

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

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**REPORT ON THE AUDIT OF  
FINANCIAL STATEMENTS IN ACCORDANCE  
WITH OMB CIRCULAR A-133**

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**YEAR ENDED SEPTEMBER 30, 1998**

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**YEAR ENDED SEPTEMBER 30, 1998**

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FEDERATED STATES OF MICRONESIA**

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**STATE OF KOSRAE  
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**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

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**INDEPENDENT AUDITORS' REPORT ON  
GENERAL PURPOSE FINANCIAL STATEMENTS**

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**YEAR ENDED SEPTEMBER 30, 1998**



## **INDEPENDENT AUDITORS' REPORT**

Honorable Rensley A. Sigrah  
Governor, State of Kosrae  
Federated States of Micronesia:

We have audited the accompanying general purpose financial statements of the State of Kosrae, as of September 30, 1998, and for the year then ended, as set forth in Section II of the foregoing table of contents. These general purpose financial statements are the responsibility of the management of the State of Kosrae. Our responsibility is to express an opinion on these general purpose financial statements based on our audit.

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

We were not able to apply sufficient alternative procedures to assure ourselves as to the correctness of fund balances reserved for continuing appropriations, other term deposits and advance receivables for all Governmental Fund Types; inventories of the Proprietary Fund Types; loans receivable of the Fiduciary Fund Type, and accounts payable for all fund types as of September 30, 1998.

The State of Kosrae has not adequately updated its General Fixed Assets Account Group during the year ended September 30, 1998, nor were we able to apply sufficient alternative procedures to assure ourselves as to the correctness of the balances set forth in the accompanying general purpose financial statements. Accordingly, a statement of changes in general fixed assets has not been included within the accompanying general purpose financial statements.

The general purpose financial statements referred to above do not include the Micronesia Petroleum Company (MPC), a Component Unit – Proprietary Fund, and the Kosrae Community Action Program (KCAP), a Component Unit – Governmental Fund, which, in our opinion, should be included to conform with generally accepted accounting principles. MPC and KCAP were unable to produce financial statements and the effect on the accompanying general purpose financial statements is unknown.

We were not able to obtain financial statements of the Agriculture Revolving Fund (ARF), Production Loan Fund (PLF) or Tourism Revolving Fund (TRF), Fiduciary Fund Type - Expendable Trust Funds. In our opinion, presentation of these funds should be included to conform with generally accepted accounting principles.

We were provided unaudited financial statements to support Kosrae State's investment in SEMO Micronesia and Pacific Tuna Industries and were not provided financial statements to support Kosrae State's investment in Kosrae Sea Ventures, Inc. Accordingly, we were not able to verify the carrying value of Kosrae State's investment in these entities (recorded as equity investments in the Governmental Fund Type – Capital Projects Fund) and whether all disclosures related to these investees have been included in the accompanying financial statements.

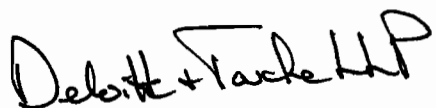
In our opinion, except for the effects on the general purpose financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to; 1) assure ourselves as to the propriety of fund balances reserved for continuing appropriations, other term deposits and advances receivable of all Governmental Fund Types; inventories of the Proprietary Fund Types; loans receivable of the Fiduciary Fund Type; accounts payable for all fund types; and fixed assets of the General Fixed Assets Account Group; and 2) examine evidence regarding the investments in Kosrae Sea Ventures, Inc., SEMO Micronesia, and Pacific Tuna Industries as discussed in the third, fourth and seventh paragraphs above, and except for the omissions of MPC, KCAP, ARF, PLF and TRF, discussed in the fourth and fifth paragraphs, such general purpose financial statements, as set forth in Section II of the table of contents, except for the General Fixed Assets Account Group upon which we are unable to express an opinion because of the matters set forth in the fourth paragraph above, present fairly, in all material respects, the financial position of the State of Kosrae as of September 30, 1998, and the results of its operations and the cash flows of its proprietary funds for the year then ended in conformity with generally accepted accounting principles.

During the year ended September 30, 1998, the State of Kosrae changed its method of accounting for investments.

Government Accounting Standards Board Technical Bulletin 98-1, *Disclosures about Year 2000 Issues*, requires disclosures of certain matters regarding the year 2000 issue. Kosrae State Government has included such disclosures in the accompanying supplemental information listed in Section III of the foregoing table of contents. Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Accordingly, insufficient audit evidence exists to support Kosrae State's disclosures with respect to the year 2000 issue. Further, we do not provide assurance that Kosrae State will be year 2000 ready, that Kosrae State's year 2000 remediation efforts will be successful in whole or in part, or that parties with which Kosrae State does business will be year 2000 ready.

Our audit was conducted for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The combining and individual fund financial statements and schedules listed in Section IV of the foregoing table of contents, which are also the responsibility of the management of the State of Kosrae, are presented for purposes of additional analysis and are not a required part of the general purpose financial statements of the State of Kosrae. Such additional information has been subjected to the auditing procedures applied in our audit of the general purpose financial statements and, except for the effects of the items described in the third, sixth and seventh paragraphs above, in our opinion, is fairly stated in all material respects when considered in relation to the general purpose financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 4, 1999 on our consideration of the State of Kosrae's (Primary Government only) internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.



May 4, 1999

STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA

Combined Balance Sheet - All Fund Types, Account Groups and Discretely Presented Component Unit  
September 30, 1998  
(With comparative totals as of September 30, 1997)

	Governmental Fund Types			Proprietary Fund Type	Fiduciary Fund Type	Account Groups		Totals Primary Government (Memorandum Only)	Component Unit Kosrae Utilities Authority	Totals Reporting Entity (Memorandum Only)	
	General	Special Revenue	Capital Projects	Internal Service	Expendable Trust	General Fixed Assets	General Long-Term Debt			1998	1997
<b>ASSETS</b>											
Cash and equivalents (note 2)	\$ -	\$ -	\$ -	\$ -	\$ 191,860	\$ -	\$ -	\$ 191,860	\$ 1,686,501	\$ 1,878,361	\$ 1,244,232
Other term deposits (note 2)	49,076	-	827,917	-	-	-	-	876,993	-	876,993	939,125
Investments (note 2)	1,893,033	284,920	790,573	-	-	-	-	2,968,526	-	2,968,526	1,710,664
Equity investments (note 5)	-	-	2,525,247	-	-	-	-	2,525,247	-	2,525,247	1,312,268
Receivables from federal agencies (note 3)	-	1,214,250	502,440	-	-	-	-	1,716,690	81,807	1,798,497	2,064,921
Receivables from other governments (note 3)	278,152	14,599	1,674,996	-	-	-	-	1,967,747	108,374	2,076,121	2,055,814
General receivables, net (note 4)	136,459	191,123	-	773	46,334	-	-	374,689	387,169	761,858	816,948
Advances (note 4)	381,957	410,661	297,804	-	8,660	-	-	1,099,082	-	1,099,082	1,062,255
Loans receivable, net (note 4)	-	-	95,000	-	455,944	-	-	550,944	-	550,944	517,429
Due from other funds (note 8)	1,723,869	258,858	2,142,670	-	641,903	-	-	4,767,300	-	4,767,300	5,251,387
Inventories, at cost	-	-	-	59,556	-	-	-	59,556	267,226	326,782	1,071,445
Interest receivable	12,094	-	-	-	-	-	-	12,094	-	12,094	12,094
Prepayments	-	-	-	-	-	-	-	-	2,383	2,383	5,081
Fixed assets, net	-	-	-	-	-	1,264,375	-	1,264,375	4,602,968	5,867,343	9,327,658
Amount to be provided for retirement of long-term debt	-	-	-	-	-	-	1,572,574	1,572,574	-	1,572,574	1,028,899
Amount available in designated expendable trust fund	-	-	-	-	-	-	191,860	191,860	-	191,860	-
<b>Total assets</b>	<b>\$ 4,474,640</b>	<b>\$ 2,374,411</b>	<b>\$ 8,856,647</b>	<b>\$ 60,329</b>	<b>\$ 1,344,701</b>	<b>\$ 1,264,375</b>	<b>\$ 1,764,434</b>	<b>\$ 20,139,537</b>	<b>\$ 7,136,428</b>	<b>\$ 27,275,965</b>	<b>\$ 28,420,220</b>

See accompanying notes to financial statements.



STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA

Combined Balance Sheet - All Fund Types, Account Groups and Discretely Presented Component Unit  
September 30, 1998  
(With comparative totals as of September 30, 1997)

	Governmental Fund Types			Proprietary	Fiduciary	Account Groups		Totals	Component	Totals	
	General	Special	Capital	Fund Type	Fund Type	General	General	Primary	Unit	Reporting Entity	
		Revenue	Projects	Internal	Expendable	Fixed	Long-Term	Government	Kosrae	(Memorandum Only)	
				Service	Trust	Assets	Debt	(Memorandum Only)	Utilities Authority	1998	1997
<b>LIABILITIES AND FUND EQUITY (DEFICIENCY)</b>											
<b>Liabilities:</b>											
Bank overdraft	\$ 958,372	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 958,372	\$ -	\$ 958,372	\$ 364,506
Accounts payable	98,205	193,808	358,433	-	67,946	-	-	718,392	55,745	774,137	962,871
Accrued payroll and others	263,154	92,846	20,788	-	-	-	-	376,788	14,805	391,593	253,350
Due to other funds (note 8)	359,612	2,043,751	2,216,202	139,015	8,720	-	-	4,767,300	-	4,767,300	5,251,387
Deferred revenues	-	28,095	-	-	-	-	-	28,095	-	28,095	28,095
Due to other governments	180,636	-	-	-	-	-	-	180,636	-	180,636	180,636
Short-term borrowings	-	-	-	-	-	-	-	-	-	-	247,712
Long-term notes payable (note 10)	-	-	-	-	-	-	1,094,102	1,094,102	-	1,094,102	294,021
Vacation leave accrual	-	-	-	-	-	-	670,332	670,332	18,813	689,145	759,501
Other payables	318,469	-	-	-	-	-	-	318,469	-	318,469	415,799
<b>Total liabilities</b>	<b>2,178,448</b>	<b>2,358,500</b>	<b>2,595,423</b>	<b>139,015</b>	<b>76,666</b>	<b>-</b>	<b>1,764,434</b>	<b>9,112,486</b>	<b>89,363</b>	<b>9,201,849</b>	<b>8,757,878</b>
<b>Fund equity (deficiency):</b>											
Investment in general fixed assets	-	-	-	-	-	1,264,375	-	1,264,375	-	1,264,375	1,264,375
Retained earnings (deficit)	-	-	-	(78,686)	-	-	-	(78,686)	2,891,497	2,812,811	1,958,847
Contributed capital	-	-	-	-	-	-	-	-	4,155,568	4,155,568	8,690,179
<b>Fund balances (deficit):</b>											
<b>Reserved for:</b>											
Related assets	4,342,383	-	3,220,247	-	647,804	-	-	8,210,434	-	8,210,434	6,781,905
Encumbrances	268,138	733,180	2,552,796	-	213,199	-	-	3,767,313	-	3,767,313	2,821,245
Continuing appropriations (note 9)	65,550	542,196	2,467,487	-	-	-	-	3,075,233	-	3,075,233	3,899,629
Unreserved	(2,379,879)	(1,259,465)	(1,979,306)	-	407,032	-	-	(5,211,618)	-	(5,211,618)	(5,753,838)
<b>Total fund equity (deficiency)</b>	<b>2,296,192</b>	<b>15,911</b>	<b>6,261,224</b>	<b>(78,686)</b>	<b>1,268,035</b>	<b>1,264,375</b>	<b>-</b>	<b>11,027,051</b>	<b>7,047,065</b>	<b>18,074,116</b>	<b>19,662,342</b>
<b>Contingencies (note 6)</b>											
<b>Total liabilities and fund equity (deficiency)</b>	<b>\$ 4,474,640</b>	<b>\$ 2,374,411</b>	<b>\$ 8,856,647</b>	<b>\$ 60,329</b>	<b>\$ 1,344,701</b>	<b>\$ 1,264,375</b>	<b>\$ 1,764,434</b>	<b>\$ 20,139,537</b>	<b>\$ 7,136,428</b>	<b>\$ 27,275,965</b>	<b>\$ 28,420,220</b>
See accompanying notes to financial statements.											

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Combined Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) -  
All Governmental Fund Types and Expendable Trust Funds  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	Governmental Fund Types			Fiduciary Fund Type	Totals Reporting Entity (Memorandum Only)	
	General	Special Revenue	Capital Projects	Expendable Trust	1998	1997
<b>Revenues:</b>						
Compact of Free Association:						
Base amount	\$ 2,189,600	\$ 1,687,122	\$ 1,918,400	\$ -	\$ 5,795,122	\$ 5,928,544
Inflation adjustment	1,160,488	371,000	1,016,752	-	2,548,240	2,404,000
U.S. Department of the Interior grants	-	-	227,854	-	227,854	538,872
Revenue sharing	868,395	-	-	-	868,395	810,661
Federal contributions	-	1,433,817	405,976	-	1,839,793	2,862,605
Taxes and licenses	149,033	-	-	-	149,033	157,677
Investment income (note 2)	307,506	-	-	-	307,506	416,107
Other	222,604	28,162	-	1,502,299	1,753,065	881,720
<b>Total revenues</b>	<b>4,897,626</b>	<b>3,520,101</b>	<b>3,568,982</b>	<b>1,502,299</b>	<b>13,489,008</b>	<b>14,000,186</b>
<b>Expenditures:</b>						
General government	1,764,189	1,978,291	-	-	3,742,480	3,261,969
Education	1,376,904	86,939	-	-	1,463,843	1,956,453
Health services	665,631	160,564	-	-	826,195	1,017,874
Economic development	562,946	-	-	-	562,946	669,616
Public works	236,199	-	-	-	236,199	338,746
Public safety	264,995	-	-	-	264,995	312,424
Community affairs	187,720	37,114	-	-	224,834	344,330
Capital projects	-	-	2,514,662	-	2,514,662	3,777,428
Other	17,039	5,662	-	1,301,435	1,324,136	1,020,809
<b>Total expenditures</b>	<b>5,075,623</b>	<b>2,268,570</b>	<b>2,514,662</b>	<b>1,301,435</b>	<b>11,160,290</b>	<b>12,699,649</b>
<b>Excess (deficiency) of revenues over (under) expenditures</b>	<b>(177,997)</b>	<b>1,251,531</b>	<b>1,054,320</b>	<b>200,864</b>	<b>2,328,718</b>	<b>1,300,537</b>
<b>Other financing sources (uses):</b>						
Equity loss on investment (note 5)	-	-	(40,771)	-	(40,771)	(249,766)
Operating transfers in (out) (note 12)	(191,860)	(499,500)	-	191,860	(499,500)	(1,076,049)
Other income	-	-	-	-	-	-
<b>Total other financing sources (uses), net</b>	<b>(191,860)</b>	<b>(499,500)</b>	<b>(40,771)</b>	<b>191,860</b>	<b>(540,271)</b>	<b>(1,325,815)</b>
<b>Excess (deficiency) of revenues over (under) expenditures and other uses before the cumulative effect of a change in accounting principle</b>	<b>(369,857)</b>	<b>752,031</b>	<b>1,013,549</b>	<b>392,724</b>	<b>1,788,447</b>	<b>(25,278)</b>
<b>Add: cumulative effect of a change in accounting principle (note 2)</b>	<b>303,974</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>303,974</b>	<b>-</b>
<b>Excess (deficiency) of revenues over (under) expenditures and other uses</b>	<b>(65,883)</b>	<b>752,031</b>	<b>1,013,549</b>	<b>392,724</b>	<b>2,092,421</b>	<b>(25,278)</b>
<b>Fund balances (deficit) at beginning of year</b>	<b>2,362,075</b>	<b>(736,120)</b>	<b>5,247,675</b>	<b>875,311</b>	<b>7,748,941</b>	<b>7,774,219</b>
<b>Fund balances at end of year</b>	<b>\$ 2,296,192</b>	<b>\$ 15,911</b>	<b>\$ 6,261,224</b>	<b>\$ 1,268,035</b>	<b>\$ 9,841,362</b>	<b>\$ 7,748,941</b>

See accompanying notes to financial statements.

