

**STATE OF POHNPEI  
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, 2003**

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

YEAR ENDED SEPTEMBER 30, 2003

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**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

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**INDEPENDENT AUDITORS' REPORT  
AND FINANCIAL STATEMENTS  
AND ADDITIONAL INFORMATION**

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**YEAR ENDED SEPTEMBER 30, 2003**

## INDEPENDENT AUDITORS' REPORT

Honorable Johnny P. David  
Governor, State of Pohnpei  
Federated States of Micronesia:

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei, as of and for the year ended September 30, 2003, which collectively comprise the State of Pohnpei's basic financial statements as set forth in Section II of the foregoing table of contents. These financial statements are the responsibility of the management of the State of Pohnpei. Our responsibility is to express an opinion on the respective financial statements based on our audit. We did not audit the financial statements of the Small Business Guarantee and Finance Corporation, which represent 3% and 0.1%, respectively, of the assets and revenues of the State of Pohnpei's discretely presented component units. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Small Business Guarantee and Finance Corporation, is based solely on the report of the other auditors.

Except as discussed in the following paragraphs, 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 respective financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the State of Pohnpei's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

Because of the inadequacy of accounting records over financial reporting, we were unable to form an opinion regarding the amount at which advances are recorded in the Governmental Funds Balance Sheet for the aggregate remaining fund information, or the amounts at which reserve for encumbrances are recorded in the Governmental Funds Balance Sheet for each major fund and the aggregate remaining fund information.

The financial statements referred to above include unaudited financial statements of the Pohnpei Economic Development Authority (EDA), the Pohnpei State Housing Authority (PSHA), and the Pohnpei Transportation Authority (PTA), whose financial activities are included in the aggregate discretely presented component units and represent 11% and 24%, respectively, of the assets and revenues of the State of Pohnpei's discretely presented component units. The entities comprising these financial activities did not produce audited financial statements and the effect on the accompanying financial statements of this matter is unknown.

We were not able to apply sufficient alternative procedures to assure ourselves as to the propriety of accounts payable and related expenses in the amount of \$300,000 relating to the procurement of a master plan for the Pohnpei Port Authority as of and for the year ended September 30, 2003, whose financial activities are included in the aggregate discretely presented component units.

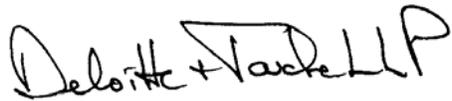
In our opinion, based on our audit and the report of the other auditors, except for the effects on the respective financial statements of such adjustments, if any, as might have been determined to be necessary had 1) accounting records regarding advances recorded within the aggregate remaining fund information and reserves for encumbrances recorded within each major fund and the aggregate remaining fund information been adequate; 2) the propriety of certain accounts payable and related expenses of the Pohnpei Port Authority been determinable; and 3) EDA, PSHA and PTA been audited, as discussed in the third through fifth paragraphs above, such financial statements, as set forth in Section II of the foregoing table of contents, present fairly, in all material respects, the respective financial position of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei as of September 30, 2003, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, during the year ended September 30, 2003, the State of Pohnpei adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, GASB Statement No. 37, *Basic Financial Statements and Management Discussion and Analysis for State and Local Governments; Omnibus*, and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. The implementation of these standards changed the basic financial statement reporting model to include government-wide, full accrual statements and created a modified reporting of the fund perspective financial statements. Implementing these standards also required reporting of infrastructure assets, and included the requirement for reporting a Management's Discussion and Analysis as required supplementary information. Beginning net asset and fund balances have been restated to account for the implementation of these accounting standards.

The Management's Discussion and Analysis, on pages 4 through 10, as well as the Schedule of Revenues, Expenditures, and Changes in Unreserved Fund Balance - Budget and Actual - General Fund and notes thereto, on pages 42 and 43, are not a required part of the basic financial statements but are supplementary information required by GASB. Such information is the responsibility of the management of the State of Pohnpei. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic 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 Pohnpei, are presented for purposes of additional analysis and are not a required part of the basic financial statements of the State of Pohnpei. Such additional information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, except for the matter specified in the third paragraph above, is fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2005, on our consideration of the State of Pohnpei's (Primary Government only) internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

A handwritten signature in black ink that reads "Deloitte + Tatchell LLP". The signature is written in a cursive, slightly stylized font.

September 30, 2005

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis  
September 30, 2003

This section of Pohnpei State's financial report presents our Management's Discussion and Analysis (MD&A) for the fiscal year ended September 30, 2003. This is the first year that MD&A is prepared in compliance with the GASB-34 requirement. Readers are requested to read this MD&A in conjunction with the State's financial statements, which follow this section.

**FINANCIAL HIGHLIGHTS**

- The Pohnpei State's primary government's total net assets for this year are \$ 39,594,589.
- The net change in governmental fund balance is \$3,379,982. The total revenues reported are \$39,339,776 with the total expenditures of \$35,959,794.
- Actual revenues for the general fund were \$73,783 higher than budgeted revenues, however, the total expenditures, budgetary basis showed an unfavorable variance of \$3,614,938. The general fund reported an unreserved deficit of \$1,329,099 for the fiscal year.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This annual report consists of four parts-management's discussion and analysis (this section), the basic financial statements, required supplementary information and the notes to the financial statements.

The basic financial statements include two kinds of statements that present different views of the State:

Government-Wide Financial Statements

The government-wide financial statements report information about the State as a whole using accounting method similar to those used by the private-sector companies. It provides both long-term and short-term information about the State's financial status.

The statement of net assets includes all of the government's assets and liabilities. The difference between the two is called net assets. Over time, increases or decreases in the State's net assets serve as an indicator to measure the State's financial position.

The statement of activities, on the other hand, accounts for the State's current year's revenues and expenses regardless of when cash is received or paid.

The government-wide financial statements of the State consist of its governmental activities, which include public works, health, education and general administration. Sales taxes, revenue sharing and federal grants are the major sources of these activities. Governmental activities are also financed by the Compact grant; however fiscal year 2003 is the last year of Compact I funding.

Fund Financial Statements

The fund financial statements provide more detailed information about the State's significant funds. The State uses fund accounting to comply with financial related legal requirements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis  
September 30, 2003

- Governmental funds. Most of the State's basic services are included in governmental funds' which focus on how cash and other financial assets that can readily be converted to cash flow in and out and the balances left at year-end that are available for spending. Unlike the government-wide financial statements, the governmental funds statements focus on the short-term financial requirements of the State. Because this information does not encompass the additional long-term focus of the government wide statements, we provide reconciliation at the bottom of the governmental funds statement, or on the subsequent page to explain the relationship between them. The State maintains individual governmental funds, which are categorized as major and non-major. The major fund includes the General Fund. The other major funds are consisting of the Federal Grants and Compact CIP.

**FINANCIAL ANALYSIS OF THE STATE AS A WHOLE (GOVERNMENT-WIDE)**

The following is a summary of the State's net assets as of September 30, 2003:

	<u>Governmental Activities</u>
Current and other assets	\$ 23,975,725
Capital assets	16,404,598
Other non current assets	<u>8,102,204</u>
Total assets	<u>48,482,527</u>
Current liabilities	3,558,674
Long-term debt	4,200,000
Other liabilities	<u>1,129,264</u>
Total liabilities	<u>8,887,938</u>
Net Assets:	
Invested in capital assets, net of related debt	16,404,598
Restricted	21,987,627
Unrestricted	<u>1,202,364</u>
Total net assets	\$ <u>39,594,589</u>

Changes in net assets. The State's statement of Changes in Net Assets for the fiscal year 2003 follows:

