FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK

(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED DECEMBER 31, 2021 AND 2020

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Table of Contents
Years Ended December 31, 2021 and 2020

		Page No.
I.	FINANCIAL STATEMENTS	
	Federated States of Micronesia Development Bank	
	Independent Auditors' Report	1
	Management's Discussion and Analysis	4
	Statements of Net Position	7
	Statements of Revenues, Expenses and Changes in Net Position	8
	Statements of Cash Flows	9
	Notes to Financial Statements	11
	Schedule of European Investment Bank December 2018 and August 2010 Finance Contract Ratios	26
	Schedules of Required Supplementary Information Trust Funds Administered by the Federated States of Micronesia Development Bank	
	Statement of Fiduciary Net Position	27
	Statement of Changes in Fiduciary Net Position	28
II.	INDEPENDENT AUDITORS' REPORTS ON COMPLIANCE WITH LAWS AND REGULATIONS	
	Federated States of Micronesia Development Bank	
	Independent Auditors' 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*	29
	Summary of Findings and Responses	31

Deloitte & Touche LLP
361 South Marine Corps Drive
Tamuning, GU 96913
USA

Tel: +1 (671) 646-3884
Fax: +1 (671) 649-4265

www.deloitte.com

INDEPENDENT AUDITORS' REPORT

Board of Directors
Federated States of Micronesia Development Bank:

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of the Federated States of Micronesia (FSM) Development Bank (the Bank), a component unit of the FSM National Government, which comprise the statements of net position as of December 31, 2021 and 2020, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the financial position of the FSM Development Bank as of December 31, 2021 and 2020, and the changes in its net position and its cashflows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States *(Government Auditing Standards)*. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Bank and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Emphasis-of-Matters

Financial Statement Presentation

As discussed in Note 1 to the financial statements, the Bank elected to present an unclassified statement of net position because current assets are not matched with current liabilities. Our opinion is not modified with respect to this matter.

Noncompliance with Loan Agreement Covenants

As discussed in Note 7 to the financial statements, the Bank is not in compliance with certain loan covenants. Our opinion is not modified with respect to this matter.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Bank's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we

- exercise professional judgment and maintain professional skepticism throughout the audit.
- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- obtain an understanding of internal control relevant to the audit 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 Bank's internal control. Accordingly, no such opinion is expressed.
- evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Bank's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Deloitte.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 6 and the Statement of Fiduciary Net Position and Statement of Changes in Fiduciary Net Position for Trust Funds administered by the Bank on pages 27 and 28 be presented to supplement the financial statements. Such information is the responsibility of management and, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the 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.

Other Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Schedule of European Investment Bank December 2018 and August 2010 Finance Contract Ratios (Other Supplementary Information) on page 26 is presented for purposes of additional analysis and is not a required part of the financial statements. The Other Supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Other Supplementary Information is fairly stated, in all material respects, in relation to the 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 November 9, 2022, on our consideration of the Bank'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 solely 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 effectiveness of the Bank's 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 the Bank's internal control over financial reporting and compliance.

Deloitte & Touche LLP

November 9, 2022

The following is a discussion and analysis of the Federated States of Micronesia Development Bank's (the Bank) financial performance for the fiscal year ended December 31, 2021.

Since the pandemic hit the world two years ago, Pacific Island Countries, including the FSM, have been one of hardest hit, especially in the tourism sector. Throughout the entirety of 2021, this country was on full and semi-lock downs, only allowing in a few citizens and FSM residents – which affected the Bank's largest sector of customers in the travel-related industry.

At the end of December 2021, our outstanding loans stood at $41.8 million. Total assets grew to $72 million, an increase of about 4% from December 2020. The increase was mainly due to a $3 million grant from the government Health Program from the Asian Development Bank. On the liability side, the Bank's lone long-term debt to the European Investment Bank (EIB) has helped finance some of the Bank's projects. At the end of 2021, that balance was at $3.3 million, down from $3.7 million in 2020. The Bank's borrowed funds represents only 5% of total assets. For additional information concerning the Bank's debt, please refer to Note 7 in the financial statements. There are no significant capital asset transactions during 2021. For additional information concerning the Bank's capital assets, please refer to Note 5 in the financial statements.

Summary Statements of Net Position

	2021	2020	2019
Assets	$ 72,161,441	$ 69,496,756	$ 64,191,496
Liabilities	3,585,425	4,084,966	2,007,974
Net position:			
Net investment in capital assets	1,428,805	1,381,429	1,411,271
Unrestricted	67,147,211	64,030,361	60,772,251
Total net position	68,576,016	65,411,790	62,183,522
Total liabilities and net position	$ 72,161,441	$ 69,496,756	$ 64,191,496

Financially, the Bank ended the year with a net operating loss of $1.7 million. This was mainly due to the drop in lending in 2021 as businesses became reluctant to increase their debt during the border lockdown. Even non-tourism industry businesses suffered due to breakdowns in the supply chains, limited resources/supplies and increased cost of shipping. The Bank's bottom-line financial performance for the year 2021 ended with a net increase in assets of $3.16 million. Included in this was a one-off $3 million grant for the establishment of a new Micro & Small Loans Program, which the Bank introduced in 2021 in collaboration with the Asian Development Bank and the FSM National Government. This was established as part of FSM Government's COVID-19 resiliency program, a transformative program that the Bank embraced as an added part of its response to the effects of COVID-19 as well. In 2021, there were 280 micro and small loans amounting to $2.4 million representing first time business loan borrowers in small retail shops for tailors and dress sellers, food take-out operators/caterers, retail stores in remote areas, laundry-mat owners, taxi operators and truck rental owners, as well as small scale farmers and fishermen, among the many. The Bank proudly highlights that about 57% of these small-to-micro businesses are women-owned businesses.

Despite the net increase in assets, there was an operating loss due to the limited growth in revenues generated from the Bank's loan portfolio. It was necessary to increase loan loss provisioning in 2021 to provide for the loan becoming non-performing due to the prolonged loan repayment deferment and increasing uncertainly of when the economy will return to normal. Although this was a non-cash expense, it was necessary to protect the Bank in case of losses due to increasing non-performing loans resulting from the impacts of the COVID 19 pandemic. There was a dividend payment from the shares at Bank of FSM that helped cover the shortfall in loan interest income. The mark to market value of the Bank's financial investment portfolio abroad increased by $2 million, contributing to the overall positive outcome.

