to the Municipalities within the first ten days of each month. Such advances are payable from the amount to be received from 1% Municipal Transfer as a result of Act No. 19 and from the FAM as a result of Act No. 18. If such cash advances exceed the amount corresponding to the 1% Municipal Transfer and the FAM, the excess is deducted on a prorate basis from the next fiscal year cash advances. Otherwise, the excess amount is paid to the municipalities.

On August, 2016 GDB informed that the COFIM board of directors approved a preliminary settlement of the 1% Municipal Transfer (Act No. 19) of fiscal year 2015-2016 in which actual cash collections exceeded cash advances by $42,862. The Municipality received monthly cash advances related to the Municipal Development Fund and the IVU Municipal Redemption Fund until March, 2016 and April, 2016 respectively. No other funds related to these categories have been received after that date.

For the fiscal year ended June 30, 2016 the Municipality recorded as revenue $1,752,637 in the general fund of which (a) $1,542,345 corresponds to the 1% Municipal Transfer and (2) $210,292 corresponds to the Municipal Development Fund. The debt service fund reported revenues of $444,941 corresponding to the IVU Municipal Redemption Fund.

## NOTE L – SALES AND USE TAXES - Continued

Once a reserve equivalent to twelve months of debt service on all outstanding general obligations is funded, any surplus in the IVU Municipal Redemption Fund is placed at the disposal of the Municipality. Upon request, these surplus funds, known as "excess IVU funds" are distributed to the Municipality at any time and whenever requested. Generally, these funds are transferred to the Municipality's general fund. Instead, GDB informed the Municipality that these excess funds are subject to the withdrawal restrictions imposed by the Commonwealth's moratorium Acts and executive orders. In accordance with these restrictions, GDB invested the excess IVU funds in nonnegotiable certificates of deposits held by GDB in the Municipality's name. The final transfer to the Municipality of funds held on deposit at GDB are restricted to those reasonable and necessary to ensure the provision of essential services, as determined by the Commonwealth. The Municipality recorded these excess IVU funds as transfers-out in the debt service fund and as transfers-in the general fund.

Effective July 22, 2016 the Commonwealth approved Act No. 84 of 2016 which amends Acts 18 and 19 of 2014 to establish, among other provisions, that (1) the FAM, and accordingly, the Municipal Development Fund, Municipal Redemption Fund and the Municipal Improvements Fund are no longer under custody of GDB but instead under custody of one or more private financial institutions as designated by COFIM and (2) effective July 1, 2016 neither GDB nor the FAFAA have the authority to make advances payable from the 1% Municipal Transfer. During fiscal year 2016-2017 COFIM make a monthly distribution of the actual 1% SUT revenue to the municipalities. Funds related to the Municipal Development Fund and the IVU Municipal Redemption Fund are not being actually distributed.

## NOTE M – INTERGOVERNMENTAL REVENUES AND FEES, FINES AND CHARGES FOR SERVICES - GENERAL FUND

*1.* Intergovernmental revenues in the General Fund are comprised of the following:

| | Amount |
|---|---|
| Amount of municipal equalization fund sent by CRIM | $ 4,803,483 |
| Reimbursement from P.R. Department of Treasury - Christmas Bonus reimbursement | 136,326 |
| Additional uniform contribution and special laws and pensioner additional benefits subsidy from Commonwealth Government | 309,812 |
| | **$ 5,249,621** |

*2.* Fees, fines and charges for services revenues reported in the general fund are comprised of the following:

| | Amount |
|---|---|
| Compensation in lieu of tax from the Puerto Rico Electric Power Authority (PREPA) | $ 5,661,186 |
| P.R. Department of Education – transportation services to students | 352,426 |
| Construction excise tax | 265,350 |
| Rental income | 148,863 |
| Licenses and permits | 65,905 |
| Land lots sales | 165,105 |
| Other | 125,926 |
| | **$ 6,784,761** |

## NOTE N – RETIREMENT PLAN

### *1. Plan description*

The Municipality is a participating employer in a retirement plan administered by the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). ERS covered all regular full-time public employees working for the executive and legislative branches of the Commonwealth and the municipalities of Puerto Rico (including mayors); the firefighters and police of Puerto Rico and employees of certain public corporations not having their own retirement systems. Prior to July 1, 2013 the system operated under the following benefits structures:

- Act No. 447 of May 15, 1951 ("Act 447") effective on January 1, 1952 for members hired up to March 31, 1990,
- *Act No. 1 of February 16, 1990* ("Act 1") for members hired on or after April 1, 1990 and ending on or before December 31, 1999,
- *Act No. 305 of September 24, 1999* (which amended Act 447 and Act 1) for members hired from January 1, 2000 up to June 3, 2013.

Employees under Act 447 and Act 1 are participants of a cost-sharing multiple employer defined benefit plan. Act 305 members are participants under a pension program known as System 2000, a hybrid defined contribution plan. Under System 2000 there was a pool of pension assets invested by the System, together with those of the current defined benefit plan. Benefits at retirement age were not guaranteed by the Commonwealth and were subjected to the total accumulated balance of the savings account. Effective on July 1, 2013 Act No. 3 of 2013 ("Act 3") amends the provisions of the different benefits structures under the ERS. Act 3 moves all participants (employees) under the defined benefit pension plans (Act 447 and Act 1) and the defined contribution plan (System 2000) to a new defined contribution hybrid plan. Contributions are maintained by each participant in individual accounts. Credits to the individual accounts include (1) contributions by all members of ERS Act 447 and Act 1 defined benefit pension plans after June 30, 2013; (2) the retirement savings account as of June 30, 2013 of System 2000 participants and, (3) the investment yield for each semester of the fiscal year.

### *2. Benefits provided*

*Eligibility for retirement.* Act 3 establish the following retirement eligibility requirements: (1) Act 447 regular employees upon attaining a range between 59 to 61 years (depending of date of birth) and 10 years of creditable service, (2) Act 1 employees upon attaining 55 years with 30 years of creditable service, (3) System 2000 regular employees upon attaining a range between 61 to 65 years (depending of date of birth) and, (4) Act 3 employees hired after July 1, 2013 upon reaching 67 years. High risk employees (state and municipal police, firefighters and custody officials) under Act 447 and Act 1 will be eligible at 55 years with 30 years of creditable service, for System 2000 employees at 55 years of service and for Act 1 employees hired after July 1, 2013 upon reaching 58 years.

