

**POHNPEI STATE HOUSING AUTHORITY**

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**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT**

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**YEAR ENDED SEPTEMBER 30, 2000**

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## INDEPENDENT AUDITORS' REPORT

Board of Directors  
Pohnpei State Housing Authority:

We have audited the accompanying balance sheet of the Pohnpei State Housing Authority (the Authority), a component unit of the State of Pohnpei, as of September 30, 2000, and the related statements of revenues, expenses and changes in fund equity and cash flows for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Authority as of September 30, 2000, and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 4, 2001, on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

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October 4, 2001

# POHNPEI STATE HOUSING AUTHORITY

Balance Sheet  
September 30, 2000

## ASSETS

|                                      |                     |
|--------------------------------------|---------------------|
| Cash                                 | \$ 145,237          |
| Advances                             | 26,218              |
| Due from primary government (note 2) | 85,830              |
| Loans receivable, net (note 3)       | 3,667,865           |
| Inventory                            | 1,969               |
| Property and equipment, net (note 4) | <u>47,791</u>       |
|                                      | <u>\$ 3,974,910</u> |

## LIABILITIES AND FUND EQUITY

|   |                     |
|---|---------------------|
| Liabilities:                                  |                     |
| Accounts payable                              | \$ 19,774           |
| Accrued liabilities                           | <u>830</u>          |
| Total liabilities                             | <u>20,604</u>       |
| Fund equity:                                  |                     |
| Contributed capital                           | 3,999,915           |
| Deficit                                       | <u>(45,609)</u>     |
| Total fund equity                             | <u>3,954,306</u>    |
| Commitments and contingencies (notes 5 and 6) |                     |
|   | <u>\$ 3,974,910</u> |

See accompanying notes to financial statements.

## POHNPEI STATE HOUSING AUTHORITY

### Statement of Revenues, Expenses and Changes in Fund Equity Year Ended September 30, 2000

|   |                            |
|---|----------------------------|
| Operating revenues:                       |                            |
| Interest and fees on loans                | \$ <u>245,857</u>          |
| Operating expenses:                       |                            |
| Bad debts                                 | 255,523                    |
| Salaries                                  | 104,168                    |
| Contractual services                      | 20,659                     |
| Supplies and materials                    | 5,630                      |
| Repairs and maintenance                   | 4,302                      |
| Utilities                                 | 1,444                      |
| Miscellaneous and others                  | <u>11,195</u>              |
| Total operating expenses                  | <u>402,921</u>             |
| Operating loss                            | <u>(157,064)</u>           |
| Nonoperating revenues:                    |                            |
| Operating subsidy from primary government | 126,931                    |
| Interest income and others                | <u>3,119</u>               |
| Total nonoperating revenues               | <u>130,050</u>             |
| Net loss                                  | (27,014)                   |
| Deficit at beginning of year              | <u>(18,595)</u>            |
| Deficit at end of year                    | <u>(45,609)</u>            |
| Contributed capital at beginning of year  | 3,999,915                  |
| Capital contributions                     | <u>-</u>                   |
| Contributed capital at end of year        | <u>3,999,915</u>           |
| Fund equity at end of year                | \$ <u><u>3,954,306</u></u> |

See accompanying notes to financial statements.

# POHNPEI STATE HOUSING AUTHORITY

## Statement of Cash Flows Year Ended September 30, 2000

|   |                          |
|---|--------------------------|
| Cash flows from operating activities:   |                          |
| Operating loss  | \$ (157,064)             |
| Adjustments to reconcile operating loss to net cash used in operating activities: |                          |
| Bad debt expense  | 255,523                  |
| (Increase) decrease in assets:  |                          |
| Advances  | (10,545)                 |
| Loans receivable  | (288,277)                |
| Inventory   | 25                       |
| Increase in liabilities:  |                          |
| Accounts payable  | <u>3,631</u>             |
| Net cash used in operating activities   | <u>(196,707)</u>         |
| Cash flows from capital and related activities:                                   |                          |
| Acquisition of fixed assets   | <u>(22,656)</u>          |
| Cash flows from noncapital activities:  |                          |
| Operating subsidy from primary government   | <u>169,542</u>           |
| Cash flows from investing activities:   |                          |
| Interest income and others  | <u>3,119</u>             |
| Net decrease in cash  | (46,702)                 |
| Cash at beginning of year   | <u>191,939</u>           |
| Cash at end of year   | <u><u>\$ 145,237</u></u> |

See accompanying notes to financial statements.

