CHUUK STATE HEALTH CARE PLAN
(A COMPONENT UNIT OF THE STATE OF CHUUK)

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2008 AND 2007

Deloitte.

Deloitte & Touche LLP
361 South Marine Corps Drive
Tamuning, GU 96913-3911
USA
Tel: (671)646-3884
Fax: (671)649-4932
www.deloitte.com

INDEPENDENT AUDITORS' REPORT

The Board of Trustees
Chuuk State Health Care Plan

We have audited the accompanying statements of net assets of the Chuuk State Health Care Plan (the "Plan"), a component unit of the State of Chuuk, as of September 30, 2008 and 2007, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Plan's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Chuuk State Health Care Plan as of September 30, 2008 and 2007, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 8 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Chuuk State Health Care Plan's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 29, 2009, on our consideration of Chuuk State Health Care Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte + Touche LLP

June 29, 2009

This analysis, prepared by the management of the Chuuk State Health Care Plan (the "Plan"), offers readers a narrative overview of the activities of the Plan for the fiscal year ended September 30, 2008. We encourage readers to consider this information in conjunction with the Plan's financial statements, which follow. Fiscal year 2007 and 2006 comparative information has been included, where appropriate. This information is required by the Government Accounting Standards Board, (GASB), which provides guidelines on what must be included and excluded from the analysis.

There are three financial statements presented: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows.

Financial Highlights

- For the fiscal year ended September 30, 2008, the Chuuk State Health Care Plan's net assets decreased by $0.225 million (down 24.7%) from $0.911 million in the prior year to $0.686 million. The decrease is primarily attributable to decreased premium receipts that no longer cover claims expense and operating expenses.

- During fiscal year 2008 the Plan had premium revenues of $0.775 million compared to $0.835 million in fiscal year 2007. The $0.059 million decrease (or 7%) was the result of a declining public sector enrollees as the result of the Chuuk State government reduction in force. Medical claim expenses were $0.76 million in fiscal year 2008 compared to $0.78 million in fiscal year 2007 (down 2.7%). Although claims expenses declined they continued to rise as a percentage of Plan premiums (98%).

- During fiscal year 2008, the Plan incurred a net loss of $0.225 million compared with the net loss of $0.15 million in fiscal year 2007 (up 50%). The loss reflected the declining premiums, disproportionate claims expenses in comparison to those premiums, and an inability to reduce general and administrative expenses.

The Statement of Net Assets

The Statement of Net Assets presents the assets, liabilities and net assets of the Plan as of the fiscal year end and represents a "snapshot" financial statement. The Statement of Net Assets presents end-of-year data concerning assets (current and noncurrent), liabilities (current and noncurrent), and net assets (assets minus liabilities). The difference between current and noncurrent assets and liabilities will be discussed in the footnotes to the financial statements.

From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the operations of the Plan. They are also able to determine how much the Plan owes vendors and others. Finally, the Statement of Net Assets provides a picture of the net assets (assets minus liabilities) that the Plan has available for future expenditures by the Plan.

Net assets are divided into two major categories. The first category, invested in capital assets, net of related debt, provides the institution's equity in property, plant and equipment owned by the Plan. The next asset category is restricted assets, which is divided into two categories, nonexpendable and expendable. The corpus of nonexpendable restricted assets is only available for investment purposes; the Plan has no nonexpendable restricted assets. Expendable restricted net assets are available for expenditures by the Plan but must be spent for purposes determined by donors and/or external entities that have place, time or purpose restrictions on the use of the assets. All the Plan assets that are not otherwise invested in capital assets are restricted by law to be used for health care services.