*Accrued benefits.* All members are entitled to a lifetime annuity based on the balance of the deferred contribution individual account at the time of the retirement calculated based on a factor that will incorporate the individual's life expectancy and a rate of return. For Act 447 and Act 1 active participants all retirement benefits accrued through June 30, 2013 were frozen, and thereafter, all future benefits accrue under Act 3 plan. These participants will receive a pension at retirement age equivalent to what they have accrued under Act 447 and Act 1 up to June 30, 2013 plus the lifetime annuity corresponding to contributions made to the individual account after July 1, 2013 as described above. Act 447 participants, except police and mayors, may elect to coordinate coverage with Social Security benefits ("Coordinated plan"). Under this option participants are subject to a benefit recalculation upon attainment of the Social Security Retirement Age. For all members, if the balance of the defined contribution individual account is less than $10,000 the amount shall be paid as a lump sum instead of an annuity. Effective July 1, 2013 the minimum monthly pension amount for members who retired or disabled before July 1, 2013 is $500.

**NOTE N – RETIREMENT PLAN - Continued**

*Termination benefits.* Members are eligible to a lump sum payment of the defined contribution individual account as of the date of the permanent separation of service upon termination of service prior to 5 years of service or if the balance of the defined contribution individual account is less than $10,000.

*Deferred retirement.* Members are eligible at the applicable retirement eligibility age to a lifetime annuity based on the balance of the deferred contribution individual account plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members) upon termination of service with 5 or more years of service (10 years of creditable service for Act 447 and Act1 members) but prior to the applicable retirement eligibility, provided the member has not taken a lump sum withdrawal from the defined contribution individual account.

*Death benefits.* For non-retired members their designated beneficiaries will receive a refund of the balance of the deferred contribution individual account plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members). For pensioned members retired prior to June 30, 2013 the annual income to a widow or widower or dependent children is equal to 60% of the retirement benefit payable for life for a surviving spouse or disabled children and payable until age 18 or age 25 if pursuing studies for non-disabled children. For pensioned members retired after June 30, 2013 payments to beneficiaries will be the excess, if any, of the balance of the deferred contribution individual account plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members) over the total annuity payments paid to the member and any beneficiaries.

*Disability benefits.* Members who are permanently separated from service due to total and permanent disability, due to disability pursuant to Act No. 127 of June 27, 1958, as amended, or due to terminal illness, as determined by the Administrator, shall be entitled to the balance of the deferred contribution individual account in a lump sum, or through the grant of an annuity, or any other optional form of payment pursuant to Section 5-110 of Act No. 447, at the option of the participant, plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members) at the applicable retirement eligibility age. Beginning on June 30, 2013, no disability pensions shall be awarded pursuant to Sections 2-107 thru 2-111 of Act No. 447. A disability benefits program is established which shall provide a temporary annuity in the event of total and permanent disability. Disability benefits may be provided through one or more disability insurance contracts with one or more insurance companies authorized by the Office of the Commissioner of Insurance of Puerto Rico to conduct business in Puerto Rico. The determination as to whether a person is partially or totally and permanently disabled, shall be made by the insurance company that issues the insurance policy covering the participant.

*Special laws and pensioner additional benefits.* The Municipality is required to cover other retirement benefits of its retired employees (if retired prior to July 1, 2013) as required by Commonwealth's laws, including: (1) various special laws – ad-hoc cost of living allowance adjustments (COLA) provided in prior years; (2) various special laws –additional minimum pension benefits and, (3) Act 3 retired pensioners "Additional Benefits Program". All of these other retirement benefits are applicable only to employees who retired prior to July 1, 2013 under Act 447 and Act 1. The "Additional Benefits Program" includes: (1) a medication bonus of $100 per member which shall be paid no later than July 15 of each year; (2) a Christmas bonus of $200 per member which shall be paid no later than December 20 of each year and, (3) a matching share of $1,200 for healthcare insurance plan. These healthcare benefits are provided through insurance companies whose premiums are paid by the retired employees with the matching share financed by the Municipality.

3. ***Contributions***

The Act No. 3 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. Contribution rates are not actuarially determined.

**NOTE N – RETIREMENT PLAN - Continued**

*Members.* All participants (non-coordinated plan) are required to contribute 10% of gross salary. Participants under the Coordinated plan (only Act 447 participants with benefits coordinated with social security benefits, as described above) are required to contribute 10% of gross salary effective July 1, 2015. Members may voluntarily make additional contributions to their defined contribution individual account.

*Payroll-based employer contribution.* The Municipality contributed 14.275% of gross salary for fiscal year 2015-2016. Act 3 requires an additional 1% annually for each of the next fiscal year and 1.25% annually for each of the five years thereafter, reaching an aggregate contribution rate of 20.525% effective July 1, 2020. The Municipality contributed $634,297 during fiscal year 2015-2016. These amount represented the 100% of the required contribution for the corresponding year.

*Additional uniform contribution.* To improve the liquidity and solvency of the ERS, the Commonwealth enacted Act No. 32 of 2013, which amended Act 447 to provide for an Additional Uniform Contribution ("AUC"). The AUC will be financed by all participating employers (including the Municipality) of the ERS. Beginning with the 2014-2015 until 2032-2033 fiscal year, the AUC will be the uniform contribution certified by the external actuary of the ERS at least 120 days prior to the start of each fiscal year, as necessary to avoid having the projected gross assets of the ERS, during any subsequent fiscal year, to fall below $1,000,000,000. The ERS will determine the amount of AUC to be billed and paid by each employer during each fiscal year. Commonwealth laws provide for a subsidy of the AUC obligation, applicable to all participating employers (including the Municipality) of the ERS that the Puerto Rico Office of Management and Budget ("OMB") determine do not have financial capability to pay the AUC obligation. For fiscal year 2015-2016 the Municipality's AUC obligation amounted to $167,722 and the OMB provided a subsidy of $41,930.

*Disability insurance.* As described above, a disability benefits program is established which shall provide a temporary annuity in the event of total and permanent disability. All members shall mandatorily contribute to a disability insurance established by Act 3 for which participants shall have to contribute such sums, fixed in dollars or a percent of the salary determined by the ERS. The contribution required is equal to or less than .25% of the participant's salary. This contribution shall not be credited to the participant's deferred contribution individual account.