**STATE OF KOSRAE**  
**FEDERATED STATES OF MICRONESIA**

Combined Statement of Revenues, Expenditures and Changes in Fund Balance (Deficit) -  
 Budgetary Basis - General Fund  
 Year Ended September 30, 1998

	Budget	Actual	Variance
<b>Revenues:</b>			
Compact funding:			
Base amount	\$ 2,189,600	\$ 2,189,600	\$ -
Inflation adjustment	1,051,008	1,160,488	109,480
Revenue sharing	779,400	868,395	88,995
State taxes and licenses	168,500	149,033	(19,467)
Investment income	50,000	307,506	257,506
Miscellaneous	372,280	222,604	(149,676)
<b>Total revenues</b>	<b>4,610,788</b>	<b>4,897,626</b>	<b>286,838</b>
<b>Expenditures:</b>			
General government	1,736,802	1,806,637	(69,835)
Education	1,192,851	1,372,568	(179,717)
Health services	580,668	670,225	(89,557)
Economic development	556,814	554,001	2,813
Transportation and utility	235,538	237,204	(1,666)
Public safety	270,480	267,028	3,452
Community affairs	306,378	215,934	90,444
<b>Total expenditures</b>	<b>4,879,531</b>	<b>5,123,597</b>	<b>(244,066)</b>
Excess (deficiency) of revenues over (under) expenditures	(268,743)	(225,971)	42,772
<b>Other financing sources (uses):</b>			
Operating transfer out (note 12)	(191,860)	(191,860)	-
Excess (deficiency) of revenues over (under) expenditures and other uses before the cumulative effect of a change in accounting principle	(460,603)	(417,831)	(42,772)
Add: cumulative effect of a change in accounting principle (note 2)	-	303,974	303,974
Excess (deficiency) of revenues over (under) expenditures and other uses	(460,603)	(113,857)	346,746
Unreserved fund deficit at beginning of year	(2,710,784)	(2,710,784)	-
<b>Other changes in unreserved fund deficit:</b>			
Decrease in reserve for related assets	-	444,762	444,762
Unreserved fund deficit at end of year	\$ (3,171,387)	\$ (2,379,879)	\$ 791,508

See accompanying notes to financial statements.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Combined Statement of Revenues, Expenses and Changes in Fund Equity (Deficiency)  
All Proprietary Fund Types and Discretely Presented Component Unit  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	Proprietary Fund Type Internal Service	Totals Primary Government (Memorandum Only)	Component Unit Kosrae Utilities Authority	Totals Reporting Entity (Memorandum Only)	
				1998	1997
Operating revenues:					
Charges for services	\$ 17,982	\$ 17,982	\$ 1,228,210	\$ 1,246,192	\$ 3,431,471
Operating expenses:					
Cost of goods sold	23,289	23,289	-	23,289	1,645,333
Taxes	-	-	-	-	201,941
Personnel services	-	-	378,716	378,716	597,602
Insurance	-	-	-	-	167,362
Professional fees	-	-	-	-	134,863
Travel and entertainment	-	-	-	-	103,260
Supplies and materials	-	-	-	-	42,880
Fuel	-	-	661,503	661,503	697,998
Depreciation	-	-	439,298	439,298	365,138
Administration and general	-	-	191,380	191,380	162,545
Repair and maintenance	-	-	68,505	68,505	118,524
Other	-	-	-	-	162,960
Total operating expenses	23,289	23,289	1,739,402	1,762,691	4,400,406
Operating income (loss)	(5,307)	(5,307)	(511,192)	(516,499)	(968,935)
Nonoperating revenues (expenses):					
Operating transfers in (note 12)	-	-	499,500	499,500	496,125
Interest income	-	-	55,473	55,473	55,697
Other income (expenses)	-	-	88,468	88,468	133,595
Total nonoperating revenues	-	-	643,441	643,441	685,417
Net income (loss)	(5,307)	(5,307)	132,249	126,942	(283,518)
Add depreciation on fixed assets acquired by capital contributions that reduce contributed capital	-	-	380,512	380,512	394,458
Increase in retained earnings (deficit)	(5,307)	(5,307)	512,761	507,454	110,940
Retained earnings (deficit) at beginning of year	(73,379)	(73,379)	2,378,736	2,305,357	1,847,907
Retained earnings (deficit) at end of year	(78,686)	(78,686)	2,891,497	2,812,811	1,958,847
Contributed capital at beginning of year	-	-	4,438,156	4,438,156	4,305,400
Contributions	-	-	97,924	97,924	4,779,237
Less amortization of contributed capital	-	-	(380,512)	(380,512)	(394,458)
Contributed capital at end of year	-	-	4,155,568	4,155,568	8,690,179
Fund equity (deficiency) at end of year	\$ (78,686)	\$ (78,686)	\$ 7,047,065	\$ 6,968,379	\$ 10,649,026

See accompanying notes to financial statements.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Combined Statement of Cash Flows -  
All Proprietary Fund Types and Discretely Presented Component Unit  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	Proprietary Fund Type	Totals Primary Government (Memorandum Only)	Component Unit Kosrae Utilities Authority	Totals Reporting Entity (Memorandum Only)	
	Internal Service			1998	1997
<b>Cash flows from operating activities:</b>					
Operating income (loss)	\$ (5,307)	\$ -	\$ (511,192)	\$ (511,192)	\$ (542,683)
Adjustment to reconcile operating loss to net cash provided by (used for) operating activities:					
Depreciation	-	-	439,298	439,298	365,138
Interest income	-	-	55,473	55,473	55,697
Other income	-	-	1,554	1,554	48,888
	<u>(5,307)</u>	<u>-</u>	<u>(14,867)</u>	<u>(14,867)</u>	<u>(72,960)</u>
<b>Changes in assets and liabilities:</b>					
General receivables, net	(773)	(773)	(32,930)	(33,703)	144,654
Inventory	-	-	(14,306)	(14,306)	28,629
Prepayments	-	-	2,698	2,698	(5,081)
Other receivables-OMIP	-	-	292,979	292,979	(262,301)
Other receivables-FSM National Government	-	-	(97,924)	(97,924)	(10,450)
Accounts payable	1,257	1,257	(2,100)	(843)	(62,731)
Accrued payroll and others	-	-	(4,503)	(4,503)	(7,131)
Due to other funds	4,823	4,823	-	4,823	(10,305)
	<u>5,307</u>	<u>5,307</u>	<u>143,914</u>	<u>149,221</u>	<u>(184,716)</u>
Net cash provided by (used for) operating activities	<u>-</u>	<u>5,307</u>	<u>129,047</u>	<u>134,354</u>	<u>(257,676)</u>
<b>Cash flows from noncapital financing activities:</b>					
Operating and other transfers in (note 12)	-	-	581,307	581,307	580,680
Net cash provided by noncapital financing activities	<u>-</u>	<u>-</u>	<u>581,307</u>	<u>581,307</u>	<u>580,680</u>
<b>Cash flows from capital and related financing activities:</b>					
Additions to fixed assets	-	-	(171,212)	(171,212)	(404,590)
Construction work in progress	-	-	-	-	(526,589)
Capital contributions	-	-	97,924	97,924	447,607
Net cash used for capital and related financing activities	<u>-</u>	<u>-</u>	<u>(73,288)</u>	<u>(73,288)</u>	<u>(483,572)</u>
Net increase (decrease) in cash and equivalents	-	5,307	637,066	642,373	(160,568)
Cash and equivalents at beginning of year	-	-	1,049,435	1,049,435	1,210,003
Cash and equivalents at end of year	<u>\$ -</u>	<u>\$ 5,307</u>	<u>\$ 1,686,501</u>	<u>\$ 1,691,808</u>	<u>\$ 1,049,435</u>

See accompanying notes to financial statements.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(1) Summary of Significant Accounting Policies

The general purpose financial statements of the State of Kosrae have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the State of Kosrae's accounting policies are described below.

A. Reporting Entity

The general purpose financial statements of the State of Kosrae have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. Government 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 Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The State of Kosrae has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

As required by generally accepted accounting principles, the general purpose financial statements of the State of Kosrae present the government and its component units; entities for which the government is considered to be financially accountable. Blended component units, although legally separate entities, are, in substance, part of the government's operations so data from these units are combined with data of the primary government. Discretely presented component units, on the other hand, are reported in a separate column in the general purpose financial statements to emphasize that they are legally separate from the government. There are no blended component units attributable to Kosrae State and three discretely presented component units which should be presented in the accompanying general purpose financial statements. However, Kosrae Community Action Program and Micronesia Petroleum Corporation were not able to provide financial statements for inclusion in the general purpose financial statements.

Discretely Presented Component Units

Kosrae Utilities Authority (KUA) is responsible for providing power services for the State which includes the government's jurisdiction. The members of the governing board are appointed by the governor with the consent of the state legislature. The government is potentially liable for the operating deficit (to date, KUA has not experienced an operating deficit) and would be secondarily liable for any debt issuances of KUA (currently, there is no debt outstanding). KUA is presented as a component unit - proprietary fund.

Micronesia Petroleum Corporation (MPC) was established on November 14, 1996 by Kosrae State Law L.B. No. 6-191, L.D. 2. The primary purpose of the Corporation is to operate and manage the State's fuel storage facilities and to engage in the business of buying and selling petroleum products. The Corporation is managed by a five member board consisting of representatives of the State Government and its private sector. MPC was not able to provide financial statements for inclusion in the accompanying general purpose financial statements.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(1) Summary of Significant Accounting Policies, Continued

**B. Fund Accounting**

The State of Kosrae uses funds and account groups to report on its financial position and the results of its operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain Kosrae State functions or activities.

A fund is a separate accounting entity with a self-balancing set of accounts. An account group, on the other hand, is a financial reporting device designed to provide accountability for certain assets and liabilities that are not recorded in the funds because they do not directly affect net expendable available financial resources. They are concerned only with the measurement of financial position and are not involved with measurement of results of operations.

Funds are classified into three categories: governmental, proprietary and fiduciary. Each category, in turn, is divided into separate "fund types."

Governmental funds are used to account for all or most of a government's general activities, including the collection and disbursement of earmarked monies (special revenue funds) and the acquisition or construction of general fixed assets (capital projects funds). The general fund is used to account for all activities of the general government not accounted for in some other fund.

Proprietary funds are used to account for activities similar to those found in the private sector, where the determination of net income is necessary or useful to sound financial administration. Goods or services from such activities can be provided either to outside parties (enterprise funds) or to other departments or agencies primarily within the government (internal service funds).

The Internal Service Fund is used to account for the stock supply operation of a self-sustaining state agency rendering services to other state agencies on a cost reimbursement basis.

Fiduciary funds are used to account for assets held on behalf of outside parties, including other governments, or on behalf of other funds within the State of Kosrae. When these assets are held under the terms of a formal trust agreement, either a pension trust fund, a nonexpendable trust fund or an expendable trust fund is used. The terms "nonexpendable" and "expendable" refer to whether or not the State of Kosrae is under an obligation to maintain the trust principal.

There are two account groups. The General Fixed Assets Account Group is used to account for fixed assets not accounted for in proprietary funds. The General Long-Term Debt Account Group is used to account for general long-term debt and certain other liabilities that are not specific liabilities of proprietary funds.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(1) Summary of Significant Accounting Policies, Continued

C. Basis of Presentation

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds and expendable trust funds are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital and retained earnings components. Proprietary fund type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

The modified accrual basis of accounting is used by all governmental fund types and expendable trust funds. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they become both measurable and available). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recorded when the related fund liability is incurred, except for certain compensated absences and claims and judgments which are recognized when the obligations are expected to be liquidated with expendable available financial resources.

The State of Kosrae considers all revenues available if they are collected within sixty days after year end. Expenditures are recorded when the related fund liability is incurred, except for unmatured interest on general long-term debt which is recognized when due, and certain compensated absences and claims and judgments which are recognized when the obligations are expected to be liquidated with expendable available financial resources.

Taxes, licenses and interest are susceptible to accrual. Sales taxes collected and held by the state at year end on behalf of the government are also recognized as revenue. Other receipts and taxes become measurable and available when cash is received by the government and are recognized as revenue at that time.

The accrual basis of accounting is utilized by proprietary fund types. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

D. Budgetary Process

Legislation requires the Governor to present a budget proposal to the Legislature at the beginning of each annual session. The Legislature then appropriates operating budgets which are limited in total by estimated fund revenues. Before signing an Appropriations Bill, the Governor may veto or reduce any specific appropriation; this veto is also subject to legislative override.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(1) Summary of Significant Accounting Policies, Continued

D. Budgetary Process, Continued

Encumbrance accounting is utilized for budgetary control purposes. Encumbrances outstanding at year end are reported as reservations of fund balance, and remain reservations of fund balance until becoming expended or canceled. Amounts included on the Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual - General Fund (which are presented on a non-GAAP budgetary basis) are reconciled to unreserved fund balance of the combined balance sheet within the other changes in unreserved fund balance section of that statement.

During fiscal year 1998, supplemental appropriations were made for both operating and capital purposes, to reflect revised financial priorities of Kosrae State Government.

Budgetary control is maintained at the departmental level. Budget revisions during the year, reflecting program changes or intra-departmental transfers of an administrative nature, may be effected with Executive and Legislative branch approval.

Unencumbered appropriations normally lapse at the end of each fiscal year unless designated as continuing appropriations.

E. Receivables

Receivables in the State's governmental funds consist primarily of taxes and federal revenues. Since few governmental fund type revenues are susceptible to accrual prior to receipt, most taxes, licenses, fees, permits and similar items are recognized on the cash basis.

F. Interfund Transactions

The State of Kosrae utilizes three types of potential interfund transactions:

1. The majority of the State's financial operations are centrally administered, and this administration is facilitated by the use of a "pooled" cash account; for practical purposes, cash is primarily maintained in a single bank account which is considered to be an asset of the State's general fund. As a result of this cash pooling practice, cash transactions normally include entries which adjust the relative balances of affected funds' interfund asset/liability accounts; each fund's interfund balance therefore represents a net interest in the State's actual cash.
2. Operating appropriations/subsidies which are accounted for as operating transfers of resources between funds.
3. Residual equity transfers which record the transfer of residual fund balances upon the termination of a fund's operations. These transfers are accounted for as additions to or deductions from governmental type fund balances or proprietary fund type fund equities.

For all funds, the combining balance sheet separately classifies interfund activity with the General Fund.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(1) Summary of Significant Accounting Policies, Continued

G. Inventory

Inventories of materials and supplies are determined by physical count and are valued at the lower of cost (principally average cost) or market.

H. Investments

Effective October 1, 1997, the State elected to implement the standards of GASB 31. GASB 31 provides that governmental activities shall, with certain exceptions, report investments at fair value in the balance sheet. Fair value is the amount which an investment could be exchanged in a current transaction between willing parties. Investments in the equity of companies are carried at cost if less than twenty percent of the companies' total equity, on the equity method if greater than twenty percent and less than fifty percent, and on a consolidated basis if greater than fifty percent. (See Note 2).

I. Fixed Assets

Governmental general fixed assets are carried in the General Fixed Assets Account Group. No depreciation is provided for on these assets. Assets are stated at cost or estimated cost. Fixed assets of Kosrae State Government also include capital infrastructure.

The State has not recorded additions or deletions to this Account Group in recent years and therefore, no statement of changes in general fixed assets is included in the accompanying general purpose financial statements.

Fixed assets of the Kosrae Utilities Authority, a component unit - proprietary fund, are comprised of various utility plant assets which are depreciated by the straight-line method over the estimated useful lives, as follows:

	<u>Estimated Useful Lives</u>	
Production plant	5 - 40 years	\$ 4,031,704
Distribution plant	5 - 30 years	1,833,999
General plant	3 - 20 years	<u>284,792</u>
Electric plant in service		6,150,495
Less accumulated depreciation		<u>(1,751,185)</u>
		4,399,310
Construction in progress		<u>203,658</u>
		\$ <u>4,602,968</u>

J. Actual Expenditures Contrasted With Budgetary Expenditures

Actual expenditures are charges which represent the total of all current year liabilities incurred which were attributable to operations; such liabilities may represent liquidations of either current or prior year encumbrances.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(1) Summary of Significant Accounting Policies, Continued

J. Actual Expenditures Contrasted With Budgetary Expenditures. Continued

In contrast, budgetary expenditures represent current charges against appropriations; current charges consist of all current year liquidated and unliquidated encumbrances. Budgetary expenditures are determined by subtracting both current year liquidations of prior year encumbrances and unliquidated prior year encumbrances from the combined total of current year actual expenditures and all unliquidated encumbrances. When viewed in relation to respective budgets, budgetary expenditures provide the principal means of evaluating current year operating performance and management stewardship.

K. Fund Balance Reserves

The State's fund balance reserves represent those portions of fund balance (1) not appropriable for expenditure or (2) legally segregated for a specific future use. Reserves for related assets such as inventories and long-term receivables are examples of the former. Reserves for encumbrances, continuing appropriations and other specific purposes are examples of the latter.

Reserves for related assets in the general purpose financial statements at September 30, 1998, are generally as follows:

General Fund:

General receivables and advances	\$ 447,115
Federal assistance fund (deficit)	251,998
Kosrae Transportation Fund receivable	162,563
Compact scholarship (deficit)	81,828
O&M assistance fund (deficit)	52,149
Non-U.S. grant (deficit)	113,588
Due from other governments-Federal grants fund	1,214,251
Due from other governments-CFSM Projects	1,674,996
Due from other governments-TTPI CIP fund	<u>343,895</u>
	\$ <u>4,342,383</u>

Capital Projects Funds:

Equity investments	\$ 2,525,247
Loan receivable	95,000
Term deposits	<u>600,000</u>
	\$ <u>3,220,247</u>

Expendable Trust Funds:

Loans receivable	\$ 455,944
Cash restricted for debt service (notes 11 and 12)	<u>191,860</u>
	\$ <u>647,804</u>

L. Cash and Equivalents

The State defines cash and equivalents as cash on deposit in banks including time certificates of deposit with an initial maturity of ninety days or less.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(1) Summary of Significant Accounting Policies, Continued

M. Compensated Absences

Vested or accumulated vacation leave that is expected to be liquidated with expendable available financial resources is reported as an expenditure and a fund liability of the governmental fund that will pay it. Amounts of vested or accumulated vacation leave that are not expected to be liquidated with expendable available financial resources are reported in the general long-term debt account group. The liability as of September 30, 1998 is \$670,332. No expenditure is reported for these amounts.

N. Totals - Memorandum Only

The "Totals - Memorandum Only" columns represent an aggregate of the individual combined financial statements. The total column is presented for overview informational purposes and does not represent consolidated financial information.

O. Management Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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.

(2) Cash and Investments

The State has adopted the by-laws of the Federated Development Authority as the agency to establish the overall development goals, policies and strategies of funds received and invested pursuant to the Compact of Free Association. The Federated States of Micronesia, Secretary of Finance, maintains such accounting system and records as are necessary to account for investment funds placed with the Authority on behalf of Kosrae State.

The Federated Development Authority has selected investment managers who are given authority to buy and sell securities as follows:

- A. Investment managers may invest in stocks, bonds and cash equivalents. Minimum standards of quality for investments at the time of purchase shall be:
1. Stocks - A "B" rating by a national rating service. Non-rated stocks such as banks or insurance companies must be equal in quality or higher.
  2. Bonds - Confined to issues rated "A" or higher by a national rating service, except in the case of U.S. Treasury or Agency securities which are not rated.
  3. Cash and equivalents - The manager may engage in all normally accepted short-term investment practices including, but not limited to: U.S. Treasury and Agency securities, bankers acceptances, certificates of deposit, commercial paper and repurchase agreements using any of the foregoing as collateral. The following restrictions apply:

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(2) Cash and Investments, Continued

- a. Commercial paper must be rated A-1/P-1 or higher by Standard & Poors Corporation and Moodys Investor Services.
  - b. Certificates of deposit must be from FDIC insured banks of which must have assets in excess of two billion dollars. Deposits in smaller institutions are acceptable, but must not exceed the amount of the insurance unless collateralized by U. S. Treasury Securities at 102%.
- B. The equity portfolio shall be diversified among issues and industry classifications. No more than 25% of the equity portfolio may be invested in any single classification, as described by the Standard and Poors 500 Index, unless prior approval is received from the Secretary of Finance.
- C. No investment may be made in a single corporate entity which exceeds 5% of the total assets of the fund at the time of purchase without prior approval of the Secretary of Finance.