SUMMARY STATEMENT OF NET ASSETS
(In '000's)

	2008	2007	2006
ASSETS:			
Current assets	$763	$1,060	$1,105
Capital assets, net	35	26	23
Total assets	$798	$1,086	$1,128
LIABILITIES:			
Current liabilities	$112	$175	$67
Non-current liabilities	-	-	-
Total liabilities	112	175	67
NET ASSETS			
Invested in capital assets	35	26	23
Restricted	651	885	1,038
Total net assets	686	911	1,061
Total liabilities and net assets	$798	$1,086	$1,128

The total assets at the end of fiscal year 2008 of $0.798 million exceed the total liabilities of $0.112 million, resulting in net assets of $0.686 million. Of the total net assets, $0.613 million are held in cash, cash equivalents or short-term investments. Another $0.15 million are in the form of accounts receivable. This contrasts to fiscal year 2007 when $0.773 million of the total assets were held in cash or investment equivalents and accounts receivables were $0.287 million. The deteriorating cash and TCD investment position of the Plan in fiscal year 2008 indicates the necessity of the Plan to use cash reserves accumulated in prior years to meet current year expenses. The improved accounts receivable position in fiscal year 2008 reflects collection of prior year receivables from the Chuuk State government. Although, the Plan's 6:1 ratio of current assets to current liabilities still indicates the ability of the Plan to meet its liabilities, the increasing net losses and declining cash reserves represent a trend that must be brought under control if the Plan is to viably meet future operating needs.

Statement of Revenues, Expenses, and Changes in Net Assets

Changes in total net assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of the statement is to present the revenues received by the Plan, both operating and non-operating, and the expenses paid by the institution, operating and non-operating.

Generally speaking, operating revenues are received from income provided by collecting health care premiums from Plan members. Other non-operating revenues are for interest income earning from short-term investments of Plan assets. Operating expenses can be classified as of two types: (i) medical service expenditures provided to eligible enrollees by accredited health care providers, and (ii) other operating expenses necessary to administer the Plan.

SUMMARY STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
(In '000's)

	2008	**2007**	**2006**
REVENUES			
Premiums	$775	$835	$872
Other Revenues	7	10	-
Provisions for Premium losses	(31)	-	-
Claims expenses	(758)	(780)	(639)
Net revenues	(7)	65	233
EXPENSES:			
Other operating expenses	234	242	229
Total other operating expenses	234	242	229
Net earnings (loss)	(242)	(178)	38
Interest Income	17	28	34
Net assets at beginning of year	911	1,061	1,023
Net assets at end of year	$686	$911	$1,061

For the second consecutive year, the Statement of Revenues, Expenses, and Changes in Net Assets reflects a negative year in fiscal year 2008, with an overall $0.225 million decrease (or 24.7%) in net assets from the prior year. Some highlights of the information presented on the Statement of Revenues, Expenses, and Changes in Net Assets are as follows:

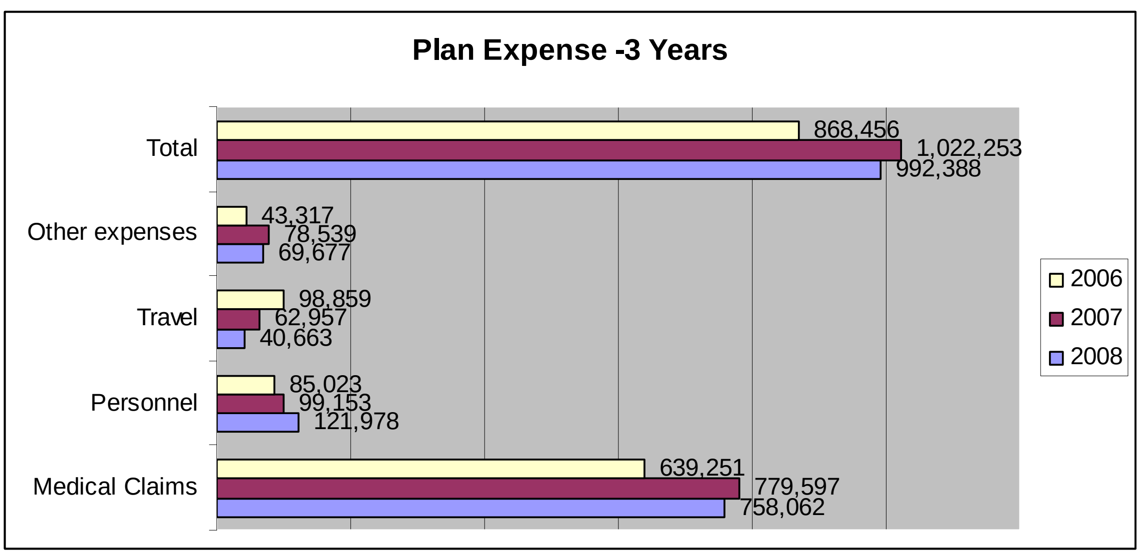
- Premium revenues represent receipts from Plan enrollees. The following table indicates premium revenue activity for fiscal years 2008, 2007 & 2006 for both public and private sector enrollees:

MEMBER COMPOSITION	FY- 2008 # ENROLLED @ 9-30-08	PREMIUMS PAID (000's)	FY- 2007 # ENROLLED @ 9-30-07	PREMIUMS PAID (000's)	FY- 2006 # ENROLLED @ 9-30-06	PREMIUMS PAID (000's)
Public Sector	11,886	$ 715	22,160	$ 776	21,495	$ 845
Private Sector	1,844	60	1,679	58	1,084	27
TOTALS	13,730	$ 775	23,839	$ 834	22,579	$ 872

The chart reflects the marked decline in public sector Plan enrollees in fiscal year 2008, declining from 22,160 in fiscal year 2007 to 11,886 (or 46%) in fiscal year 2008. Two events account for this: (1) the reduction in force (RIF) implemented by the State government in fiscal year 2008 in which 317 employees received termination notices, and (2) the decision by the Plan Board to restrict the number of dependents for each enrollee to a maximum of five (5). The resulting decrease (7%) in Plan premiums is explained by these actions.

- In fiscal year 2008, the Plan recorded a special provision for premium losses of $31 thousand related to uncollectible premiums due from the Chuuk Public Utility Corporation. When all components of premiums, related claims and the special loss provision are rolled together they disclose a comprehensive revenue picture that is actually negative; the first time in the five years of the Plan's existence.

- The major components of Plan expenses during fiscal years 2008, 2007 and 2006 are highlighted by the following graph:



Plan expenses in fiscal year 2008, while showing nominal overall decreases (down 2.9%) from the prior year, are still contributing to ever-widening net losses. The root of this problem is that medical claim expenses are comprising ever larger portions of Plan premiums, leaving little leftover to cover general and administrative expenses. The table below discloses this relationship:

FISCAL YEAR	PREMIUMS	CLAIMS EXPENSE	CLAIMS AS A % OF PREMIUMS
2008	$ 775,114	$ 758,062	**98%**
2007	834,562	779,597	**93%**
2006	872,006	639,251	**73%**

Other operating expenses in 2008 reflect relatively the same levels as the prior year, with increases in personnel expenses (including the Coordinator's fee) and decreases in travel.

Statement of Cash Flows

The final statement presented by the Chuuk State Health Care Plan is the Statement of Cash Flows. The Statement of Cash Flows presents detailed information about the cash activity during the year. The statement is divided into four parts. The first part deals with operating cash flows from noncapital financing activities of the Plan. The second section reflects cash flows from capital and related financing activities. This section deals with the cash used for the acquisition and construction of capital and related items. The third section reflects the cash flows from investing activities and shows the purchases, proceeds and interest received from investing activities. The fourth section reconciles the net cash used in operating activities to operating income or loss reflected on the Statement of Revenues, Expenses, and Changes in Net Assets.

SUMMARY STATEMENT OF CASH FLOWS
(In '000's)

	2008	2007	2006
Cash provided by (used in):			
Operating activities	$ (155)	$ (316)	$ 62
Capital and related financing activities	(22)	(8)	-
Investing activities	267	28	(165)
Net change in cash and cash equivalents	90	(296)	(103)
Cash and cash equivalents, beginning of year	73	369	472
Cash and cash equivalents, end of year	$ 163	$ 73	$ 369

The Plan's cash and cash equivalent resources increased by $0.09 million (or 123%) in fiscal year 2008, from $0.073 million in the prior year to $0.163 million. This increase, however, was primarily the result of cashing-in a $250,000 TCD investment as negative operating results continue to erode the overall cash position of the Plan.

Capital Asset and Debt Administration

The Plan's net investment in capital assets totaled $35 thousand in fiscal year 2008, an increase of $9 thousand (or 36%) from fiscal year 2007.