The Bank would not have been able to perform this way if not for national government assistance in the form of an interest subsidy amounting to $641,275 in 2021 which directly offset loan interest for travel related customers in the deferred-loans program (introduced in 2020 due to COVID-19), as well as ADB grant assistance.

In terms of lending, total loans approved for 2021 were $14.41 million -- $12.1 million in regular loans and over $2.3 million in micro and small loans. Of this $14.4 million figure, $6.8 million went to commercial loans, $617K for residential loans, and $4.6 million for consumer loans.

The total ratio of non-performing loans to total loans at the end of the 2021 based on EIB financial covenants was 49% and the ratio of the allowance for loan losses to non-performing loans was 37%. Despite these ratios, the Bank endeavors to improve its loan portfolio going forward.

Summary Statements of Revenues, Expenses and Changes in Net Position

	2021	2020	2019
Operating revenues	$ 3,194,395	$ 3,289,006	$ 3,232,492
Provision for loan losses	(3,083,405)	(805,044)	(1,014,698)
Operating and interest expenses	(1,806,242)	(1,743,433)	(1,881,616)
(Loss) earnings from operations	(1,695,252)	740,529	336,178
Non-operating revenues, net	4,859,478	2,487,739	3,335,393
Change in net position	3,164,226	3,228,268	3,671,571
Net position at beginning of year	65,411,790	62,183,522	58,511,951
Net position at end of year	$ 68,576,016	$ 65,411,790	$ 62,183,522

The Bank manages two trust funds, namely, the Investment Development Fund (IDF) and Yap Development Loan Fund (YDLF). The total assets for each of these funds at the end of 2021 were $2,046,262 and $279,072 respectively. As of December 31, 2021, there were no more active IDF or YDLF loans.

Economic Outlook

FSMDB continues to endure and look for ways it can sustain itself and remain in operations to fulfill its mandate and to serve its customers. Furthermore, the Bank aspires to be a good corporate citizen and do what it can to help its FSM community, enabling sustainable economic development over the entire nation, stimulating economic growth and improving the livelihoods of people in our country.

The Bank is very hopeful that with the opening of the FSM borders and the associated anticipated changes in the Bank's communities due to fewer travel restrictions, the Bank will continue to see improvements in the economies which will lead to more favorable outcomes in the Bank's revenue generating abilities going forward.

Contacting Financial Management

The Management's Discussion and Analysis report is intended to provide information concerning known facts and conditions affecting the Bank's operations. This financial report is designed to provide a general overview of the Bank's finances and to demonstrate the Bank's accountability for the funds it receives and expends.

Management's Discussion and Analysis for the year ended December 31, 2020 is set forth in the Bank's report on the audit of financial statements, which is dated June 21, 2021. That Discussion and Analysis explains the major factors impacting the 2020 financial statements and can be viewed at the Bank's website at www.fsmdb.fm or Office of the Public Auditor's website at www.fsmopa.fm.

For additional information about this report, please contact Ms. Anna Mendiola, President/Chief Executive Officer, P.O. Box M, Kolonia, Pohnpei 96941 or visit the website at www.fsmdb.fm.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Net Position
December 31, 2021 and 2020

	2021	2020
ASSETS		
Cash and cash equivalents	$ 13,178,567	$ 4,613,227
Time certificates of deposit	-	3,154,282
Investments	16,394,599	15,293,784
Interest and other receivables	318,740	545,224
Loans receivable, net of allowance for loan losses	34,285,850	37,907,565
Equity investment	6,554,880	6,599,280
Prepaid expenses	-	1,965
Depreciable capital assets, net	1,428,805	1,381,429
Total assets	$ 72,161,441	$ 69,496,756
LIABILITIES AND NET POSITION		
Liabilities:		
Accounts payable	$ 41,984	$ 68,398
Accrued interest payable	25,042	39,650
Long-term debt	3,337,830	3,777,102
Credit life payable	14,320	18,899
Payable to trust funds	44,589	42,607
Unearned grant revenues	121,660	138,310
Total liabilities	3,585,425	4,084,966
Commitments and contingencies		
Net position:		
Net investment in capital assets	1,428,805	1,381,429
Unrestricted	67,147,211	64,030,361
Total net position	68,576,016	65,411,790
Total liabilities and net position	$ 72,161,441	$ 69,496,756

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2021 and 2020

	2021	2020
Operating revenues:		
Interest income on loans	$ 2,896,264	$ 3,072,864
Loan fees	104,570	95,113
Rental	29,700	31,482
Interest income on time certificates of deposit	2,756	8,539
Miscellaneous	161,105	81,008
Total operating revenues	3,194,395	3,289,006
Provision for loan losses	(3,083,405)	(805,044)
Net operating revenues	110,990	2,483,962
Operating expenses:		
Interest expense	83,133	122,795
General and administrative expenses:		
Personnel services	1,057,506	1,017,169
Depreciation	153,399	141,267
Contractual services	85,940	78,881
Rent	85,102	75,716
Retirement plan contributions	66,424	64,353
Utilities	49,827	43,793
Communication	49,072	46,483
Branch automation	30,229	19,478
Supplies	27,387	24,653
Travel	22,742	36,344
Equipment	16,463	8,267
Staff relations	14,868	7,260
Community development	14,145	13,970
Insurance	9,787	6,237
Fuel, oil and petroleum	9,204	6,841
Repair and maintenance	8,913	4,915
Training	4,578	1,670
Printing	962	1,441
Miscellaneous	16,561	21,900
Total general and administrative expenses	1,723,109	1,620,638
(Loss) earnings from operations	(1,695,252)	740,529
Nonoperating revenues, net:		
Grants and subsidies	3,000,000	-
Investment earnings, net	1,858,623	2,487,739
Gain on sale of capital assets	855	-
Total nonoperating revenues, net	4,859,478	2,487,739
Change in net position	3,164,226	3,228,268
Net position at beginning of year	65,411,790	62,183,522
Net position at end of year	$ 68,576,016	$ 65,411,790