# POHNPEI STATE HOUSING AUTHORITY

Notes to Financial Statements  
September 30, 2000

## (1) Summary of Significant Accounting Policies

### A. Reporting Entity

The Pohnpei State Housing Authority (the Authority) was established in 1988 by Pohnpei State Public Law 2L-81-88. The purpose of the Authority is to facilitate, through low-interest loans, the construction of safe and sanitary residential housing for low income families of Pohnpei State. Additionally, the Authority monitors Housing Preservation Grant (HPG) loan funds extended by the United States Department of Agriculture through the Rural Services.

The affairs of the Authority are managed by a five-member Board of Directors, consisting of representatives of the Pohnpei State Government appointed by the Governor to four-year terms. Daily operation of the Authority is delegated to an executive director, who is also appointed by the Governor and serves at the pleasure of the Board.

The Authority is a component unit (a discretely presented proprietary fund) of the Pohnpei State Government. The financial statements in this report do not represent the financial position, results of operations or cash flows of the State of Pohnpei as a whole.

### B. Fund Structure, Measurement Focus, and Basis of Accounting

The accounts of the Authority are organized as a proprietary fund type of the Pohnpei State Government. Proprietary fund types are used by governmental units to account for operations that are financed and operated in a manner similar to private business enterprises. The purpose of a proprietary fund type is to provide periodic determination of revenues, expenses and net income, with maintenance of capital. Proprietary fund types are accounted for on a flow of economic resources measurement focus, whereby all assets and liabilities associated with the operations of the funds are included on the balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital and retained earnings components. Operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

Basis of accounting refers to when revenues and expenses are recorded in the accounts and reported in the financial statements. The Authority uses the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when cash is received or payment is made.

### C. Budget

The Authority operates on an annual budget appropriated by the Legislature which is accounted for by the Pohnpei State Department of Treasury. Appropriation Acts require that funds be administered in accordance with the provisions of the Financial Management Act. The enabling legislation does provide the Authority the power to expend revenues generated by projects maintained by the Authority. Such expenditures must, however, be in accordance with the provisions of the Financial Management Act and other applicable laws and regulations.

### D. Cash

For the purposes of the balance sheet and statement of cash flows, cash is defined as cash in checking accounts, savings accounts and cash on hand. Of this amount, \$104,585 is insured through the FDIC, with the remaining balance exceeding insurable limits. The Authority does not require collateralization of its deposits by its banks. Therefore, the amounts which exceed the FDIC insurable limits are characterized as uncollateralized.

# POHNPEI STATE HOUSING AUTHORITY

Notes to Financial Statements  
September 30, 2000

## (1) Summary of Significant Accounting Policies, Continued

### E. Inventory

Inventory is stated at the lower of cost or market using the first-in, first-out (FIFO) costing method.

### F. Depreciation

Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the respective assets. Lives of property and equipment range from three to ten years.

### G. Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefit accrues to employees. No liability is recorded for nonvesting accumulating rights to receive sick leave pay benefits. The related sick leave pay expense is recorded when the benefit is actually taken.

### H. Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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) Due From Primary Government

Due from primary government represents the accumulation of the unobligated portion of the State's annual operating subsidy, which under the Authority's enabling legislation (Pohnpei State Public Law 5-37) is to be transferred to the Authority's loan fund.

## (3) Loans Receivable

The Authority's loan portfolio is comprised of two loan funds, Pohnpei State Housing Authority (PSHA) loan fund and the Housing Preservation Grant (HPG) loan fund.

**POHNPEI STATE HOUSING AUTHORITY**

Notes to Financial Statements  
September 30, 2000

(3) Loans Receivable, Continued

The PSHA loans derive from the capital contributions of Compact of Free Association Capital Account Funds - Capital Projects by Pohnpei State to fund the Housing Development Loan Fund. The HPG loans are from a grant extended by the United States Department of Agriculture through the Rural Services Office. Loans are stated at face value, net of an allowance for loan losses. The allowance represents an amount which, in management's judgment, will be adequate to absorb possible losses on existing loans that may become uncollectible. Management's judgment in determining the adequacy of the allowance is based on evaluations of the collectibility of loans. A summary of loans receivable as of September 30, 2000, is presented below:

|                                |                     |
|--------------------------------|---------------------|
| PSHA Loans                     | \$ 5,047,296        |
| HPG Loans                      | <u>364,947</u>      |
|                                | 5,412,243           |
| Less allowance for loan losses | (1,744,378)         |
| Loans receivable, net          | \$ <u>3,667,865</u> |

Future maturities of loans receivable, due to existing nonrepayment causes, will not represent predictive information and therefore, such is not presented.