*Special laws and pensioner additional benefits.* These other retirement benefits are funded on a pay-as-you-go basis and billed by ERS to the Municipality at the beginning of each fiscal year. As required by Act 3, the invoice includes a supplemental contribution of $2,000 per pensioner to finance the Additional Benefits Program. The Municipality recorded $404,088 as expenditure in the general fund for these additional benefits for the fiscal year 2015-2016 and the OMB provided a subsidy of $207,307.

The Municipality recorded as other assets in the government-wide and fund statements $309,812 of excess credits related to the AUC and special laws and additional pensioner benefits which will be applied to fiscal year 2016-2017 expenditures.

4. ***Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions; Actuarial assumptions; Discount rate; Sensitivity of the Municipality's proportionate share of the net pension asset to changes in the discount rate; Pension plan fiduciary net position.***

The ERS has not issued audited financial statements as of and for the fiscal year ended June 30, 2015 nor has provided to the Municipality the required information to record transactions related to GASB Statement No. 68 as of and for the fiscal year ended June 30, 2016. Amounts reported in the government-wide financial statements as deferred outflows of resources, deferred inflows of resources and net pension liability are the same amounts reported in the 2015 financial statements. Accordingly, additional disclosures required by GASB Statement No. 68 and required supplementary information have been omitted.

## NOTE O – 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 $157,012. 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, 2016 of $1,786,221 for construction, improvements or renovation of certain municipal facilities.

### *3. Encumbrances*

As of June 30, 2016, the Municipality has encumbrances outstanding totaling $300,935 which represent the estimated amount of expenditures required to complete contracts, purchase orders and other commitments in process of completion at fiscal year-end. Outstanding encumbrances as of June 30, 2016, are reported as unassigned amounts in the general fund. Purpose classification follows:

| Purpose | General Fund-unassigned fund balance |
|---|---|
| General public works and sanitation | $ 132,921 |
| Culture and recreation | 28,000 |
| Welfare | 4,692 |
| General government and other purposes | 135,322 |
| | **$ 300,935** |

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 P - 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.

### *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. For cases not to be covered by insurance, the Municipality accrued as long-term debt $25,000 as of June 30, 2016. 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 - CONTINGENCIES – Continued

*3. **Deposits in governmental bank***

As fully described in Note B (2), GDB is facing fiscal, operational and liquidity difficulties. Based on these facts, the Municipality's management determined that an uncertainty exists on whether the Municipality may or may not recover in the value of the investments in deposits in GDB. This uncertainty is caused by the lack of sufficient and accurate information about GDB's future outcome or any certain determination of GDB's or Commonwealth's authorities with regard to its investments in bank deposits of the municipalities and other Commonwealth's entities. At present, GDB has not issued its audited financial statements for the fiscal years 2015 and 2016. Furthermore, the final outcome of GDB's fiscal plan submitted to the Financial Oversight and Management Board for Puerto Rico ("the Board") for evaluation and approval, as well as its future role as a Commonwealth's governmental entity are uncertain. The Commonwealth's intents to honor withdrawals and mitigate the possibility of unrecoverable amounts. As stated in the moratorium Acts and executive orders issued, although governmental entities, including municipalities, are currently suffering restrictions to access its funds deposited in GDB, such deposits are currently honored and will continue to be honored subject to GDB's adequate liquidity levels and compliance by governmental entities of request requirements of such moratorium Acts and executive orders. After year-end, the Municipality received certain amounts of cash deposits held at GDB subject to the limitation imposed by moratorium regulations including installment payments of certificates of deposits and escrow amounts of undisbursed proceeds of bonds and notes. GDB continued to pay principal and interest on general and special obligation bonds and notes.

Since is reasonably possible that the recoverability of deposits in GDB may be affected, the Municipality performed a detailed analysis of its deposits in GDB in order to determine if a proper estimate of an impairment in the value of the investments in deposits in GDB may be calculated and disclosed. As a result of the analysis the Municipality determined the net amounts of deposits at GDB per fund and category as of March, 2017. Notwithstanding, the Municipality concluded that, from these net amounts of deposits, an amount of an impairment loss in the value of the net deposits in GDB cannot be reasonably estimated to be disclosed. There are no competent and accurate sources of information to determine if the total amount is impaired, to determine a percent of impairment or to determine a range of loss of impairment. The calculation of an estimate is affected by the lack of GDB's actualized financial data and the uncertainty related to the final outcome of the bank deposits by GDB.

These matters are ongoing and the Municipality cannot predict when and how will be its final outcome.

## NOTE Q – SUBSEQUENT EVENTS

The Municipality has evaluated subsequent events through March XX, 2017, which is the date the financial statements were available to be issued. The following events were identified which management decided should be disclosed:

*1. **Amendments to moratorium Act***

As described in Note B (2), Act No. 21 of 2016 was amended by Act No. 2 of January 18, 2017 16 to create under a separate Act the Puerto Rico Fiscal Agency and Financial Advisory Authority ("FAFAA") and by Act No. 5 of January 29, 2017 known as the *Puerto Rico Financial Emergency and Fiscal Responsibility Act* to expand the Act enforcement powers pursuant to the approval by the U.S. Government of PL 114-187 known as the *Puerto Rico Oversight, Management and Economic Stability Act* ("PROMESA"). The FAFAA was created for the purpose of acting as fiscal agent, financial advisor and reporting agent of the Commonwealth and its public corporations, instrumentalities, commissions, authorities, municipalities and political subdivisions, to assist such entities in confronting the grave fiscal and economic emergency that the Commonwealth is currently experiencing and to perform oversight supervision of fiscal plans of applicable Commonwealth entities, including GDB, resulting from the requirements of PROMESA. All fiscal agency, financial advisory, and reporting functions of GDB were transferred to FAFAA.

**NOTE Q – SUBSEQUENT EVENTS - Continued**

2. ***Act No. 84 of 2016***

As described in Note L, effective July 22, 2016 the Commonwealth approved Act No. 84 of 2016 which amends Acts 18 and 19 of 2014 to establish, among other provisions, that (1) the FAM, and accordingly, the Municipal Development Fund, Municipal Redemption Fund and the Municipal Improvements Fund are no longer under custody of GDB but instead under custody of one or more private financial institutions as designated by COFIM and (2) effective July 1, 2016 neither GDB nor the FAFAA have the authority to make advances payable from the 1% Municipal Transfer. Funds related to the Municipal Development Fund and the Municipal Redemption Fund are not being actually distributed to the municipalities.