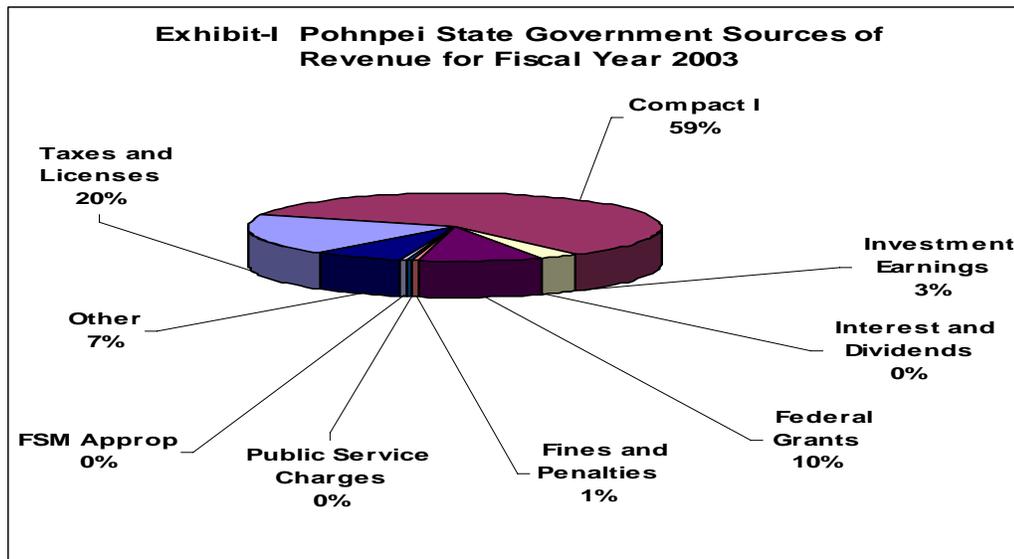
	<u>Governmental Activities</u>
Revenues:	
Program revenues:	
Charges for services	\$ 2,631,450
Operating grants and contributions	8,117,773
Capital grants and contributions	8,095,814
General revenues:	
Compact	11,237,118
Taxes	7,776,122
Investment earnings	1,179,973
Other	<u>301,526</u>
Total revenues	<u>39,339,776</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis  
September 30, 2003

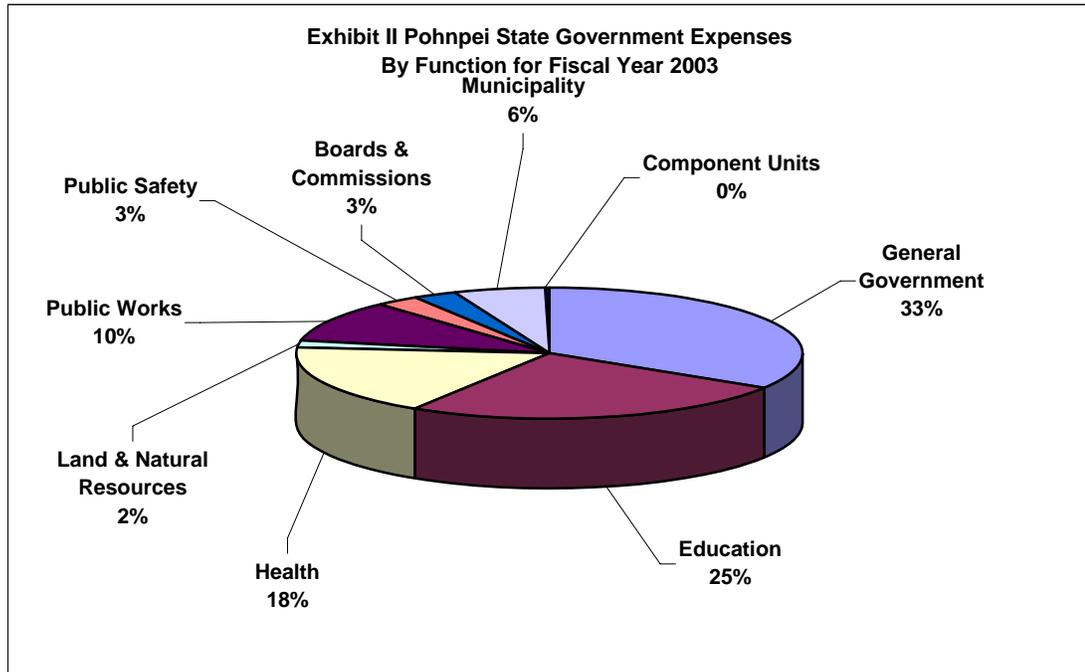
	<u>Governmental Activities</u>
Expenses:	
General Government	12,871,988
Education	8,989,191
Health services	6,458,362
Land and natural resources	807,377
Public works	3,977,107
Public safety	1,031,874
Boards, Commission and other appropriations	1,038,363
Other Miscellaneous	<u>2,164,822</u>
 Total expenses	 <u>37,359,084</u>
 Change in net assets	 \$ <u>1,980,692</u>

Based on Exhibit I presented below, more than half of the State's revenues came from Compact 1 and 20% from taxes and licenses. As mentioned earlier, Compact I funding will be replaced by Compact II funding in fiscal year 2004. The State's expenses encompass a range of services. Exhibit II showed that general government and education represent the highest percentage, which is 33% and 25%, respectively, of the State's total expenses.



**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis  
September 30, 2003



**GOVERNMENTAL ACTIVITIES**

**General Fund**

The revenues increased by only \$700 compared to FY 2002 figures while the total expenditures increased by \$3,230,116. The increases in expenditures were due to the write-off of prior year travel advances and receivables from the FSM National Government for federal and CFSM funded projects. The impact on the fund balance is a reduction of unreserved deficit because these receivables were reserved as related assets in the prior years.

**Special Revenue**

The increase or decrease in revenues and expenditures of the fund cannot be compared due to transfer of most of the funds into the non-major funds.

**Capital Projects**

The increase or decrease in revenues and expenditures of the fund cannot be compared due to transfer of most of the funds into the non-major funds.

**Other Governmental Funds**

All the non-major funds from the Special revenue and CIP funds were grouped under this category.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis  
September 30, 2003

**FINANCIAL ANALYSIS OF THE STATE GOVERNMENT'S FUNDS**

The State's governmental fund changes in fund balances for the year ended September 30, 2003 are shown below.

Changes in Fund Balances

	<u>General Fund</u>	<u>Other Funds</u>	<u>Total</u>
Revenues:			
Taxes	\$ 6,254,450	\$ 1,521,672	\$ 7,776,122
Compact	11,237,118	12,044,412	23,281,530
Other	<u>1,165,147</u>	<u>7,116,977</u>	<u>8,282,124</u>
 Total revenues	 <u>18,656,715</u>	 <u>20,683,061</u>	 <u>39,339,776</u>
 Expenditures	 <u>20,369,491</u>	 <u>15,590,303</u>	 <u>35,959,794</u>
 Net change in fund balance	 \$ <u>(1,712,776)</u>	 \$ <u>5,092,758</u>	 \$ <u>3,379,982</u>

General Fund Budgetary Highlights

During the year, the State revised its budget several times to accommodate supplemental funding for departments and offices requiring increases in appropriations to avoid budget overruns.

The State's general fund balance of \$ 3,928,565 differs from the general fund budgetary fund deficit of \$1,329,099 reported in the Schedule of Budgetary Expenditures (Non-GAAP) because the schedule includes encumbrances as expenditures and the effect of continuing appropriations for budgetary purposes.

**CAPITAL ASSET AND DEBT ADMINISTRATION**

Capital Assets

The State's capital assets at the end of fiscal year 2003 consist basically of equipment, buildings, roads, bridges, water and sewer lines. The summary of capital assets at the end of the year is shown below:

	<u>Primary Government Governmental Activities</u>
Buildings	\$ 10,025,675
Infrastructure	14,358,270
Machinery, equipment and others	<u>3,624,089</u>
 Total	 \$ <u>28,008,034</u>

The notes to the financial statements present more information about the State's capital assets.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis  
September 30, 2003

Long-Term Debt

At year-end, the State had long-term debt of \$5,721,119 as shown below:

	<u>Governmental Activities</u>
Early Retirement	\$ 4,200,000
Compensated absences	799,437
Claims and litigation	<u>721,682</u>
Total	\$ <u>5,721,119</u>

Economic Factors and Next Year's Budget

Funding for the operations of most of the government service in fiscal year 2004 will be coming from the Compact II.

Fiscal year 2004 is the beginning of the implementation of the economic assistance under the Compact II/ Amended funding which replaces the funding sources from the old Compact I. Under the amended compact, annual funding for the following will be available as follows:

- The education sector grant that shall support and improve the educational system of the Federated States of Micronesia, including, without limitation, the systems for primary, secondary, and post-secondary education.
- The health sector grant that shall support and improve the delivery of preventive, curative and environmental care, and develop the human and material resources necessary for the Federated States of Micronesia to perform these services.
- The sector grant for private sector development shall support the efforts of the Federated of Micronesia to attract new foreign investment and increase indigenous business activity. Priorities will be in advancing the private development of fisheries, tourism and agriculture; employing new telecommunications technologies; and analyzing and developing new systems, laws, and policies to foster private sector development, to facilitate investment by potential private investors, and develop business and entrepreneurial skills.
- The sector for capacity building shall support the efforts of the Federated States of Micronesia to build effective, accountable and transparent national and local government and other public sector institutions and systems.
- The environment sector shall support the efforts of the Federated States of Micronesia to protect the Nation's land and marine environment and to conserve and achieve sustainable use of its natural resources.
- Public Infrastructure grant shall give priority to primary and secondary education capital projects and programs that directly affect health and safety including water and wastewater projects, solid waste disposal projects and health care facilities.