(4) Property and Equipment

A summary of the Authority's property and equipment at September 30, 2000, is as follows:

|                               | <u>Estimated<br/>Useful Life</u> |                  |
|-------------------------------|----------------------------------|------------------|
| Building                      | 10 years                         | \$ 27,271        |
| Machinery and equipment       | 3-5 years                        | <u>104,614</u>   |
|                               |                                  | 131,885          |
| Less accumulated depreciation |                                  | <u>(84,094)</u>  |
| Property and equipment, net   |                                  | \$ <u>47,791</u> |

(5) Commitments and Contingencies

Loan Commitments

The Authority has loan commitments to borrowers aggregating \$215,638 as of September 30, 2000. These loan commitments represent the remaining balances of approved loans for borrower housing projects.

Federal Program Questioned Costs

The Authority is a subrecipient of U.S. Federally assisted programs subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Currently, \$184,842 in questioned costs exist for fiscal year 1993 through 2000 grants. If these questioned costs are ultimately disallowed, the Authority may bear responsibility for absorbing the amount disallowed. No provision for any liability that may result from this matter has been recorded in the accompanying financial statements.

# POHNPEI STATE HOUSING AUTHORITY

Notes to Financial Statements  
September 30, 2000

## (6) Risk Management

The Authority carries life insurance. The Authority is substantially self-insured for all other risks. Management is of the opinion that no material losses have been sustained as a result of this practice.



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

Board of Directors  
Pohnpei State Housing Authority:

We have audited the financial statements of the Pohnpei State Housing Authority (the Authority), as of and for the year ended September 30, 2000, and have issued our report thereon dated October 4, 2001. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Compliance**

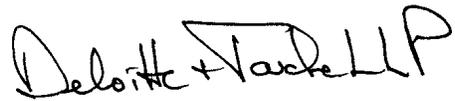
As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on 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 16 to 27) as items 2000-02, 2000-05, 2000-07 and 2000-11.

**Internal Control Over Financial Reporting**

In planning the audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the 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 operation of the internal control over financial reporting that, in our judgment, could adversely affect the Authority's ability to record, process, summarize and report financial data consistent with assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 2000-1 through 2000-12.

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 2000-02, 2000-05, 2000-06, 2000-07, 2000-08 and 2000-09 to be material weaknesses.

This report is intended for the information of the Pohnpei State Housing Authority, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

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October 4, 2001



**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**

Board of Directors  
Pohnpei State Housing Authority:

Compliance

We have audited the compliance of Pohnpei State Housing Authority (the Authority) 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, 2000. The Authority's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (page 13). Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Authority's management. Our responsibility is to express an opinion on the Authority's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Authority'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 Authority's compliance with those requirements.

As described in findings 2000-5 through 2000-8 in the accompanying Schedule of Findings and Questioned Costs, the Authority did not comply with requirements regarding special terms and conditions applicable to its federally funded loan program that are applicable to its major federal programs. Compliance with such requirements is necessary, in our opinion, for the Authority to comply with requirements applicable to its one major federal program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Authority complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended September 30, 2000.

### Internal Control Over Compliance

The management of the Authority 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 Authority'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.

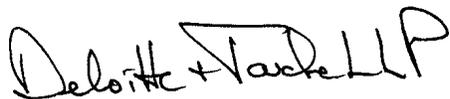
We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Authority'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 2000-05, 2000-06, 2000-07 and 2000-08.

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, we believe all of the reportable conditions described above are considered to be material weaknesses.

### Schedule of Expenditures of Federal Awards

We have audited the financial statements of the Pohnpei State Housing Authority (the Authority), as of and for the year ended September 30, 2000, and have issued our report thereon dated October 4, 2001. Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying schedule of expenditures of federal awards (page 12) is presented for the purpose of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. This schedule is the responsibility of the management of the Authority. Such information has been subjected to the auditing procedures applied in our audit of the financial statements and, in our opinion, is fairly stated, in all material respects when considered in relation to the financial statements taken as a whole.

This report is intended for the information of the management of the Pohnpei State Housing Authority, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

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October 4, 2001

## POHNPEI STATE HOUSING AUTHORITY

### Schedule of Expenditures of Federal Awards Year Ended September 30, 2000

| <u>Grant Title</u>   | <u>Grantor Agency</u>                    | <u>CFDA No.</u> | <u>Amount</u>       |
|--|--|-----------------|---------------------|
| Compact of Free Association:<br>Capital Accounts Funds -<br>Capital Projects,<br>Section 211 (A) | U.S. Department of<br>the Interior – OIA | 15.875          | \$ <u>5,047,296</u> |
| Rural Services:<br>Housing Preservation Grant  | U.S. Department of<br>Agriculture        | 10.433          | \$ <u>364,947</u>   |

Note: The Compact of Free Association funds are disbursed through the U.S. Department of the Interior (DOI), Office of Insular Affairs (OIA), to the FSM National Government which reallots such to the component States. Pohnpei State subsequently passed certain of these funds through the Pohnpei State Housing Authority. The Housing Preservation Grant Funds are received in a subgrantee capacity through the Rural Services to the Pohnpei State Government.