3. ***Commonwealth's Fiscal Plans***

As part of the requirements of PL 114-187 known as the *Puerto Rico Oversight, Management and Economic Stability Act* ("PROMESA"), on February 21, 2017 and February 28, 2017 GDB, other Commonwealth entities as well as the Commonwealth itself submitted drafts of it fiscal plans to the *Financial Oversight and Management Board for Puerto Rico* ("the Board") for evaluation and approval. The Commonwealth's fiscal plan was approved by the Board on March 13, 2017. The final plans and future role of the other governmental entities, including GDB, is uncertain since the drafts are still under evaluation by the Board.

The Commonwealth's approved fiscal plan discusses important reforms that may have a significant impact on the municipalities' finances as follows:

- ***Modernization the property tax regime*** - proposed measures will gradually eliminate the Commonwealth's $350MM subsidy to the municipalities and provide municipalities with a modernized property tax regime in order to fill the gap. The Commonwealth expects that the new system will produce a total of $426 million in revenues, at least $350 million to the municipalities and approximately $76 million to the central government with streamlined operations at the CRIM producing incremental savings and increased collection rates. Changes will gradually be implemented starting in fiscal year 2017-2018.

- ***Retirement plans reform*** - the Plan includes a comprehensive reform of the retirement plans including switch to pay-as-you-go model to cover remaining defined benefit obligations, segregate prospective employee contributions into new and separated defined contribution plans, facilitate enrollment in social security for qualifying participants and improve investment alternatives offered to participants, taking into consideration personal retirement objectives. These measures face significant challenges including legislation to finally determine the necessary changes in legal and operational structure of the retirement systems. As the municipalities role as a participating employer of ERS, some of these initiatives such as switching to a pay-as-you-go model and the enactment of a new and separated defined contribution plan may have a significant impact in the municipalities fiscal operations. Changes are currently under implementation and due in fiscal year 2017-2018.

- ***Health reform*** - the Plan includes a reform of the Governmental Health Insurance Plan ("Plan Mi Salud"), which includes, among other initiatives, (1) establish uniformed fee schedules for providers and ancillary services; (2) establish a MFCU office to investigate and prosecute Medicaid to investigate and prosecute providers and patients that misuse Medicaid funds; (3) establish MMIS platform to process the credentialing of providers, determine eligibility, authorize and pay claims; (4) implementing cost-savings strategies to control outpatient drug spending and (5) evaluate services that could be capped and/or eliminated from the current benefit package. At large, the process will end in a new healthcare model in which the Commonwealth pays for less costly benefits and the

**NOTE Q – SUBSEQUENT EVENTS - Continued**

patient pays for premium services selected resulting in cost reductions attributed to greater competition. At present, the municipalities contribute to the Puerto Rico Health Insurance Administration ("ASES") to fund Plan Mi Salud through budgetary appropriations for direct health services in areas covered by the government health plan. The charges made by ASES based on established percentages applied to the corresponding municipalities' operational budget for the lesser of current year or fiscal year 2003-2004 as set forth in Act No. 72 of September 7, 1993, as amended. These contributions are withheld by the Municipal Revenue Collection Center from money assigned to the municipalities and remitted to ASES on a monthly basis. The final impact of the health care reform on the Municipality's financial position or operations cannot be determined.

4. ***New Regulations - Contribution in lieu of taxes from PREPA and Municipality's claim***

The contribution in lieu of taxes ("CELI") is the mechanism, established by the Puerto Rico Electric Power Authority's ("PREPA") Organic Act, by which the utility compensates municipalities with power, in exchange for municipal tax exemption. To meet these goals, the Puerto Rico Energy Commission ("PREC ") approved Regulation Number 8818 of September 17, 2016 on CELI (an amendment to Regulation Number 8653 of October, 2015) to ensure the adoption of the necessary regulations to implement the compensation mechanism. The guidelines limit the subsidy that can be received by the municipalities by establishing a maximum threshold amount of energy consumption charges that can be incurred. In addition, it determines, after an evaluation process of the Municipality's properties, which properties can be covered by the CELI and which not. Municipalities would be billed and subject to pay from their unrestricted resources energy consumption charges from properties excluded from CELI's coverage. Regulations provide different methods for payment (including payment plans) and objection procedures. These new Regulations are effective for fiscal year 2016-2017 and thereafter.

SGME, a Municipal Enterprise, is reported as a blended component unit in the Municipality's financial statements. Since February, 2015 the Municipality assumed the responsibility for the payment of those charges, under the CELI's coverage applicable to Municipality's units. A claim by the Municipality is still under evaluation by PREPA as of March, 2017 by which the Municipality is requesting the coverage under CELI of SGME energy consumption charges under the new Regulations. The ultimate resolution of this matter could not be determined.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SAN GERMAN
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2016

| | Budgeted amounts | | Actual amounts | Variance with final budget |
|---|---|---|---|---|
| | Original | Final | (Budgetary basis) | Positive (Negative) |
| **Revenues:** | | | | |
| Taxes: | | | | |
| Property taxes | $ 4,025,785 | $ 4,025,785 | $ 4,025,785 | $ - |
| Municipal license taxes | 2,550,494 | 2,550,494 | 3,097,900 | 547,406 |
| Sales and use taxes | 2,006,597 | 2,006,597 | 1,735,929 | (270,668) |
| Intergovernmental | 3,806,069 | 3,806,069 | 3,957,207 | 151,138 |
| Rental income and charges for services | 5,648,772 | 5,788,772 | 3,697,919 | (2,090,853) |
| Fines and forfeitures | 15,000 | 15,000 | 8,334 | (6,666) |
| Interest | 250,000 | 250,000 | 104,462 | (145,538) |
| Other | 188,282 | 48,282 | 54,951 | 6,669 |
| **Total Revenues** | 18,490,999 | 18,490,999 | 16,682,487 | (1,808,512) |
| **Expenditures:** | | | | |
| Current: | | | | |
| General government | 7,336,482 | 6,642,506 | 5,862,960 | 779,546 |
| Public safety | 1,523,025 | 1,327,461 | 1,327,186 | 275 |
| Public works and sanitation | 7,206,121 | 7,331,081 | 7,289,989 | 41,092 |
| Health | 786,764 | 786,764 | 786,763 | 1 |
| Welfare | 580,507 | 504,490 | 503,400 | 1,090 |
| Culture and recreation | 613,660 | 580,413 | 576,627 | 3,786 |
| Debt service- Interest | 444,440 | - | - | - |
| **Total expenditures** | 18,490,999 | 17,172,715 | 16,346,925 | 825,790 |
| **Excess (deficiency) of revenues over expenditures** | - | 1,318,284 | 335,562 | (982,722) |
| **Other financing sources (uses)** | | | | |
| Transfers - out | - | (1,318,284) | (1,316,455) | 1,829 |
| **Total other financing sources (uses)** | - | (1,318,284) | (1,316,455) | 1,829 |
| **Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses** | $ - | $ - | $ (980,893) | $ (980,893) |