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Cash Flows
Years Ended December 31, 2021 and 2020

	2021	2020
Cash flows from operating activities:		
Cash received from customers	$ 3,418,123	$ 2,856,097
Cash paid to suppliers for goods and services	(557,882)	(481,636)
Cash paid to employees for services	(1,057,506)	(1,017,169)
Net cash provided by operating activities	1,802,735	1,357,292
Cash flows from noncapital financing activities:		
Proceeds from long-term debt	-	3,193,637
Cash received from grantor	3,000,000	-
Principal repayment of long-term debt	(439,272)	(151,985)
Net transfers in from (out to) trust funds	1,982	(968,466)
Interest paid	(97,741)	(98,205)
Net cash provided by noncapital financing activities	2,464,969	1,974,981
Cash flows from capital and related financing activities:		
Proceeds from sale of capital assets	1,335	-
Acquisition of capital assets	(201,255)	(111,425)
Net cash used in capital and related financing activities	(199,920)	(111,425)
Cash flows from investing activities:		
Loan origination and principal disbursements, net	538,310	(1,465,689)
Decrease (increase) in time certificates of deposit	3,157,038	(40,524)
Proceeds from sale of investments, net	541,207	118,938
Dividends received	261,001	321,751
Net cash provided by (used in) investing activities	4,497,556	(1,065,524)
Net change in cash and cash equivalents	8,565,340	2,155,324
Cash and cash equivalents at beginning of year	4,613,227	2,457,903
Cash and cash equivalents at end of year	$ 13,178,567	$ 4,613,227

See accompanying notes to financial statements.

Statements of Cash Flows, Continued
Years Ended December 31, 2021 and 2020

	2021	2020
Reconciliation of (loss) earnings from operations to net cash provided by operating activities:		
(Loss) earnings from operations	$ (1,695,252)	$ 740,529
Adjustments to reconcile (loss) earnings from operations to net cash provided by operating activities:		
Provision for loan losses	3,083,405	805,044
Depreciation	153,399	141,267
Others	80,377	114,256
(Increase) decrease in assets:		
Interest and other receivables	226,484	(424,370)
Prepaid expenses	1,965	1,350
Increase (decrease) in liabilities:		
Accounts payable	(26,414)	9,407
Credit life payable	(4,579)	5,822
Unearned grant revenues	(16,650)	(36,013)
Net cash provided by operating activities	$ 1,802,735	$ 1,357,292

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

Reporting Entities

The Federated States of Micronesia (FSM) Development Bank (the Bank) was created in 1979 by Public Law 1-37 of the First Congress of the Federated States of Micronesia. The Bank began its operations on October 1, 1980. The Bank was reorganized in January 1994 by Public Law 8-47 of the Eighth Congress of the FSM. The purpose of the Bank is to provide loans for economic development of the FSM. Such loans may otherwise be too risky for commercial banks to underwrite. Additionally, the Bank's repayment terms tend to be longer than those offered by commercial banks. As of December 31, 2021, the Bank has issued 3,236,883 shares to the FSM National Government (98.80%), Chuuk State (0.92%) and Kosrae State (0.28%). These shares do not convey ownership and have been made in accordance with the aforementioned law but these shares have no financial impact on the accompanying financial statements.

The Investment Development Fund (IDF) was established by Public Law 5-122 in January 1989. The purpose of the IDF is to finance projects which will (1) have their operations primarily located within the FSM; (2) improve the balance of payments position of the FSM; (3) increase the value of visible and invisible exports or result in import substitutions; (4) demonstrate positive economic returns; and (5) contribute to the furtherance of close economic relations with the United States.

The Yap Development Loan Fund (YDLF) is administered by the Bank in a Trust capacity. All loan decisions are made by executives of the respective state governments.

The Bank is a component unit (a discretely presented proprietary fund type) of the FSM National Government. The financial statements in this report do not represent the financial position, results of operations or cash flows of the FSM National Government as a whole. The financial statements of the Bank are not obligations of the FSM National Government unless specifically authorized by the FSM National Government. To date, no such authorizations have been made.

Fund Structure and Basis of Accounting

The accounts of the Bank are organized as a discretely presented component unit - proprietary fund of the FSM National Government. Proprietary funds are used by governmental units to account for operations that are financed and operated in a manner similar to a private business. This accounting is appropriate when costs of providing goods or services to the general public are to be financed primarily through user charges or where the periodic determination of net income is appropriate for accountability purposes.

The Bank follows the pronouncements of the Governmental Accounting Standards Board (GASB), which is the nationally accepted standard setting body for establishing generally accepted accounting principles (GAAP) for governmental entities.

GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments,* requires assets and liabilities of enterprise funds be presented in a classified format to distinguish between current and long-term assets and liabilities. The Bank is a government-owned bank. Banks do not present a classified statement of net position because current assets are not matched with current liabilities. The statements of net position of the Bank present assets and liabilities in order of their relative liquidity, rather than in a classified format.

(1) Summary of Significant Accounting Policies, Continued

Fund Structure and Basis of Accounting, Continued

The accounts of the IDF and YDLF are accounted for as fiduciary fund types as the amounts are to be reported on the respective entities' financial statements (the FSM National Government and Yap State, respectively).

The Bank utilizes the flow of economic resources measurement focus.

The statement of net position presents all of the Bank's non-fiduciary assets, deferred outflows of resources, liabilities and deferred inflows of resources, with the difference reported as net position. Net position is classified for accounting and reporting purposes into the following three net position categories:

- Net investment in capital assets - capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets as well as deferred outflows of resources and deferred inflows of resources that are attributable to those assets or related debt.

- Restricted - restricted assets reduced by liabilities and deferred inflows of resources related to those assets that are subject to externally imposed stipulations.

- Unrestricted - 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.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Cash and Cash Equivalents

For the purposes of the statements of net position and the statements of cash flows, cash and cash equivalents are defined as cash in bank checking and savings accounts, money market funds, and commercial paper with original maturities of three months or less from the date of acquisition.