The locally generated revenues and the revenue shares from the National Government are expected to remain at a range of \$ 7,000,000 plus per year. Although the discontinuance of the added tax revenue in fiscal year 2004 is expected to impact the capital projects and other programs of the State in the ensuing years.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis  
September 30, 2003

But the final carry-over balances from the Compact I may be authorized to be used to fund other operations of the government.

**FINANCIAL CONTACT**

This financial report is designed to provide all interested users with a general overview of the State of Pohnpei's finances. If you have questions about this report or need additional financial information, please contact the Office of the Director of Treasury and Administration, P.O. Box 1567 Kolonia, Pohnpei FM 96941.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Statement of Net Assets  
September 30, 2003

	Primary Government	Component Units
<b><u>ASSETS</u></b>		
Current assets:		
Cash and cash equivalents	\$ 1,148,141	\$ 2,194,230
Investments	20,225,482	524,000
Receivables, net of allowance for uncollectibles:		
General	-	4,789,621
From other governments	2,172,853	48,375
Federal agencies	957,512	-
Taxes and leases	28	-
Advances	315,633	289,234
Loans	94,697	3,525,592
Interest	9,473	7,386
Inventories	51,906	1,307,565
Other current assets	-	865,969
	24,975,725	13,551,972
Noncurrent assets:		
Investments	1,000,000	-
Restricted assets:		
Cash and cash equivalents	848,555	-
Investments	3,248,887	502,400
Due from component units	3,004,762	-
Other assets	-	44,103
Capital assets, net of accumulated depreciation	16,404,598	36,833,098
	24,506,802	37,379,601
	\$ 49,482,527	\$ 50,931,573
<b><u>LIABILITIES</u></b>		
Current liabilities:		
Current portion of long-term obligations	\$ -	\$ 187,888
Accounts payable	1,017,843	2,431,305
Accrued payroll and others	536,933	355,762
Compensated absences payable	391,855	96,116
Deferred revenue	-	469,297
Other payables	1,612,043	-
	3,558,674	3,540,368
Noncurrent liabilities:		
Noncurrent portion of long-term obligations	4,200,000	2,555,221
Compensated absences payable	407,582	-
Due to primary government	-	4,079,555
Other noncurrent liabilities	721,682	-
	5,329,264	6,634,776
	8,887,938	10,175,144
<b><u>NET ASSETS</u></b>		
Invested in capital assets, net of related debt	16,404,598	34,375,447
Restricted for:		
Compact related	16,266,397	-
Retirement of indebtedness	42,474	-
Capital projects	3,495,394	-
Other purposes	2,183,362	2,252,144
Unrestricted	1,202,364	4,128,838
	39,594,589	40,756,429
	\$ 48,482,527	\$ 50,931,573

See accompanying notes to basic financial statements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Statement of Activities  
Year Ended September 30, 2003

	Program Revenues				Net (Expenses) Revenues and Changes in Net Assets	
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government	Component Units
<b>Functions/Programs</b>						
<b>Primary government:</b>						
<b>Governmental activities:</b>						
General Government	\$ 12,871,988	\$ 1,929,255	\$ 1,844,744	\$ -	\$ (9,097,989)	\$ -
Education	8,989,191	-	4,760,250	-	(4,228,941)	-
Health Services	6,458,362	408,019	1,149,974	-	(4,900,369)	-
Land and Natural Resources	807,377	-	-	-	(807,377)	-
Public Works	3,997,107	249,420	337,982	8,095,814	4,686,109	-
Public Safety	1,031,874	44,756	24,822	-	(962,296)	-
Boards, commission, and others	1,038,363	-	-	-	(1,038,363)	-
Municipal governments	2,066,974	-	-	-	(2,066,974)	-
Component units	97,848	-	-	-	(97,848)	-
<b>Total primary government</b>	<b>\$ 37,359,084</b>	<b>\$ 2,631,450</b>	<b>\$ 8,117,773</b>	<b>\$ 8,095,814</b>	<b>(18,514,047)</b>	<b>-</b>
<b>Component units:</b>						
Pohnpei Utilities Corporation	\$ 9,378,216	\$ 8,087,222	\$ -	\$ -	-	(1,290,994)
Pohnpei Port Authority	1,433,103	1,134,705	-	-	-	(298,398)
Pohnpei Fisheries Corporation	1,132,491	632,141	-	-	-	(500,350)
Small Business Guarantee Corporation	153,520	6,956	-	-	-	(146,564)
Pohnpei Transportation Authority	2,435,545	1,811,743	-	-	-	(623,802)
Economic Development Authority	1,237,002	1,003,027	-	-	-	(233,975)
Pohnpei State Housing Authority	475,073	274,330	-	-	-	(200,743)
<b>Total State component units</b>	<b>\$ 16,244,950</b>	<b>\$ 12,950,124</b>	<b>\$ -</b>	<b>\$ -</b>	<b>-</b>	<b>(3,294,826)</b>
<b>General revenues:</b>						
<b>Taxes and licenses:</b>						
Revenue share					5,621,143	-
Sales tax					1,555,204	-
Others					599,775	-
Compact					7,112,100	-
Compact Inflation					4,125,018	-
Unrestricted investment earnings					839,435	-
Interest and dividends					340,538	41,982
Contributions from primary government					-	471,133
Other					301,526	319,940
<b>Total general revenues and transfers</b>					<b>20,494,739</b>	<b>833,055</b>
<b>Change in net assets</b>					<b>1,980,692</b>	<b>(2,461,771)</b>
<b>Net assets at the beginning of the year</b>					<b>37,613,897</b>	<b>43,218,200</b>
<b>Net assets at the end of the year</b>					<b>\$ 39,594,589</b>	<b>\$ 40,756,429</b>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Balance Sheet  
Governmental Funds  
September 30, 2003

	General	Special Revenue U.S Federal Grants	Capital Projects Compact Capital Projects	Other Governmental Funds	Total
<b>ASSETS</b>					
Cash and cash equivalents	\$ 1,148,141	\$ -	\$ -	\$ -	\$ 1,148,141
Investments	8,349,755	-	9,282,874	2,592,853	20,225,482
Receivables, net:					
From other governments	1,213,634	-	-	959,219	2,172,853
Federal agencies	-	957,512	-	-	957,512
Taxes and lease	28	-	-	-	28
Advances	46,460	29,397	13,370	226,406	315,633
Loans	-	-	94,697	-	94,697
Interest	5,111	-	434	3,928	9,473
Due from Component Units	554,762	-	2,450,000	-	3,004,762
Due from other funds	2,750,978	-	2,433,834	5,316,800	10,501,612
Inventories	8,806	-	-	43,100	51,906
Restricted assets:					
Cash and cash equivalents	96,899	-	751,656	-	848,555
Investments	-	-	-	3,248,887	3,248,887
Total assets	<u>\$ 14,174,574</u>	<u>\$ 986,909</u>	<u>\$ 15,026,865</u>	<u>\$ 12,391,193</u>	<u>\$ 42,579,541</u>

**LIABILITIES AND FUND BALANCES**

<b>Liabilities:</b>					
Accounts payable	\$ 551,095	\$ 131,666	\$ 92,844	\$ 242,238	\$ 1,017,843
Other liabilities and accruals	332,237	28,455	-	176,241	536,933
Due to other funds	7,750,634	985,616	726,193	1,039,169	10,501,612
Other liabilities	1,612,043	-	-	-	1,612,043
Total liabilities	<u>10,246,009</u>	<u>1,145,737</u>	<u>819,037</u>	<u>1,457,648</u>	<u>13,668,431</u>
<b>Fund balances (deficits):</b>					
Reserved for:					
Related assets	1,870,875	-	4,337,297	3,291,360	9,499,532
Encumbrances	717,430	956,134	2,492,514	814,559	4,980,637
Continuing appropriations	2,669,359	-	8,808,783	1,048,194	12,526,336
Compact Special Block	-	-	-	191,236	191,236
Other Compact Grants	-	-	-	1,696,269	1,696,269
Unreserved (deficits), reported in:					
General fund	(1,329,099)	-	-	-	(1,329,099)
Special revenue funds	-	(1,114,962)	-	1,791,165	676,203
Capital projects funds	-	-	(1,430,766)	2,100,762	669,996
Total fund balances (deficits)	<u>3,928,565</u>	<u>(158,828)</u>	<u>14,207,828</u>	<u>10,933,545</u>	<u>28,911,110</u>
Total liabilities and fund balances	<u>\$ 14,174,574</u>	<u>\$ 986,909</u>	<u>\$ 15,026,865</u>	<u>\$ 12,391,193</u>	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	\$ 16,404,598
Long-term liabilities, including loans payable, are not due and payable in the current period and therefore are not reported in the funds. The liabilities include:	
Accrued claims payable	(721,682)
Loans payable	(4,200,000)
Compensated absences payable	(799,437)