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

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMÁN**
**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION -**
**BUDGETARY COMPARISON SCHEDULE – GENERAL FUND**
**June 30, 2016**

## 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 1991, 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 accounting principles generally accepted in the United States of America ("US 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 or contracts) are considered expenditures when a commitment is made. On a US GAAP basis encumbrances outstanding at year-end are reported in the governmental fund balance sheet 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 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, 2016**

**NOTE B - BUDGET TO GAAP RECONCILIATION - Continued**

| | | |
|---|---|---|
| **Excess of revenues and other financing sources over expenditures and other financing uses (budgetary basis):** | **$** | **(980,893)** |
| Budget to GAAP differences: | | |
| Non-budgeted funds recorded as revenues for financial reporting purposes: | | 152,564 |
| Non-budgeted funds recorded as expenditures for financial reporting: | | (230,325) |
| Non budgeted transfers out: | | (43,131) |
| Revenues recorded for financial reporting purposes but not in budgetary basis: | | 5,254,071 |
| Expenditures recorded in budgetary basis but not for financial reporting purposes: | | 54,135 |
| Expenditures recorded for financial reporting purposes but not in budgetary basis: | | (3,590,258) |
| Current year encumbrances recorded as expenditures for budgetary reporting purposes: | | 300,935 |
| Prior year encumbrances recorded as expenditures for financial reporting purposes: | | (231,391) |
| **Net change in fund balance (GAAP basis):** | **$** | **685,706** |

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE**
**BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION**
**JUNE 30, 2016**

| | | 14.871 |
|---|---|---|
| **Line Item No.** | **Description** | **Housing Choice Vouchers** |
| | **Balance Sheet** | |
| 111 | Cash - unrestricted | $ 34,421 |
| 113 | Cash - other restricted | $ 12,100 |
| 100 | **Total cash** | **$ 46,521** |
| 121 | Accounts receivable - PHA projects | $ 1,450 |
| 125 | Accounts receivable - miscellaneous | $ 1,150 |
| 126.2 | Allowance for doubtful accounts - other | $ (1,265) |
| 128 | Fraud recovery | $ 9,940 |
| 128.1 | Allowance for doubtful accounts - fraud | $ (3,848) |
| 120 | Total receivables, net of allowance for doubtful accounts | $ 7,427 |
| 150 | **Total Current Assets** | **$ 53,948** |
| 164 | Furniture, equipment and machinery - administration | $ 67,450 |
| 166 | Accumulated depreciation | $ (47,682) |
| 160 | Total capital assets, net of accumulated depreciation | $ 19,768 |
| 180 | **Total Non-current Assets** | **$ 19,768** |
| 190 | **Total Assets** | **$ 73,716** |
| 200 | **Deferred Outflows of Resources** | **$ -** |
| 290 | **Total Assets and Deferred Outflows of Resources** | **$ 73,716** |
| 313 | Accounts payable > 90 days past due | $ - |
| 322 | Accrued compensated absences - current portion | $ 8,611 |
| 332 | Accounts Payable - PHA Projects | $ 6,891 |
| 333 | Accounts payable - other government | $ 621 |
| 310 | **Total Current Liabilities** | **$ 16,123** |
| 353 | Non-current liabilities - other | $ 956 |
| 354 | Accrued compensated absences - non current | $ 234 |
| 350 | **Total Non-current Liabilities** | **$ 1,190** |
| 300 | **Total Liabilities** | **$ 17,313** |
| 300 | **Deferred Inflows of Resources** | **$ -** |
| 508.1 | Net Investment in Capital Assets | $ 19,768 |
| 511.1 | Restricted Net Position | $ 17,236 |
| 512.1 | Unrestricted Net Position | $ 19,399 |
| 513 | **Total Equity/Net Position** | **$ 56,403** |
| 600 | **Total Liabilities, Deferred Inflows of Resources and Equity/Net Position** | **$ 73,716** |
| | **Income Statement** | |
| 70600-010 | Housing assistance payments | $ 350,807 |
| 70600-020 | Ongoing administrative fees earned | $ 63,424 |
| 70600-031 | FFS Coordinator Grant | $ 39,490 |
| 70600 | **HUD PHA operating grants** | **$ 453,721** |
| 71100-010 | Housing Assistance Payment | $ - |
| 71100-020 | Administrative Fee | $ - |
| 71100 | Investment income - unrestricted | $ 71 |