Time certificates of deposit with original maturities of greater than three months are separately classified.

Investments

Investments and related investment earnings are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the date as of which the fair value of an asset or liability is determined.

An equity investment in the common stock of Bank of the FSM (investee) is stated at the net asset value (NAV). The NAV is used as a practical expedient to estimate fair value. The NAV is determined based on the total shareholders' equities reported by the investee.

(1) Summary of Significant Accounting Policies, Continued

Loans and Allowance for Loan Losses

Loans receivable are stated at unpaid principal balance less the allowance for loan losses.

Management maintains the allowance for loan losses at a level adequate to absorb probable losses. Management determines the adequacy of the allowance based upon reviews of individual loans, recent loss experience, current economic conditions, the risk characteristics of the various categories of loans and other pertinent factors. Loans deemed uncollectible are charged to the allowance. Provisions for losses and recoveries on loans previously charged off are added to the allowance.

Interest on loans is accrued and credited to income based on the principal amount outstanding. The accrual of interest on loans is discontinued when, in the opinion of management, there is an indication that the borrower may be unable to meet payments as they become due. Upon such discontinuance, all unpaid accrued interest is reversed.

Capital Assets

Capital assets are stated at cost, less accumulated depreciation. Depreciation is based on the straight-line method over the estimated useful lives of the respective assets. All assets have estimated useful lives of three to five years.

The Bank’s policy on capital assets requires that assets with a purchase value of $5,000 and over are capitalized and depreciated based on their useful lives. Assets with a purchase value less than $5,000 are expensed fully in the year of purchase.

Unearned Grant Revenues

Unearned grant revenues represent amounts received from grant and contract sponsors that have not yet been earned.

Compensated Absences

Earned but unused annual leave is paid to employees upon termination of their employment. Accordingly, vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. It is the policy of the Bank to record the cost of sick leave when leave is actually taken and an expense is actually incurred. Accordingly, no liability is recorded for non-vesting accumulating rights to receive sick pay benefits, which approximated $185,000 and $207,000 at December 31, 2021 and 2020, respectively.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Bank enters into off-balance sheet financial instruments consisting of commitments to extend credit and loan guarantees. Such financial instruments are recorded in the financial statements when they become payable.

(1) Summary of Significant Accounting Policies, Continued

Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for loan losses.

New Accounting Standards

In 2020, GASB issued Statement No. 95, *Postponement of the Effective Dates of Certain Authoritative Guidance*, which postponed the effective dates of GASB Statement No. 84, 89, 90, 91, 92 and 93 by one year and GASB Statement No. 87 by 18 months; however, earlier application of the provisions addressed in GASB Statement No. 95 is encouraged and is permitted to the extent specified in each pronouncement as originally issued. In accordance with GASB Statement No. 95, management has elected to postpone implementation of these statements except for GASB Statement No. 90, which was implemented during the year ended December 31, 2019.

During the year ended December 31, 2021, the Bank implemented the following pronouncements:

- GASB Statement No. 89, *Accounting for Interest Cost Incurred Before the End of a Construction Period*, which enhances the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and simplifies accounting for interest cost incurred before the end of a construction period.

- GASB Statement No. 93, *Replacement of Interbank Offered Rates*, which establishes accounting and reporting requirements related to the replacement of Interbank Offered Rates such as the London Interbank Offered Rate (LIBOR) for hedging derivative instruments. The provision removing LIBOR as an appropriate benchmark interest rate for the evaluation of the effectiveness of derivative instruments is effective for the year ended December 31, 2022.

The implementation of this statement did not have a material effect on the accompanying financial statements.

In June 2017, GASB issued Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and as inflows of resources or outflows of resources recognized based on the payment provisions of the contract. Management believes that this Statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 87 will be effective for fiscal year ending December 31, 2022.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In May 2019, GASB issued Statement No. 91, *Conduit Debt Obligations*. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 91 will be effective for fiscal year ending December 31, 2023.

In January 2020, GASB issued statement No. 92, *Omnibus 2020*. The objectives of this Statement are to enhance comparability in accounting and financial reporting and to improve the consistency of authoritative literature by addressing practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about the effective date of Statement No. 87, *Leases*, and Implementation Guide No. 2019-3, *Leases*, for interim financial reports, the terminology used to refer to derivative instruments and the applicability of certain requirements of Statement No. 84, *Fiduciary Activities*, to postemployment benefits. The requirements related to the effective date of GASB Statement No. 87 and Implementation Guide 2019-3, reissuance recoveries and terminology used to refer to derivative instruments are effective upon issuance. In accordance with GASB Statement No. 95, the remaining requirements of GASB Statement No. 92 is effective for the fiscal year ending December 31, 2022.

In March 2020, GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The primary objective of this Statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements. This Statement also provides guidance for accounting and financial reporting for availability payment arrangements. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 94 will be effective for fiscal year ending December 31, 2023.

In May 2020, GASB issued Statement No. 96, *Subscription-Based Information Technology Arrangements*. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset - an intangible asset - and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 96 will be effective for fiscal year ending December 31, 2023.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In June 2020, GASB issued Statement No. 97, *Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans - an amendment of GASB Statements No. 14 and No. 84, and a supersession of GASB Statement No. 32*. The primary objectives of this Statement are to (1) increase consistency and comparability related to the reporting of fiduciary component units in circumstances in which a potential component unit does not have a governing board and the primary government performs the duties that a governing board typically would perform; (2) mitigate costs associated with the reporting of certain defined contribution pension plans, defined contribution other postemployment benefit (OPEB) plans, and employee benefit plans other than pension plans or OPEB plans (other employee benefit plans) as fiduciary component units in fiduciary fund financial statements; and (3) enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans. GASB Statement No. 97 will be effective for fiscal year ending December 31, 2022.

In October 2021, GASB issued Statement No. 98, *The Annual Comprehensive Financial Report*. This Statement establishes the term annual comprehensive financial report and its acronym ACFR. That new term and acronym replace instances of comprehensive annual financial report and its acronym in generally accepted accounting principles for state and local governments. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 98 will be effective for fiscal year ending December 31, 2022.