At September 30, 1998, the market value of the State's investment was \$2,968,526. These investments have been reported at fair value in accordance with GASB 31 and are classified in the financial statements follows:

Cash and equivalents	\$ 26,331
Investments in equity securities	<u>2,942,195</u>
	<u>\$ 2,968,526</u>

Kosrae State has opted to implement Government Accounting Standards (GAS) 31 as of October 1, 1997. GAS 31 requires that governmental entities who have external investment pools report such investments at fair value in the balance sheet. Following is an analysis of the effect of this change in accounting principle in the current and prior year:

Current effect on 1998 investment income	\$ (34,005)
Cumulative effect on prior years	<u>303,974</u>
Total increase in investment income as a result of using market value in place of the lower of cost or market	269,969
Investment income for the year ended September 30, 1998 without this change	<u>316,139</u>
Total investment income reported for the year ended September 30, 1998 and the cumulative effect of a change in accounting principles, without recognition of interest income on time certificates of deposit	<u>\$ 586,108</u>

It is the policy of the State that earnings from pooled cash and investments generally accrue to the General Fund.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(2) Cash and Investments, Continued

The State does not require collateralization of its bank deposits. The Primary Government has \$300,000 of cash and equivalents subject to FDIC insurance; \$200,000 for the Kosrae Utilities Authority. The remaining balances of cash and equivalents are uncollateralized. At September 30, 1998, the State had deposits as follows (in each situation, cost approximates market value):

General Fund

Certificates of deposit with FDIC insured bank	\$ 49,076
------------------------------------------------	-----------

Capital Projects Funds

Certificates of deposit with FDIC insured bank	<u>827,917</u>
------------------------------------------------	----------------

\$ 876,993

Credit risk associated with investments is categorized into three levels generally described as follows:

- |              |                                                                                                                       |
|--------------|-----------------------------------------------------------------------------------------------------------------------|
| Category 1 - | Insured or registered, or securities held by the State or its agent in the State's name.                              |
| Category 2 - | Uninsured and unregistered, or securities held by a party other than the State or its agent, but in the State's name. |
| Category 3 - | Uninsured and unregistered, with securities held by a party other than the State and not in the State's name.         |

All investments held by the State or Trustee have been classified as category 2 investments in accordance with GASB #3 as all investments are held in the name of the Federated Development Authority.

Investment income for the year ended September 30, 1998, is comprised of the following items:

Compact Related Investments

Gross investment gains	\$ 246,262
Interest and dividends	230,924
Management and other fees	(161,047)
	316,139
Unrealized gains/losses	(34,005)

Noncompact Investments

Interest and dividends – local investments in time certificates of deposit	<u>25,372</u>
	\$ <u>307,506</u>

(3) Receivables From Other Governments and Federal Agencies

Amounts due from other governments include those funds which are earned and have yet to be reimbursed by the FSM National Government for U. S. federal assistance programs, U.S. Department of the Interior Capital Projects Grant, and those grants received from the Congress of the Federated States of Micronesia for capital projects.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(3) Receivables From Other Governments and Federal Agencies, Continued

Amounts due from federal agencies are funds which are reimbursed directly from U. S. federal agencies.

(4) Receivables

Various Expendable Trust Funds have loans and other receivables of \$446,121 and \$22,478, respectively. These balances are fully reserved within the related asset component of fund balance in the applicable funds.

The Capital Project Funds has a \$95,000 loan receivable from Pacific Tuna Industries, a related party (See Note 5) at 3 percent to be repaid in eight installments beginning September, 1995.

The General Fund, Special Revenue Funds and Capital Project Funds, have \$381,957, \$407,416, and \$297,804, respectively, of advances made to State government employees and medical referral patients for travel related expenditures. These advances are to be liquidated by submission of vouchers following the completion of travel.

General fund general receivables consist of general and miscellaneous receivables. The amount in the accompanying financial statements is net of an allowance for doubtful accounts of \$40,000, with the net balance being fully reserved in the related asset component of fund balance.

Receivables of the Kosrae Utilities Authority are for utility services rendered and are net of an allowance for doubtful accounts of \$140,719.

(5) Equity Investments

During the year ended September 30, 1998, the State has 50,000 shares in the Bank of the Federated States of Micronesia at a total cost of \$500,000. The Government's 50,000 shares represent approximately 5% of the Bank's total shares at September 30, 1998. This investment is recorded at cost, is considered long-term and has been fully reserved in the related asset component of fund balance. As of September 30, 1998, Kosrae State Government has \$876,993 in certificates of deposit with the bank.

Kosrae State Government acquired 100% of the stock of Pacific Tuna Industries (PTI), a for profit corporation organized under the laws of the Federated States of Micronesia. The investment is accounted for using the equity method. The carrying value of this investment has been reduced to \$-.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(5) Equity Investments, Continued

The FSM National Government contributed \$850,000 for Kosrae State Government's 50% share in Kosrae Sea Venture (KSVI) as mandated by FSM Public Law 7-107. The investment is recorded using the equity method and has been fully reserved for as a related asset of the capital projects funds. Kosrae Sea Venture commenced operations in fiscal year 1994. The investment's carrying value was \$362,268 at September 30, 1997. No subsequent financial information has been received to allow adjustment for 1998 results.

During the year ended September 30, 1998, Kosrae State made an additional investment of \$100,000 in Pacific Island Development Bank. The total investment of \$200,000 is recorded in the Capital Improvement Project Fund. The market value of these shares is difficult to assess as they are not publicly traded so a market versus cost analysis could not be performed. This investment in stock has therefore been carried at cost. Since the investment is considered unavailable to finance expenditures for the ensuing fiscal year, the investment is restricted in the reserve for related assets component of the fund balance.

During the year ended September 30, 1998, Kosrae made an additional investment of \$1,153,730 in SEMO Micronesia. The investment is recorded in the Capital Improvement Project Fund. The market value of these shares is difficult to assess as they are not publicly traded so a market versus cost analysis could not be performed. This investment in stock has therefore been carried at cost. Since the investment is considered unavailable to finance expenditures for the ensuing fiscal year, the investment is restricted in the reserve for related assets component of the fund balance.

Carrying value at October 1, 1997	\$ 350,000
FY98 additional investments	1,153,750
State's share of SEMO Micronesia's net loss for the year ended September 30, 1998	<u>(40,771)</u>
Carrying value at September 30, 1998	\$ <u>1,462,979</u>

(6) Contingencies

The State participates in a number of U.S. federally assisted programs. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. In 1998, cumulative questioned costs of \$332,440 remain unresolved for fiscal years 1996 through 1998. If these questioned costs are ultimately disallowed, the General Fund may bear responsibility for absorbing the amounts so disallowed. Pursuant to Title I, Section 105 of United States Public Law 99-239 (Compact of Free Association), the Government of the Federated States of Micronesia (FSM) is no longer liable for debts to U. S. federal agencies arising prior to the date of the implementation of the Compact of Free Association. This matter has not yet been officially resolved with the U.S. Government. Due to an inability to predict the ultimate outcome of this matter, no provision for any liability that may result has been made in the accompanying general purpose financial statements.

Sick Leave

It is the policy of the State of Kosrae to record the cost of sick leave when leave is actually taken and a liability is actually incurred. The accumulated estimated amount of unused sick leave at September 30, 1998, was \$2,022,114.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

**(6) Contingencies, Continued**

**Litigation**

The State of Kosrae is party to numerous legal proceedings, many of which are normal recurrences in governmental operations. The Attorney General of the State of Kosrae is of the opinion that the probable outcome of suits existing at September 30, 1998, is not predictable but will have no material impact on the accompanying general purpose financial statements.

Additionally, as described in note 5, the State acquired an investment which was not made in accordance with local laws. It is not possible to assess the ultimate impact of this matter on the accompanying general purpose financial statements.

**Loan Collateralization**

At September 30, 1998, a time certificate of deposit in the amount of \$600,000 for Kosrae State Government was held by a local bank as collateral for a loan to Micronesia Petroleum Corporation, a component unit-proprietary fund.

**Risk Management**

The State of Kosrae does not purchase insurance covering its potential risks. The State is self insured for all risks. The State is of the opinion that no material losses have been sustained as a result of this practice.

**(7) Material Fund Deficits**

The following funds reflect material fund deficits as of September 30, 1998. If operations of these funds cannot recover prior losses, the State's General Fund may have to absorb these amounts or a portion thereof.

Internal Service Fund	\$ <u>78,686</u>
Compact Scholarship Fund	\$ <u>81,828</u>
U.S. Department of the Interior Fund	\$ <u>52,149</u>
Federal Grants Assistance	\$ <u>251,998</u>
Foreign Assistance	\$ <u>113,588</u>
CFSM Capital Projects Fund	\$ <u>49,924</u>
Scholarship Revolving Fund	\$ <u>18,207</u>

Of the above, the total fund deficits for the Federal Grants Assistance, Compact Special Block Grant, Compact Scholarship, U.S. Department of the Interior and the Foreign Assistance funds have been reserved in the General Fund as related assets since the interfund due to the General Fund relating to the aforementioned fund deficits may not be collectible within the following year.

**(8) Interfund Receivables and Payables**

As of September 30, 1998, interfund receivables and payables resulting from various interfund transactions are as follows:

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(8) Interfund Receivables and Payable, Continued

	Due to other Funds	Due from other Funds
General Fund	\$ 359,612	\$ 1,723,869
Special Revenue Funds:		
Compact-Special Block	23,047	-
Compact-Health and Medical	-	75,676
Compact Post Secondary Education	251,852	-
Compact Energy	4,309	-
Compact Special Development	-	139,847
Fishermen's Revolving Fund	-	1,026
U.S. Department of the Interior Fund	-	42,309
Federal Grants Assistance Fund	1,629,313	-
Foreign Assistance Fund	135,230	-
Capital Project Funds:		
Compact Capital Projects Fund	-	1,805,967
CFSM State Projects	1,804,790	-
TTG - Capital Project Fund	411,412	336,703
Expendable Trust Funds:		
Airport Trust Fund	-	148,303
Production Loan Fund	-	1,495
Scholarship Revolving Fund	8,720	-
Housing Revolving Fund	-	341,927
Aluminum Recycling Fund	-	30,918
Health Care Fund	-	43,134
Sports Council Fund	-	517
Early Retirement Program	-	75,609
Internal Service Fund	<u>139,015</u>	<u>-</u>
	<u>\$ 4,767,300</u>	<u>\$ 4,767,300</u>

(9) Continuing Appropriations

Continuing appropriations as of September 30, 1998, are summarized as follows:

General Fund

New Broadcast Facility	\$ 1,390
Communication Network	1,146
Vehicle License Plate	1,195
Printing of State Laws	280
Population Housing Census	186
Peritoneal Dialysis Program	38,256
Medical Cost Senior Citizens	4,000
Second Constitutional Convention	78
Payment of legal obligations	712
Chiplin Conference	37
Scholarship	<u>18,270</u>
	<u>\$ 65,550</u>

**STATE OF KOSRAE**  
**FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(9) Continuing Appropriations, Continued

Special Revenue Funds

Kosraen Chants	\$ 4,478
KUA Establishment	21,941
Power Systems	199,877
KUA OMIP	315,000
Compact Scholarship	<u>900</u>

\$ 542,196

Capital Project Funds

Compact of Free Association Capital Account -	
Various State approved projects	\$ 1,444,891
Various CFSM approved projects	258,336
Various TTPI approved projects	<u>764,260</u>

\$ 2,467,487

(10) Notes Payable

During fiscal year ended September 30, 1995, Kosrae State Government borrowed \$386,000 from a bank for the purchase of a residential property for its medical referral program in Honolulu. Monthly installments of \$5,101 are to be paid over 10 years. The note is collateralized by a mortgage on the residential property and an assignment of tenant lease rental income and a security interest in all of the property's furniture, fixtures and equipment used in connection with the property. The outstanding notes payable balance as of September 30, 1998 is \$285,962. Future principal installments due on this loan are as follows:

1999	\$ 32,731
2000	36,338
2001	40,343
2002	44,789
2003	49,725
Thereafter	<u>82,036</u>

\$ 285,962

During the fiscal year ended September 30, 1998, Kosrae State Government implemented an early retirement program for employees within the public service system. The program is funded through a loan from the Asian Development Bank through the FSM National Government of \$2,000,000. As of September 30, 1998, Kosrae State has an outstanding loan balance of \$1,000,000 under this program. (See note 11).

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 1998

(11) Early Retirement Program

During the year ended September 30, 1998, the State implemented an Early Retirement Scheme (ERS) in which employees holding certain nonessential positions as identified by the State were retired early with a payout of the equivalent of two-years wages. The ERS program is funded by a \$2,000,000 loan from the Asian Development Bank through the FSM National Government. During the year ended September 30, 1998, \$1,000,000 of the loan was released to the FSM National Government, which was then transferred to the State of Kosrae. The activities of the ERS Program as recorded in an expendable trust fund. Program expenditures as of September 30, 1998 consisted of employees' retirement payouts and training costs.

The ADB loan has a grace period of ten years with the first payment due in February 2008 and the last payment in August 2038. However, pursuant to the terms of the Financing Agreement between the State of Kosrae and the FSM National Government, the State is required to deposit into the ERS Trust account held in the name of Kosrae State within the FSM National Government investment portfolio, 100% of the outstanding principal balance by September 30, 2001. The estimated principal balances to be repaid in future years approximate \$300,000 in fiscal year 1999, \$300,000 in fiscal year 2000 and \$400,000 in fiscal year 2001.

Funds for the repayment of the ADB loan are expected to be derived from the annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The Financing Agreement requires the State to continue to appropriate salaries for the abolished positions and deposit the appropriate funds into the ERS Trust Account. State management has restricted cash in the expendable trust fund in the amount of \$191,860 designated for the repayment of this debt. (See note 12).

(12) Operating Transfers Out

Operating transfers out for the year ended September 30, 1998, are as follows:

Transfer from Special Revenue Fund to Kosrae Utility Authority (KUA)	\$ <u>499,500</u>
Transfer from General Fund to Expendable Trust Fund	\$ <u>191,860</u>

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Supplemental Year 2000 Information  
September 30, 1998

Like other organizations and individuals around the world, Kosrae State could be adversely affected if the computer systems it uses and those used by significant third parties (e.g. vendors, customers, third party administrators, etc.) do not properly process and calculate date-related information and data. This is commonly known as the "Year 2000 issue." Management is assessing its computer systems and business processes and intends to initiate actions to address the Y2K needs identified. Management is also assessing the actions being taken by significant third parties that interface with the State. The State has identified that its current accounting software system is not year 2000 compliant. As a result, the State has decided to purchase and implement new accounting software to ensure year 2000 compatability. Management is of the opinion that it is still on schedule to receive a production ready product by the end of 1999. Other hardware and operating system upgrades are also scheduled to be implemented in early 1999. At this time, management is not able to determine the estimated costs of remediation of the year 2000 issue.

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account -  
All Governmental Fund Types and Expendable Trust Funds  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	<u>Governmental Fund Types</u>			<u>Fiduciary Fund Type</u>	<u>Totals</u>	
	<u>General</u>	<u>Special Revenue</u>	<u>Capital Projects</u>	<u>Expendable Trust</u>	<u>(Memorandum Only)</u>	
					<u>1998</u>	<u>1997</u>
Expenditures:						
Personnel	\$ 3,968,189	\$ 601,723	\$ 418,464	\$ -	\$ 4,988,376	\$ 6,200,029
Travel	148,727	380,886	113,445	-	643,058	451,274
Supplies and materials	164,446	-	-	-	164,446	-
POL	1,896	44,542	17,807	-	64,245	37,331
Capital outlay	171,478	162,252	140,071	-	473,801	269,734
Contractual services	47,594	411,574	1,084,530	-	1,543,698	-
Other	573,293	667,593	740,345	1,301,435	3,282,666	5,741,281
Total expenditures	<u>\$ 5,075,623</u>	<u>\$ 2,268,570</u>	<u>\$ 2,514,662</u>	<u>\$ 1,301,435</u>	<u>\$ 11,160,290</u>	<u>\$ 12,699,649</u>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

General Fund  
September 30, 1998

The general fund is used to account for resources traditionally associated with government which are not required legally or by sound financial management to be accounted for in another fund.

The State of Kosrae maintains separate and distinct general funds as required by local law. The operations of the Executive Branch are accounted for primarily in the U.S. Grants Fund, while the operations of the Legislative Branch are accounted for in the State Revenue Fund.