The Plan has no debt and there are no foreseen circumstances that would affect the Plan's access to future capital financing.

Further information on the Plan's capital assets can be found in note (4) to the financial statements.

Economic Outlook

In fiscal year 2009, Plan management is faced with the stark realities of a Plan that for the last three years has seen its assets erode by 35%. Stagnant economic conditions in Chuuk State suggest that there will be no significant growth in enrollees or premiums in either the public or private sectors. Moreover, the same relatively sluggish conditions suggest that an increase in premiums would be a difficult in such an environment. Consequently, management's emphasis will be to rationalize Plan expenses within the lower premium levels indicated in fiscal year 2008. Such measures will include strict adherence to referral policies, better controls on claims reviews and settlement, limitation on dependent expenses, and greater cost containment of general and administrative expenses.

Contacting the Chuuk State Health Care Plan's Management

This financial report is designed to provide our citizens, Plan enrollees, accredited health care providers, and other users of our financial information, a general overview of the Plan's finances to demonstrate its accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Executive Director, Chuuk State Health Care Plan; P.O Box 1679; Weno, Chuuk; FM 96942.

CHUUK STATE HEALTH CARE PLAN

Statements of Net Assets
September 30, 2008 and 2007

ASSETS	2008	2007
Current assets:		
Cash and cash equivalents	$ 162,816	$ 73,116
Short-term investments	450,000	700,000
Premiums receivable, net of an allowance for doubtful premium of $31,407 in 2008	99,594	237,056
Other receivables	50,000	50,000
Other assets	350	446
Total current assets	762,760	1,060,618
Property and equipment, net	34,915	25,743
Total assets	$ 797,675	$ 1,086,361
LIABILITIES AND NET ASSETS		
Current liabilities:		
Medical claims and benefits payable	$ 101,292	$ 165,708
Accounts payable and accrued expenses	10,235	9,441
Total liabilities	111,527	175,149
Commitment		
Net assets:		
Invested in capital assets	34,915	25,743
Restricted	651,233	885,469
Total net assets	686,148	911,212
Total liabilities and net assets	$ 797,675	$ 1,086,361

See accompanying notes to financial statements.

CHUUK STATE HEALTH CARE PLAN

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2008 and 2007

	2008	2007
Revenues:		
Premiums	$ 775,114	$ 834,562
Others	6,574	9,583
	781,688	844,145
Benefits paid:		
Claims expenses	758,062	779,597
Net revenues	23,626	64,548
Provision for premium losses	31,407	-
Net (losses) revenues, after provision for premium losses	(7,781)	64,548
Other operating expenses:		
Salaries, wages and other benefits	91,428	80,253
Travel	40,663	62,957
Coordinator's fee	22,550	18,900
Consultant fee	20,000	28,000
Depreciation	13,278	5,786
Housing allowance	9,550	5,850
Rent	8,400	8,400
Office/computer supplies	5,283	4,831
Telephone and telegraph	5,159	2,633
Social security expense	4,635	4,479
Representation - board luncheon meeting	2,942	2,929
Gasoline and fuel	2,350	2,105
Board allowance	2,160	3,260
CSHCP premium and other health care contributions	2,158	1,932
Utilities	1,349	1,392
Promotional	1,310	4,825
Miscellaneous	1,111	4,124
Total other operating expenses	234,326	242,656
Net loss from operations	(242,107)	(178,108)
Interest income	17,043	28,118
Net loss	(225,064)	(149,990)
Net assets at beginning of year	911,212	1,061,202
Net assets at end of year	$ 686,148	$ 911,212

See accompanying notes to financial statements.