10,683,479

Net assets of governmental activities \$ 39,594,589

See accompanying notes to basic financial statements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures, and Changes in Fund Balances (Deficits)  
Governmental Funds  
Year Ended September 30, 2003

	General	Special Revenue U.S Federal Grants	Capital Projects Compact Capital Projects	Other Governmental Funds	Total
<b>Revenues:</b>					
Taxes and licenses:					
Revenue share	\$ 4,099,471	\$ -	\$ -	\$ 1,521,672	\$ 5,621,143
Sales tax	2,109,139	-	-	-	2,109,139
Others	45,840	-	-	-	45,840
Compact	7,112,100	-	5,123,933	3,407,268	15,643,301
Compact inflation	4,125,018	-	2,971,881	541,330	7,638,229
Investment earnings	839,435	-	-	315,882	1,155,317
Interest and dividends	-	-	24,606	-	24,606
Federal grants	-	3,823,975	-	-	3,823,975
Fines and penalties	246,780	-	-	-	246,780
Public service charges	24,186	-	-	53,541	77,727
FSM appropriations	-	-	-	173,171	173,171
Other	54,746	-	-	2,725,802	2,780,548
<b>Total revenues</b>	<b>18,656,715</b>	<b>3,823,975</b>	<b>8,120,420</b>	<b>8,738,666</b>	<b>39,339,776</b>
<b>Expenditures:</b>					
Current:					
General government	9,036,097	684,787	-	2,424,881	12,145,765
Education	3,362,810	2,441,904	-	3,260,554	9,065,268
Health	3,436,739	679,625	-	2,183,488	6,299,852
Land and natural resources	441,280	-	-	111,017	552,297
Public works	-	17,659	3,123,471	526,537	3,667,667
Public safety	1,025,760	-	-	-	1,025,760
Boards, commission, others	901,983	-	-	136,380	1,038,363
Municipal government	2,066,974	-	-	-	2,066,974
Payments to component units	97,848	-	-	-	97,848
<b>Total expenditures</b>	<b>20,369,491</b>	<b>3,823,975</b>	<b>3,123,471</b>	<b>8,642,857</b>	<b>35,959,794</b>
<b>Net change in fund balances</b>	<b>(1,712,776)</b>	<b>-</b>	<b>4,996,949</b>	<b>95,809</b>	<b>3,379,982</b>
<b>Fund balances (deficits) at the beginning of the year</b>	<b>5,641,341</b>	<b>(158,828)</b>	<b>9,210,879</b>	<b>10,837,736</b>	<b>25,531,128</b>
<b>Fund balances (deficits) at the end of the year</b>	<b>\$ 3,928,565</b>	<b>\$ (158,828)</b>	<b>\$ 14,207,828</b>	<b>\$ 10,933,545</b>	<b>\$ 28,911,110</b>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Reconciliation of the Statement of Revenues, Expenditure, and Changes in Fund  
Balances of Governmental Funds to the Statement of Activities  
Year Ended September 30, 2003

Amounts reported for governmental activities in the statement of activities on page 12 are different because:

Net change in fund balances - total governmental funds from page 14	\$ 3,379,982
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period	(805,502)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore, are not reported as expenditures in governmental funds. These expenses include accrued annual leave and claims and judgment payable that are reported in the statement of activities, but not in funds	<u>(593,788)</u>
Change in net assets of governmental activities as presented on page 12	\$ <u>1,980,692</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

COMPONENT UNITS  
Combining Statement of Net Assets  
September 30, 2003

	Pohnpei Utilities Corporation	Pohnpei Port Authority	Pohnpei Fisheries Corporation	Pohnpei Transportation Authority	Small Business Guarantee	Economic Development Authority	Pohnpei Housing Authority	Total
<b>ASSETS</b>								
Current assets:								
Cash and cash equivalents	\$ 384,911	\$ 184,739	\$ 20,278	\$ -	\$ 1,642,815	\$ (43,939)	\$ 5,426	\$ 2,194,230
Investments	524,000	-	-	-	-	-	-	524,000
Receivables, net:								
General	4,263,322	108,820	55,212	211,516	6,040	144,711	-	4,789,621
Other governments	48,375	-	-	-	-	-	-	48,375
Advances	42,375	33,130	-	-	4,059	-	209,670	289,234
Loans	-	-	-	-	44,872	-	3,480,720	3,525,592
Interest	-	6,628	-	-	758	-	-	7,386
Inventories	940,314	-	125,775	239,858	-	-	1,618	1,307,565
Other current assets	479,448	319,967	-	17,708	-	48,846	-	865,969
<b>Total current assets</b>	<b>6,682,745</b>	<b>653,284</b>	<b>201,265</b>	<b>469,082</b>	<b>1,698,544</b>	<b>149,618</b>	<b>3,697,434</b>	<b>13,551,972</b>
Noncurrent assets:								
Other assets	-	-	44,103	-	-	-	-	44,103
Investments	-	-	-	-	-	502,400	-	502,400
Capital assets, net of accumulated depreciation	29,450,475	5,293,026	1,448,907	460,295	8,479	114,109	57,807	36,833,098
<b>Total noncurrent assets</b>	<b>29,450,475</b>	<b>5,293,026</b>	<b>1,493,010</b>	<b>460,295</b>	<b>8,479</b>	<b>616,509</b>	<b>57,807</b>	<b>37,379,601</b>
<b>Total assets</b>	<b>\$ 36,133,220</b>	<b>\$ 5,946,310</b>	<b>\$ 1,694,275</b>	<b>\$ 929,377</b>	<b>\$ 1,707,023</b>	<b>\$ 766,127</b>	<b>\$ 3,755,241</b>	<b>\$ 50,931,573</b>
<b>LIABILITIES</b>								
Current liabilities:								
Current portion of long-term debt	\$ 94,486	\$ 12,542	\$ 80,860	\$ -	\$ -	\$ -	\$ -	\$ 187,888
Accounts payable	265,265	348,852	1,157,067	20,918	-	606,829	32,374	2,431,305
Other liabilities and accruals	139,255	139,495	-	70,985	5,197	-	830	355,762
Compensated absences	52,011	44,105	-	-	-	-	-	96,116
Deferred revenue	79,362	389,935	-	-	-	-	-	469,297
Due to primary government	-	-	3,429,793	554,762	-	95,000	-	4,079,555
<b>Total current liabilities</b>	<b>630,379</b>	<b>934,929</b>	<b>4,667,720</b>	<b>646,665</b>	<b>5,197</b>	<b>701,829</b>	<b>33,204</b>	<b>7,619,923</b>
Noncurrent liabilities:								
Noncurrent portion of long-term debt	2,407,268	-	147,953	-	-	-	-	2,555,221
<b>Total noncurrent liabilities</b>	<b>2,407,268</b>	<b>-</b>	<b>147,953</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>2,555,221</b>
<b>Total liabilities</b>	<b>3,037,647</b>	<b>934,929</b>	<b>4,815,673</b>	<b>646,665</b>	<b>5,197</b>	<b>701,829</b>	<b>33,204</b>	<b>10,175,144</b>
<b>NET ASSETS</b>								
Invested in capital assets, net of related debt	26,948,721	5,293,026	1,493,010	460,295	8,479	114,109	57,807	34,375,447
Restricted	274,437	319,967	-	-	1,657,740	-	-	2,252,144
Unrestricted	5,872,415	(601,612)	(4,614,408)	(177,583)	35,607	(49,811)	3,664,230	4,128,838
<b>Total net assets</b>	<b>33,095,573</b>	<b>5,011,381</b>	<b>(3,121,398)</b>	<b>282,712</b>	<b>1,701,826</b>	<b>64,298</b>	<b>3,722,037</b>	<b>40,756,429</b>
<b>Total liabilities and net assets</b>	<b>\$ 36,133,220</b>	<b>\$ 5,946,310</b>	<b>\$ 1,694,275</b>	<b>\$ 929,377</b>	<b>\$ 1,707,023</b>	<b>\$ 766,127</b>	<b>\$ 3,755,241</b>	<b>\$ 50,931,573</b>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