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND  
Combining Balance Sheet  
September 30, 1998  
(With comparative totals as of September 30, 1997)**

	<u>U.S. Grant</u>	<u>State Revenue</u>	<u>Totals</u>	
			<u>1998</u>	<u>1997</u>
<b><u>ASSETS</u></b>				
Cash and equivalents	\$ -	\$ -	\$ -	\$ 113,581
Other term deposits	-	49,076	49,076	49,076
Investments	1,893,033	-	1,893,033	1,594,927
Receivables from other governments	180,636	97,516	278,152	249,807
General receivables, net	40,062	96,397	136,459	43,091
Advances	-	381,957	381,957	338,774
Due from other funds	1,723,869	-	1,723,869	1,555,559
Interest receivable	12,094	-	12,094	12,094
Total assets	<u>\$ 3,849,694</u>	<u>\$ 624,946</u>	<u>\$ 4,474,640</u>	<u>\$ 3,956,909</u>
 <b><u>LIABILITIES AND FUND BALANCES</u></b>				
<b>Liabilities:</b>				
Bank overdraft	\$ 958,372	\$ -	\$ 958,372	\$ 364,506
Accounts payable	27,813	70,392	98,205	287,585
Accrued payroll and others	250,189	12,965	263,154	214,166
Due to other funds	236,299	123,313	359,612	232,878
Due to other governments	180,636	-	180,636	180,636
Other payables	318,469	-	318,469	315,063
Total liabilities	<u>1,971,778</u>	<u>206,670</u>	<u>2,178,448</u>	<u>1,594,834</u>
<b>Fund balances:</b>				
Reserved for:				
Related assets	3,772,767	569,616	4,342,383	4,787,145
Encumbrances	146,793	121,345	268,138	220,164
Continuing appropriations	4,197	61,353	65,550	65,550
Unreserved	<u>(2,045,841)</u>	<u>(334,038)</u>	<u>(2,379,879)</u>	<u>(2,710,784)</u>
Total fund balances	<u>1,877,916</u>	<u>418,276</u>	<u>2,296,192</u>	<u>2,362,075</u>
Total liabilities and fund balances	<u>\$ 3,849,694</u>	<u>\$ 624,946</u>	<u>\$ 4,474,640</u>	<u>\$ 3,956,909</u>

See Accompanying Independent Auditors' Report.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND**

Combining Statement of Revenues, Expenditures  
by Function and Changes in Fund Balances

Year Ended September 30, 1998

(With comparative totals for the year ended September 30, 1997)

	U.S. Grant	State Revenue	Totals 1998	1997
<b>Revenues:</b>				
Compact of Free Association:				
Base amount	\$ 2,189,600	\$ -	\$ 2,189,600	\$ 2,189,600
Inflation adjustment	1,160,488	-	1,160,488	1,094,800
Revenue sharing	-	868,395	868,395	810,661
Taxes and licenses	-	149,033	149,033	157,677
Investment income	282,134	25,372	307,506	416,107
Other	-	222,604	222,604	300,122
<b>Total revenues</b>	<b>3,632,222</b>	<b>1,265,404</b>	<b>4,897,626</b>	<b>4,968,967</b>
<b>Expenditures:</b>				
General government	786,074	978,115	1,764,189	1,855,160
Education	1,375,842	1,062	1,376,904	922,073
Health services	665,631	-	665,631	826,648
Economic development	530,450	32,496	562,946	669,616
Public works	236,199	-	236,199	338,746
Public safety	264,995	-	264,995	312,424
Community affairs	41,027	146,693	187,720	288,664
Other	17,039	-	17,039	150,441
<b>Total expenditures</b>	<b>3,917,257</b>	<b>1,158,366</b>	<b>5,075,623</b>	<b>5,363,772</b>
Excess (deficiency) of revenues over (under) expenditures	(285,035)	107,038	(177,997)	(394,805)
<b>Other financing sources (uses):</b>				
Operating transfer out	-	(191,860)	(191,860)	-
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses before the cumulative effect of a change in accounting principle	(285,035)	(84,822)	(369,857)	(394,805)
<b>Add: cumulative effect of a change in     accounting principle</b>	<b>303,974</b>	<b>-</b>	<b>303,974</b>	<b>-</b>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	18,939	(84,822)	(65,883)	(394,805)
<b>Fund balances at beginning of year</b>	<b>1,858,977</b>	<b>503,098</b>	<b>2,362,075</b>	<b>2,756,880</b>
<b>Fund balances at end of year</b>	<b>\$ 1,877,916</b>	<b>\$ 418,276</b>	<b>\$ 2,296,192</b>	<b>\$ 2,362,075</b>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND  
Combining Statement of Revenues, Expenditures  
by Account and Changes in Fund Balances  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)**

	<u>U.S. Grant</u>	<u>State Revenue</u>	<u>Totals</u>	
			<u>1998</u>	<u>1997</u>
<b>Revenues:</b>				
Compact of Free Association:				
Base amount	\$ 2,189,600	\$ -	\$ 2,189,600	\$ 2,189,600
Inflation adjustment	1,160,488	-	1,160,488	1,094,800
Revenue sharing	-	868,395	868,395	810,661
Taxes and licenses	-	149,033	149,033	157,677
Investment income	282,134	25,372	307,506	416,107
Other	-	222,604	222,604	300,122
<b>Total revenues</b>	<u>3,632,222</u>	<u>1,265,404</u>	<u>4,897,626</u>	<u>4,968,967</u>
<b>Expenditures:</b>				
Personnel	3,170,796	797,393	3,968,189	4,312,677
Travel	44,388	104,339	148,727	122,576
Supplies and materials	136,787	27,659	164,446	-
POL	54	1,842	1,896	2,256
Capital outlay	167,931	3,547	171,478	34,378
Contractual services	41,013	6,581	47,594	-
Other	356,288	217,005	573,293	891,885
<b>Total expenditures</b>	<u>3,917,257</u>	<u>1,158,366</u>	<u>5,075,623</u>	<u>5,363,772</u>
Excess (deficiency) of revenues over (under) expenditures	(285,035)	107,038	(177,997)	(394,805)
<b>Other financing sources (uses):</b>				
Operating transfer out	<u>-</u>	<u>(191,860)</u>	<u>(191,860)</u>	<u>-</u>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses before the cumulative effect of a change in accounting principle	(285,035)	(84,822)	(369,857)	(394,805)
<b>Add: cumulative effect of a change in     accounting principle</b>	<u>303,974</u>	<u>-</u>	<u>303,974</u>	<u>-</u>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	18,939	(84,822)	(65,883)	(394,805)
<b>Fund balances at beginning of year</b>	<u>1,858,977</u>	<u>503,098</u>	<u>2,362,075</u>	<u>2,756,880</u>
<b>Fund balances at end of year</b>	<u>\$ 1,877,916</u>	<u>\$ 418,276</u>	<u>\$ 2,296,192</u>	<u>\$ 2,362,075</u>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND  
Combining Statement of Revenues, Expenditures and  
Changes in Fund Balances; Budgetary Basis  
Year Ended September 30, 1998**

	U.S. Grant Fund			State Revenue Fund			Total General Fund		
	Budget	Actual	Variance	Budget	Actual	Variance	Budget	Actual	Variance
<b>Revenues:</b>									
Compact funding:									
Base amount	\$ 2,189,600	\$ 2,189,600	\$ -	\$ -	\$ -	\$ -	\$ 2,189,600	\$ 2,189,600	\$ -
Inflation adjustment	1,051,008	1,160,488	109,480	-	-	-	1,051,008	1,160,488	109,480
Revenue sharing	-	-	-	779,400	868,395	88,995	779,400	868,395	88,995
State taxes and licenses	-	-	-	168,500	149,033	(19,467)	168,500	149,033	(19,467)
Investment income	-	282,134	282,134	50,000	25,372	(24,628)	50,000	307,506	257,506
Miscellaneous	-	-	-	372,280	222,604	(149,676)	372,280	222,604	(149,676)
<b>Total revenues</b>	<b>3,240,608</b>	<b>3,632,222</b>	<b>391,614</b>	<b>1,370,180</b>	<b>1,265,404</b>	<b>(104,776)</b>	<b>4,610,788</b>	<b>4,897,626</b>	<b>286,838</b>
<b>Expenditures:</b>									
General government	771,758	788,924	(17,166)	965,044	1,017,713	(52,669)	1,736,802	1,806,637	(69,835)
Education	1,190,984	1,370,636	(179,652)	1,867	1,932	(65)	1,192,851	1,372,568	(179,717)
Health services	580,668	670,225	(89,557)	-	-	-	580,668	670,225	(89,557)
Economic development	556,814	554,001	2,813	-	-	-	556,814	554,001	2,813
Transportation and utility	235,538	237,204	(1,666)	-	-	-	235,538	237,204	(1,666)
Public safety	270,480	267,028	3,452	-	-	-	270,480	267,028	3,452
Community affairs	87,500	30,616	56,884	218,878	185,318	33,560	306,378	215,934	90,444
<b>Total expenditures</b>	<b>3,693,742</b>	<b>3,918,634</b>	<b>(224,892)</b>	<b>1,185,789</b>	<b>1,204,963</b>	<b>(19,174)</b>	<b>4,879,531</b>	<b>5,123,597</b>	<b>(244,066)</b>
Excess (deficiency) of revenues over (under) expenditures	(453,134)	(286,412)	166,722	184,391	60,441	(123,950)	(268,743)	(225,971)	42,772
<b>Other financing sources (uses):</b>									
Operating transfer out	-	-	-	(191,860)	(191,860)	-	(191,860)	(191,860)	-
Excess (deficiency) of revenues over (under) expenditures and other uses before the cumulative effect of change in accounting principle	(453,134)	(286,412)	(166,722)	(7,469)	(131,419)	123,950	(460,603)	(417,831)	(42,772)
<b>Add: cumulative effect of a change in accounting principle</b>	<b>-</b>	<b>303,974</b>	<b>(303,974)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>303,974</b>	<b>303,974</b>
Excess (deficiency) of revenues over (under) expenditures and other uses	(453,134)	17,562	(470,696)	(7,469)	(131,419)	123,950	(460,603)	(113,857)	(346,746)
<b>Unreserved fund balances at beginning of year</b>	<b>(2,653,024)</b>	<b>(2,653,024)</b>	<b>-</b>	<b>(57,760)</b>	<b>(57,760)</b>	<b>-</b>	<b>(2,710,784)</b>	<b>(2,710,784)</b>	<b>-</b>
<b>Other changes in unreserved fund balances:</b>									
Decrease in reserve for related assets	-	589,621	(589,621)	-	(144,859)	144,859	-	444,762	(444,762)
<b>Unreserved fund deficit at end of year</b>	<b>\$ (3,106,158)</b>	<b>\$ (2,045,841)</b>	<b>\$ (1,060,317)</b>	<b>\$ (65,229)</b>	<b>\$ (334,038)</b>	<b>\$ 268,809</b>	<b>\$ (3,171,387)</b>	<b>\$ (2,379,879)</b>	<b>\$ (791,508)</b>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

GENERAL FUND  
Combined Statement of Revenues, Expenditures by Function  
and Department and Changes in Fund Balance  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	1998		1997
<b>Revenues:</b>			
Compact of Free Association:			
Base amount	\$ 2,189,600		\$ 2,189,600
Inflation adjustment	1,160,488		1,094,800
FSM revenue sharing	868,395		810,661
State taxes and licenses:			
Cigarette tax	\$ 13,194		\$ 12,588
General sales tax	59,528		52,148
Alcohol	46,532		62,670
Motor vehicle sales tax	9,597		10,257
Licenses and fees	13,995		15,994
Court fines	6,187	149,033	4,020
			157,677
Other revenues:			
Medical and dental services	1,208		-
Miscellaneous	221,396	222,604	300,122
Investment income		307,506	416,107
			4,968,967
Total revenues	4,897,626		
<b>Expenditures:</b>			
General government:			
Governor and staff		341,923	227,538
Department of Administration:			
Director of Administration	33,329		58,811
Division of Planning and Statistics	53,550		55,197
Division of Finance and Budget	198,852		240,928
Division of Construction and Engineering	50,187		67,639
Division of Personnel and Employment	52,950		63,807
Centralize Leasing/Housing	62,450	451,318	54,961
			541,343
Kosrae State Court:			
Court Operations		124,725	143,153
Legislative Branch:			
Legislative members	251,934		282,830
Standing committees	48,668		41,583
Staff	277,586	578,188	336,276
			660,689
Land commission		129,818	154,570
Legislative appropriations-election		138,217	127,867
			1,855,160
Total general government	1,764,189		

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND**

Combined Statement of Revenues, Expenditures by Function  
and Department and Changes in Fund Balance, Continued  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	<u>1998</u>		<u>1997</u>
Expenditures by department, continued:			
Department of Education:			
Director's Office	48,593		58,275
Division of Instructional Services	1,022,017		468,462
Division of Curriculum Development	121,506		166,359
Facilities Special Services	53,182		82,654
Community Development	30,544		61,552
Scholarship Board	1,932		2,811
Scholarship Supplement	99,130		81,960
	<u>1,376,904</u>		<u>922,073</u>
Department of Health Services:			
Director of Health Services	97,630		19,945
Division of Hospital Services	483,577		637,467
Division of Sanitation	20,950		54,794
Division of Dental Services	22,507		38,429
Division of Public Health	40,967		76,013
	<u>665,631</u>		<u>826,648</u>
Economic Development:			
Department of Fisheries and Marines			
Director of Fisheries and Marines	24,237		30,198
Division of Fisheries and Surveillance	22,453		23,601
Division of Marine Resources	31,064	77,754	30,800
			84,599
Department of Agriculture and Land			
Director of Agriculture and Land	58,646		77,531
Division of Crop Production & Research	63,125		93,787
Division of Livestock Prod. & Research	53,356		41,817
Division of Land Management and Pres.	39,051		47,658
Division of Surveying and Mapping	64,791	278,969	111,258
			372,051
Department of Commerce and Industry:			
Director of Commerce and Industry	39,468		41,506
Division of Market and Research	6,291		6,723
Division of Housing C & I	52,460		42,578
Division of Industrial Development	32,899		35,373
Division of Consumer Services	25,174		27,953
Division of Tourism	16,649		17,806
Legislative appropriations-economic dev.	787	173,728	-
			171,939
Foreign Investment Board	-		906
Development Review Commission	32,495		40,121
Total economic development	<u>562,946</u>		<u>669,616</u>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND**

Combined Statement of Revenues, Expenditures by Function  
and Department and Changes in Fund Balance, Continued  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	<u>1998</u>	<u>1997</u>
Expenditures by department, continued:		
Department of Public Works:		
Director of Transportation and Utility	37,502	50,443
Division of Road and Public Trans.	136,477	202,463
Division of Water and Wastewater	22,348	36,867
Division of Airport/Dock/Harbot	39,872	48,973
Total public works	<u>236,199</u>	<u>338,746</u>
Department of Justice:		
Director of Justice	22,991	40,296
Police Division	182,552	173,639
Division of Law	59,452	97,459
'92 Police COM Network NE	-	1,030
Total justice	<u>264,995</u>	<u>312,424</u>
Community Affairs:		
Sports Operation	36,546	33,637
Lelu Senior Citizens	1,190	89
Malem Senior Citizens	422	105
Tafunsak Senior Citizens	1,709	-
KCAP Operations - legislative	20,952	36,866
FY94 Census Pop/Housing	-	3,437
FY-96 Chip-in	-	1,463
Parole Board	240	367
FY-97 2nd FSM Games	1,500	112,866
MLSC Operations	36,000	36,000
Broadcast Authority - Legislative	49,634	63,834
Civic Action Team	30,000	-
FY98 Utwe ConCon	2,490	-
FY98 Tafunsak ConCon	4,340	-
FY95 Legislative Opp.	2,697	-
Total community affairs	<u>187,720</u>	<u>288,664</u>
Other	<u>17,039</u>	<u>150,441</u>
Total expenditures	<u>5,075,623</u>	<u>5,363,772</u>
Deficiency of revenues under expenditures	(177,997)	(394,805)

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND**

Combined Statement of Revenues, Expenditures by Function  
and Department and Changes in Fund Balance, Continued  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	<u>1998</u>	<u>1997</u>
Other financing sources (uses):		
Operating transfer out	<u>(191,860)</u>	<u>-</u>
Deficiency of revenues and other financing sources under expenditures and other financing uses before the cumulative effect of a change in accounting principle	 (369,857)	 (394,805)
Add: cumulative effect of a change in accounting principle	<u>303,974</u>	<u>-</u>
Deficiency of revenues and other financing sources under expenditures and other financing uses	 (65,883)	 (394,805)
Fund balance at beginning of year	<u>2,362,075</u>	<u>2,756,880</u>
Fund balance at end of year	<u>\$ 2,296,192</u>	<u>\$ 2,362,075</u>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Special Revenue Funds  
September 30, 1998

Specific revenues that are legally restricted to expenditures for particular purposes are accounted for in Special Revenue Funds. A brief discussion of Kosrae State's Special Revenue Funds as of September 30, 1998, follows:

Compact - Special Block Grant - Health and Education, Title Two, Article I, Section 221 (b)

This fund accounts for the funds granted under the Compact of Free Association with the United States, specifically restricted for health and education programs.

Compact - Health and Medical - Section 216 (a) 2

This fund is restricted for health and medical programs including referrals to hospital and treatment centers.

Compact - Post Secondary Education - Section 216 (a) 3

This fund is restricted for scholarship funds or funds to support the post secondary education of FSM citizens.

Compact - Energy Block Grant - Section 214

This fund accounts for the funds granted under the Compact of Free Association with the United States, specifically restricted for the purchase of fuel to operate the State's power generating facilities and other energy related projects.

Compact - Special Development Assistance - Section 212(b)

This fund accounts for the funds granted under the Compact of Free Association with the United States, specifically restricted for economic development projects.

Fishermen's Revolving Fund

This fund was established on May 1, 1987, by State Law 4-8 to account for the sale of fishing supplies to local fishermen on a non-profit basis.

U.S. Department of the Interior

This fund accounts for all U.S. Congressional appropriations for specified project operation and maintenance subsidies which are granted through the U.S. Department of the Interior.

Federal Grants Assistance Fund

This fund accounts for all activities of United States special federal assistance grants utilized by the State of Kosrae to finance general governmental operations.

Foreign Assistance

This fund accounts for financial transactions related to federal assistance from other countries received directly by the State of Kosrae.