CHUUK STATE HEALTH CARE PLAN

Statements of Cash Flows
Years Ended September 30, 2008 and 2007

	2008	2007
Cash flows from operating activities:		
Premiums received	$ 881,169	$ 633,150
Other cash receipts	6,574	9,583
Advances and other prepayments	96	(50,043)
Medical claims and benefits paid	(822,478)	(671,546)
Other expenses paid	(220,253)	(236,880)
Net cash used in operating activities	(154,892)	(315,736)
Cash flows from capital and related financing activities:		
Acquisition of property and equipment	(22,450)	(8,627)
Net cash used in capital and related financing activities	(22,450)	(8,627)
Cash flows from investing activities:		
Net change in time certificates of deposit	250,000	-
Interest income received	17,042	28,118
Net cash provided by investing activities	267,042	28,118
Net change in cash and cash equivalents	89,700	(296,245)
Cash and cash equivalents at beginning of year	73,116	369,361
Cash and cash equivalents at end of year	$ 162,816	$ 73,116
Reconciliation of net loss from operations to net cash used in operating activities:		
Net loss from operations	$ (242,107)	$ (178,108)
Adjustments to reconcile net loss from operations to net cash used in operating activities:		
Depreciation	13,278	5,786
Provision for premium losses	31,407	-
Changes in assets and liabilities:		
Decrease (increase) in premiums receivable	106,055	(201,412)
(Increase) in other receivables	-	(50,000)
Decrease (increase) in other assets	96	(43)
(Decrease) increase in medical claims and benefits payable	(64,416)	108,051
Increase (decrease) in accounts payable and accrued expenses	795	(10)
Net cash used in operating activities	$ (154,892)	$ (315,736)

See accompanying notes to financial statements.

(1) Nature of Operations

Commencement of Operations

Chuuk State Health Care Plan (the Plan), a component unit of the State of Chuuk, was originally established under the Chuuk Health Care Plan Act of 1994 to provide eligible residents of Chuuk State with quality health care. The Plan commenced operations in September 2003 after final approval from the Board of Trustees, with Chuuk State Hospital (CSH) as the primary health care provider.

Entity's Activities

As per Chuuk State Law No. 2-94-06 (Act No: 2-25), the Plan is dedicated to serve as a financial system to provide universal coverage of an essential level of health care for all eligible enrollees by collecting health care premiums under a plan and ensuring medical services to all members through its accredited health care providers.

Aside from CSH being its primary health provider, the Plan has also accredited two medical clinics in Chuuk – Family Clinic and Sefin Health Clinic, and six hospitals in the Philippines – Cardinal Santos Medical Center, Medical City, Capitol Medical Center, and Kidney and Transplant Institute, Philippines Heart Center and St. Luke's Hospital to provide medical services to members of the Plan.

The Plan enables all eligible government employees to be members by contributing health premiums (50% employee share and 50% employer share) so as to claim medical benefits through the accredited health care providers. The Plan has also been extended to private sector employers and employees.

(2) Summary of Significant Accounting Policies

The accounting policies of the Plan conform to accounting principles generally accepted in the United States of America as applicable to governmental entities, specifically proprietary funds. Governmental Accounting Standards Board (GASB) Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting," requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principle Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Plan has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

The Plan has adopted GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* (GASB 34), as amended by GASB Statement No. 37, *Basic Financial Statements – Management's Discussion and Analysis for State and Local Governments: Omnibus* and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. GASB Statement No. 34 establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into the following four net asset categories:

(2) Summary of Significant Accounting Policies, Continued

- Invested in capital assets, net of related debt:

  Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted:

  - Nonexpendable – Net assets subject to externally imposed stipulations that require the Plan to maintain them permanently. For the years ended September 30, 2008 and 2007, the Plan does not have nonexpendable net assets.
  - Expendable – Net assets whose use by the Plan is subject to externally imposed stipulations that can be fulfilled by actions of the Plan pursuant to those stipulations or that expire by the passage of time.

- Unrestricted:

  Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action by management or the Board of Trustees or may otherwise be limited by contractual agreements with outside parties.

All of the Plan's net assets that are not otherwise invested in capital assets are restricted by law to be used for health care services.

Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of the fund are included in the statements of net assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenditures and expenses during the reporting period. Actual results may differ from those estimates.

Revenue and Expense Recognition

Health care premiums from enrolled members of the Plan are reported as revenue in the period such become due. The Plan considers health care premium revenues and costs that are directly related to the provision health care to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

Medical Claims and Benefits Payable

Medical claims and benefits payable represent the actual liability on claims reported to the Plan. The liabilities for claims are determined based on actual billings received from accredited hospitals and clinics, representing medical procedures performed for members through the financial statement date.