The Schedule of Expenditures of Federal Awards is prepared on the accrual basis of accounting.

# POHNPEI STATE HOUSING AUTHORITY

## Schedule of Findings and Questioned Costs Year Ended September 30, 2000

### Part I - Summary of Auditors' Results

1. The Independent Auditors' Report on the financial statements expressed an unqualified 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 awards programs were identified.
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 Organization's major programs were:

| <u>Name of Federal Program</u> | <u>CFDA Number</u> |
|--------------------------------|--------------------|
| Housing Preservation Grant     | 10.433             |
| Compact of Free Association    | 15.875             |

8. The U.S. Department of Agriculture program which is administered by the Authority, is considered as Type B program, as defined in OMB Circular A-133.
9. The Authority 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> |
|-------------------------|---|-------------------------|
| 2000-01                 | Segregation of Duties                                 | \$ -                    |
| 2000-02                 | Employee Advances                                     | \$ -                    |
| 2000-03                 | Payment Support                                       | \$ -                    |
| 2000-04                 | Fixed Assets  | \$ -                    |
| 2000-05                 | Board of Director Minutes                             | \$ -                    |
| 2000-06                 | Loan Enforcement and the Allowance for<br>Loan Losses | \$ -                    |
| 2000-07                 | Compliance with Loan Rules and Regulations            | \$ -                    |
| 2000-08                 | Loan File Documentation                               | \$ -                    |
| 2000-09                 | Interest Accruals on Delinquent Loans                 | \$ -                    |
| 2000-10                 | Recorded Appropriations Receivable                    | \$ -                    |
| 2000-11                 | Contract Employee Payrolls                            | \$ -                    |
| 2000-12                 | Voided Cash Receipts                                  | \$ -                    |
| 2000-13                 | Transfer of Loan Funds to Operations                  | \$ -                    |

**POHNPEI STATE HOUSING AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

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

| <u>Reference Number</u> | <u>Findings</u>                                       | <u>Questioned Costs</u> |
|-------------------------|---|-------------------------|
| 2000-05                 | Board of Director Minutes                             | \$ -                    |
| 2000-06                 | Loan Enforcement and the Allowance for<br>Loan Losses | \$ -                    |
| 2000-07                 | Compliance with Loan Rules and Regulations            | \$ -                    |
| 2000-08                 | Loan File Documentation                               | \$ -                    |

## **POHNPEI STATE HOUSING AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

### **GENERAL COMMENTS**

The Pohnpei State Housing Authority (the Authority) utilizes a manual accounting system that does not appear to have changed in recent years and also appears to be inadequate for the Authority's requirements. For example, due to inadequate accounting systems, loan principal balances contain both principal and unpaid interest. Statements are rarely provided borrowers and interest continues to be accrued, even if the balance is seriously delinquent.

Additionally, loan enforcement procedures appear virtually non-existent. It does not appear as if loan foreclosures occur, a policy that may contravene federal requirements attendant to the federal loan program. Additionally, the non-enforcement of loan criteria and repayment appear to have a negative effect on the Authority's cash flows. Management of the Authority is tasked with forming an allowance for doubtful accounts in the financial statements. Given the lack of enforcement, it appears that the loan reserve should be evaluated by management and increased in line with delinquent accounts. Management has not addressed this matter and has left the allowance to be an audit consideration.

Given the lack of improvement in the Authority's accounting, we recommend consideration of acquiring adequate loan software or contracting with a financial institution to properly maintain the loan portfolio.

We additionally recommend that the Board of Directors review existing policy with respect to loan limits, loan documents required and loan enforcement and determine if existing policies should be modified, since frequent noncompliance has occurred with these policies in the past.

**POHNPEI STATE HOUSING AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

Segregation of Duties

Finding No. 2000-01

Criteria: Adequate segregation of duties should exist to protect the Authority from the risk of fraud.

Condition: No member of management is tasked with reviewing the work of the two accountants in the areas of collection, recording and banking cash.

Cause: The cause of this condition appears to be inadequate definition of duties.

Effect: There is no known effect on the financial statements as a direct result of this condition.

Recommendation: Given the current state of the accounting records, the lack of timely reconciliation and other matters that are noted hereafter, we recommend that management ensure that this issue is addressed.