See Accompanying Independent Auditors' Report.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**SPECIAL REVENUE FUNDS  
Combining Balance Sheet  
September 30, 1998  
(With comparative totals as of September 30, 1997)**

ASSETS	Compact Special Block Grant 221(b)	Compact Health and Medical 216(a)(2)	Compact Scholarship 216(a)(3)	Compact Energy Block Grant 214	Compact Special Development 212(b)	Fishermen's Revolving	U.S. Department of the Interior	Federal Grants Assistance	Foreign Assistance	Totals	
										1998	1997
Cash and equivalents	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 8,534
Investments	-	56,063	-	139,850	89,007	-	-	-	-	284,920	93,983
Receivables from:											
Federal agencies	-	-	-	-	-	-	-	1,214,250	-	1,214,250	1,079,137
Other Governments	-	-	-	-	-	-	-	-	14,599	14,599	11,550
General receivables, net	21,099	-	170,024	-	-	-	-	-	-	191,123	155,875
Advances	39,175	34,710	-	4,718	52,439	-	36,746	235,830	7,043	410,661	400,588
Due from other funds	-	75,676	-	-	139,847	1,026	42,309	-	-	258,858	336,658
<b>Total assets</b>	<b>\$ 60,274</b>	<b>\$ 166,449</b>	<b>\$ 170,024</b>	<b>\$ 144,568</b>	<b>\$ 281,293</b>	<b>\$ 1,026</b>	<b>\$ 79,055</b>	<b>\$ 1,450,080</b>	<b>\$ 21,642</b>	<b>\$ 2,374,411</b>	<b>\$ 2,086,325</b>
<b>LIABILITIES AND FUND BALANCES (DEFICIT)</b>											
Liabilities:											
Accounts payable	\$ -	\$ 9,682	\$ -	\$ 57,690	\$ 21,263	\$ -	\$ 41,992	\$ 63,181	\$ -	\$ 193,808	\$ 38,327
Accrued payroll and others	22,145	-	-	-	-	-	61,117	9,584	-	92,846	21,269
Due to other funds	23,047	-	251,852	4,309	-	-	-	1,629,313	135,230	2,043,751	2,734,754
Deferred revenues	-	-	-	-	-	-	28,095	-	-	28,095	28,095
<b>Total liabilities</b>	<b>45,192</b>	<b>9,682</b>	<b>251,852</b>	<b>61,999</b>	<b>21,263</b>	<b>-</b>	<b>131,204</b>	<b>1,702,078</b>	<b>135,230</b>	<b>2,358,500</b>	<b>2,822,445</b>
Fund balances (deficit):											
Reserved for:											
Encumbrances	31,012	42,995	-	8,819	34,938	-	154,346	443,942	17,128	733,180	460,920
Continuing appropriations	-	-	900	-	-	-	541,296	-	-	542,196	542,196
Unreserved	(15,930)	113,772	(82,728)	73,750	225,092	1,026	(747,791)	(695,940)	(130,716)	(1,259,465)	(1,739,236)
<b>Total fund balances (deficit)</b>	<b>15,082</b>	<b>156,767</b>	<b>(81,828)</b>	<b>82,569</b>	<b>260,030</b>	<b>1,026</b>	<b>(52,149)</b>	<b>(251,998)</b>	<b>(113,588)</b>	<b>15,911</b>	<b>(736,120)</b>
<b>Total liabilities and fund balances (deficit)</b>	<b>\$ 60,274</b>	<b>\$ 166,449</b>	<b>\$ 170,024</b>	<b>\$ 144,568</b>	<b>\$ 281,293</b>	<b>\$ 1,026</b>	<b>\$ 79,055</b>	<b>\$ 1,450,080</b>	<b>\$ 21,642</b>	<b>\$ 2,374,411</b>	<b>\$ 2,086,325</b>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**SPECIAL REVENUE FUNDS**  
**Combining Statement of Revenues, Expenditures by Function and Changes in Fund Balances (Deficit)**  
**Year Ended September 30, 1998**  
**(With comparative totals for the year ended September 30, 1997)**

	Compact Special Block Grant 221(b)	Compact Health and Medical 216(a)(2)	Compact Scholarship 216(a)(3)	Compact Energy Block Grant 214	Compact Special Development 212(b)	Fishermen's Revolving	U.S. Department of the Interior	Federal Grants Assistance	Foreign Assistance	Totals	
										1998	1997
<b>Revenues:</b>											
Compact grants:											
Base amount	\$ 875,000	\$ 112,122	\$ -	\$ 450,000	\$ 250,000	\$ -	\$ -	\$ -	\$ -	\$ 1,687,122	\$ 1,820,544
Inflation adjustment	-	-	-	238,500	132,500	-	-	-	-	371,000	350,000
Federal contributions	-	-	-	-	-	-	10,367	1,423,450	-	1,433,817	1,286,205
Other	-	-	-	-	-	-	-	-	28,162	28,162	57,962
Total revenues	<u>875,000</u>	<u>112,122</u>	<u>-</u>	<u>688,500</u>	<u>382,500</u>	<u>-</u>	<u>10,367</u>	<u>1,423,450</u>	<u>28,162</u>	<u>3,520,101</u>	<u>3,514,711</u>
<b>Expenditures:</b>											
General government	-	-	-	145,396	399,078	-	10,367	1,423,450	-	1,978,291	1,406,809
Education	73,733	-	(1,300)	-	14,506	-	-	-	-	86,939	1,034,380
Health services	96,858	63,706	-	-	-	-	-	-	-	160,564	191,226
Community affairs	-	-	-	-	-	-	-	-	37,114	37,114	55,666
Other	-	-	5,662	-	-	-	-	-	-	5,662	381,770
Total expenditures	<u>170,591</u>	<u>63,706</u>	<u>4,362</u>	<u>145,396</u>	<u>413,584</u>	<u>-</u>	<u>10,367</u>	<u>1,423,450</u>	<u>37,114</u>	<u>2,268,570</u>	<u>3,069,851</u>
Excess (deficiency) of revenues over (under) expenditures	704,409	48,416	(4,362)	543,104	(31,084)	-	-	-	(8,952)	1,251,531	444,860
<b>Other financing uses:</b>											
Operating transfers out	-	-	-	(499,500)	-	-	-	-	-	(499,500)	(496,125)
Excess (deficiency) of revenues over (under) expenditures and other financing uses	704,409	48,416	(4,362)	43,604	(31,084)	-	-	-	(8,952)	752,031	(51,265)
Fund balances (deficit) at beginning of year	<u>(689,327)</u>	<u>108,351</u>	<u>(77,466)</u>	<u>38,965</u>	<u>291,114</u>	<u>1,026</u>	<u>(52,149)</u>	<u>(251,998)</u>	<u>(104,636)</u>	<u>(736,120)</u>	<u>(684,855)</u>
Fund balances (deficit) at end of year	<u>\$ 15,082</u>	<u>\$ 156,767</u>	<u>\$ (81,828)</u>	<u>\$ 82,569</u>	<u>\$ 260,030</u>	<u>\$ 1,026</u>	<u>\$ (52,149)</u>	<u>\$ (251,998)</u>	<u>\$ (113,588)</u>	<u>\$ 15,911</u>	<u>\$ (736,120)</u>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**SPECIAL REVENUE FUNDS**  
Combining Statement of Revenues, Expenditures by Account and Changes in Fund Balances (Deficit)  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	Compact Special Block Grant 221(B)	Compact Health and Medical 216(A)(2)	Compact Scholarship 216(A)(3)	Compact Energy Block Grant 214	Compact Special Development 212(B)	Fishermen's Revolving	U.S. Department of the Interior	Federal Grants Assistance	Foreign Assistance	Totals	
										1998	1997
<b>Revenues:</b>											
Compact grants:											
Base amount	\$ 875,000	\$ 112,122	\$ -	\$ 450,000	\$ 250,000	\$ -	\$ -	\$ -	\$ -	\$ 1,687,122	\$ 1,820,544
Inflation adjustment	-	-	-	238,500	132,500	-	-	-	-	371,000	350,000
Federal contributions	-	-	-	-	-	-	10,367	1,423,450	-	1,433,817	1,286,205
Other	-	-	-	-	-	-	-	-	28,162	28,162	57,962
Total revenues	<u>875,000</u>	<u>112,122</u>	<u>-</u>	<u>688,500</u>	<u>382,500</u>	<u>-</u>	<u>10,367</u>	<u>1,423,450</u>	<u>28,162</u>	<u>3,520,101</u>	<u>3,514,711</u>
<b>Expenditures:</b>											
Personnel	158,162	-	-	-	-	-	-	443,561	-	601,723	1,391,002
Travel	-	23,290	-	-	85,101	-	-	271,416	1,079	380,886	281,596
POL	-	-	-	-	42,507	-	-	2,035	-	44,542	24,924
Capital outlay	-	-	-	-	-	-	-	162,252	-	162,252	28,606
Contractual services	-	-	-	-	261,486	-	2,779	145,924	1,385	411,574	-
Other	<u>12,429</u>	<u>40,416</u>	<u>4,362</u>	<u>145,396</u>	<u>24,490</u>	<u>-</u>	<u>7,588</u>	<u>398,262</u>	<u>34,650</u>	<u>667,593</u>	<u>1,343,723</u>
Total expenditures	<u>170,591</u>	<u>63,706</u>	<u>4,362</u>	<u>145,396</u>	<u>413,584</u>	<u>-</u>	<u>10,367</u>	<u>1,423,450</u>	<u>37,114</u>	<u>2,268,570</u>	<u>3,069,851</u>
Excess (deficiency) of revenues over (under) expenditures	704,409	48,416	(4,362)	543,104	(31,084)	-	-	-	(8,952)	1,251,531	444,860
<b>Other financing uses:</b>											
Operating transfers out	-	-	-	(499,500)	-	-	-	-	-	(499,500)	(496,125)
Excess (deficiency) of revenues over (under) expenditures and other financing uses	704,409	48,416	(4,362)	43,604	(31,084)	-	-	-	(8,952)	752,031	(51,265)
Fund balances (deficit) at beginning of year	<u>(689,327)</u>	<u>108,351</u>	<u>(77,466)</u>	<u>38,965</u>	<u>291,114</u>	<u>1,026</u>	<u>(52,149)</u>	<u>(251,998)</u>	<u>(104,636)</u>	<u>(736,120)</u>	<u>(684,855)</u>
Fund balances (deficit) at end of year	<u>\$ 15,082</u>	<u>\$ 156,767</u>	<u>\$ (81,828)</u>	<u>\$ 82,569</u>	<u>\$ 260,030</u>	<u>\$ 1,026</u>	<u>\$ (52,149)</u>	<u>\$ (251,998)</u>	<u>\$ (113,588)</u>	<u>\$ 15,911</u>	<u>\$ (736,120)</u>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Capital Projects Funds  
September 30, 1998

The acquisition and construction of major capital facilities, other than those financed by proprietary funds and trust funds are accounted for in Capital Projects Funds. A brief discussion of Kosrae State's Capital Projects Funds as of September 30, 1998, follows:

**Compact Capital Projects**

This fund is used to account for various capital projects funded by the Compact of Free Association with the United States, Title Two, Article 1, Section 211.

**CFSM Capital Projects**

This fund accounts for the various capital projects funded by the Congress of the Federated States of Micronesia.

**TTG - Capital Projects**

This fund accounts for various capital projects received under grant awards from the Trust Territory Government.

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**CAPITAL PROJECTS FUNDS  
Combining Balance Sheet  
September 30, 1998  
(With comparative totals as of September 30, 1997)**

	Compact Capital Projects	CFSM Capital Projects	TTG Capital Projects	Totals	
				1998	1997
<b><u>ASSETS</u></b>					
Other term deposits	\$ 827,917	\$ -	\$ -	\$ 827,917	\$ 890,049
Investments	790,573	-	-	790,573	21,754
Equity investments	2,525,247	-	-	2,525,247	1,312,268
Receivables from U.S.					
Department of the Interior	-	-	502,440	502,440	610,998
Receivables from FSM Gov't	-	1,674,996	-	1,674,996	1,784,007
General receivables, net	-	-	-	-	(13,002)
Advances	195,143	88,397	14,264	297,804	317,335
Loans receivable, net	95,000	-	-	95,000	95,000
Due from other funds	1,805,967	-	336,703	2,142,670	2,940,663
<b>Total assets</b>	<b>\$ 6,239,847</b>	<b>\$ 1,763,393</b>	<b>\$ 853,407</b>	<b>\$ 8,856,647</b>	<b>\$ 7,959,072</b>
<b><u>LIABILITIES AND FUND BALANCES (DEFICIT)</u></b>					
<b>Liabilities:</b>					
Accounts payable	\$ 236,597	\$ 8,527	\$ 113,309	\$ 358,433	\$ 569,234
Accrued payroll and others	15,237	-	5,551	20,788	4,417
Due to other funds	-	1,804,790	411,412	2,216,202	2,137,746
<b>Total liabilities</b>	<b>251,834</b>	<b>1,813,317</b>	<b>530,272</b>	<b>2,595,423</b>	<b>2,711,397</b>
<b>Fund balances (deficit):</b>					
Reserved for:					
Related assets	3,220,247	-	-	3,220,247	1,538,816
Encumbrances	2,333,351	218,984	461	2,552,796	1,944,004
Continuing appropriations	1,444,891	258,336	764,260	2,467,487	3,291,883
Unreserved	(1,010,476)	(527,244)	(441,586)	(1,979,306)	(1,527,028)
<b>Total fund balances (deficit)</b>	<b>5,988,013</b>	<b>(49,924)</b>	<b>323,135</b>	<b>6,261,224</b>	<b>5,247,675</b>
<b>Total liabilities and fund balances (deficit)</b>	<b>\$ 6,239,847</b>	<b>\$ 1,763,393</b>	<b>\$ 853,407</b>	<b>\$ 8,856,647</b>	<b>\$ 7,959,072</b>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**CAPITAL PROJECTS FUNDS**

Combining Statement of Revenues, Expenditures by Function and Changes in Fund Balances (Deficit)

Year Ended September 30, 1998

(With comparative totals for the year ended September 30, 1997)

	Compact Capital Projects	CFSM Capital Projects	TTG Capital Projects	Totals	
				1998	1997
<b>Revenues:</b>					
Compact of Free Association:					
Base amount	\$ 1,918,400	\$ -	\$ -	\$ 1,918,400	\$ 1,918,400
Inflation adjustment	1,016,752	-	-	1,016,752	959,200
U.S. Department of the					
Interior grants	-	-	227,854	227,854	538,872
FSM Nat'l Gov't Contribution	-	405,976	-	405,976	1,576,400
<b>Total revenues</b>	<b>2,935,152</b>	<b>405,976</b>	<b>227,854</b>	<b>3,568,982</b>	<b>4,992,872</b>
<b>Expenditures:</b>					
Capital projects	1,880,832	405,976	227,854	2,514,662	3,777,428
<b>Total expenditures</b>	<b>1,880,832</b>	<b>405,976</b>	<b>227,854</b>	<b>2,514,662</b>	<b>3,777,428</b>
Excess (deficiency) of revenues over (under) expenditures	1,054,320	-	-	1,054,320	1,215,444
<b>Other financing sources (uses):</b>					
Equity loss on investment	(40,771)	-	-	(40,771)	(249,766)
Operating transfers out	-	-	-	-	(579,924)
<b>Total other financing sources (uses), net</b>	<b>(40,771)</b>	<b>-</b>	<b>-</b>	<b>(40,771)</b>	<b>(829,690)</b>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	1,013,549	-	-	1,013,549	385,754
<b>Fund balances (deficit) at   beginning of year</b>	<b>4,974,464</b>	<b>(49,924)</b>	<b>323,135</b>	<b>5,247,675</b>	<b>4,861,921</b>
<b>Fund balances (deficit) at end of year</b>	<b>\$ 5,988,013</b>	<b>\$ (49,924)</b>	<b>\$ 323,135</b>	<b>\$ 6,261,224</b>	<b>\$ 5,247,675</b>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**CAPITAL PROJECTS FUNDS**

Combining Statement of Revenues, Expenditures by Account and Changes in Fund Balances (Deficit)

Year Ended September 30, 1998

(With comparative totals for the year ended September 30, 1997)

	Compact Capital Projects	CFSM Capital Projects	TTG Capital Projects	Totals	
				1998	1997
<b>Revenues:</b>					
Compact of Free Association:					
Base amount	\$ 1,918,400	\$ -	\$ -	\$ 1,918,400	\$ 1,918,400
Inflation adjustment	1,016,752	-	-	1,016,752	959,200
U.S. Department of the					
Interior grants	-	-	227,854	227,854	538,872
FSM National Gov't contribution	-	405,976	-	405,976	1,576,400
<b>Total revenues</b>	<b>2,935,152</b>	<b>405,976</b>	<b>227,854</b>	<b>3,568,982</b>	<b>4,992,872</b>
<b>Expenditures:</b>					
Personnel	254,807	163,657	-	418,464	496,350
Travel	97,350	16,095	-	113,445	47,102
POL	17,807	-	-	17,807	10,151
Capital outlay	117,301	22,770	-	140,071	206,750
Contractual services	820,984	35,692	227,854	1,084,530	-
Other	572,583	167,762	-	740,345	3,017,075
<b>Total expenditures</b>	<b>1,880,832</b>	<b>405,976</b>	<b>227,854</b>	<b>2,514,662</b>	<b>3,777,428</b>
Excess (deficiency) of revenues over (under) expenditures	1,054,320	-	-	1,054,320	1,215,444
<b>Other financing sources (uses):</b>					
Equity loss on investment	(40,771)	-	-	(40,771)	(249,766)
Operating transfer out	-	-	-	-	(579,924)
<b>Total other financing sources (uses), net</b>	<b>(40,771)</b>	<b>-</b>	<b>-</b>	<b>(40,771)</b>	<b>(829,690)</b>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	1,013,549	-	-	1,013,549	385,754
<b>Fund balances (deficit) at beginning   of year</b>	<b>4,974,464</b>	<b>(49,924)</b>	<b>323,135</b>	<b>5,247,675</b>	<b>4,861,921</b>
<b>Fund balances (deficit) at end of year</b>	<b>\$ 5,988,013</b>	<b>\$ (49,924)</b>	<b>\$ 323,135</b>	<b>\$ 6,261,224</b>	<b>\$ 5,247,675</b>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Expendable Trust Funds  
September 30, 1998

Expendable trust funds are used to account for assets held by a government unit in a trustee capacity for individuals, private organizations, or other governmental units, whose resources, including both principal and earnings, may be expended. Expendable trust funds are accounted for in essentially the same manner as governmental funds. A brief discussion of the State's Expendable Trust Funds follows:

Airport Trust Fund

This fund accounts for the airport departure fee.

Agriculture Revolving Fund

This fund accounts for the sale of agriculture feed and livestock to farmers.

Production Loan Fund

This fund accounts for low interest loans made to individuals for the purpose of economic development.

Scholarship Revolving Loan Fund

This fund accounts for low interest loans made to eligible post-secondary students.

Housing Revolving Fund

This fund accounts for low interest loans which improve housing conditions on Kosrae.

Aluminum Recycling Fund

This fund was established for the Aluminum Can Recycling Project.

Tourism Revolving Fund

This fund accounts for sales of post cards, books, handicrafts, and other tourism material.

Health Care Fund

This fund accounts for health and medical fees collected by the State to be used for purchase of medical supplies.

Sports Council Fund

This fund accounts for fees collected at the State gymnasium to be used for the purchase of sports equipment.

Early Retirement Fund

This fund accounts for the Asian Development Bank loan proceeds, retirement pay-out, and the loan repayments relating to the Early Retirement Program .