(2) Summary of Significant Accounting Policies, Continued

Cash and Cash Equivalents and Time Certificates of Deposit

For purposes of the statements of net assets and cash flows, cash and cash equivalents is defined as amounts in demand deposits as well as short-term investments maturing within three months of the date acquired.

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1 Deposits that are federally insured or collateralized with securities held by the financial institution or its agent in the Plan's name;

Category 2 Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the Plan's name; or

Category 3 Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in the Plan's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Plan's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Plan does not have a deposit policy for custodial credit risk.

Cash and cash equivalents include cash in various bank accounts and time certificates of deposit with an original maturity date of ninety days or less. Short-term investments in time certificates of deposit with original maturity dates greater than ninety days are separately classified. As of September 30, 2008 and 2007, the carrying amount of the Plan's cash and cash equivalents and time certificates of deposit were $612,816 and $773,116, respectively, and the corresponding bank balances were $612,810 and $789,717, respectively. Of the bank balance amounts, $611,803 and $771,080, respectively, were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. The remaining amounts of $1,007 and $18,638, respectively, represent deposits maintained in dollar and Philippine Peso denominated bank accounts maintained offshore. Accordingly, these deposits are exposed to foreign currency risk. As of September 30, 2008 and 2007, bank deposits in the amount of $464,065 and $200,000, respectively, were FDIC insured. The Plan does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

(2) Summary of Significant Accounting Policies, Continued

Short-Term Investments

Interest-bearing deposits in banks mature within one year and are carried at cost.

Premiums Receivable

Premiums receivable are primarily due from the Chuuk State Government and are interest free and uncollateralized. The allowance for uncollectible accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on the credit risk of specific customers, historical trends and other information. The allowance is established through a provision for bad debts charged to expense.

Property and Equipment

Property and equipment is stated at cost less accumulated depreciation. Routine repairs and maintenance costs are expensed as incurred. Depreciation is calculated using the straight-line method based on the estimated useful lives of the assets.

The Plan capitalizes equipment with acquisition values of $250 and above.

Reclassifications

Certain reclassifications have been made to the 2007 financial statements to correspond with the 2008 presentation.

New Accounting Standards

During fiscal year 2008, the Plan implemented GASB Statement No. 43, *Financial Reporting for Postemployment Benefits Plans Other Than Pension Plans*, GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues*, and GASB Statement No. 50, *Pension Disclosures an amendment of GASB Statements No. 25 and 27*. GASB Statement No. 43 establishes uniform financial reporting for other postemployment benefit plans by state and local governments and GASB Statement No. 50 more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits. GASB Statement No. 48 establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing, and includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other postemployment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB Statement No. 49 provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

In June 2007, GASB issued statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. GASB Statement No. 51 addresses whether and when intangible assets should be considered capital assets for financial reporting purposes. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

In November 2007, GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, which improves the quality of financial reporting by requiring endowments to report their land and other real estate investments at fair value, creating consistency in reporting among similar entities that exist to invest resources for the purpose of generating income. The provisions of this statement are effective for periods beginning after June 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which is intended to improve how state and local governments report information about derivative instruments – financial arrangements used by governments to manage specific risks or make investments – in their financial statements. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

Risk Management

The Plan carries workmen’s compensation liability insurance for all employees of the Plan; however, the Plan is substantially self-insured for all other risks. Management is of the opinion that no material losses have been sustained as a result of this practice during the past three years.

(3) Short-Term Investments

The Plan has time certificates of deposit with a federally insured bank of $450,000 and $700,000 as of September 30, 2008 and 2007, respectively. These deposits have initial maturity dates of one year and have interest rates ranging from 2.25% to 4.42%.