**COMPONENT UNITS  
Combining Statement of Revenues, Expenses, and Changes in Net Assets  
Year Ended September 30, 2003**

	Pohnpei Utilities Corporation	Pohnpei Port Authority	Pohnpei Fisheries Corporation	Pohnpei Transportation Authority	Small Business Guarantee	Economic Development Authority	Pohnpei Housing Authority	Total
Operating revenues:								
Charges for services	\$ 8,087,222	\$ 1,134,705	\$ 632,141	\$ 1,811,743	\$ 4,268	\$ 1,003,027	\$ 274,330	\$ 12,947,436
Other	-	-	-	-	2,688	-	-	2,688
Total operating revenues	<u>8,087,222</u>	<u>1,134,705</u>	<u>632,141</u>	<u>1,811,743</u>	<u>6,956</u>	<u>1,003,027</u>	<u>274,330</u>	<u>12,950,124</u>
Operating expenses:								
Cost of services	5,605,634	-	978,688	1,752,649	-	1,237,002	-	9,573,973
Administration costs	1,666,977	1,013,148	148,410	-	153,520	-	475,073	3,457,128
Depreciation and amortization	2,105,605	419,955	5,393	682,896	-	-	-	3,213,849
Total operating expenses	<u>9,378,216</u>	<u>1,433,103</u>	<u>1,132,491</u>	<u>2,435,545</u>	<u>153,520</u>	<u>1,237,002</u>	<u>475,073</u>	<u>16,244,950</u>
Operating loss	<u>(1,290,994)</u>	<u>(298,398)</u>	<u>(500,350)</u>	<u>(623,802)</u>	<u>(146,564)</u>	<u>(233,975)</u>	<u>(200,743)</u>	<u>(3,294,826)</u>
Nonoperating revenues (expenses):								
Interest income	-	14,575	-	-	27,407	-	-	41,982
Contributions from the primary government	263,352	-	-	-	70,560	-	137,221	471,133
Interest expense	-	-	(18,782)	-	-	-	-	(18,782)
Other	278,738	(43,879)	2,432	-	(2,741)	103,803	369	338,722
Total nonoperating revenues (expenses), net	<u>542,090</u>	<u>(29,304)</u>	<u>(16,350)</u>	<u>-</u>	<u>95,226</u>	<u>103,803</u>	<u>137,590</u>	<u>833,055</u>
Net loss	<u>(748,904)</u>	<u>(327,702)</u>	<u>(516,700)</u>	<u>(623,802)</u>	<u>(51,338)</u>	<u>(130,172)</u>	<u>(63,153)</u>	<u>(2,461,771)</u>
Net assets at the beginning of the year	<u>33,844,477</u>	<u>5,339,083</u>	<u>(2,604,698)</u>	<u>906,514</u>	<u>1,753,164</u>	<u>194,470</u>	<u>3,785,190</u>	<u>43,218,200</u>
Net assets at the end of the year	<u>\$ 33,095,573</u>	<u>\$ 5,011,381</u>	<u>\$ (3,121,398)</u>	<u>\$ 282,712</u>	<u>\$ 1,701,826</u>	<u>\$ 64,298</u>	<u>\$ 3,722,037</u>	<u>\$ 40,756,429</u>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies

The financial statements of the State of Pohnpei (the State) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the State's accounting policies are described below.

A. Reporting Entity

The State is one of the four states that make up the Federated States of Micronesia (FSM), along with the states of Chuuk, Kosrae and Yap. The State is a constitutional government comprised of three branches: the Legislative Branch, consisting of 23 members elected for a term of four years by qualified voters of their respective election districts; the Executive Branch, headed by the Governor and Lt. Governor who are primarily responsible for executing the laws and administering state government services; and the Judiciary Branch made up of the State Supreme Court, which consists of a Chief Justice and up to four Associate Justices, and other courts that may be created by law.

For financial reporting purposes, the State has included all funds, organizations, agencies, boards, commissions and institutions. The State has also considered all potential component units for which it is financially accountable as well as other entities for which the nature and significance of their relationship with the State are such that exclusion would cause the State's financial statements to be misleading or incomplete. The criteria to be considered in determining financial accountability include whether the State, as the primary government, has appointed a voting majority of an organization's governing body and either has the ability to impose its will on that organization or there is potential for the organization to provide specific financial benefits to or impose specific financial burdens on the State. Financial accountability also exists if an organization is determined to be fiscally dependent on the primary government, although the primary government does not appoint a voting majority of the organization's governing board.

Each blended and discretely presented component unit of the State has a September 30 year-end.

Once financial accountability has been determined for a potential component unit, that component unit is either blended into the primary government or discretely presented from the primary government. Potential component units that do not meet the financial accountability criteria, but where a voting majority of the governing board is appointed by the State, are deemed to be related organizations. The nature and relationship of the State's component units and related organizations are disclosed in the following section.

Blended component units are entities that are legally separate from the State, but are so related to the State that they are, in substance, the same as the State or entities providing services entirely or almost entirely to the State. The net assets and results of operations of the following legally separate entities are presented as part of the State's operations:

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

i. Discretely Presented Component Units

Discretely presented component units are entities which are legally separate from the State, but are financially accountable to the State, or whose relationships with the State are such that exclusion would cause the State's basic financial statements to be misleading or incomplete. The component units' column of the basic financial statements includes the financial data of the following major component units:

Pohnpei Utilities Corporation (PUC): PUC was created by Pohnpei State Public Law (PSPL) No. 2L-179-91 and is responsible for providing electrical, water and sewer services to the people of Pohnpei through the operation of the electric power, water and sewer systems. PUC is governed by a seven-member Board of Directors appointed by the Governor with the advice and consent of the Legislature.

Pohnpei Port Authority (PPA): PPA was created by PSPL No. 2L-224-91 and is responsible for overseeing the use and maintenance of the State's sea and air ports. PPA is governed by a seven-member Board of Directors, consisting of representatives of the State appointed by the Governor.

Pohnpei Fisheries Corporation (PFC): PFC was created by PSPL No. 3L-28-93 and is responsible for the operation and management of the fish processing plant, boats owned by the plant and the cold storage facility. PFC is governed by a seven-member Board of Directors, consisting of representatives of the State appointed by the Governor.

Pohnpei Transportation Authority (PTA): PTA was created by PSPL No. 169-69 and is responsible for promotion, development, and improving transportation facilities of the State. PTA is governed by a seven-member Board of Directors, consisting of representatives of the State appointed by the Governor.

Small Business Guarantee and Finance Corporation (SBGFC): SBGFC was created by PSPL No. 3L-86-95 to provide, promote, develop and widen in both scope and services reach various alternative modes of financing for small enterprises, including, but not limited to, direct and indirect project lending, venture capital, financial leasing, secondary mortgage and rediscounting of loan papers to small businesses. SBGFC is governed by a seven-member Board of Directors, consisting of four representatives of the State and three representatives from the private sector appointed by the Governor.

Pohnpei Economic Development Authority (PEDA): PEDA was created by PSPL No. 4L-159-78 for the purpose of promoting economic development through expansion of agriculture, marine resources, tourism, industry, energy development, banking, transportation and community development in Pohnpei. PEDA is also designated to succeed the Ponape District Fishing Authority as the sole entity to promote, develop, and support commercial utilization of living marine resources as provided in Public Law No. 7-110 of the Trust Territory Code. PEDA is governed by a seven-member Board of Developers appointed by the Governor with the advice and consent of the Legislature.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

i. Discretely Presented Component Units, Continued

Pohnpei State Housing Authority (PSHA): 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 State's component units, departments, and funds that are separately audited issue their own financial statements. These statements may be obtained by directly contacting the various entities or obtaining them directly from the Office of the Public Auditor.

P.O. Box 370  
Kolonia, Pohnpei, FSM 96941

B. Government-Wide Financial Statements

The Statement of Net Assets and the Statement of Activities report financial information on all of the non-fiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been eliminated from these statements except for other charges between the primary government and the discretely presented component units. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Primary government activities are defined as either governmental or business-type activities. Governmental activities, which normally are supported by taxes, intergovernmental revenues and other non-exchange revenues, are reported separately from business-type activities, which rely to a significant extent on fees charged to external parties for goods or services. As such, business-type activities account for operations similarly to a for-profit business. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable. Discretely presented component unit activities are presented with their business-type focus.