## POHNPEI STATE HOUSING AUTHORITY

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2000

#### Employee Advances

##### Finding No. 2000-02

**Criteria:** Employee advances are not allowed per Section 4.3 of the Pohnpei State Financial Management Regulations.

**Condition:** Despite repeated audit findings in prior years citing noncompliance with the criteria, employee advances increased almost \$10,000 during the year (from approximately \$15,000 to \$25,000).

**Cause:** The cause of this condition is apparent disregard for the aforementioned regulations and prior year audit findings.

**Effect:** The effect of this condition is that as advances are increasing, the ability of employees to repay the advances becomes questionable. This point is especially of concern as it appears that some employee housing loan balances continue to increase due to non-repayments.

**Recommendation:** We recommend that the Board of Directors either petition the Pohnpei State Legislature for exemption from the aforementioned regulations or comply with such requirements. Additionally, we recommend that the Board of Directors determine the reason for employee non-repayment of advances and loans.

## POHNPEI STATE HOUSING AUTHORITY

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

### Payment Support

#### Finding No. 2000-03

Criteria: Payments should be adequately supported by authoritative documents.

Condition: Two payments (check numbers 2292 and 2333) did not contain adequate authoritative documents to support the basis of the payment.

Additionally, for three loan disbursements (6879, 6911 and 6998), the supporting contracts could not be located.

Cause: The cause of this condition appears to be due to inadequate filing procedures employed by the Authority.

Effect: The effect of this condition is that documentation underlying the financial statements may not exist. Additionally, improper payments may be made without ensuring the adequacy of underlying support.

Recommendation: All disbursements should be adequately supported.

## POHNPEI STATE HOUSING AUTHORITY

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2000

#### Fixed Assets

##### Finding No. 2000-04

Criteria: Detail lists of Authority's fixed assets should be maintained and depreciation recognized on the assets in accordance with accounting principles generally accepted in the United States of America.

Condition: The Authority does not possess a detailed list of fixed assets owned and did not record any depreciation expense during the year ended September 30, 2000.

Cause: The cause of this condition appears to be inadequacies in the Authority's accounting records.

Effect: The effect of this condition is that fixed assets and expenses could be immaterially misstated in the financial statements.

Recommendation: A detailed list of fixed assets should be maintained that reconciles with the general ledger balance and depreciation should be calculated and recorded at least annually.

## POHNPEI STATE HOUSING AUTHORITY

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2000

#### Board of Director Minutes

#### Finding No. 2000-05

Criteria: Minutes of Board meetings should be maintained to document policy directives, important matters deliberated and important decisions made.

Condition: As in the prior year, the Authority did not maintain minutes of its Board meetings during the year ended September 30, 2000.

Cause: The cause of this condition appears to be that the Board has not enforced the necessity of maintaining Board of Director minutes.

Effect: It is not possible to ascertain the effect of this matter on the financial statements.

Recommendation: The Board should ensure that minutes of its meetings are maintained.

## POHNPEI STATE HOUSING AUTHORITY

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

### Loan Enforcement and the Allowance for Loan Loss Reserves (ALL)

#### Finding No. 2000-06

Criteria: A critical management representation is the adequacy of the ALL. A major assumption in forming the ALL is that management will enforce existing policy and that it will attempt to protect the Authority's assets and ensure repayment of outstanding loans.

Condition: Management has not determined the adequacy of its ALL and has not taken steps to protect its assets by enforcing collection of outstanding loans.

Cause: The cause of this condition appears to be the lack of management involvement in the financial statements and the lack of loan collections.

Effect: The effect of this condition is reduced cash flow available to fund additional loans and a steadily increasing loan loss reserve.

Recommendation: Management should ensure compliance with loan agreements and should ensure that the ALL is reflective of the present value of expected loan collections.

**POHNPEI STATE HOUSING AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

Compliance with Loan Rules and Regulations

Finding No. 2000-07

Criteria: Loans granted should comply with stated policies and procedures.

Condition: Of thirty-two loans granted during the year ended September 30, 2000, the following was noted:

- We were unable to review Board approval of loans due to an absence of Board minutes.
- For nine borrowers, we were unable to ensure that loan amounts and/or terms complied with applicable Authority rules and regulations.
- For fifteen borrowers, no evidence of income verification could be provided.
- For one borrower, the loan term exceeded the lease term on the underlying real estate.
- For four borrowers, loan documents were signed but were not fully completed.
- For eight borrowers, mandatory loan documents are not on file.
- For two loans, loan agreements and promissory notes were not signed by the Executive Director.
- Two loan files could not be found.
- For three loans, the maximum allowed loan balance of \$35,000 was exceeded.