(4) Property and Equipment

A summary of the Plan's property and equipment at September 30, 2008 and 2007, is as follows:

	Estimated Useful Lives	Balance at October 1, 2007	Transfers and Additions	Transfers and Deletions	Balance at September 30, 2008
Office furniture and equipment	5 - 10 years	$ 24,564	$ 4,450	$(6,820)	$ 22,194
Vehicle	5 years	31,660	18,000	-	49,660
		56,224	22,450	(6,820)	71,854
Less accumulated depreciation		(30,481)	(13,278)	6,820	(36,939)
Property and equipment, net		$ 25,743	$ 9,172	$ -	$ 34,915

	Estimated Useful Lives	Balance at October 1, 2006	Transfers and Additions	Transfers and Deletions	Balance at September 30, 2007
Office furniture and equipment	5 - 10 years	$ 15,937	$ 8,627	$ -	$ 24,564
Vehicle	5 years	31,660	-	-	31,660
		47,597	8,627	-	56,224
Less accumulated depreciation		(24,695)	(5,786)	-	(30,481)
Property and equipment, net		$ 22,902	$ 2,841	$ -	$ 25,743

(5) Commitment

Lease Commitment

The Plan leases office space under an operating lease. Rental expense for the years ended September 30, 2008 and 2007 amounted to $8,400 and is included as a component of other operating expenses in the accompanying financial statements. At September 30, 2008, aggregate future minimum lease payments are summarized as follows:

Year ending September 30,	Amount
2009	$ 8,400
2010	3,500
	$ 11,900

(6) Related Parties

As of September 30, 2008 and 2007, premium receivables from Chuuk State Government amounted to $95,165 and $234,639, respectively, and related premium revenue earned for the years then ended amounted to $682,451 and $781,253, respectively. Additionally, as of September 30, 2008 and 2007, the Plan has an outstanding receivable of $50,000 from the Chuuk State Government, representing advances made to a component unit of the State.

(6) Related Parties, Continued

The Plan paid medical claims and benefits totaling $94,029 during the year ended September 30, 2008 to Family Clinic and Pharmacy, whose part-owner is a current member of the Board of Trustees. Additionally, outstanding premium receivable from the same clinic amounted to $8,616 as of September 30, 2008.

Deloitte & Touche LLP
361 South Marine Corps Drive
Tamuning, GU 96913-3911
USA
Tel: (671)646-3884
Fax: (671)649-4932
www.deloitte.com

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

The Board of Trustees
Chuuk State Health Care Plan:

We have audited the financial statements of the Chuuk State Health Care Plan (the Plan), as of and for the year ended September 30, 2008, and have issued our report thereon dated June 29, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Responses (pages 20 through 23) as items 2008-1 through 2008-3 to be significant deficiencies in internal control over financial reporting.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that the significant deficiencies described above are material weaknesses.

Compliance and Other Matters

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

We noted certain matters that we have reported to management of the Plan in a separate letter dated June 29, 2009.

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

This report is intended for the information of the management and Board of Trustees of the Plan, the Office of the Public Auditor of the Federated States of Micronesia, federal awarding agencies, pass-through entities and the cognizant audit and other federal agencies, and is not intended to be and should not be used by anyone other than those specified parties.

Deloitte & Touche LLP

June 29, 2009

Finding 2008-01 – Reiteration of Prior Year Finding

Criteria: The Plan should establish policies governing asset capitalization.

Condition: The issue of an absence of a fixed asset capitalization policy was previously identified during the 2005 to 2007 audits and has remained uncorrected in 2008.

Cause: The cause of this condition is the lack of necessary action to address the cited prior year finding.

Effect: The effect of this condition is noncompliance with the criteria.

Recommendation: We recommend that corrective action be taken to address this matter.

Auditee Response and Corrective Action Plan:

We agree with the finding and recommendation. Plan management will propose for adoption by its Board of Directors at its July meeting the same capitalization policy as in effect by most other FSM entities, with the following thresholds:

Buildings	$100,000
Equipment:	50,000
Vehicles:	All

Effectively, given the range of Plan purchases, only vehicles will probably be capitalized.

Finding 2008-02 – Reiteration of Prior Year Finding

Criteria: Utilization of an accounting system and adequate monitoring of the accounting process is necessary to carry out day-to-day accounting operations.