The Statement of Net Assets presents all of the reporting entity's non-fiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt that are attributed to the acquisition, construction or improvement of those assets.
- Restricted net assets result when constraints placed on net asset use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements, Continued

- Unrestricted net assets consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, (for example, internally restricted), to indicate that management does not consider them to be available for general operations.

The government-wide Statement of Net Assets reports \$21,987,627 of restricted net assets, of which \$2,183,362 is restricted by enabling legislation.

The Statement of Activities demonstrates the degree to which the direct expenses of given functions or segments are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function or segment. Program revenues include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items not meeting the definition of program revenues are, instead, reported as general revenue.

C. Fund Financial Statements

The fund financial statements present a balance sheet and a statement of revenues, expenditures, and changes in fund balances for its major and aggregated non-major funds.

Major individual governmental funds are reported as separate columns in the fund financial statements pursuant to GASB reporting standards, with nonmajor governmental funds being combined into a single column.

The State reports its financial position and results of operations in funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures/expenses. Transactions between funds within a fund type, if any, have not been eliminated.

D. Measurement Focus and Basis of Accounting

The government-wide financial statements are reported using the economic resources management focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements account for the general governmental activities of the State and are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as they become susceptible to accrual; generally when they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

Significant revenues susceptible to accrual include income and gross revenue taxes, federal grants, federal reimbursements and other reimbursements for use of materials and services. Miscellaneous revenues from other financing sources are recognized when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available. Investments and related investment earnings are recorded at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Expenditures generally are recorded in the period in which the related fund liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Amounts reported as program revenue include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as general revenues rather than as program revenues. General revenue is derived from taxation, investment income and other fees that are not allocated to specific programs.

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

The State reports the following fund types:

1. Governmental Funds

i. General Fund

This fund is the primary operating fund of the State. It is used to account for all governmental transactions, except those required to be accounted for in another fund.

ii. Special Revenue Funds

These funds account for specific revenue sources that have been aggregated according to enabling legislation to support specific governmental activities.

iii. Debt Service Funds

These funds account for accumulation of resources, principally transfer from other funds, for the payment of long-term debt principal and interest.

iv. Capital Projects Funds

These funds account for the acquisition or construction of major the State capital facilities financed primarily from loans and federal reimbursements.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

1. Governmental Funds, Continued

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - For State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - Omnibus*, sets forth minimum criteria (percentage of the assets, liabilities, revenues or expenditures/expenses for either fund category or the governmental and enterprise combined) for the determination of major funds. Major individual governmental funds are reported as separate columns in the fund financial statements. The nonmajor funds are combined in a column in the fund financial statements and detailed in the combining statements. The State reports the following major funds:

U.S. Federal Grants Fund, a Governmental Fund Type - Special Revenue Fund. This fund accounts for all financial transactions of federally assisted funds, which are subgranted to the Pohnpei State Government, as well as other direct federal grants that the Pohnpei State Government received from the United States government.

Compact Capital Projects Fund, a Governmental Fund Type - Capital Projects Fund. This fund accounts for United States Congress appropriations under United States Public Law 99-239, Title 2, Article 1, Section 211(a)(1) and approved by FSM Congress. The aforementioned section requires no less than 40% of the total amounts appropriated by the United States Congress to be applied to the capital account.

E. Reporting Standards

As allowed by GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the State's proprietary funds follow all GASB pronouncements and those Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins that were issued on or before November 30, 1989, except those that conflict with a GASB pronouncement.

F. Cash and Cash Equivalents

The State pools cash resources of its various funds in order to facilitate the management of cash. Unless otherwise required by law, interest income received on pooled cash accrues to the General Fund. Cash and cash equivalents applicable to a particular fund are readily identifiable. Cash and cash equivalents include cash held in demand accounts as well as short-term investments with a maturity date within three months of the date acquired by the State. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified on the statement of net assets/balance sheet.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

G. Investments

Investments are recorded at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. 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.

H. Receivables

In general, tax revenue is recognized on the government-wide financial statements when assessed or levied and on the governmental fund financial statements to the extent that it is both measurable and available. Receivables in the State's governmental funds primarily consist of taxes and federal revenues. Federal receivables include those funds which are earned, primarily from FSM National Government administered federal grants, which have yet to be reimbursed by applicable grantor.

I. Advances and Prepaid Items

Prepayments represent amounts paid in advance to vendors. Certain advances and prepayments are offset by inclusion in a fund balance reserve account as they do not constitute expendable available resources and are therefore not available for appropriation.

J. Due From/To Other Funds

During the course of its operations, the State records transactions between individual funds for goods provided or services rendered. Receivables and payables resulting from transactions between funds are classified as "due from other funds" or "due to other funds" on the governmental fund balance sheet.

These balances result from time lag between the dates that 1) interfund goods and services are provided or reimbursable expenditures occur, 2) transactions are recorded in the accounting system, and 3) payments between funds are made, and are scheduled to be collected in the subsequent year.

K. Inventories

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

Inventories of the discretely presented component units are valued at the lower of cost (FIFO) or market

L. Restricted Assets

Certain assets of the primary government are classified as restricted assets because their use is completely restricted through enabling legislations and loan agreements. As of September 30, 2003, \$848,555 in cash and equivalents and \$3,248,887 were restricted for loan programs, capital improvement projects, and medical supplies in short-term investment.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

M. Capital Assets

Capital assets, which include property, plant, equipment and infrastructure (e.g. roads, bridges, ramps and other similar items), are reported in the applicable governmental or business-type activities columns of the government-wide financial statements. Singular pieces of equipment, vehicles, computer equipment and software that equal or exceed \$50,000 are capitalized as are individual pieces of equipment acquired with federal funds that equal or exceed \$5,000. Buildings and infrastructure projects with a cost that equals or exceeds \$100,000 are capitalized. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at fair market value at the date of donation.

Property, plant and equipment of the primary government, as well as the discretely presented component units, is depreciated, when assessed, using the straight-line method over the following estimated useful lives:

Buildings	50 years
Infrastructure – roads, and bridges	50 years
Machinery and equipment	3 - 20 years
Furniture and fixtures	3 - 10 years
Ships	25 years
Motor vehicles	3 years
Over-the-road vehicles	3 years

N. Interfund Transactions

As a general rule, the effect of interfund activity has been eliminated in the government-wide statements. Exceptions to this rule are: 1) activities between funds reported as governmental activities and funds reported as business-type activities and 2) activities between funds that are reported in different functional categories in either the governmental or business-type activities column. Elimination of these activities would distort the direct costs and program revenues for the functions concerned.

O. Compensated Absences

It is the government's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. There is no liability for unpaid accumulated sick leave since the government does not have a policy to pay any amounts when employees separate from service with the government. All vacation pay is accrued when incurred in the government-wide and fiduciary fund financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements. Annual leave accumulates at the rate of 4 hours biweekly, if less than 3 years of service, 6 hours biweekly, if between 3 and 10 years of service, and 8 hours biweekly if over 10 years of service, limited to 45 working days.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

P. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

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. In the accompanying combined balance sheet, reserves for related assets such as investments and advances are examples of the former. Reserves for encumbrances, contracts and continuing appropriations are examples of the latter.

Reserves for related assets as of September 30, 2003, are as follows:

	<u>General</u>	<u>Compact Capital Projects</u>	<u>Other Governmental Funds</u>	<u>Totals</u>
Receivables and advances	\$ 24,255	\$ -	\$ -	\$ 24,255
U.S. Federal Assistance fund deficit	158,828	-	-	158,828
Other Direct Assistance fund deficit	61,140	-	-	61,140
CFSM State Projects fund deficit	37,783	-	-	37,783
Public Land Trust fund deficit	82,993	-	-	82,993
Advances to PTA	554,762	-	-	554,762
Loan guarantee escrow fund and deficiency	-	792,600	-	792,600
Investment in Pacific Islands Development Bank	-	1,000,000	-	1,000,000
Receivable from Pohnpei Fisheries Corporation, a Component Unit – Proprietary Fund	-	2,450,000	-	2,450,000
Loan Receivable – FHA delinquent loan	-	94,697	-	94,697
Reserved for Early Retirement debt	<u>951,114</u>	<u>-</u>	<u>3,291,360</u>	<u>4,242,474</u>
	<u>\$ 1,870,875</u>	<u>\$ 4,337,297</u>	<u>\$ 3,291,360</u>	<u>\$ 9,499,532</u>

Q. Risk Financing

The State is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. It is the policy of the primary government not to purchase commercial insurance for the risks of loss to which it is exposed. Instead, the State management believes it is more economical to manage its risks internally. In the event of claim settlements and judgments, the State reports all of its risk management activities in its General Fund. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

R. Reclassification and Restatements

During fiscal 2003, the State implemented GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - For State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - Omnibus*, establishes new financial reporting standards for state and local governments. The requirements of this statement result in a significant change in the financial reporting model used by governments, including statement formats and changes in fund types. In addition to the traditional fund financial statements, governments are required to report government-wide financial statements, prepared using the accrual basis of accounting and the economic resources measurement focus. As a result, fund reclassifications and adjustments to the fund equities reported in the prior financial statements were required.