(2) Deposits and Investments

The deposit and investment policies of the Bank are governed by its enabling legislation. The Board is required to engage one or more fund custodians to assume responsibility for the physical possession of the Bank's investments. Legally authorized investments are as follows:

(i) Government obligations - Obligations issued or guaranteed as to principal and interest by the National Government and/or State governments of the Federated States of Micronesia or by the Government of the United States, provided that the principal and interest on each obligation are payable in the currency of the United States.

(ii) Corporate obligations and mortgage-backed securities - Obligations of any public or private entity or corporation created or existing under the laws of the Federated States of Micronesia or of the United States or any state, territory or commonwealth thereof, or obligations of any other government or economic community which are payable in United States dollars, or other mortgage-backed securities provided that the obligation is an agency of the United States Government, the National Government of the Federated States of Micronesia, or is rated in one of the three highest categories by two nationally recognized rating agencies. No investment under this heading shall exceed ten percent of the market value of the investment fund or ten percent of the outstanding value of the issue at the time of purchase.

(2) Deposits and Investments, Continued

(iii) Preferred and common stocks - Shares of preferred or common stocks of any corporation created or existing under the laws of the Federated States of Micronesia or under the laws of the United States or any state, territory or commonwealth thereof provided that the purchase of such shares shall be considered reasonable and prudent by the Bank's investment advisor at the time of purchase, that not more than five percent of the market value of its investments shall be invested in the stock of any one corporation, and that not more than ten percent of the market value of its investments shall be invested in any one industry group.

(iv) Insurance company obligations - Contracts and agreements supplemental thereto providing for participation in one or more accounts of a life insurance company authorized to do business in the Federated States of Micronesia or in any state, territory or commonwealth of the United States provided that the total market value of these investments at no time shall exceed ten percent of all investments.

A. Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Bank'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 Bank does not have a deposit policy for custodial credit risk.

As of December 31, 2021 and 2020, the carrying amount of the Bank's total cash and cash equivalents and time certificates of deposit was $13,178,567 and $7,767,509, respectively, and the corresponding bank balances were $13,259,256 and $7,798,298, respectively, which were all maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2021 and 2020, bank deposits in the amounts of $1,748,963 and $4,137,397, respectively, were FDIC insured. The Bank does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk. Management's confidence in the financial strength of their banking institutions was the basis of the decision to not require collateralization. No losses as a result of this practice were incurred for the years ended December 31, 2021 and 2020.

B. Investments

As of December 31, 2021 and 2020, investments at fair value are as follows:

	2021	2020
Fixed income securities:		
Domestic fixed income	$ 4,979,132	$ 4,735,176
Equity securities:		
Domestic equities	9,761,092	9,396,728
Shares in a mutual fund	1,654,375	1,161,880
	$ 16,394,599	$ 15,293,784

(2) Deposits and Investments, Continued

B. Investments, Continued

As of December 31, 2021, investments in domestic fixed income securities are as follows:

	Moody's Credit Rating	Investment maturities (in Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Government securities:						
U.S. Treasury Notes	Aaa	$ 623,495	$ -	$ 1,117,076	$ -	$ 1,740,571
U.S. Treasury Notes	Not rated	599,938	-	-	-	599,938
U.S. Government agencies:						
Federal Agricultural Mortgage Corp.	Not rated	279,983	-	-	-	279,983
Fannie Mae Pool	Not rated	-	-	-	1,040,554	1,040,554
Freddie Mac Group	Not rated	-	-	-	358,617	358,617
Corporate bonds	A1	-	125,923	303,623	-	429,546
Corporate bonds	A2	-	-	93,711	-	93,711
Corporate bonds	A3	-	160,446	60,766	-	221,212
Corporate bonds	Not rated	215,000	-	-	-	215,000
		$ 1,718,416	$ 286,369	$ 1,575,176	$ 1,399,171	$ 4,979,132

As of December 31, 2020, investments in domestic fixed income securities are as follows:

	Moody's Credit Rating	Investment maturities (in Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Government securities:						
U.S. Treasury Notes	Aaa	$ -	$ -	$ 721,636	$ -	$ 721,636
U.S. Government agencies:						
Federal Home Loan Bank	Aaa	1,010,313	-	-	-	1,010,313
Federal Farm Credit Bank	Aaa	484,891	-	-	-	484,891
Federal Agricultural Mortgage Corp.	Not rated	254,924	279,882	-	-	534,806
Freddie Mac Group	Not rated	-	-	-	177,378	177,378
Corporate bonds	A1	-	127,118	-	-	127,118
Corporate bonds	A2	-	96,804	842,314	-	939,118
Corporate bonds	A3	-	147,088	237,089	139,456	523,633
Corporate bonds	A-	-	216,283	-	-	216,283
		$ 1,750,128	$ 867,175	$ 1,801,039	$ 316,834	$ 4,735,176

The Bank categorizes its fair value measurements within the fair value hierarchy established by GASB Statement No. 72. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The Bank has the following recurring fair value measurements as of December 31, 2021 and 2020:

(2) Deposits and Investments, Continued

B. Investments, Continued

	December 31, 2021	Fair Value Measurements Using Level 1	Level 2	Level 3
Fixed income:				
U.S. Treasury obligations	$ 2,340,509	$ -	$ 2,340,509	$ -
U.S. Government agencies	1,679,154	-	1,679,154	-
Corporate notes	959,469	-	959,469	-
Total fixed income	4,979,132	-	4,979,132	-
Equity securities:				
U.S. equities	9,761,092	9,761,092	-	-
Mutual fund shares	1,654,375	1,654,375	-	-
Total investments at fair value	$ 16,394,599	$ 11,415,467	$ 4,979,132	$ -

	December 31, 2020	Fair Value Measurements Using Level 1	Level 2	Level 3
Fixed income:				
U.S. Treasury obligations	$ 721,636	$ -	$ 721,636	$ -
U.S. Government agencies	2,207,388	-	2,207,388	-
Corporate notes	1,806,152	-	1,806,152	-
Total fixed income	4,735,176	-	4,735,176	-
Equity securities:				
U.S. equities	9,396,728	9,396,728	-	-
Mutual fund shares	1,161,880	1,161,880	-	-
Total investments at fair value	$ 15,293,784	$ 10,558,608	$ 4,735,176	$ -

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Bank will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Bank's investments are held and administered by trustees. Accordingly, these investments are exposed to custodial credit risk. Based on negotiated trust and custody contracts, all of these investments were held in the Bank's name by the Bank's custodial financial institution at December 31, 2021 and 2020.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the Bank. As of December 31, 2021, the Bank's investment in securities of U.S Treasury Notes and agency obligations of the Fannie Mae Pool and Federal Home Loan Bank constituted 14% and 6%, respectively, of its total investments. As of December 31, 2020, the Bank's investment in agency obligations of the Federal Home Loan Bank constituted 7% of its total investments.