Cause: As in prior years, the above condition results from noncompliance with established Authority requirements.

Effect: The effect of this condition is that if the Authority ever attempts loan foreclosure, the Authority's efforts will be impeded due to inadequate loan documents.

Recommendation: Compliance with stated policies and procedures should occur.

**POHNPEI STATE HOUSING AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

Loan File Documentation

Finding No. 2000-08

Criteria: Loan files should contain properly executed documents that allow the Authority to foreclose on delinquent loans.

Condition: Out of 135 loan files reviewed, we noted the following:

- The loan files for eight borrowers could not be located.
- For eleven loans, we could not agree the loan balances per the subsidiary ledger to the loan documents. Further analysis indicated that the Authority adds loan principal and interest over the term of the loan and states that total on the loan documents.
- For eight borrowers, the loan documents were signed but were not fully completed.

Cause: The cause of this condition is that the Authority's filing and loan documentation procedures appear inadequate.

Effect: The effect of this condition is that the Authority may not possess adequate documentation to allow for foreclosure in the event that such is attempted.

Recommendation: The Authority should ensure that its loan documents are properly executed and filed.

## POHNPEI STATE HOUSING AUTHORITY

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

### Interest Accruals on Delinquent Loans

#### Finding No. 2000-09

Criteria: Accounting principles generally accepted in the United States of America (GAAP) require that interest accruals cease when a loan is impaired and may be uncollectible. All collections should be initially applied against principal and only then may the interest income be recognized in the financial statements.

Condition: The Authority's policy contravenes the criteria.

Cause: The cause of this condition appears to be an accounting system that is inadequate for the Authority's needs.

Effect: The effect of this condition is that the Authority is recognizing interest income that it will not actually collect.

Recommendation: The Authority should recognize interest income in accordance with GAAP.

**POHNPEI STATE HOUSING AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

Recorded Appropriations Receivable

Finding No. 2000-10

Criteria: Receivables should be recorded at their net realizable value.

Condition: Receivables are recorded for operating appropriations that were not received in prior years.

Cause: The cause of this condition appears to be that the Authority believes that such will ultimately be collected.

Effect: The effect of this condition is that the stated receivables from the General Fund may be uncollectible.

Recommendation: We recommend that the Authority determine the collectibility of the amount and make appropriate adjustment in the financial statements, if required.

## POHNPEI STATE HOUSING AUTHORITY

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

### Contract Employee Payrolls

#### Finding No. 2000-11

Criteria: Payroll should be processed in a correct manner.

Condition: The Authority processes and disburses payroll for its contract employees. Payrolls of non-contract employees is processed by the State Finance Office. The following matters were noted during the audit:

- a. One individual was paid at a rate of \$4 per hour but the approved contract specified \$3.60.
- b. One personnel file could not be located.
- c. Social security taxes were not withheld from one employee's pay check.
- d. No detail of sick leave and annual leave for contract employees could be produced.

Cause: The cause of this condition appears to be inadequacies in the Authority's accounting system.

Effect: The effect of this condition is incorrect payments of payroll, incorrect payments of sick and annual leave, and incorrect withholdings.

Recommendation: All payroll should be processed by the State Finance Office.

**POHNPEI STATE HOUSING AUTHORITY**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2000

Voided Cash Receipts

Finding No. 2000-12

Criteria: If a cash receipt is marked as voided, the original copy should be maintained to substantiate the propriety of the transaction.

Condition: Of twenty-five cash receipts tested, receipt no. 11439 was annotated as being voided. However, the original receipt could not be produced.

Cause: The cause of this condition is a lack of internal controls.

Effect: The effect of this condition is that cash payments could be misappropriated and not be detected in the normal course of business.

Recommendation: All voided receipts should reflect the original copy on file.

**POHNPEI STATE HOUSING AUTHORITY**

Schedule of Unresolved Prior Year Questioned Costs  
Year Ended September 30, 2000

The following is a summary of questioned costs noted and prior year unresolved federal questioned costs for the Pohnpei State Housing Authority:

|   | Questioned Costs<br>Set Forth in<br>Prior Audit Report<br><u>1999</u> | Questioned<br>Costs Resolved<br>in Fiscal Year<br><u>2000</u> | Questioned Costs at<br><u>September 30, 2000</u> |
|---|---|---|--|
|   | \$ 184,842  | -   | \$ 184,842                                       |
| Questioned Costs per the 2000<br>Audit Report | -   | -   | <u>-</u>   |
|   |   |   | \$ <u>184,842</u>                                |