See Accompanying Independent Auditors' Report.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**EXPENDABLE TRUST FUNDS  
Combining Balance Sheet  
September 30, 1998  
(With comparative totals as of September 30, 1997)**

	Airport Trust	Production Loan	Scholarship Revolving Loan	Housing Revolving	Aluminum Recycling	Health Care Fund	Sports Council Fund	Early Retirement Program	Totals	
									1998	1997
<b><u>ASSETS</u></b>										
Cash and equivalents	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 191,860	\$ 191,860	\$ -
General receivables, net	1,334	-	-	-	-	45,000	-	-	46,334	50,006
Advances	8,660	-	-	-	-	-	-	-	8,660	(1,642)
Loans receivable, net	-	-	-	455,944	-	-	-	-	455,944	422,429
Due from other funds	148,303	1,495	-	341,927	30,918	43,134	517	75,609	641,903	418,507
Total assets	<u>\$ 158,297</u>	<u>\$ 1,495</u>	<u>\$ -</u>	<u>\$ 797,871</u>	<u>\$ 30,918</u>	<u>\$ 88,134</u>	<u>\$ 517</u>	<u>\$ 267,469</u>	<u>\$ 1,344,701</u>	<u>\$ 889,300</u>
<b><u>LIABILITIES AND FUND BALANCES</u></b>										
<b>Liabilities:</b>										
Accounts payable	\$ 4,154	\$ -	\$ 9,487	\$ 44,204	\$ -	\$ 10,101	\$ -	\$ -	\$ 67,946	\$ 2,172
Due to other funds	-	-	8,720	-	-	-	-	-	8,720	11,817
Total liabilities	<u>4,154</u>	<u>-</u>	<u>18,207</u>	<u>44,204</u>	<u>-</u>	<u>10,101</u>	<u>-</u>	<u>-</u>	<u>76,666</u>	<u>13,989</u>
<b>Fund balances:</b>										
Reserved for:										
Related assets	-	-	-	455,944	-	-	-	191,860	647,804	455,944
Encumbrances	9,252	-	-	172,696	-	31,151	100	-	213,199	196,157
Unreserved	144,891	1,495	(18,207)	125,027	30,918	46,882	417	75,609	407,032	223,210
Total fund balances	<u>154,143</u>	<u>1,495</u>	<u>(18,207)</u>	<u>753,667</u>	<u>30,918</u>	<u>78,033</u>	<u>517</u>	<u>267,469</u>	<u>1,268,035</u>	<u>875,311</u>
Total liabilities and fund balances	<u>\$ 158,297</u>	<u>\$ 1,495</u>	<u>\$ -</u>	<u>\$ 797,871</u>	<u>\$ 30,918</u>	<u>\$ 88,134</u>	<u>\$ 517</u>	<u>\$ 267,469</u>	<u>\$ 1,344,701</u>	<u>\$ 889,300</u>

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**EXPENDABLE TRUST FUNDS**  
Combining Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit)  
Year Ended September 30, 1998  
(With comparative totals for the year ended September 30, 1997)

	Airport Trust	Production Loan	Scholarship Revolving Loan	Housing Revolving	Aluminum Recycling	Health Care Fund	Sports Council Fund	Early Retirement Program	Totals	
									1998	1997
<b>Revenues:</b>										
Sales	\$ -	\$ -	\$ -	\$ -	\$ 67,371	\$ 108,813	\$ 850	\$ -	\$ 177,034	\$ 209,158
Others	82,217	-	4,287	238,761	-	-	-	1,000,000	1,325,265	314,478
<b>Total revenues</b>	<b>82,217</b>	<b>-</b>	<b>4,287</b>	<b>238,761</b>	<b>67,371</b>	<b>108,813</b>	<b>850</b>	<b>1,000,000</b>	<b>1,502,299</b>	<b>523,636</b>
<b>Expenditures:</b>										
Cost of sales	-	-	-	-	36,627	-	-	-	36,627	86,002
Others	75,693	-	1,190	164,710	-	93,497	5,327	924,391	1,264,808	402,596
<b>Total expenditures</b>	<b>75,693</b>	<b>-</b>	<b>1,190</b>	<b>164,710</b>	<b>36,627</b>	<b>93,497</b>	<b>5,327</b>	<b>924,391</b>	<b>1,301,435</b>	<b>488,598</b>
<b>Excess (deficiency) of revenues over (under) expenditures</b>	<b>6,524</b>	<b>-</b>	<b>3,097</b>	<b>74,051</b>	<b>30,744</b>	<b>15,316</b>	<b>(4,477)</b>	<b>75,609</b>	<b>200,864</b>	<b>35,038</b>
<b>Other financing sources (uses):</b>										
Operating transfer in	-	-	-	-	-	-	-	191,860	191,860	-
<b>Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses</b>	<b>6,524</b>	<b>-</b>	<b>3,097</b>	<b>74,051</b>	<b>30,744</b>	<b>15,316</b>	<b>(4,477)</b>	<b>267,469</b>	<b>392,724</b>	<b>35,038</b>
<b>Fund balances (deficit) at beginning of year</b>	<b>147,619</b>	<b>1,495</b>	<b>(21,304)</b>	<b>679,616</b>	<b>174</b>	<b>62,717</b>	<b>4,994</b>	<b>-</b>	<b>875,311</b>	<b>840,273</b>
<b>Fund balances at end of year</b>	<b>\$ 154,143</b>	<b>\$ 1,495</b>	<b>\$ (18,207)</b>	<b>\$ 753,667</b>	<b>\$ 30,918</b>	<b>\$ 78,033</b>	<b>\$ 517</b>	<b>\$ 267,469</b>	<b>\$ 1,268,035</b>	<b>\$ 875,311</b>

See Accompanying Independent Auditors' Report.

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

Honorable Rensley A. Sigrah  
Governor, State of Kosrae  
Federated States of Micronesia:

We have audited the general purpose financial statements of the State of Kosrae as of and for the year ended September 30, 1998, and have issued our report thereon dated May 4, 1999, which report was qualified due to our inability to 1) assure ourselves as to the propriety of fund balances reserved for continuing appropriations, other term deposits and advances receivable of all Governmental Fund Types; inventories of the Proprietary Fund Types; loans receivable of the Fiduciary Fund Type; accounts payable for all fund types; and fixed assets of the General Fixed Assets Account Group; and 2) examine evidence regarding the investments in Kosrae Sea Ventures, Inc., SEMO Micronesia, and Pacific Tuna Industries; 3) obtain financial statements for the Agriculture Revolving Fund, Production Loan Fund and Tourism Revolving Fund, Fiduciary Fund Type - Expendable Trust Funds; and 4) obtain financial statements of Micronesia Petroleum Company, a Component Unit - Proprietary Fund Type, and the Kosrae Community Action Program, a Component Unit - Governmental Fund Type. Except as discussed in the preceding sentence, we conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Compliance**

As part of obtaining reasonable assurance about whether State of Kosrae's general purpose financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 instances of noncompliance that are required to be reported under *Government Auditing Standards*, which are described in the accompanying Schedule of Findings and Questioned Costs (pages 68 through 90) as finding numbers 98-1 and 98-2.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the State of Kosrae's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operations of the internal control over financial reporting that, in our judgment, could adversely affect the State of Kosrae's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 98-3 through 98-20.



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

Honorable Rensley A. Sigrah  
Governor, State of Kosrae  
Federated States of Micronesia:

We have audited the general purpose financial statements of the State of Kosrae as of and for the year ended September 30, 1998, and have issued our report thereon dated May 4, 1999, which report was qualified due to our inability to 1) assure ourselves as to the propriety of fund balances reserved for continuing appropriations, other term deposits and advances receivable of all Governmental Fund Types; inventories of the Proprietary Fund Types; loans receivable of the Fiduciary Fund Type; accounts payable for all fund types; and fixed assets of the General Fixed Assets Account Group; and 2) examine evidence regarding the investments in Kosrae Sea Ventures, Inc., SEMO Micronesia, and Pacific Tuna Industries; 3) obtain financial statements for the Agriculture Revolving Fund, Production Loan Fund and Tourism Revolving Fund, Fiduciary Fund Type - Expendable Trust Funds; and 4) obtain financial statements of Micronesia Petroleum Company, a Component Unit - Proprietary Fund Type, and the Kosrae Community Action Program, a Component Unit - Governmental Fund Type. Except as discussed in the preceding sentence, we conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Compliance**

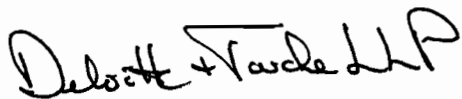
As part of obtaining reasonable assurance about whether State of Kosrae's general purpose financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material 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 instances of noncompliance that are required to be reported under *Government Auditing Standards*, which are described in the accompanying Schedule of Findings and Questioned Costs (pages 68 through 90) as finding numbers 98-1 and 98-2.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the State of Kosrae's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operations of the internal control over financial reporting that, in our judgment, could adversely affect the State of Kosrae's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 98-3 through 98-20.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 98-3, 98-4, 98-5, 98-6, 98-7, 98-8, 98-9, 98-13, 98-14 and 98-17 to be material weaknesses.

This report is intended for the information of the management of the State of Kosrae, federal awarding agencies, pass-through entities and the cognizant audit and other federal agencies. However, this report is a matter of public record and its distribution is not limited.

A handwritten signature in black ink, appearing to read "Deloitte + Touche LLP", is written in a cursive, stylized script.

May 4, 1999

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND  
INTERNAL CONTROL OVER COMPLIANCE APPLICABLE TO EACH  
MAJOR FEDERAL AWARD PROGRAM AND ON THE SCHEDULE OF  
EXPENDITURES OF FEDERAL AWARDS**

Honorable Rensley A. Sigrah  
Governor, State of Kosrae  
Federated States of Micronesia:

**Compliance**

We have audited the compliance of the State of Kosrae with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 1998. The State of Kosrae's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs (pages 68 through 90). Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the State of Kosrae's management. Our responsibility is to express an opinion on the State of Kosrae's compliance based on our audit.

We conducted our audit of compliance in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of Kosrae's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the State of Kosrae's compliance with those requirements.

As described in item 98-1 in the accompanying Schedule of Findings and Questioned Costs, the State of Kosrae did not comply with requirements regarding reporting for U.S. Department of Education TFAS Educational Grant (CFDA 84.256) and Vocational Education Grant (CFDA 84.994). Compliance with such requirements is necessary, in our opinion, for the State of Kosrae to comply with requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the State of Kosrae complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 1998.



**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND  
INTERNAL CONTROL OVER COMPLIANCE APPLICABLE TO EACH  
MAJOR FEDERAL AWARD PROGRAM AND ON THE SCHEDULE OF  
EXPENDITURES OF FEDERAL AWARDS**

Honorable Rensley A. Sigrav  
Governor, State of Kosrae  
Federated States of Micronesia:

**Compliance**

We have audited the compliance of the State of Kosrae with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 1998. The State of Kosrae's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs (pages 68 through 90). Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the State of Kosrae's management. Our responsibility is to express an opinion on the State of Kosrae's compliance based on our audit.

We conducted our audit of compliance in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of Kosrae's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the State of Kosrae's compliance with those requirements.

As described in item 98-1 in the accompanying Schedule of Findings and Questioned Costs, the State of Kosrae did not comply with requirements regarding reporting for U.S. Department of Education TFAS Educational Grant (CFDA 84.256) and Vocational Education Grant (CFDA 84.994). Compliance with such requirements is necessary, in our opinion, for the State of Kosrae to comply with requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the State of Kosrae complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 1998.

### Internal Control Over Compliance

The management of the State of Kosrae is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the State of Kosrae's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect Kosrae State's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 98-1, 98-2 and 98-6.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we believe Finding 98-6 to be a material weakness.

### Schedule of Expenditures of Federal Awards

We have audited the general purpose financial statements of the State of Kosrae as of and for the year ended September 30, 1998, and have issued our report thereon dated May 4, 1999, which report was qualified due to our inability to 1) assure ourselves as to the propriety of fund balances reserved for continuing appropriations, other term deposits and advances receivable of all Governmental Fund Types; inventories of the Proprietary Fund Types; loans receivable of the Fiduciary Fund Type; accounts payable for all fund types; and fixed assets of the General Fixed Assets Account Group; and 2) examine evidence regarding the investments in Kosrae Sea Ventures, Inc., SEMO Micronesia, and Pacific Tuna Industries; 3) obtain financial statements for the Agriculture Revolving Fund, Production Loan Fund and Tourism Revolving Fund, Fiduciary Fund Type - Expendable Trust Funds; and 4) obtain financial statements of Micronesia Petroleum Company, a Component Unit - Proprietary Fund Type, and the Kosrae Community Action Program, a Component Unit - Governmental Fund Type. Our audit was performed for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The accompanying schedule of expenditures of federal awards (pages 51 through 64) is presented for the purpose of additional analysis as required by OMB Circular A-133 and is not a required part of the general purpose financial statements. This schedule is the responsibility of the management of the State of Kosrae. Such information has been subjected to the auditing procedures applied in our audit of the general purpose financial statements and, in our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had the propriety of travel advance receivables and accounts payable of all Governmental Fund Types been determinable, is fairly stated, in all material respects when considered in relation to the general purpose financial statements taken as a whole.



This report is intended for the information of the management of the State of Kosrae, federal awarding agencies, pass-through entities and the cognizant audit and other federal agencies. However, this report is a matter of public record and its distribution is not limited.

*Deloitte Touche LLP*

May 4, 1999

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards  
U.S. Federal and Other Assistance Fund  
Year Ended September 30, 1998

Grantor Program Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
<u>U.S. Dept. of Education:</u>			
FY95 Special Education	84.027	7729	\$ 905
FY97 Special Education	84.027	3023	446,677
Total CFDA 84.027			447,582
FY96 TFAS Educational Grant	84.256	5846	53,929
FY97 TFAS Educational Grant	84.256	5847	299,678
FY98-99 TFAS Educational Grant	84.256	5848	170,864
Total CFDA 84.256			524,471
FY96 Goal 2000 Program	84.276	3012	102
FY97 Goal 2000 Program	84.276	3029	3,735
Total CFDA 84.276			3,837
Voc. Education Improvement Prog.	84.994	3938	18,575
FY98 Voc. Education PREL	84.994	3948	86,921
TCP Nutrition Program	84.994	3973	131
Total CFDA 84.994			105,627
Total U.S. Department of Education			1,081,517
<u>U.S. Dept. of Labor:</u>			
FY95 School to Work	17.249	3181	14,853
FY96 JTPA Administration	17.250	3155	(4,824)
FY96 JTPA Adult Program	17.250	3156	5,323
FY96 JTPA Youth	17.250	3157	(1,070)
FY96 JTPA Elderly	17.250	3166	60
FY97 JTPA Administration	17.250	3172	12,121
FY97 JTPA Adult Program	17.250	3173	21,939
FY97 JTPA Youth Program	17.250	3174	9,877
FY97 JTPA Participant Support	17.250	3175	968
FY97 JTPA Elderly Program	17.250	3180	13,779
FY95 JTPA Adult Program	17.250	3204	279
FY95 JTPA Elderly Program	17.250	3214	84
Total U.S. Department of Labor (CFDA #17.250)			58,536
Total U.S. Department of Labor			73,389
<u>U.S. Dept. of Agriculture:</u>			
FY97 Forestry/Seedling	10.664	3312	62
FY98 Forestry Program	10.664	3316	7,454
FY97 Fire Prevention	10.664	3412	7,984
Total U.S. Department of Agriculture (CFDA #10.664)			15,500
<u>U.S. Dept. of Health and Human Services:</u>			
FY97 Tuberculosis & AIDS	93.116	3718	5,193
FY98 Tuberculosis & AIDS	93.116	3773	6,330
Total CFDA 93.116			11,523
Balance forward			1,170,406

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
U.S. Federal and Other Assistance Fund, Continued  
Year Ended September 30, 1998

Balance forwarded			\$ 1,170,406
<b><u>U.S. Dept. of Health and Human Services, Continued</u></b>			
FY97 Family Planning	93.217	3675	667
3745 Family Planning	93.217	3676	28,795
Total CFDA 93.217			29,462
FY97 Immunization	93.268	3711	3,906
FY98 Immunization	93.268	3769	14,070
Total CFDA 93.268			17,976
FY97 Aids Prevention	93.940	3725	7,650
FY98 Aids Prevention	93.940	3789	7,673
Total CFDA 93.940			15,323
FY96 Substance Abuse	93.959	3700	15,974
FY97 Substance Abuse	93.959	3756	48,968
Total CFDA 93.959			64,942
FY97 Diabetes Program	93.988	3752	6,000
Total CFDA 93.988			6,000
FY96 MCH Program	93.994	3689	309
FY97 MCH Program	93.994	3738	38,821
Total CFDA 93.994			39,130
Total U.S. Department of Health and Human Services			184,356
<b><u>U.S. Dept. of the Interior:</u></b>			
FY95 Historic Preservation	15.904	3451	1,365
FY96 Historic Preservation	15.904	3456	28,281
FY97 Historic Preservation	15.904	3460	35,171
Total U.S. Department of Interior (CFDA #15.904)			64,817
<b><u>Federal Emergency Management Agency</u></b>			
FY98 HMGP FEMA Administration	83.519	3860	3,871
Total Federal Emergency Management Agency (CFDA #83.519)			3,871
Total federal and other assistance expenditures			\$ 1,423,450

Note: The above grants are received in a subgrantee capacity through the FSM National Government except for the TFAS grants (84.256) which are received in a direct capacity from the U.S. Department of Education and the Vocational Rehabilitation programs (CFDA #84.994) which were received through Pacific Regional Education Laboratory (PREL).