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE**
**BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION**
**JUNE 30, 2016**

| | | 14.871 |
|---|---|---|
| **Line Item No.** | **Description** | **Housing Choice Vouchers** |
| | **Balance Sheet** | |
| 71400-010 | Housing Assistance Payment | $ - |
| 71400-020 | Administrative Fee | $ - |
| 71400 | Fraud recovery | $ 414 |
| 71500 | Other revenue | $ 75,664 |
| 700 | **Total Revenue** | **$ 529,870** |
| 91100 | Administrative salaries | $ 45,070 |
| 91500 | Employee benefit contributions- administrative | $ 11,712 |
| 91600 | Office expenses | $ 7,157 |
| 91000 | **Total Operating - Administrative** | **$ 63,939** |
| 92100 | Tenant services - salaries | $ 1,400 |
| 92300 | Employee benefit contributions- tenant services | $ 107 |
| 92400 | Tenant services - other | $ 39,175 |
| 96000 | **Total Tenant Services** | **$ 40,682** |
| 96900 | **Total Operating Expenses** | **$ 104,621** |
| 97000 | **Excess Revenue Over Operating Expenses** | **$ 425,249** |
| 97300-050 | All Other | $ 356,021 |
| 97300 | **Housing assistance payments** | **$ 356,021** |
| 97350 | **HAP Portability-in** | $ 59,049 |
| 97400 | Depreciation expense | $ 3,193 |
| 900 | **Total Expenses** | **$ 522,884** |
| 10000 | **Excess (Deficiency) of Revenue Over (Under) Expenses** | **$ 6,986** |
| 11030 | Beginning equity | $ 49,417 |
| 11770-001 | Administrative Fee Equity - Beginning Balance | $ 33,630 |
| 11170-010 | Administrative Fee Revenue | $ 63,424 |
| 11170-021 | FSS Coordinator Grant | $ 39,490 |
| 11170-040 | Investment Income | $ 63 |
| 11170-045 | Fraud Recovery Revenue | $ 207 |
| 11170-050 | Other Revenue | $ 69,216 |
| 11170-051 | Comment For Other Revenue | This amount corresponds to the administrative fees earned on the portability-in vouchers administered by the Municipality ($10,167) plus the reimbursement received from the initial PHAs of the HAP rent payments made on behalf of the portability-in units during 15-156($59,049). |
| 11170-060 | Total Admin Fee Revenues | $ 172,400 |
| 11170-080 | Total Operating Expenses | $ 104,621 |
| 11170-090 | Depreciation | $ 3,193 |
| 11170-095 | Housing Assistance Portability In | $ 59,049 |
| 11170-101 | Comment For Other Expense | |
| 11170-110 | Total Expenses | $ 166,863 |
| 11170-002 | Net Administrative Fee | $ 5,537 |
| 11170-003 | Administrative Fee Equity - Ending Balance | $ 39,167 |
| 11170 | **Administrative Fee Equity** | **$ 39,167** |

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE**
**BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION**
**JUNE 30, 2016**

| | | 14.871 |
|---|---|---|
| **Line Item No.** | **Description** | **Housing Choice Vouchers** |
| | **Balance Sheet** | |
| 11170-005 | Pre-2004 Admininstrative Fee Reserves | $ 15,980 |
| 11170-006 | Post-2003 Admininstrative Fee Reserves | $ 23,187 |
| 11180-001 | Housing Assistance Payments Equity - Beginning Balance | $ 15,787 |
| 11180-010 | Housing Assistance Payments Revenues | $ 350,807 |
| 11180-015 | Fraud Recovery Revenue | $ 207 |
| 11180-020 | Other Revenue | $ 6,448 |
| 11180-021 | Comment For Other Revenue | This amouunt corresponds to the forteiture of an accumulated escrow fund for a family self-sufficiency participant non recertificaed during the year. |
| 11180-025 | Investment Income | $ 8 |
| 11180-030 | Total HAP Revenues | $ 357,470 |
| 11180-080 | Housing Assistance Payments | $ 356,021 |
| 11180-100 | Total Housing Assistance Payments Expenses | $ 356,021 |
| 11180-002 | Net Housing Assistance Payments | $ 1,449 |
| 11180-003 | Housing Assistance Payments Equity - Ending Balance | $ 17,236 |
| 11180 | **Housing Assistance Payments Equity** | **$ 17,236** |
| 11190-210 | Total ACC HCV Units | 1,053 |
| 11190 | **Unit Months Available** | **1,053** |
| 11210 | **Unit Months Leased** | **997** |

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE**
**BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION**
**JUNE 30, 2016**

| | | 14.896 |
|---|---|---|
| **Line Item No.** | **Description** | **Family Self-Sufficiency** |
| | **Balance Sheet** | |
| 115 | Cash - restricted for payment of current liability | $ - |
| 100 | **Total cash** | $ - |
| | | |
| 150 | **Total Current Assets** | $ - |
| | | |
| 190 | **Total Assets** | $ - |
| | | |
| 200 | **Deferred Outlows of Resources** | $ - |
| | | |
| 290 | **Total Assets and Deferred Outflows of Resources** | $ - |
| | | |
| 333 | Accounts payable - other government | $ - |
| 310 | **Total Current Liabilities** | $ - |
| | | |
| 300 | **Total Liabilities** | $ - |
| | | |
| 300 | **Deferred Inflows of Resources** | $ - |
| | | |
| 508.1 | Net Investment in Capital Assets | $ - |
| 511.1 | Restricted Net Position | $ - |
| 512.1 | Unrestricted Net Position | $ - |
| 513 | **Total Equity/Net Position** | $ - |
| | | |
| 600 | **Total Liabilities, Deferred Inflows of Resources and Equity/Net Position** | $ - |
| | | |
| | **Income Statement** | |
| 70600-031 | FFS Coordinator Grant | $ 19,273 |
| 70600 | **HUD PHA operating grants** | $ **19,273** |
| | | |
| 700 | **Total Revenue** | $ **19,273** |
| | | |
| 92100 | Tenant services - salaries | $ 15,600 |
| 92300 | Employee benefit contributions- tenant services | $ 3,673 |
| 96000 | **Total Tenant Services** | $ **19,273** |
| | | |
| 96900 | **Total Operating Expenses** | $ **19,273** |
| | | |
| 97000 | **Excess Revenue Over Operating Expenses** | $ - |
| | | |
| 900 | **Total Expenses** | $ **19,273** |
| | | |
| 10000 | **Excess (Deficiency) of Revenue Over (Under) Expenses** | $ - |
| | | |
| 11030 | Beginning equity | $ - |
| | | |
| 11770-001 | Administrative Fee Equity - Beginning Balance | $ - |
| 11170-021 | FSS Coordinator Grant | $ 19,273 |
| 11170-060 | Total Admin Fee Revenues | $ 19,273 |
| 11170-080 | Total Operating Expenses | $ 19,273 |
| 11170-110 | Total Expenses | $ 19,273 |
| 11170-002 | Net Administrative Fee | $ - |
| 11170-003 | Administrative Fee Equity - Ending Balance | $ - |
| 11170 | **Administrative Fee Equity** | $ - |
| 11170-005 | Pre-2004 Admininstrative Fee Reserves | $ - |
| 11170-006 | Post-2003 Admininstrative Fee Reserves | $ - |
| | | |
| 11180-001 | Housing Assistance Payments Equity - Beginning Balance | $ - |
| 11180-030 | Total HAP Revenues | $ - |
| 11180-080 | Housing Assistance Payments | $ - |
| 11180-100 | Total Housing Assistance Payments Expenses | $ - |
| 11180-002 | Net Housing Assistance Payments | $ - |
| 11180-003 | Housing Assistance Payments Equity - Ending Balance | $ - |
| 11180 | **Housing Assistance Payments Equity** | $ - |
| | | |
| 11190-210 | Total ACC HCV Units | - |
| 11190 | **Unit Months Available** | - |
| 11210 | **Unit Months Leased** | - |