Condition: The absence of a formal accounting system was cited as a finding in the 2005 to 2007 audits and in spite of repeated recommendations, corrective action has not occurred. Transactions have continued to be recorded in an EXCEL file and no formal journal entries were prepared to support the recording of transactions. This results in inadequate controls over maintenance and monitoring of account ledgers. Additionally, as noted in prior years, the issue of segregation of duties has remained unresolved. While management planned for purchase and installation of accounting software, this has not materialized and remains an outstanding issue. Further, in 2008, there was a computer breakdown and corruption of files that resulted in EXCEL files of journal entries being inaccessible. For this reason, tests of journal entries were not possible. In spite of prior year recommendations, the problems associated with computer viruses have not been addressed and this has led to further corruption of files and computer breakdowns

Cause: The cause of this condition is the lack of necessary management involvement in addressing the recurring issues identified.

Effect: The effect of this condition is noncompliance with the criteria.

Recommendation We urge management to institute immediate action concerning these long outstanding issues that continue to impact the accounting operations. As recommended in prior years, the need to establish a formal accounting system should be considered to facilitate processing of accounting transactions in a systematic manner. Maintenance of back-up files is a standard procedure that should be utilized to assist recovery in the event of the loss of data files. Additionally, as recommended in prior years, adequate segregation of duties should exist and all journal entries should be documented and be approved by a higher level of management.

Auditee Response and Corrective Action Plan:

We agree with the finding and recommendation. The former controller's services ended on May 31, 2009. Although the Plan had purchased the Quickbooks software two years ago, this system was not implemented for unknown reasons. Management made an attempt to send someone to be trained for the Quickbooks in Guam, through the coordination of the Deloitte office. However, because of the high cost of that type of training, we were kind of giving a second thought to it. Perhaps, if can find someone to train our girls here in our office, it might be more economical. But, anyhow, if we can find a good accountant who is familiar with the Quickbooks, that will surely help. Grant money is being requested from OMIP to hire a Controller by the end of July 2009. One of the requirements for filling this position will be the new Controller must implement an automated accounting system with Quickbooks effective by the beginning of fiscal year October 1, 2009.

We agree to the finding and recommendation for a backup file to secure important information for our plan. We bought a computer unit which is designated only for that purpose.

We also agree to the finding and recommendation of having a segregated duties and responsibilities, especially for cross-checking purposes. We have already implemented that and it is now reflected in our journal entries. Every check issued is being signed by the Executive Director and the Board Chairman.

Finding 2008-03 - Absence of Strict Monitoring of Travel Expenses

Criteria: Travel expenses should be monitored.

Condition: In the prior year, a comment on the travel expenses-related control weakness was due to seemingly excessive amounts of travel expenses during the year. For the year ended September 30, 2008, total travel expenses of $40,663 approximate 17% of total Plan general and administrative expenses. Despite the Plan's efforts to reduce travel expense, current year expense still indicates that travel costs during the year appear excessive. Further, the following details the background of certain travel expenses:

Date of Travel	Amount (Airfare and Per diem)	Check no.	Particulars
October 16-21, 2007	$6,700	237	Travel for five people to Manila to attend an investment conference
February 14-27, 2008	$3,981	2326	Travel for two people for the purpose of meeting with a service provider in Guam and then proceeding to Manila to effectuate bank transactions.
February 16-27, 2008	$2,099	2366	Travel by one officer to Guam and Manila to meet with a service provider and perform bank transactions in Philippines
September 23 to October 1, 2008	$2,060	2513	Travel by two people to Guam to meet concerning investment transactions and to meet with the third party administrator in the Philippines for the renewal of a contract between CSHCP and its hospitals.

Cause: The cause of this condition is the lack of cost benefit analysis of the undertaken travel.

Effect: The effect of this condition is potential noncompliance with the criteria.

Recommendation: We reiterate the need to monitor travel expenses, ensuring that only valid business travel is charged to the Plan. The Plan should also perform a cost-benefit analysis prior to travel to minimize unnecessary expenses. We recommend that compliance with the newly revised travel policy be observed.

Auditee Response and Corrective Action Plan:

We agree with the finding and recommendation that strict control over travels must be exercised. In fiscal year 2009, travel expenses totaled $7,000 at June 30, 2009, a significant reduction from fiscal year 2008. As the pressure on operating margins continues in 2009, management will continue to prioritize control over travel expenses.