(2) Deposits and Investments, Continued

B. Investments, Continued

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The Bank has a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

(3) Equity Investment

At December 31, 2021 and 2020, the equity investment in Bank of the FSM represents 225,001 common shares and approximately 24% ownership interest. Total shareholders' equity reported by Bank of the FSM approximated $27,312,000 and $27,497,000 at December 31, 2021 and 2020, respectively.

(4) Loans Receivable

A summary of loans receivable at December 31, 2021 and 2020 follows:

	2021	2020
Unpaid principal balance	$ 41,807,569	$ 43,290,779
Allowance for loan losses	(7,521,719)	(5,383,214)
	$ 34,285,850	$ 37,907,565

At December 31, 2021, estimated total principal collections and loan maturities in 2022 approximated $9,799,000.

Movements in the allowance for loan losses during the years ended December 31, 2021 and 2020, are as follow:

	2021	2020
Balance at beginning of year	$ 5,383,214	$ 5,400,019
Provision for loan losses	3,083,405	805,044
Loans charged off	(1,592,866)	(1,303,325)
Loan recoveries from previously charged off loans	647,966	481,476
Balance at end of year	$ 7,521,719	$ 5,383,214

At December 31, 2021 and 2020, $2.73 million and $2.65 million, respectively of the allowance is related to a Yap loan, which was fully provided due to management's assessment of remote collectability.

In an effort to constructively work with borrowers affected by the COVID-19 pandemic, the Bank initiated temporary programs beginning in February 2020 to allow for loan repayment deferrals for eligible borrowers. At December 31, 2021 and 2020, twenty-six loans and forty loans with total outstanding balances of $12.4 million and $13.3 million, respectively, are under the active deferral program. In December 2020, the FSM National Government enacted Public Law No. 21-211 (the Act) towards providing financial assistance to the private sector to mitigate the impact of the COVID-19 pandemic.

(4) Loans Receivable, Continued

In accordance with the Act, the Bank was appropriated $641,275 and $651,600 for interest payments for eligible loans in the years ended December 31, 2021 and 2020, respectively, of which $174,174 and $415,327 is included as accrued interest receivable as of December 31, 2021 and 2020, respectively, in the accompanying statement of net position, which was subsequently collected in August 2022 and February 2021, respectively.

(5) Capital Assets

A summary of capital assets as of December 31, 2021 and 2020, is as follows:

	Beginning January 1, 2021	Additions/ Transfers	Deletions/ Transfers	Ending December 31, 2021
Land	$ -	$ 7,889	$ -	$ 7,889
Building	1,674,348	-	-	1,674,348
Computers and software	682,880	19,910	(26,745)	676,045
Vehicles	161,478	85,456	-	246,934
Office furniture, fixtures and equipment	23,157	-	(7,499)	15,658
	2,541,863	113,255	(34,244)	2,620,874
Less accumulated depreciation	(1,160,434)	(153,399)	33,764	(1,280,069)
	1,381,429	(40,144)	(480)	1,340,805
Software installation in progress	-	88,000	-	88,000
Capital assets, net	$ 1,381,429	$ 47,856	$ (480)	$ 1,428,805

	Beginning January 1, 2020	Additions/ Transfers	Deletions/ Transfers	Ending December 31, 2020
Building	$ 1,674,348	$ -	$ -	$ 1,674,348
Computers and software	571,455	111,425	-	682,880
Vehicles	161,478	-	-	161,478
Office furniture, fixtures and equipment	23,157	-	-	23,157
	2,430,438	111,425	-	2,541,863
Less accumulated depreciation	(1,019,167)	(141,267)	-	(1,160,434)
Capital assets, net	$ 1,411,271	$ (29,842)	$ -	$ 1,381,429

(6) Related Party Transactions

As of December 31, 2021 and 2020, the Bank has direct loans with outstanding balances of $192,450 and $171,771, respectively, to employees of the Bank and project loans extended to businesses owned by or affiliated with employees and component units of FSM governments of $5,011,110 and $5,308,753, respectively. These loans were made under similar terms and conditions as exist with other borrowers. Officers and Board members are not eligible to borrow from the Bank.

During the years ended December 31, 2021 and 2020, the Bank recognized interest income of $641,275 and $651,600, respectively, which was granted by the FSM National Government (see Note 4).

(6) Related Party Transactions, Continued

During the year ended December 31, 2021, the Bank received a $3,000,000 grant from the FSM National Government for the FSM Health Expenditure and Livelihood Support Program which is supported by the Asian Development Bank Group. The grant is for the Bank to launch its micro and small business loans for the program.