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMÁN**
**NOTES TO SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULES**
**June 30, 2016**

## NOTE A – BASIS OF PRESENTATION

The accompanying financial data schedules ("FDS") are trial balances of the financial statements of the Section 8 Housing Choice Voucher and Family Self-Sufficiency Programs administered by the Municipality. The FDS were 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. Because the FDS present only a selected portion of the operations of Municipality, they are not intended to, and do not present, the financial position and changes in net position of the Municipality.

## NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

In accordance with the guidelines for reporting and attestation requirements of UFRS, the accompanying FDS are 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, 2016

| Federal Grantor/Pass Through Grantor/Program Title | Federal CFDA Number | Pass-Through Entity Identifying Number | Pass-through to Subrecipients | Federal Expenditures |
|---|---|---|---|---|
| **U.S. Department of Agriculture** | | | | |
| Direct programs: | | | | |
| Passed-through program from: | | | | |
| P.R. Department of Education | | | | |
| Child and Adult Care Food Program | 10.558 | CCC-269 | $ - | $ 97,491 |
| **U.S. Department of Housing and Urban Development** | | | | |
| Direct programs: | | | | |
| Community Development Block Grants / Entitlement Grants | 14.218 | N/A | - | 546,606 |
| Community Development Block Grants - Program Income | 14.218 | N/A | - | 497 |
| Shelter Plus Care | 14.238 | N/A | - | 56,685 |
| Section 8 Housing Choice Vouchers Program | 14.871 | N/A | - | 453,721 |
| Family Self-Sufficiency (FSS) Program | 14.896 | N/A | - | 19,273 |
| Passed-through program from: | | | | |
| P.R. Department of Family: | | | | |
| Emergency Shelter Grants Program | 14.231 | S08DC720001, S09DC720001 | - | 29,265 |
| P.R. Department of Health: | | | | |
| Housing Opportunities for Persons with AIDS (HOPWA) | 14.241 | 2008-DS 0618 | - | 45,777 |
| P.R. Department of Housing - (Puerto Rico Public Housing Administration "PRPHA"): | | | | |
| Public and Indian Housing | 14.850 | RQ003091, RQ005145 | - | 1,575,279 |
| **Subtotal U.S. Department of Housing and Urban Development** | | | - | 2,727,102 |
| **U.S. Department of Transportation** | | | | |
| Passed-through program from: | | | | |
| P.R. Traffic Safety Commission | | | | |
| State and Community Highway Safety | 20.600 | 10-06-28, 10-03-76 | - | 94,308 |
| **U.S. Department of Health and Human Services** | | | | |
| Direct programs: | | | | |
| Early Head Start | 93.600 | N/A | - | 2,137,289 |
| Passed-through programs from: | | | | |
| P.R. Office of the Ombudsman for the Elderly: | | | | |
| Special Programs for the Aging_Title III, Part C_Nutrition Services | 93.045 | N/AV | - | 308,961 |
| **Subtotal U.S. Department of Health and Human Services:** | | | - | 2,446,250 |
| **Total Expenditures of Federal Awards** | | | $ - | $ 5,365,151 |

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMÁN**
**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**
**June 30, 2016**

## NOTE A – BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards ("the schedule") includes the federal grant activity of the Municipality under programs of the federal government for the year ended June 30, 2016. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulation (CFR Part 200), Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards* ("Uniform Guidance"). 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 position 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). Expenditures are recognized when the related liability is incurred following the cost principles contained in the Uniform Guidance, 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. The Uniform Guidance 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 sub recipient. 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 |
|---|---|
| 10.558 | $ 97,491 |
| 14.871 | 453,721 |
| 14.896 | 19,273 |
| 14.218 | 546,606 |
| 14.218 (Program Income) | 497 |
| 14.238 | 56,685 |
| 14.231 | 29,265 |
| 14.241 | 45,777 |

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

| CFDA No. / Description | Other Governmental Funds |
|---|---|
| 14.850 | 1,575,279 |
| 20.600 | 94,308 |
| 93.045 | 308,961 |
| 93.600 | 2,137,289 |
| Total federal awards expenditures: | 5,365,151 |
| Additional amount recorded as expenditures under modified accrual basis for Section 8 HCV Program and Public and Indian Housing: | 143,285 |
| Total non-federal awards expenditures: | 2,298,800 |
| Total expenditures, fund statements: | **$ 7,807,236** |

**NOTE D – INDIRECT COST RATE**

The Municipality has elected to use the 10-percent de minimis cost rate allowed under the Uniform Guidance.

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

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

We have audited, in accordance with the 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, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Municipality of San German, Puerto Rico as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise Municipality of San German, Puerto Rico's basic financial statements, and have issued our report thereon dated March 29, 2017. The report on governmental activities was qualified because the Municipality did not record the current pension expense, changes in deferred outflows/inflows of resources and net pension liability, and additional disclosures required by ***GASB Statement No. 68*** and required supplementary information have been omitted.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered Municipality of San German, Puerto Rico's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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 German, Puerto Rico's internal control. Accordingly, we do not express an opinion on the effectiveness of Municipality of San German, Puerto Rico's internal control.

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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Municipality of San German, Puerto Rico's financial statements are free from 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 instance of noncompliance or other matters that are required to be reported under Government Auditing Standards.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

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

Yauco, Puerto Rico
March 29, 2017

Stamp #E256557 was affixed to
the original report

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## INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

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

**Report on Compliance for Each Major Federal Program**

We have audited Municipality of San German, Puerto Rico's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of Municipality of San German, Puerto Rico's major federal programs for the year ended June 30, 2016. Municipality of San German, 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.