In addition, the State implemented the following new accounting standards issued by GASB:

GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, amends certain note disclosures and adds additional note disclosure requirements related to GASB Statement Nos. 34, 35 and 37.

GASB Statement No. 41, *Budgetary Comparison Schedules - Perspective Differences*, amends required supplemental information disclosure of adopted budget and actual amounts per GASB Statement No. 34. Should there be a perspective difference between these amounts and fund perspective revenues and expenditures, reconciliation is required.

Due to the implementation of GASB Statement Nos. 34, 35 and 37, the beginning net assets of the governmental activities in the statement of net assets have been restated. Fund balances of the governmental funds at September 30, 2002 (as disclosed below) were increased by \$12,082,769 for the cumulative effect of these changes on years prior to fiscal year 2003:

The effect of those items is as follows:

Fund balances reported as of September 30, 2002	\$ 25,531,128
Adjustments:	
Long-term debt payable	(4,200,000)
Accrued litigation/claims payable	(400,000)
Compensated absences payable	(527,330)
Capital assets	27,308,861
Accumulated depreciation	<u>(10,098,761)</u>
	<u>12,082,769</u>
Beginning net assets as of September 30, 2002	\$ <u>37,613,897</u>

Due to the implementation of GASB Statement No. 34, certain governmental funds have been reclassified to conform with the GASB Statement No. 34 reporting model. The effects of such are as follows:

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

R. Reclassification and Restatements, Continued

	September 30, 2002 As Previously Reported	Fund Reclassifications	Adjustments	September 30, 2002 As Restated
<u>Governmental Funds and Activities</u>				
Major governmental funds:				
General Fund	\$ 5,641,341	\$ -	\$ -	\$ 5,641,341
Previously reported as Special Revenue Funds:				
U.S. Federal Grants Fund	-	(158,828)	-	(158,828)
Previously reported as Capital Projects Funds:				
Section 211 Capital Account Fund	<u>-</u>	<u>9,210,879</u>	<u>-</u>	<u>9,210,879</u>
	<u>\$ 5,641,341</u>	<u>\$ 9,052,051</u>	<u>\$ -</u>	<u>\$ 14,693,392</u>
Nonmajor governmental funds:				
Special Revenue Funds	\$ 4,412,103	\$ -	\$ -	\$ 4,412,103
Previously reported as Special Revenue Funds:				
U.S. Federal Grants Fund	-	158,828	-	158,828
Previously reported as Expendable Trust Funds:				
Public Land Trust Fund	<u>-</u>	<u>(82,992)</u>	<u>-</u>	<u>(82,992)</u>
	<u>4,412,103</u>	<u>75,836</u>	<u>-</u>	<u>4,487,939</u>
Previously reported as Capital Projects Funds:				
Capital Projects Funds	12,585,198	-	-	12,585,198
Compact Capital Fund	<u>-</u>	<u>(9,210,879)</u>	<u>-</u>	<u>(9,210,879)</u>
	<u>12,585,198</u>	<u>(9,210,879)</u>	<u>-</u>	<u>3,374,319</u>
Previously reported as Debt Service Funds:				
Debt Service Fund	<u>2,975,478</u>	<u>-</u>	<u>-</u>	<u>2,975,478</u>
Previously reported as Expendable Trust Funds:				
Expendable Trust Funds	(82,992)			(82,992)
Public Land Trust Fund	<u>-</u>	<u>82,992</u>	<u>-</u>	<u>82,992</u>
	<u>(82,992)</u>	<u>82,992</u>	<u>-</u>	<u>-</u>
	<u>\$ 19,889,787</u>	<u>\$ (9,052,051)</u>	<u>\$ -</u>	<u>\$ 10,837,736</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(1) Summary of Significant Accounting Policies, Continued

S. New Accounting Standards

In May 2002, GASB issued Statement No. 39, *Determining Whether Certain Organizations Are Component Units* (an amendment of GASB Statement 14), which provides additional guidance on GASB Statement No.14, in determining whether an entity should be reported as a component unit based on the nature and significance of its relationship with a primary government. The provisions of this Statement are effective for periods beginning after June 15, 2003. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In March 2003, GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3), which addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest risk, GASB Statement No. 40 requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. The provisions of this Statement are effective for periods beginning after June 15, 2004. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In June 2003, GASB issued Technical Bulletin No. 2003-1, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets*, which clarifies guidance on derivative disclosures, pending the results of the GASB's project on reporting and measurement of derivatives and hedging activities. This Technical Bulletin applies to derivatives that are not reported at fair value on the statement of net assets. The provisions of this Technical Bulletin are effective for periods beginning after June 15, 2003. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

T. Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

(2) Cash and Cash Equivalents and Investments

A. Deposit

As of September 30, 2003, the carrying amount of the primary government's total cash and cash equivalents were \$1,996,696 and the corresponding bank balances were \$4,258,390. Of the bank balance amounts, \$974,204 are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. Pohnpei State does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(2) Cash and Cash Equivalents and Investments, Continued

The State's demand and time deposits are non-categorized investments in accordance with GASB Statement No. 3.

Cash – Restricted (Medical Supplies Revolving)

As of September 30, 2003, \$88,943 was held in deposit with local banks for purchase of medical supplies for the state hospital.

Cash – Restricted (Early Retirement)

As of September 30, 2003, \$7,956 was held in deposit with local bank as a remaining loan proceeds of the \$4.2million Early Retirement loan with Asian Development Bank.

Cash - Restricted (Loan Guarantee Escrow Account-Capital Projects Fund)

The State Legislature appropriated a total of \$500,000 through a continuing appropriation for the sole purpose of loan collateralization made through the USDA Rural Development. The escrow account may be drawn down in the event of a borrower's default on the obligation under the terms of the promissory note and the deed of trust security instrument supporting such note and for which such note is guaranteed by the Pohnpei State Housing Authority, the trustee of the Loan Guarantee Escrow Account. During the year, the State accounted for the Escrow Account under the Compact Capital Fund. As of September 30, 2003, the escrow account has earned and reinvested \$10,147 of interest earnings. Therefore a total of \$510,147 has been reserved as restricted cash in the foregoing financial statements.

Cash - Restricted (TTPI Deficiency Fund-Capital Projects Fund)

As of September 30, 2003, the State had \$241,509 held in deposit with local banks for TTPI CIP Deficiency Projects. Funds can only be used for renovation of the Pohnpei International Airport and Pohnpei State Hospital. This deposit is recorded in the Compact Capital Fund.

As of September 30, 2003, the carrying amount of the discretely presented component units' total cash and cash equivalents were \$2,194,230 and the corresponding bank balances were \$3,143,665. Of the bank balance amounts, \$936,750 are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. The component units do not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized.

**B. 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 the accounting system and records necessary to account for investment funds placed with the Authority on behalf of Pohnpei State.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(2) Cash and Cash Equivalents and Investments, Continued

B. Investments, Continued

A. Investment managers may invest in stocks, bonds and cash equivalents. Minimum standards of quality for investments at the time of purchase are:

1. Stocks - A "B" rating by a national rating service. Non-rated or international 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 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:
  - 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 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 FSM 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.

GASB Statement No. 3 requires government entities to categorize investments in the following categories to give an indication of the level of risk assumed by the entity at year end.