(7) Long-Term Debt

Direct Borrowings:

Long-term debt consists of the following at December 31, 2021 and 2020:

	2021	2020
Unsecured loans payable to European Investment Bank (EIB) under an August 2010 master finance contract of EUR 4 million:		
Drawn on August 20, 2014; original amount of $334,550 (equivalent EUR 250,000), bearing interest fixed at 4.520%, and payable through semi-annual principal and interest installments of $17,997 on January 15, 2015 and equal installments of $19,467 beginning on July 15, 2015 through maturity on July 15, 2025.	$ 124,740	$ 172,509
Drawn on August 20, 2014; original amount of $796,976 (equivalent EUR 595,558), bearing interest fixed at 4.520%, and payable through semi-annual principal and interest installments of $42,873 on January 15, 2015 and equal installments of $46,375 beginning on July 15, 2015 through maturity on July 15, 2025.	297,161	410,956
Unsecured loans payable to European Investment Bank (EIB) under a December 2018 master finance contract of USD 4 million:		
Drawn on March 9, 2020; original amount of $3,193,637, bearing interest fixed at 2,774%, and payable through semi-annual interest payment beginning on September 9, 2020 and principal installments of $138,854 beginning on March 9, 2021 through maturity on March 9, 2032.	2,915,929	3,193,637
	$ 3,337,830	$ 3,777,102

Under the 2010 and 2018 Agreements, including Amendments dated March 2021, the EIB (or the "Lender") loans contain (1) a provision that in an event of default, the timing of repayment of outstanding amounts may become immediately due if: the capital to total assets ratio is not above 20%; nonperforming loans to total loans ratio exceeds certain ratios (effective 45% at December 31, 2021); provision for loan losses to nonperforming loans ratio is less than certain ratios (effective 50% at December 31, 2021), and (2) a provision that the Bank shall repay the loan or any part thereof, together with accrued interest and other accrued sums immediately, forthwith upon demand by the Lender if:

a. the Bank fails on due date to repay any part of the loan, to pay interest thereon or to make any other payment to the Lender;
b. if any information or document given to the Lender by the Bank or on its behalf is or proves to be incorrect, incomplete or misleading in any material respect;

(7) Long-Term Debt, Continued

Direct Borrowings, Continued:

c. the Bank is unable to pay its debts, or makes or seeks to make a composition with its creditors;
d. an order is made or an effective resolution is passed for the winding up of the Bank, or the Bank takes steps towards a substantial reduction in its capital, is declared insolvent or ceases or resolves to cease to carry on the whole or any substantial part of its business or activities;
e. an encumbrancer takes possession of, or a receiver, liquidator, administrator, administrative receiver or similar officer is appointed, whether by a court of competent jurisdiction or by any competent administrative authority or by any person, any part of the business or assets; if any distress, execution, sequestration, or other process is levied or enforced upon the property of the Bank and is not discharged or stayed within 14 days; or if any event occurs which is likely to jeopardize the servicing of the loan or adversely affect any security therefore;
f. if any other financial indebtedness is either not paid when due, or following any default in relation thereto, is capable of being declared due and payable prior to its scheduled maturity;
g. If the Bank is liable, by reason of any default, to be required to effect immediate prepayment of any loan granted to it by the Lender from the resources of the Bank or of the European Community;
h. If a material adverse change occurs, as compared to the Bank's condition at the time of the loan agreement;
i. If it is or becomes unlawful for the Bank to perform any of its obligation under the loan agreement.

At December 31, 2021, the Bank is not in compliance with the ratios of non-performing loans to total loans and the allowance for loan losses to non-performing loans requirements, including the March 2021 amendments. Management is working on obtaining a waiver from the Lender.

Annual debt service requirements to maturity for principal and interest are as follows:

Year Ending December 31,	Principal	Interest	Total
2022	$ 334,001	$ 88,510	$ 422,511
2023	394,140	86,509	480,649
2024	399,463	73,483	472,946
2025	405,709	60,214	465,923
2026	277,708	48,148	325,856
Thereafter	1,526,809	127,110	1,653,919
	$ 3,337,830	$ 483,974	$ 3,821,804

Long-term debt changes during the years ended December 31, 2021 and 2020 are as follows:

	Balance January 1,	Additions	Reductions	Balance December 31,	Due Within One Year
2021:					
Loans payable	$ 3,777,102	$ -	$ (439,272)	$ 3,337,830	$ 334,001
2020:					
Loans payable	$ 735,450	$ 3,193,637	$ (151,985)	$ 3,777,102	$ 384,184

(8) Unearned Grant Revenues

During the year ended December 31, 2015, the Bank was awarded a $250,000 Home Energy Loan Program grant from the International Union for Conservation of Nature Resources (IUCN). $232,000 of the grant is to be awarded to the qualified borrowers for new loans to construct homes that demonstrate features and measures designed to conserve energy, reduce consumption of fossil fuels and enhance energy efficiency as principal reduction of loans, while the remaining $18,000 will be used by the Bank for renovations to improve energy efficiency. As of December 31, 2021 and 2020, unearned grant revenue was $121,660 and $138,310, respectively. A grant extension was received during the year ended December 31, 2018.

(9) Retirement Plan

The Bank's retirement plan (the Plan) is a self-administered program established to pay retirement, disability and survivor income to employees and their survivors to supplement similar benefits that employees receive from the FSM Social Security Administration. The Plan is a contributory plan in which the Bank matches 100% of the participants' contributions up to a maximum of 10% of the participant's annual salary, if the participant contributes 3% or more of his or her annual salary. Employee participation is optional. The Bank's Chief Financial Officer is the designated Plan Administrator. Matching contributions to the Plan during the years ended December 31, 2021 and 2020 were $66,424 and $64,353, respectively. Total Plan assets as of December 31, 2021 and 2020 were $1,662,780 and $1,504,688, respectively. Management is of the opinion that the Plan does not represent an asset or a liability of the Bank.

(10) Commitments and Contingencies

Guaranty

The Bank, from time-to-time, is contingently liable on loan guarantees ranging from 50% to 90% of the outstanding loan balances for commercial projects within the FSM. There were no outstanding guaranteed loan balances as of December 31, 2021 and 2020.

Loan Commitments

Undrawn balances on lines of credit and loan commitments for loans approved but undisbursed approximated $5,484,000 at December 31, 2021, of which $3,975,000 represent undisbursed funds on three loans.

Litigation

The Bank is a party to various legal proceedings, the ultimate impact of which is not currently predictable. Therefore, no liability has been recorded in the accompanying financial statements due to management's inability to predict the ultimate outcome of these proceedings.

Insurance

The Bank carries insurance to cover its potential risks from vehicle usage. The Bank 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.