# POHNPEI STATE GOVERNMENT

## HOUSING AUTHORITY

P.O.Box 1109

Kolonia, Pohnpei, FSM 96941

Francis G. Sohl  
Executive Director

Phone: (691) 320-2582/2096

Fax: (691) 320-2304  
Email: fgsohl@mail.fm

### BOARD OF DIRECTORS

Yuto Nakasone  
Chairman

Bethwel Henry  
Vice-Chairman

Kurtin Santos  
Secretary

Benjamin Rodriguez  
Member

Jerry Barbosa  
Member

4 December, 2001

Deloitte, Touche and Tohmatsu  
Kapwaresou Street  
Kolonia, Pohnpei FM 96941

Dear Gentlemen:

This is with reference to the audit findings stated in the audit report for fiscal year ended September 30, 2000 of the Pohnpei State Housing Authority.

Response to corrective action plan to said findings are hereby stated as follows:

1. ***Finding No. 2000-01. SEGREGATION OF DUTIES.*** This issue is a concern of the current administration. Since coming on board the Executive Director has planned to being involve in reviewing the work of the two accountants in areas of collection, recording and banking cash.

**Proposed corrective action plan and deadline.** The management had prepared an internal control contingency plan and had been in effective since 1 October 2001. The Administrative Officer and Executive Director are actively reviewing the daily collections, recording and banking.

2. ***Finding No. 2000-02. EMPLOYEE ADVANCES.*** The practice of giving assistance to the employees in time of urgent situation was carried from the previous management (1988) to present. PSHA treats these so called advances as staff loans and charges 4.5% per annum. Interests earned are considered miscellaneous income.

***Corrective Action Plan:*** For the purpose of clarification and resolution the Management is currently servicing the individuals involved. Furthermore, we have drafted a Financial Management Regulation for addressing the issue and hope to resolve this by 30 September 2002.

3. ***Finding No. 2000-03. PAYMENT SUPPORT.*** The management was not aware of to this isolated case. The supporting documents to these transactions have been found and filed.

***Corrective Action Plan:*** The Management will make sure that all fund disbursements are supported with proper documents. All disbursements without supporting documents will be automatically rejected by the Executive Director. There is no exception and no deadline to this item.

4. ***Finding. No. 2000-04. FIXED ASSETS.*** The Authority possesses detailed lists of fixed assets owned and did record depreciation expense during the fiscal year ended September 30, 2000. Nonetheless, the former Comptroller did not keep accurate record of these fixed assets.

***Corrective Action Plan:*** A detailed list of these fixed assets have been prepared and maintained. The same list is attached for your information and file

5. ***Finding No. 2000-05. BOARD OF DIRECTORS MINUTES.*** This has been a weakness of the previous administrations.

***Corrective Action Plan:*** The new administration is overseeing that this issue does not appear again. We have prepared and kept a secured file of the Board's meeting minutes.

6. ***Finding No. 2000-06: LOAN ENFORCEMENT AND THE ALLOWANCE FOR LOAN LOSS RESERVES.*** Circumstances for not complying with the loan agreements and Allowances for Loan Loss (ALL) is a major concern of this administration.

***Corrective Action Plan:*** The Management is using the Authority's loan and Escrow fund on this matter. Furthermore, we are concentrating one hundred percent of our efforts in collection of outstanding loans.

7. ***Finding No. 2000-07. COMPLIANCE WITH RULES AND REGULATIONS.*** As in the prior years, the above condition results from ignorance of both the Management and Board of Directors on safeguarding that the Rules and Regulations are complied with.

**Corrective Action Plan:** In all findings concerning non-compliance to PSHA Rules and Regulations, the present administration is trying its very best efforts to resolve and prevent the commission of the same problems and will ensure to perform or act prudently with the set Rules and Regulations.

8. ***FINDING NO. 2000-08. LOAN FILE DOCUMENTATION.*** As the rest of all the repeated incidents, documentation were never a practice in PSHA, it had placed the Authority on thin air as to recovery of loan arrears.

**Corrective Action Plan.** It is a requirement of the existing administration that documentation in loan files must not be tolerated. Inadequate documentations strictly prohibited and asked not to be repeated.

9. ***FINDING NO. 2000-09. INTEREST ACCRUAL ON DELINQUENT LOANS.*** The Authority supports this finding and believes it contravenes with the Accounting principles generally accepted.

**Corrective Action Plan:** We have brought this issue in front of the Board and they have approved the management's plan on correcting this problem. As of this response, the Loan division in collaboration with the Accounting personnel had managed to complete the first phase of this project and will complete the second phase by 31 December 2001.