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Foreign Assistance Fund  
Year Ended September 30, 1998

Account Title	CFDA #	Kosrae Org. #	1998 Fiscal Year Expenditures
South Pacific Commission Grants:			
Kosrae Anti Substance Abuse	N/A	7315	\$ 4,006
UNICEF Grants:			
Family Food Nutrition Program	N/A	3959	4,716
Other Grants:			
Utwe Sport Equipment	N/A	3936	2,354
FY96 Walung Water Project	N/A	3937	9
FY97 Science Lab Acquisition	N/A	3939	7,715
FY97 Mooring Buoy Project	N/A	3941	3,314
Legal Resources Project	N/A	3950	15,000
			<u>28,392</u>
Total Foreign Assistance Fund			\$ <u>37,114</u>

Note: The above grants are received directly from foreign governments and private organizations.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
TTPI Capital Projects Fund  
Year Ended September 30, 1998

Grantor Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
Kosrae Okat Dock	15.875	6350	\$ 24,122
Airport Deficiency	15.875	6351	203,000
Tofol Water Treatment	15.875	6808	732
Total TTPI CIP			<u>\$ 227,854</u>

Note: The above grants are received in a subgrantee capacity through the Trust Territory of the Pacific Islands (TTPI) Government.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
CFSM Capital Projects Fund  
Year Ended September 30, 1998

Account Title	Kosrae Org. #	1998 Fiscal Year Expenditures
FY97 Gym Extension	1191	\$ 1,875
Kosrae State Court	4612	59,209
Joint Law Enforcement	4632	69,267
FY94 Broiler Project	6900	20,852
FY98 Medical Referral	9585	25,141
FY95 CFSM Education	9588	249
FY96 Road Development	9592	45,681
FY97 School Improvement	9600	48,925
FY97 Chip Seal	9610	44,108
FY97 Tourism Development	9611	13,967
Medical Supplies	9612	29,014
Senior Citizens	9613	8,733
Agriculture Research	9614	5,102
Completion Sports	9615	24,780
FY97 Poultry Nat. Project	9752	9,073
Total CFSM CIP		<u>\$ 405,976</u>

Note: The above grants are received as a result of appropriations made by the Congress of the Federated States of Micronesia.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Operations and Maintenance Grants Fund  
Year Ended September 30, 1998

Grantor Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
<u>Office of Territorial and International Affairs</u>			
FY98 Local Closeup	15.875	3550	\$ 2,260
Solid Waste Management Program	15.875	3624	1,919
Road Maintenance Management Improvement	15.875	3625	600
FY95 School Maintenance	15.875	7320	1,500
FY95 Reorg. DPW 2nd Year	15.875	7330	3,324
FY95 Jail OMIP Maintenance	15.875	7331	764
			<hr/>
Total operations and maintenance grants fund			\$ 10,367
			<hr/> <hr/>

Note: These grants are received in a subgrantee capacity through the Federated States of Micronesia National Government.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE**  
**FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association Capital Projects Fund -  
Section 211(a) Capital Account  
Year Ended September 30, 1998

Grantor Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
<u>Office of Territorial and International Affairs</u>			
Municipal Sport Facility	15.875	6100	\$ 24,385
Manpower Development Training	15.875	6210	394
Marine Park Establishment	15.875	6461	635
FY92 Medical Equipment	15.875	6468	20,390
Fisheries Development	15.875	6788	53
Municipal Office Upgrade	15.875	6797	43,631
State, CCM Extension	15.875	6816	12,188
K0005 '93 Housing Renovation	15.875	6822	580
FY93 Municipal Water System	15.875	6826	41,487
FY94 Education OMIP Matching	15.875	6841	9,257
FY94 Public Safety Matching	15.875	6842	486
FY94 Utwe Sewer System	15.875	6849	7,985
FY95 Land Acquisition	15.875	6850	11,443
FY95 Trochus Development	15.875	6853	610
FY95 OMIP Matching/Education	15.875	6855	9,002
FY95 Cadastral Program	15.875	6858	232
FY95 Utwe Office Renovation	15.875	6862	973
FY96 Road Development	15.875	6870	254
FY96 POL Bulk Plant	15.875	6871	811
FY96 Slipway	15.875	6872	203,750
FY94 Water Resource Development	15.875	6879	239,640
FY96 Agriculture Lab. Facility	15.875	6882	152
FY96 Farmers Exchange	15.875	6884	6
FY97 Manpower Development Training	15.875	6889	11,677
FY97 Agriculture Equipment	15.875	6891	11,211
FY97 Sports Facilities	15.875	6892	146
FY97 Building Maintenance	15.875	6893	32,277
FY97 Slipway	15.875	6894	800,000
Road Development	15.875	6895	299,962
FY97 Project Administration	15.875	6897	4,076
FY98 Pacific Islands Development Bank	15.875	6901	100,000
FY98 Project Administration	15.875	6902	37,841
FY98 New Classrooms	15.875	6903	60,000
FY98 Building Maintenance	15.875	6904	66,207
FY98 Manpower Development	15.875	6905	35,051
FY98 Consultancy	15.875	6906	17,605
FY98 Water Resource Development	15.875	6907	84,298
FY98 Food Processing Plant	15.875	6908	47,536
FY98 Waste Water Facility	15.875	6909	88,155
FY98 Circumferential Road & Maintenance	15.875	6910	168,855
FY98 Land S. & Drainage	15.875	6912	94,669
FY98 Land Acquisition	15.875	6913	96,573
FY98 Road Paving	15.875	6914	136,909
Subtotal			<u>2,821,392</u>

See accompanying notes to schedule of expenditures of federal awards.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association Capital Projects Fund -  
Section 211(a) Capital Account, Continued  
Year Ended September 30, 1998

Grantor Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
Balance forwarded			\$ 2,821,392
Medical Referral Housing	15.875	6915	80,202
Human Resources Development Training	15.875	6916	82,988
Mico SEMO Corporation	15.875	6916	150,000
Equity loss on investment	15.875	6918	40,771
Total Compact of Free Association Capital Projects Fund - Section 211(a) Capital Accounts			\$ 3,175,353
Balance per the general-purpose financial statements			\$ 1,880,832
FY96 slipway - investment in SEMO		6872	203,750
FY97 slipway - investment in SEMO		6894	800,000
SEMO Micronesia		6917	150,000
Investment in PIDB		N/A	100,000
Equity loss on Investment		N/A	40,771
			\$ 3,175,353

Note: These funds are made available by Title Two, Article I, Section 211 of the Compact of Free Association and are disbursed through the Office of Insular Affairs (OIA), U.S. Department of the Interior and bear CFDA No. 15.875. The FSM National Government receives all grant awards on behalf of the FSM and reallots such to the component States.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association - Section 216(a)(2)  
Health and Medical Programs  
Year Ended September 30, 1998

Grantor Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
<u>Office of Insular Affairs</u>			
Medical Referral	15.875	2499	\$ <u>63,706</u>
 Total Compact of Free Association - Section 216(a)(2)			 \$ <u><u>63,706</u></u>

Note: These funds are made available by Title Two, Article I, Section 216(a)(2) of the Compact of Free Association, and are disbursed through the Office of Insular Affairs (OIA), U.S. Department of the Interior and bear CFDA No. 15.875. The FSM National Government receives all grant awards on behalf of the FSM and reallots such to the component States.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association - Section 212(b)  
Special Development Program  
Year Ended September 30, 1998

Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
FY95 Centralized Pol.	15.875	2819	\$ 42,507
FY97 Centralized Travel	15.875	2826	85,101
FY97 Consultancy	15.875	2828	11,486
FY97 Kosrae SDA School Contribution	15.875	2829	14,506
FY98 Lelu Liberation	15.875	2851	3,250
FY98 Tafunsak Liberation	15.875	2852	2,750
FY98 Malem Liberation	15.875	2853	2,234
FY98 Utwe Liberation	15.875	2854	1,750
Civic Action Team	15.875	2855	<u>250,000</u>
Total Compact of Free Association - Section 212(b)			<u>\$ 413,584</u>

Note: These funds are made available by Title Two, Article I, Section 212(b) of the Compact of Free Association, and are disbursed through the Office of Insular Affairs (OIA), U.S. Department of the Interior and bear CFDA No. 15.875. The FSM National Government receives all grant awards on behalf of the the FSM and reallots such to the component States.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association Section 216(a)(3)  
Scholarship Program  
Year Ended September 30, 1998

Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
FY88 Scholarship Grant	15.875	2650	\$ (192,594)
FY89 Scholarship Grant	15.875	2651	61,198
FY90 Scholarship Grant	15.875	2652	103,809
FY97 Scholarship Grant	15.875	2653	30,383
FY87 Scholarship Grant	15.875	8501	(4,096)
Other	15.875	N/A	5,662
Total Compact of Free Association - Section 216(a)(3)			<u>\$ 4,362</u>

Note: These funds are made available by Title Two, Article I, Section 216(A)(3) of the Compact of Free Association, and are disbursed through the Office of Insular Affairs (OIA), U.S. Department of the Interior and bear CFDA No. 15.875. The FSM National Government receives all grant awards on behalf of the FSM and reallots such to the component States.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association Section 221(b)  
Special Block Grant Fund  
Year Ended September 30, 1998

Grantor Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
<u>Office of Insular Affairs</u>			
Health Special Block Program	15.875	2075	\$ 96,858
Education Special Block Program	15.875	2128	<u>73,733</u>
 Total Compact of Free Association - Section 221(b)			 <u>\$ 170,591</u>

Note: These funds are made available by Title Two, Article I, Section 221(b) of the Compact of Free Association, and are disbursed through the Office of Insular Affairs (OIA), U.S. Department of the Interior and bear CFDA No. 15.875. The FSM National Government receives all grant awards on behalf of the FSM and reallocates such to the component States.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association - Section 214(b)  
Energy Grant Program  
Year Ended September 30, 1998

Account Title	CFDA I.D. #	Kosrae Org. #	1998 Fiscal Year Expenditures
Power Generation	15.875	2803	\$ 499,500
Governor Utility Billing	15.875	2807	9,920
Agriculture Utility Billing	15.875	2808	6,867
Commerce and Industry Utility Billing	15.875	2809	4,338
Fisheries Utility Billing	15.875	2810	3,175
Education Utility Billing	15.875	2811	33,063
Health Utility Billing	15.875	2812	29,569
T & U Utility Billing	15.875	2813	26,753
DOJ Utility Billing	15.875	2814	8,269
DOA Utility Billinh	15.875	2815	16,161
Broadcast Utility Billing	15.875	2816	3,720
Land Commission Utility Billing	15.875	2830	900
Sports Utility Billing	15.875	2831	2,661
Total Compact of Free Association Section 214(b)			\$ <u>644,896</u>
Balance per the fund financial statements			\$ 145,396
Transfer to Kosrae Utilities Authority	15.875	2803	<u>499,500</u>
			\$ <u>644,896</u>

Note: These funds are made available by Title Two, Article I, Section 214(b) of the Compact of Free Association, and are disbursed through the Office of Insular Affairs (OIA), U.S. Department of the Interior and bear CFDA No. 15.875. The FSM National Government receives all grant awards on behalf of the FSM and reallots such to the component States.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association Section 211(a)  
Current Account Fund  
Year Ended September 30, 1998

<u>Account Title</u>	<u>Kosrae Org. #</u>	<u>CFDA LD. #</u>	<u>1998 Fiscal Year Expenditures</u>
General Fund: Current Account	Various	15.875	\$ <u>3,350,088</u>

Note: These funds are made available by Title Two, Article I, Section 211(A) of the Compact of Free Association, and are disbursed through the Office of Insular Affairs (OIA), U.S. Department of the Interior and bear CFDA No. 15.875. The FSM National Government receives all grant awards on behalf of the FSM and then reallots such to the component States.

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF KOSRAE**  
**FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards  
Year Ended September 30, 1998

(1) Scope of Review

The Kosrae State Government is a governmental entity governed by its own Constitution. All significant operations of the State are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior has been designated as the State's cognizant agency for the Single Audit.

A. Programs Subject to Single Audit

- U.S. Department of Agriculture
- U.S. Department of Education
- U.S. Department of Health and Human Services
- U.S. Department of the Interior
- U.S. Department of Labor
- U.S. Federal Emergency Management Agency

(2) Summary of Significant Accounting Policies

A. Basis of Accounting

For purposes of this report, certain accounting procedures were followed which help illustrate the expenditures of the individual programs. All expenses and capital outlays are reported as expenditures on the modified accrual basis of accounting.

B. Reporting Entity

The Kosrae State Government, for purpose of the general purpose financial statements, includes all of the funds of the primary government as defined by Governmental Accounting Standards Board (GASB) Statement 14, "The Financial Reporting Entity".

(3) Component Units

The Kosrae Utilities Authority, a component unit - proprietary fund of the State of Kosrae separately satisfies the requirements of OMB Circular A-133. The Kosrae Utilities Authority's Schedule of Expenditures of Federal Awards is as follows:

<u>Grantor Agency/Program</u>	<u>CFDA#</u>	<u>Fiscal Year 1998 Expenditures</u>
U.S. Department of the Interior: Compact of Free Association: Energy (214B)	15.875	\$ 499,500
Operations and Maintenance: OMIP-KOS-95-1, 2nd Year	15.875	41,342
OMIP-KOS-96-1, 3rd Year	15.875	<u>159,599</u>
Total expenditures		\$ <u>700,441</u>



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards  
Year Ended September 30, 1998

(3) Component Units, Continued

The Compact of Free Association programs are received from the State of Kosrae in a subrecipient capacity. The Operations and Maintenance funds are provided to Kosrae Utilities Authority in a direct recipient capacity. The aforementioned audit did not specify the existence of any questioned costs pertinent to the above expenditures. Funds passed through to the Kosrae Utilities Authority are included within the Schedule of Expenditures of Federal Awards of Kosrae State.

The Kosrae Community Action Program, a component unit-governmental fund has not separately satisfied audit requirements of OMB Circular A-133. Kosrae State is considered to have responsibility for any questioned costs that could result from Single Audits of this entity.

**STATE OF KOSRAE**  
**FEDERATED STATES OF MICRONESIA**

Schedule of Programs Selected for  
Audit In Accordance With OMB Circular A-133  
Year Ended September 30, 1998

<u>Grantor Program Title</u>	<u>CFDA No.</u>	<u>1998 Fiscal Year Expenditures</u>
<u>Major Programs</u>		
<u>U.S. Dept. of the Interior</u>		
Compact of Free Association: 211(A) Capital Account	15.875	\$ 3,175,353
<u>U.S. Department of Education</u>		
TFAS Educational Grant	84.256	524,471
Special Education Program	84.027	447,582
PREL:		
Vocational Education Grant	84.994	<u>105,627</u>
Total U.S. Federal program expenditures selected excluding Compact Section 211 (A) Current Account expenditures		\$ <u>4,253,033</u>
Total U.S. Federal program expenditures excluding Compact Section 211 (A) Current Account expenditures		\$ <u>6,134,163</u>
% of total U.S. Federal Program expenditures covered by Major Programs excluding Compact Section 211 (A) Current Account expenditures		<u>69%</u>

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs  
Year Ended September 30, 1998

**Part I - Summary of Auditors' Results**

1. The Independent Auditors' Report on the financial statements expressed a qualified opinion.
2. Reportable conditions in internal control over financial reporting were identified, some of which are considered to be material weaknesses.
3. Instances of noncompliance considered material to the financial statements were disclosed by the audit.
4. Reportable conditions in internal control over compliance with requirements applicable to major federal award programs were identified, one of which is considered to be a material weakness.
5. The independent auditors' report on compliance with requirements applicable to major federal award programs expressed a qualified opinion.
6. The audit disclosed findings required to be reported by OMB Circular A-133.
7. The State's major programs were:

<u>Name of Federal Program or Cluster</u>	<u>CFDA Number</u>
U.S. Department of the Interior - Compact of Free Association – Capital Account	15.875
U.S. Department of Education – Special Education	84.027
U.S. Department of Education - TFAS Educational Grant	84.256
U.S. Department of Education – Vocational Education Grant	84.994

8. A threshold of \$300,000 was used to distinguish between Type A and Type B programs as those terms are defined in OMB Circular A-133.
9. The State did not qualify as a low-risk auditee as that term is defined in OMB Circular A-133.

**Part II - Financial Statement Findings Section**

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>
98-3	Continuing appropriations	\$ -
98-4	Inventory	-
98-5	Loan Receivable	-
98-6	General Fixed Assets Account Group	-
98-7	Component Units	-
98-8	Expendable Trust Funds	-
98-9	Equity Investments	-
98-10	Prior Year Encumbrances	-
98-11	Authorized Budget	-
98-12	Bank Reconciliation	-
98-13	Time Certificate of Deposits	-
98-14	Travel Advances	-
98-15	Equity Investments	-

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998**

**Part II - Financial Statement Findings Section, Continued**

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>
98-16	Stale Dated Checks	\$ -
98-17	Accounts Payable	-
98-18	Payroll	-
98-19	Payroll	-
98-20	Missing Invoices	-

**Part III - Federal Award Findings and Questioned Cost Section**

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>
98-1	TFAS Educational Grant/Vocational Education	\$ -
98-2	Compact CIP Fund	58,080
98-6	Property	-

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Federal Findings

<u>Program</u>	<u>Reason for Questioned Costs</u>	<u>Questioned Costs</u>
98-1. TFAS Educational Grant- CFDA # 84.256, and Vocational Education CFDA#84.994	<p><u>Criteria:</u> Kosrae State must follow procedures to ensure compliance with applicable grantor imposed reporting requirements.</p> <p><u>Condition:</u> Required advance/reimbursement reports and performance reports were not available for inspection.</p> <p><u>Cause:</u> Personnel responsible for the above reports have not been fully trained with respect to applicable federal rules and regulations.</p> <p><u>Effect:</u> The effect of this condition is noncompliance with federal rules and regulations.</p> <p><u>Recommendation:</u> We recommend that the Department of Administration implement procedures whereby the Administrator for Finance and Budget reviews all federal activities for compliance.</p>	

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Federal Findings, Continued

<u>Program</u>	<u>Reason for Questioned Costs</u>	<u>Questioned Costs</u>															
98-2. Compact Capital Projects Fund- CFDA # 15.875	<p><u>Criteria:</u> Kosrae State should ensure that Compact Capital Account funds are expended for allowable use as set forth in the Compact treaty.</p> <p><u>Condition:</u> We were not able to determine how the sending of athletes to regional games qualifies as an allowable use of Compact Capital Account funds.</p> <table> <tr> <th><u>APV #</u></th><th><u>Org. #</u></th><th></th></tr> <tr> <td>112454</td><td>6916</td><td>\$ 1,700</td></tr> <tr> <td>112409</td><td>6916</td><td>34,020</td></tr> <tr> <td>112660</td><td>6916</td><td><u>22,360</u></td></tr> <tr> <td></td><td></td><td><u>58,080</u></td></tr> </table> <p><u>Cause:</u> Kosrae State considers sending of athletes to regional games as an allowable use.</p> <p><u>Effect:</u> The effect of this condition is potential noncompliance with the Compact treaty.</p> <p><u>Recommendation:</u> We recommend that Kosrae State ensure that expenditures comply with the Compact and its subsidiary agreements.</p>	<u>APV #</u>	<u>Org. #</u>		112454	6916	\$ 1,700	112409	6916	34,020	112660	6916	<u>22,360</u>			<u>58,080</u>	
<u>APV #</u>	<u>Org. #</u>																
112454	6916	\$ 1,700															
112409	6916	34,020															
112660	6916	<u>22,360</u>															
		<u>58,080</u>															
	Total Questioned Costs	\$ <u>58,080</u>															

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings

Continuing Appropriations

Finding No. 98-3

Criteria: Continuing appropriations should be periodically reconciled and reviewed to determine if such represent current funding priorities.

Condition: A comprehensive schedule of continuing appropriations for all funds was not available for inspection.

Cause: The cause of this condition is unknown.

Effect: The effect of this condition could lead to a misstatement of continuing appropriations.

Recommendation: We recommend that the Department of Administration ensure that a comprehensive schedule of continuing appropriations is maintained.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Inventory**

Finding No. 98-4

Criteria: The stock revolving fund inventory should be reconciled at the end of each fiscal year.