(10) Commitments and Contingencies, Continued

Lease Commitments

The Bank has three operating leases for its State operating locations. These leases expire at varying dates through May 2031. Several of these leases provide options to renew upon expiration, based on renegotiated rates. Future minimum annual lease payments payable under the noncancellable leases are as follows:

Year ending December 31,	
2022	$ 64,770
2023	40,670
2024	39,420
2025	39,420
2026	40,620
Thereafter	142,020
	$ 366,920

The Bank leases portions of its headquarters building under three separate agreements expiring through September 2025. Future minimum annual lease income under the noncancellable leases are as follows:

Year ending December 31,	
2022	$ 27,500
2023	20,700
2024	20,700
2025	15,500
	$ 84,400

Additionally, the Bank provides housing benefits for certain contract employees with payment included as part of rent expense. The leases are between the respective landlords and the employees.

Total recorded lease expense and income under the aforementioned agreements amounted to $85,102 and $29,700, respectively, for the year ended December 31, 2021 and $75,716 and $31,482, respectively, for the year ended December 31, 2020.

(11) Risks and Uncertainties

On March 11, 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic and recommended containment and mitigation measures worldwide. In response, governments all over the world implemented actions which impacted the macroeconomic environment, increased economic uncertainty and reduced economic activities. The Bank's business and earnings are closely tied to the economies of the FSM. The impacts of travel restrictions and limited business orders have resulted in immediate adverse impact to some of the Bank's customers. During the year ended December 2020, the Bank granted temporary principal and interest payment relief for certain loans and received funds from the FSM National Government for interest payments (see Note 4). The Bank has further extended the loan deferral program during the year ended December 2021. The length of time such conditions will continue to exist as well as the significance of the impact to the Bank's ultimate realization of these underlying loans in accordance with their contractual terms is presently not determinable.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Schedule of European Investment Bank
December 2018 and August 2010 Finance Contract Ratios
December 31, 2021

1.) Ratio of Capital (paid in capital plus reserves) to total assets should be above 20%:

Total net position	$	68,576,016
Total assets	$	72,161,441
		95%

2.) Ratio of non-performing loans, as defined, to total loans do not exceed 45%:

Total non-performing loans	$	20,538,971
Total loans	$	41,807,569
		49%

3.) Ratio of allowance for loan losses to non-performing loans shall not be less than 50%:

Allowance for loan losses	$	7,521,719
Total non-performing loans	$	20,538,971
		37%

See accompanying independent auditors' report.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Schedules of Required Supplementary Information
Trust Funds' Statement of Fiduciary Net Position
December 31, 2021

	IDF	YDLF	Total
ASSETS			
Cash and cash equivalents	$ -	$ 125,814	$ 125,814
Time certificates of deposit	1,968,465	150,629	2,119,094
Receivable from FSMDB	71,935	-	71,935
Interest and other receivables	5,862	2,629	8,491
Total assets	$ 2,046,262	$ 279,072	$ 2,325,334
LIABILITIES AND NET POSITION			
Liabilities:			
Payable to FSMDB	$ 6,111	$ 21,235	$ 27,346
Unrestricted net position	2,040,151	257,837	2,297,988
Total liabilities and net position	$ 2,046,262	$ 279,072	$ 2,325,334

See accompanying independent auditors' report.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Schedules of Required Supplementary Information
Trust Funds' Statement of Changes in Fiduciary Net Position
Year Ended December 31, 2021

	IDF	YDLF	Total
Additions:			
Investment interest	$ 418	$ 765	$ 1,183
Miscellaneous	5,000	-	$ 5,000
Change in net position	5,418	765	6,183
Net position at beginning of year	2,034,733	257,072	2,291,805
Net position at end of year	$ 2,040,151	$ 257,837	$ 2,297,988

See accompanying independent auditors' report.

Deloitte & Touche LLP
361 South Marine Corps Drive
Tamuning, GU 96913
USA

Tel: +1 (671) 646-3884
Fax: +1 (671) 649-4265

www.deloitte.com

INDEPENDENT AUDITORS' 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*

The Board of Directors
Federated States of Micronesia Development Bank:

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 Federated States of Micronesia Development Bank (the Bank), which comprise the statement of net position as of December 31, 2021, and the related statements of revenues, expenses and changes in net position and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 9, 2022.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Bank'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. Accordingly, we do not express an opinion on the effectiveness of the Bank'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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiency in internal control, described in the accompanying Schedule of Findings and Responses, that we consider to be a significant deficiency as item 2021-001.

Deloitte.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Bank'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 instances 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.

Deloitte & Touche LLP

November 9, 2022

Summary of Findings and Responses
December 31, 2021

Finding No.: 2021-001
Area: Interest Income on Loans Receivable

Criteria: Interest income should be recognized based on actual loan terms and repayment histories of loans. Errors caused by the systematic issues need to be investigated by management and corrected in the loan subsidiary ledger and the general ledger.

Condition: The loan system does not accurately reflect past due dates of certain active loans beyond maturity dates due to systematic errors that have not been corrected. As a result, the Bank has to manually determine the proper past due dates for those loans but has not been able to perform such manual tracking and recalculations for all affected loans. Based on audit tests performed, interest income for the year ended December 31, 2021 and the accrued interest receivable as of December 31, 2021 may be understated by approximately $260,000.

Cause: The cause of this condition is primarily due to systematic errors in the loan system which were not investigated or corrected. An implemented manual workaround is time consuming and as such, is not implemented for all affected loans.

Effect: The effect of this condition is the potential understatement of interest income and accrued interest receivable.

Recommendation: We recommend that the Bank determine the root cause of the systematic errors in the current loan system and establish formal procedures to review and manually correct interest income and accrued interest receivable manually for all loans, if such systematic errors cannot be corrected.

Auditee Response and Corrective Action Plan: Management agrees. To correct this, the bank is currently undergoing implementation of a new loan management system, which was purchased in 2021 (procurement of it began in 2020), but unfortunately due to the travel restrictions, the bank was unable to go through with original plans of changing out the old loan system to the new last year. The bank is hopeful that the new loan management system, to go live before the year is over, will rectify the loan system errors requiring manual recalculation and avoid or minimize these kinds of system errors going forward.