10. ***FINDING NO. 2000-10. RECORDED APPROPRIATIONS RECEIVABLE.*** Pursuant to State Law 2L-81-88, section 10 subsection 5 this is true. However, in the past years there had been no action as to the collection of these amounts.

**Corrective Action Plan:** We have worked this matter out with the Department of Treasury and Administration, the State Auditor, Budget office and the Attorney General's office. As soon as the Budget office issues advice of allotment for these funds, the Authority may be able to remove this item from its findings.

11. **FINDING NO. 11. CONTRACT EMPLOYEE PAYROLLS.** Questions raised concerning this finding are true and the management cannot deny such.

**Corrective Action Plan:** The management had discussed the same with the support staff, especially the administrative personnel and collectively resolved to make sure this is not repeated again.

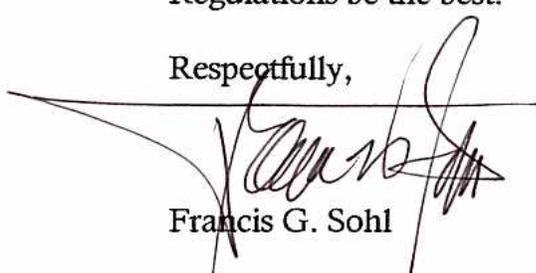
12. **FINDING NO. 2000-12. VOIDED CASH RECEIPTS.** The effect of this issue is ineffectiveness and ignorance of employees involved in accounting functions.

**Corrective Action Plan:** The management as well as the Accounting division had discussed the issue and agreed on the proper compliance by means of weekly reviews of transactions by the Management to ensure outcast of this behavior.

The PSHA management and Board of Directors will try its foremost efforts to operate soundly and effectively to meet our primary mission statement of providing Safe, Decent and Sanitary Housing for every low income family of Pohnpei. In the process, however, unavoidable and uncontrollable circumstances had caused to omit some compliance of Rules and Regulations that could not have prevented and if prevented was inevitable.

We appreciate your time and efforts for the completion of the audit and expect your recommendations to assist the Management to address the cited discrepancies. The administration also promotes teamwork with right attitude and action not ignoring honesty and loyalty for each employee of PSHA so that improved customer services and compliance to Rules and Regulations be the best.

Respectfully,



Francis G. Sohl

Cc: Governor Johnny P. David  
Chairman, Board of Directors

Fiscal Year 2000  
Property and Equipment Additions

| Item   | Date<br>Acquired | Reference | Check# | Cost     | Useful Life | Annual<br>Depn | Beg. Accum<br>Depn | Depn FY00 | End.<br>Accum<br>Depn | Book<br>Value at<br>9/30/00 |
|--|------------------|-----------|--------|----------|-------------|----------------|--------------------|-----------|-----------------------|-----------------------------|
| <b>Provided by state government:</b>   |                  |           |        |          |             |                |                    |           |                       |                             |
| Jeep Sportage (chassis# KNAJA5545PA708026)<br>(\$7,500 paid for by state govt; \$700 paid for by PSHA)   | 4/4/00           | VP6554    | 2355   | 8,200.00 | 5           | 1,640.00       | 0                  | 820.00    | 820.00                | 7,380.00                    |
| Fax Laser Printer  | 3/6/00           |           |        | 849.00   | 5           | 169.80         | 0                  | 84.90     | 84.90                 | 764.10                      |
| Type-writer  | 3/15/01          |           |        | 298.00   | 2           | 149.00         | 0                  | 74.50     | 74.50                 | 223.50                      |
| Supplemental   | 4/25/00          |           |        | 700.00   | 5           | 140.00         | 0                  | 70.00     | 70.00                 | 630.00                      |
| Compaq Pres/Printer  | 8/9/00           |           |        | 1,895.00 | 5           | 379.00         | 0                  | 189.50    | 189.50                | 1,705.50                    |
| <b>Purchase made directly by PSHA:</b>   |                  |           |        |          |             |                |                    |           |                       |                             |
| Flatbed Nissan (chassis#W2H41-000669)  | 6/7/00           | VP6894    | 7266   | 6,500.00 | 5           | 1,300.00       | 0                  | 650.00    | 650.00                | 5,850.00                    |
| Sedan Nissan (chassis#HC33-140680)<br>(\$5,000 was paid on 9/00 FY00; \$5,000 was paid on<br>11/00 FY01) | 6/7/00           | VP6894    | 7266   | 3,500.00 | 5           | 700.00         | 0                  | 350.00    | 350.00                | 3,150.00                    |
| 19ft. Footer Boat  | 7/10/00          | VP6757    | 2459   | 2,700.00 | 5           | 540.00         | 0                  | 270.00    | 270.00                | 2,430.00                    |