Condition: We found that the stock revolving fund ending inventory balance has not been reconciled to the physical count as of September 30, 1998.

Cause: The cause of this condition is unknown.

Effect: The effect of this condition is a potential misstatement of inventory balances.

Recommendation: We recommend that the Department of Administration ensure that the stock revolving fund is reconciled at the end of each fiscal year.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Loans Receivable**

**Finding No. 98-5**

Criteria: All government funds should be properly accounted for and reliable accounting records should be maintained to substantiate proper use of funds.

Condition: Detailed schedules of loans receivable for the expendable trust funds were not available for inspection.

Cause: The cause of this condition is necessary reconciliations have not been performed.

Effect: The effect of this condition could be a misstatement of the financial statements.

Recommendation: We recommend that the Department of Administration ensure that the loan receivables are reconciled at the end of each fiscal year.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**General Fixed Assets Account Group**

**Finding No. 98-6**

Criteria: The General Fixed Assets Account Group should be reconciled at the end of each fiscal year. Additionally, biennial inventories of fixed assets are required by the Common Rule.

Condition: Detailed schedules of fixed assets were not available for inspection. In addition, the general ledger fixed asset balances have not been updated in recent years. Additionally, biennial inventories have not been performed as required by the Common Rule.

Cause: The cause of this condition is unknown.

Effect: The effect of this condition is a potential for misstatement of the financial statements.

Recommendation: We recommend that the Department of Administration ensure that the General Fixed Assets Account Group is updated and reconciled to detailed property listings at the end of each fiscal year and the required inventories be performed.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998**

**Financial Statements Findings, Continued**

**Component Units**

**Finding No. 98-7**

**Criteria:** Kosrae State Government's general purpose financial statements should include financial statements of all component units.

**Condition:** The general purpose financial statements for Kosrae State Government do not include the Component Unit-Propriety Fund and Governmental Funds, comprised of Micronesia Petroleum Company and Kosrae Community Action Program.

**Cause:** The cause of this condition is that audited financial statements for MPC and KCAP were not available.

**Effect:** The effect of this condition results in a potential material misstatement of the financial statements.

**Recommendation:** We recommend that the Department of Administration ensure that all component units are included in the general purpose financial statements.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Expendable Trust Funds**

**Finding No. 98-8**

Criteria: All government funds should be properly accounted for and reliable accounting records should be maintained to substantiate proper use of the funds.

Condition: Financial statements for the Agriculture Revolving Fund, Production Loan Fund, and the Tourism Revolving Fund were not available.

Cause: The cause of this condition is unknown.

Effect: The effect of this condition is a potential for misstatement of the financial statements.

Recommendation: We recommend that the Department of Administration ensure that all government funds are included in the general purpose financial statements.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998**

**Financial Statements Findings, Continued**

**Equity Investments**

**Finding No. 98-9**

**Criteria:** Kosrae State Government should ensure that audited financial statements are furnished by all investees of Kosrae State Government at the end of each fiscal year.

**Condition:** Unaudited financial statements from SEMO Micronesia, and Pacific Tuna Industries were furnished in support of Kosrae State equity investments.

**Cause:** The cause of this condition is unknown.

**Effect:** The effect of this condition is a potential misstatement of the financial statements.

**Recommendation:** We recommend that the Department of Administration ensure that audited financial statements are furnished by its material investees at the end of each fiscal year.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Prior Year Encumbrances**

**Finding No. 98-10**

Criteria: Outstanding encumbrances at the end of each fiscal year are to be rolled forward into the next fiscal year.

Condition: Opening encumbrance balances for fiscal year 1998 did not agree with the ending encumbrance balances from 1997.

Cause: Department of Administration personnel failed to manually roll forward prior year encumbrances.

Effect: The effect of this condition is a misstatement of encumbrance balances.

Recommendation: We recommend that the Department of Administration ensure that the year-end roll over of financial statements balances is accurately performed.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Authorized Budget**

Finding No. 98-11

Criteria: A functioning system of internal control requires that the authorized budget per the financial statements be properly reconciled to the authorized budget at all times.

Condition: We were not able to trace budgets per the financial statements to the legislative appropriations.

Cause: There was no periodic reconciliation performed of budget balances reflected in the financial statements.

Effect: The effect of this condition is that potential unappropriated expenditures could result.

Recommendation: We recommend that the Department of Administration ensure that budget columns of the financial statements are periodically reconciled with the authorized budget.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998**

**Financial Statements Findings, Continued**

**Bank Reconciliation**

**Finding No. 98-12**

**Criteria:** The general ledger cash in bank balance should be reconciled to the actual bank balance on a monthly basis.

**Condition:** The Treasury Fund was out of balance by nearly \$21,000 as of September 30, 1998.

**Cause:** Management has not been reviewing monthly bank reconciliations for accuracy.

**Effect:** A misstatement of the financial statements could result from this condition.

**Recommendation:** We recommend that the Administrator for Division of Finance and Budget review and approve all monthly bank reconciliations for accuracy.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Time Certificate of Deposits**

**Finding No. 98-13**

Criteria: A functioning system of internal control requires that all bank transactions be recorded in the financial statements.

Condition: Management was not able to provide an analysis or reconciliation of time certificates of deposit (TCD's) to provide explanation regarding the unlocated decrease in the TCD bank balance.

Cause: Kosrae State has not performed reconciliations of its time certificates of deposit.

Effect: The effect of this condition is a potential misstatement of the financial statements.

Recommendation: We recommend that the Administrator for Division of Finance and Budget ensure that documentary evidence is available to support all movements in TCD's during the year.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Travel Advances**

**Finding No. 98-14**

Criteria: Kosrae State should maintain a travel advance subsidiary ledger to support the general ledger travel account balances.

Condition: We found that Kosrae State did not maintain detail subsidiary travel advance ledgers.

Cause: Travel advances have not been reconciled since the software application for travel advances was modified.

Effect: The effect of this condition is a potential misstatement of the financial statements.

Recommendation: We recommend that Kosrae State ensure that all travel advance subsidiary ledgers are maintained and reconciled to the general ledger.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Equity Investments**

Finding No. 98-15

Criteria: A functioning system of internal control requires periodic reconciliation of general ledger balances.

Condition: The equity investment accounts were materially misstated; i.e. purchases of additional stock in a local company were expended rather than capitalized.

Cause: Kosrae State has not performed reconciliations of its investment accounts.

Effect: The misstatements resulting from this weakness have been corrected through proposed audit adjustments.

Recommendation: We recommend that the Administrator for Division of Finance and Budget review and ensure that all material general ledger account balances are reconciled on a periodic basis.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Stale Dated Checks**

**Finding No. 98-16**

Criteria: A functioning system of internal control requires periodic review of the outstanding checklist so proper adjustments can be made to restore cash and accounts payable.

Condition: We found that \$136,034 of checks outstanding as of September 30, 1998 have been outstanding for over one year.

Cause: The outstanding checklist was not reviewed on a periodic basis.

Effect: There is no effect of this condition on the financial statements as reclassifications were proposed in the audit process to correct for this matter.

Recommendation: We recommend that Kosrae State make periodic review of the outstanding checklist for stale dated checks.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

Accounts Payable

Finding No. 98-17

Criteria: Detailed listings of accounts payable should be available to support general ledger control accounts.

Condition: Kosrae State could not provide the detail of accounts payable to support the 1998 fiscal year-end general ledger accounts payable balances.

Cause: There were no personnel assigned to reconcile accounts payable on a periodic basis.

Effect: We were unable to perform alternative procedures to mitigate the effect of this condition on the financial statements.

Recommendation: We recommend that Kosrae State ensure that the accounts payable subsidiary ledger is backed-up at the end of each fiscal year and that a hard copy is printed.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Payroll**

Finding No. 98-18

Criteria: The effective employee pay rate should be used in computing payroll.

Condition: We found one instance out of twenty-one items tested where an incorrect pay rate was used in computing payroll.

Cause: The effective employee pay rate was not updated in the payroll system.

Effect: The effect of this condition is a potential misstatement of personnel expenditure.

Recommendation: We recommend that Kosrae State ensure that the effective pay rate is used in the preparation of payroll.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998

Financial Statements Findings, Continued

**Payroll**

Finding No. 98-19

Criteria: Approved Personnel Action Forms should be maintained to support employee pay rates.

Condition: We found three instances out of twenty-one items tested where the Personnel Action Form was missing.

Cause: The above condition is attributable to inadequacies in the filing system.

Effect: The effect of this condition is a potential misstatement of the financial statements.

Recommendation: We recommend that Kosrae State ensure that the Personnel Action files are updated at all times.

**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 1998**

**Financial Statements Findings, Continued**

**Missing Invoices**

**Finding No. 98-20**

**Criteria:** All payments should be supported by underlying documentation such as vendor's invoices, etc.

**Condition:** We found one instance out of four tested where the accounts payable voucher (APV) lacked a vendor's invoice.

**Cause:** The above condition is attributable to inadequacies in the filing system.

**Effect:** The effect of this condition is a potential misstatement of the financial statements and a potential inability to substantiate the basis of certain payments.

**Recommendation:** We recommend that Kosrae State not file APVs that lack supporting documentation. These APVs should be kept in an open file until supporting documentation is located.



**STATE OF KOSRAE  
FEDERATED STATES OF MICRONESIA**

**Unresolved Prior Years' Findings and Questioned Costs  
Year Ended September 30, 1998**

The following is a summary of unresolved questioned costs of the State of Kosrae as of September 30, 1998:

	Questioned Costs Set Forth in Prior Audit Report <u>1997</u>	Questioned Costs Resolved in Fiscal Year <u>1998</u>	<u>Questioned Costs at September 30, 1998</u>
Unresolved Questioned Costs FY 96	\$ 274,360	\$ -	274,360
Unresolved Questioned Costs FY 98	<u>-</u>	<u>-</u>	<u>58,080</u>
	\$ <u><u>274,360</u></u>	\$ <u><u>-</u></u>	\$ <u><u>332,440</u></u>

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**KOSRAE STATE GOVERNMENT  
DEPARTMENT OF ADMINISTRATION  
OFFICE OF THE DIRECTOR  
P. O. BOX 878  
TOFOL, KOSRAE STATE, FM 96944**

Director Office: (691) 370-3400 /3163/3170\* Facsimile: (691) 370-2004  
Division of Planning & Statistics: (691) 370-3163/3797  
Division of Finance & Budget: (691) 370-3004/3170  
Division of Personnel & Employment Services: (691) 370-3401/2  
Division of Construction & Engineering: (691) 370-3169

October 28, 1999

Mr. Simao Iehsi  
Deloitte & Touche  
P.O. Box 753  
Kolonja, Pohnpei  
FSM 96941

Dear Mr. Iehsi

I am pleased to submit to you Kosrae State's documented responses and proposed corrective action plans for fiscal year 1998 Audit Report findings.

I appreciate very much the opportunity extended to us to meet with you, Mr. Dan Fitzgerald and the FSM Public Auditor to review the contents of the report. I would also like to thank you for allowing us to submit written comments to certain provisions and sections in the report that needed clarifications.

Attached are our responses and supportive documents relating to the questioned costs and other notes contained in the draft report submitted to our office.

Thank you again for the outstanding audit and I hope that our responses are favorably considered.

Sincerely,

A handwritten signature in dark ink, appearing to read "B. P. Abraham".

Boldon P. Abraham  
Director

Xc : Governor/ Lt. Governor, Kosrae State

**FISCAL YEAR 1998 KOSRAE STATE SINGLE AUDIT FINDINGS****FEDERAL FINDINGS**

No. 98-1 TFAS Education Grant – CFDA # 84.256 and Vocational Education-CFDA # 84.994

Criteria: Kosrae State must follow procedures to minimize the time between the transfer of funds from the US Treasury and the disbursement of those funds.

Auditee Response: We are fully aware of the 3 day disbursement requirement however, Since most of the time the general fund is used in advance for most of the federal grants expenditures, whenever the actual federal funds are available they replenish the general fund immediately.

Corrective Action Plan: We recommend deletion of this finding

No. 98-2 Compact Capital Projects Fund CFDA # 15.875

Criteria: Kosrae State should ensure that Compact Capital Account funds are expended for allowable uses as set forth in the Compact Treaty.

Auditee Response: See the attached Office of the Attorney General Opinion

Corrective Action Plan: We recommend deletion of this finding.

**FINANCIAL STATEMENT FINDINGS**

No. 98-3 Continuing Appropriations

Criteria: Continuing appropriations should be periodically reconciled and reviewed to determine if such represent current funding priorities.

Auditee Response: There has recently been initiated by the Department of Administration & Finance, under new administration, a project to identify all of the continuing appropriations so that the funds remaining in those continuing appropriations will be available for future appropriations. It is our belief that the funds are not over appropriated.

Corrective Action Plan: Once the continuing appropriations are identified, the Attorney General's Office will assist the Department of Administration & Finance to request the termination of these continuing appropriations from the legislature, thereby releasing any unused funds.

No. 98-4 Inventory

Criteria: The stock revolving fund inventory should be reconciled at the end of each fiscal year.

Auditee Response: We agreed to this finding. This is due to the lack of a control mechanism that can effectively keep track of stock revolving fund reconciliation.

Corrective Action Plan: The new financial management system currently installed at finance office should improve all reconciliation efforts.

No. 98-5 Loans Receivables

Criteria: All government funds should be properly accounted for and reliable accounting records should be maintained to substantiate proper use of funds. Detailed schedules of loan receivable for the expendable trust funds were not available for inspections.

Auditee Response: We agreed to this finding.

Corrective Action Plan: A new financial management system, currently installed at finance office should resolve this.

No. 98-6            General Fixed Assets Accounts Group

Criteria: The General Fixed Assets Account Group should be reconciled at the end of each fiscal year.

Auditee Response: The problem we have on this matter is that we do not have a system to account for the GFAG. Our fixed assets inventory is done manually.

Corrective Action Plan: The new financial management system will be able to account for the GFAG properly. A computer program has been identified also for the supply Office to do recording and inventory on-line. This will be installed soon.

No. 98-7            Component Units

Criteria: Kosrae State Government's general purpose financial statements should include financial statements of all component units.

Auditee Response: We agreed to this finding. As required by law, these Component Unit-Propriety Fund's and Government Funds' financial statements should be submitted to the Governor.

Corrective Action Plan: The Department of Administration & Finance, through the Governor's Office, will ensure that all the required statements are submitted as required in a timely manner.

No. 98-8            Expendable Trust Funds

Criteria: All government funds should be properly accounted for and reliable accounting records should be maintained to substantiate proper use of the funds.

Auditee Response: We will ensure that required financial statements for these funds are submitted to ensure accountability.

Corrective Action Plan: The Department of Administration & Finance will ensure, through a new financial management regulation, which is under legal review, that all required financial statements for the expendable trust funds are submitted on a regular basis.

No. 98-9            Equity Investments

Criteria: Kosrae State Government should ensure that audited financial statements are furnished by all investees of Kosrae State Government at the end of each fiscal year.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Department of Administration & Finance will ensure that all audited financial statements in support of Kosrae State Equity Investments are submitted at the end of each fiscal year.

No. 98-10      Prior Year Encumbrances

Criteria: Outstanding encumbrances at the end of each fiscal year are to be rolled forward into the next fiscal year.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Department of Administration & Finance will ensure that year-end-roll over of financial statements balances are accurately performed.

No. 98-11      Authorized Budget

Criteria: A functioning system of internal control requires that the authorized budget per the financial statements (132P) be properly reconciled to the authorized budget at all times.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Finance Office will ensure that monthly expenditure reports (132P) are printed and provided to the Budget Office for reconciliation purposes. Also a new workstation will be installed at the Budget Office by the end of the year for direct access to the financial statements.

No. 98-12      Bank Reconciliation

Criteria: The general ledger cash in bank balance should be reconciled to the actual bank balance on a monthly basis.

Auditee Response: We agreed to this finding.

Corrective Action Plan: A staff of the Finance Office will soon be assigned to bank reconciliation on a full time basis.

No. 98-13      Time Certificate of Deposits (TCDs)

Criteria: A functioning system of internal control requires that all bank transactions be recorded in the financial statements.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Administrator of Finance & Budget will ensure that documentary evidence is available to support movements in TCDs during the year.

No. 98-14 Travel Advances

Criteria: Kosrae State should maintain a travel advance subsidiary ledger to support the general ledger travel account balances.

Auditee Response: We agreed to this finding.

Corrective Action Plan: Effective immediately the Department of Administration & Finance will resume travel advances reconciliation and ensure that all travel advance subsidiary ledgers are properly maintained.

No. 98-15 Equity Investments

Criteria: A functioning system of internal control requires periodic reconciliation of general ledger balances.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Division of Finance & Budget will review and ensure that all material general account balances are reconciled on a periodic basis.

No. 98-16 State Dated Checks

Criteria: A functioning system of internal control requires periodic review of the outstanding checklist so proper adjustments can be made to restore cash and accounts payable.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Department of Administration & Finance will ensure that periodic review of the outstanding checklist is done by assigning a staff specifically for this purpose.

No. 98-17 Accounts Payable

Criteria: Detailed listings of accounts payable should be available to support general ledger control accounts.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Department of Administration & Finance will ensure that a staff is assigned to accounts payable reconciliation on a full time basis.

No. 98-18 & 19 Payroll

Criteria: The effective employee pay rate should be used in computing payroll and personnel action forms should be maintained to support employee pay rate.

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Auditee Response: This is a result of recent changes in the pay scale legislation. Adjustments were made by the Payroll Officer to reflect current law and Personnel Actions were initiated at the department levels at later dates.

Corrective Action Plan: We recommend deletion of this finding.

No. 98-20 Missing Invoices

Criteria: All payments should be supported by underlying documentation such as vendor's invoice, etc.

Auditee Response: We agreed to this finding.

Corrective Action Plan: The Department of Administration & Finance will immediately ensure that proper documentation are properly maintained.

LOCAL FINDINGS

No. 98L-1 Compact Energy Funds

Criteria: Kosrae State should ensure that it complies with the intent of the Compact treaty.

Auditee Response: We have been informed by the National Government Attorney General's Office, through a legal opinion, that the Compact Energy funds can be used for operational purposes, such as utility bills.

Corrective Action Plan: We recommend deletion of this finding.

No. 98L-2 Local Laws and Regulations

Criteria: Kosrae State should ensure that it complies with local laws and regulations.

Auditee Response: The Legislature did approve the pledge through legislative resolution.

Corrective Action Plan: We recommend deletion of this finding.