**Management's Responsibility**

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

**Auditor's Responsibility**

Our responsibility is to express an opinion on compliance for each of Municipality of San German, Puerto Rico's major federal programs based on our audit of the types of compliance requirements referred to above. 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 Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Those standards and the Uniform Guidance 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 German, 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 on compliance for each major federal program. However, our audit does not provide a legal determination of Municipality of San German, Puerto Rico's compliance.

**Opinion on Each Major Federal Program**

In our opinion, Municipality of San German, Puerto Rico, complied, in all material respects, with the types of 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, 2016.

**Other Matters**

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with the Uniform Guidance and which are described in the accompanying schedule of findings and questioned costs as items 2016-001. Our opinion on each major federal program is not modified with respect to these matters.

The Municipality of San German, Puerto Rico's response to the noncompliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Municipality of San German, Puerto Rico's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

**Report on Internal Control Over Compliance**

Management of Municipality of San German, Puerto Rico, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Municipality of San German, Puerto Rico's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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 German, 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. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified certain deficiencies in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item 2016-001 that we consider to be significant deficiencies.

The Municipality of San German, Puerto Rico's response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Municipality of San German, Puerto Rico's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

**Purpose of this Report**

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of The Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Román Toro & Co.

ROMAN TORO & CO., CPA, C.S.P.
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Yauco, Puerto Rico
March 29, 2017

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the original report

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN, PUERTO RICO**
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**
**FOR THE YEAR ENDED JUNE 30, 2016**

## SECTION I – SUMMARY OF AUDITORS' RESULTS

**Financial Statements**

| | | |
|---|---|---|
| Type of auditor's report issued: | [X] Unmodified Opinion – All Opinion Units except Government-Wide Financial Statements | [X] Qualified Opinion – on Government-Wide Financial Statements |
| | [ ] Adverse Opinion | [ ] Disclaimer |
| Internal control over financial reporting: | | |
| • Significant deficiency identified? | [ ] Yes | [X] None reported |
| • Material weakness (es) identified? | [ ] Yes | [X] No |
| Noncompliance material to financial statements noted? | [ ] Yes | [X] No |

**Federal Awards**

| | | |
|---|---|---|
| Internal control over major programs: | | |
| • Significant deficiency identified? | [X] Yes | [ ] None reported |
| • Material weakness (es) identified? | [ ] Yes | [X] No |
| Type of auditor's report issued on compliance for Major Programs: | [X] Unqualified Opinion | [ ] Qualified Opinion |
| | [ ] Adverse Opinion | [ ] Disclaimer |
| Any audit finding disclosed that are required to be reported in accordance with 2CFR§200.516(a)? | [ ] Yes | [X] No |

Identification of Major Programs:

| CFDA Number | Name of Federal Program or Cluster |
|---|---|
| 14.218 | Community Development Block Grants – Entitlement Grants |
| 14.850 | Public and Indian Housing |
| 93.600 | Head Start |

| | | |
|---|---|---|
| Dollar threshold used to distinguish between Type A and Type B Programs: | $750,000 | |
| Auditee qualified as low-risk auditee? | [ ] Yes | [X] No |

**END OF SECTION**

## SECTION II – FINANCIAL STATEMENTS FINDINGS

NONE.

**END OF SECTION**

## SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**2016-001**

Type of finding: Federal program.
Situation: Significant deficiency; Compliance of program regulations
Federal Program: Community Development Block Grant – Entitlement Grants (CFDA 14.218)
Compliance Requirements: Earmarking (G).
Prior-Year(s) Audit Finding(s): None.
Questioned Costs: $33,763.58

***Condition:***
The Municipality's CDBG program exceeded its public service expenditure limit for a grant during the program year.

***Context:***
CDBG programs are allowed to use program funds for public services to meet its objectives and goals. Public service activities include employment, crime prevention, child care, health, drug abuse, education, fair housing counseling, energy conservation, welfare (with exceptions), homebuyer down-payment assistance, and recreational needs. Most of the public services provided by the Municipality's program are employment/welfare services. During the year, the amounts expended for these services amounted to $110,840.04. Based on the entitlement grant amount of $517,958, the program invested 21.40% in public services, or $33,763.58 in excess of allowed amounts.

***Criteria:***
The amount of CDBG funds obligated during the program year for public services must not exceed 15 percent of the grant amount received for that year plus 15 percent of the program income it received during the preceding program year, as per 24 CFR section 570.201(e).

***Cause:***
At the start of the program year, the program used its funds to cover the public service requirements activity which uses both program and municipal funds, without realizing it had exceeded the budgeted amounts of the program before using municipal funds. Drawdowns performed were tagged for the activity but the percentage drawn down was not noted for the particular activity.

***Effect:***
The Municipality exceeded statutory program limits requiring reimbursement to granting agency.

***Auditor's recommendation:***
The Municipality should revise its transfers with approved budgeted amounts to assure that limits are followed with respect to the activities allowed. Documentation should be provided before approval demonstrating transfers will not exceed required limits.

***Views of responsible officials and corrective actions:***
We agree with the auditors comments. The Federal Programs Office personnel was aware of the situation before the audit finding and such situation was discussed with the awarding agency and it was stated that the Municipality of San German Public Service disbursements was 21.40% which exceeded the allowable amount as per 2 CFR section 570.201 (e).

## SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS (continued)

**2016-001, continued**

***Views of responsible officials and corrective actions (continued):***
The following action will be taken to improve the situation. The accounting division will monitor and document each transaction that involve transfers and affect the established percent. We will consolidate this documents so at the end of the program year, the sum of all transactions will not exceed the CAP allowed for the grant.

Periodic revisions of such documentation will be made by the responsible person, the Director of Federal Programs Office, to ensure that the personnel is following the establish procedures. The staff will be advised of all revisions.

***Audit finding status:***
Unresolved.

**END OF SECTION**

**COMMONWEALTH OF PUERTO RICO**
**MUNICIPALITY OF SAN GERMAN**
**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**
**FOR THE YEAR ENDED JUNE 30, 2016**

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

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

NONE.

**(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**