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 other investments held by the State or Trustee have been classified as category 2 investments in accordance with GASB Statement No. 3 as all investments are held in the name of the Federated Development Authority.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(2) Cash and Cash Equivalents and Investments, Continued

Investments of the primary government and the discretely presented component units as September 30, 2003, are as follows:

	Categories			Carrying Value
	1	2	3	
Fixed income	\$ -	\$ 6,615,157		\$ 6,615,157
Mixed income	-	2,220,835	-	2,220,835
Corporate notes and bonds	-	1,069,360	-	1,069,360
U.S. Government agencies	-	890,624	-	890,624
U.S. Government notes and bonds	-	1,982,518	-	1,982,518
Common Stock	<u>1,000,000</u>	<u>750,587</u>	<u>-</u>	<u>1,750,587</u>
	\$ <u>1,000,000</u>	\$ <u>13,529,083</u>	\$ <u>-</u>	14,529,083
Money market funds				<u>8,945,286</u>
				<u>\$ 23,474,369</u>
 <u>Discretely Presented Component Units</u>				
Corporate notes and bonds	\$ -	\$ 106,000	\$ -	\$ 106,000
U.S. Government agencies	-	180,000	-	180,000
Common Stock	<u>-</u>	<u>216,000</u>	<u>-</u>	<u>216,000</u>
	\$ <u>-</u>	\$ <u>502,000</u>	\$ <u>-</u>	502,000
Money market funds				<u>22,000</u>
				<u>\$ 524,000</u>

a) Equity Investments

The State currently holds 21.5% of the shares of the Pacific Islands Development Bank, carried at a cost of \$1,000,000. The investment is recorded in the Compact Capital Projects 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. Since the investment is considered unavailable to finance expenditures for the ensuing fiscal year, the investment is reported in the reserve for related assets component of fund balance.

b) Component Unit Investments

During 1993, Pohnpei State Economic Development Authority (EDA), a component unit - proprietary fund, invested \$500,000 in the Bank of the Federated States of Micronesia. This investment is recorded at cost.

During fiscal year 1998, Pohnpei Utilities Corporation (PUC) established a sinking fund. The purpose of this fund is to finance future expansion and upgrade of the power plant and equipment. The goal of PUC is to build this fund to \$2,000,000 in anticipation of equipment purchases and upgrades. At September 30, 2003, the balance maintained within this sinking fund amounted to \$524,000, which is invested in various U.S. Government obligations, corporate bonds and other equity securities.

On August 21, 1998, Pohnpei State became a 100% owner of Caroline Fisheries Corporation through Pohnpei State Economic Development Authority, a component unit, to which the shares were issued to.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

**(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 in its role as the primary grant recipient of U.S. federal assistance programs, Congress of the Federated States of Micronesia public project grants, and U.S. Department of the Interior capital project grants through the Trust Territory Government and amounts due to the State under the FSM tax revenue sharing program:

	<u>General</u>	<u>U.S. Federal Grants</u>	<u>Compact Capital</u>	<u>Nonmajor</u>	<u>Total Primary Government</u>	<u>Component Units</u>
General receivables	\$ -	\$ -	\$ -	\$ -	\$ -	\$7,946,872
Less: allowance for doubtful accounts	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(3,157,251)</u>
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>-</u>	<u>-</u>	<u>\$4,789,621</u>
Other governments	\$ 1,213,634	\$ -	\$ -	\$964,155	\$2,177,789	\$ 48,375
Less: allowance for doubtful accounts	<u>-</u>	<u>-</u>	<u>-</u>	<u>(4,936)</u>	<u>(4,936)</u>	<u>-</u>
	<u>1,213,634</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$959,219</u>	<u>\$2,172,853</u>	<u>\$ 48,375</u>
Federal agencies	\$ -	\$1,245,390	\$ -	\$200,419	\$1,445,809	\$ -
Less: allowance for doubtful accounts	<u>-</u>	<u>(287,878)</u>	<u>-</u>	<u>(200,419)</u>	<u>(488,297)</u>	<u>-</u>
	<u>\$ -</u>	<u>\$ 957,512</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 957,512</u>	<u>\$ -</u>
Taxes and leases	\$2,034,943	\$ -	\$ -	\$ -	\$2,034,943	\$ -
Less: allowance for doubtful accounts	<u>(2,034,915)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(2,034,915)</u>	<u>-</u>
	<u>\$ 28</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 28</u>	<u>\$ -</u>
Advances	\$ 46,640	\$ 29,397	\$13,370	\$226,406	\$ 315,633	\$ 289,234
Less: allowance for doubtful accounts	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 46,640</u>	<u>\$ 29,397</u>	<u>\$13,370</u>	<u>\$226,406</u>	<u>\$ 315,633</u>	<u>\$ 289,234</u>
Loans	\$ -	\$ -	\$94,697	\$ -	\$ 94,697	\$3,525,592
Less: allowance for doubtful accounts	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ -</u>	<u>-</u>	<u>\$94,697</u>	<u>\$ -</u>	<u>\$ 94,697</u>	<u>\$3,525,592</u>
Interest	\$ 5,111	\$ -	\$ 434	\$ 3,928	\$ 9,473	\$ 7,386
Less: allowance for doubtful accounts	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 5,111</u>	<u>\$ -</u>	<u>\$ 434</u>	<u>\$ 3,928</u>	<u>\$ 9,473</u>	<u>\$ 7,386</u>

**(4) Due from Component Units**

Under its enabling legislation, Public Law 3L-28-93, Pohnpei Fisheries Corporation (PFC) is to pay back the portion of MTN funds used in its operations. The drawdown of these funds for operations at September 30, 2003, is \$2,450,000. As this balance does not represent a currently appropriable amount as of September 30, 2003, it is reserved against fund balance as a related asset.

As of September 30, 2003, the primary government advanced to Pohnpei Transportation Authority \$554,762.

Balances due from component units do not equal balances due to primary government, primarily due to a payable recorded by the Pohnpei Fisheries Corporation that was previously recorded by the Caroline Fisheries Corporation, wherein the State has written-off this receivable from its books.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(5) Fixed Assets

Capital asset activities for the year ended September 30, 2003, are as follows:

Primary Government

	Balance October <u>1, 2002</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2003</u>
Governmental activities:				
Buildings	\$ 9,762,223	\$ 263,452	\$ -	\$ 10,025,675
Infrastructure	14,021,443	336,827	-	14,358,270
Machinery, equipment, others	<u>3,525,195</u>	<u>98,894</u>	-	<u>3,624,089</u>
	<u>27,308,861</u>	<u>699,173</u>	-	<u>28,008,034</u>
Less accumulated depreciation:				
Buildings	(4,098,092)	(181,632)	-	(4,279,724)
Infrastructure	(4,293,955)	(666,266)	-	(4,960,221)
Machinery, equipment, others	<u>(1,706,714)</u>	<u>(656,777)</u>	-	<u>(2,363,491)</u>
	<u>(10,098,761)</u>	<u>(1,504,675)</u>	-	<u>(11,603,436)</u>
	<u>\$ 17,210,100</u>	<u>\$ (805,502)</u>	<u>\$ -</u>	<u>\$ 16,404,598</u>

Discretely Presented Component Units

	Balance October <u>1, 2002</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2003</u>
Electrical plant in service	\$ 36,231,424	\$ 163,900	\$ -	\$ 36,395,324
Building and improvements	13,320,890	570,884	-	13,891,774
Water and sewer plant in service	11,779,097	114,999	-	11,894,096
Fish processing plant	10,521,293	-	-	10,521,293
Land	2,776,034	-	-	2,776,034
Machinery and equipment	10,838,163	59,559	-	10,897,722
Vehicles	108,449	22,000	(4,600)	125,849
Furniture and fixtures	<u>64,266</u>	<u>2,000</u>	-	<u>66,266</u>
	85,639,616	933,342	(4,600)	86,568,358
Less accumulated depreciation	<u>(49,847,906)</u>	<u>(3,602,793)</u>	<u>115</u>	<u>(53,450,584)</u>
	35,791,710	(2,669,451)	(4,485)	33,117,774
Construction in progress	<u>3,210,235</u>	<u>1,075,973</u>	<u>(570,884)</u>	<u>3,715,324</u>
	<u>\$ 39,001,945</u>	<u>\$ (1,593,478)</u>	<u>\$ (575,369)</u>	<u>\$ 36,833,098</u>

During the year ended September 30, 2003, depreciation expense was charged as follows:

Education	\$ 226,270
Health	158,510
Public Safety	6,113
Resources and Development	255,080
Public Works	666,266
General	<u>192,435</u>
	<u>\$ 1,504,675</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(6) Contingencies and Commitments

Federal Program Questioned Costs

The State participates in a number of U.S. federally assisted programs. These programs are subject to financial and compliance audits to ascertain whether Federal laws and guidelines have been followed.

Currently, \$230,664 in questioned costs exist for the operation of fiscal year 1996 through 2002 grants. If these questioned costs are ultimately disallowed, the General Fund 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 general purpose financial statements.

Pursuant to Title I, Section 105 of United States Public Law 99-239, the Government of the Federated States of Micronesia (FSM) (which includes the State) 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.

Sick Leave

It is the policy of the State 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, 2003, was \$3,167,740.

Litigation

The State is party to numerous legal proceedings, many of which are normal recurrences in governmental operations. The State Attorney General of Pohnpei is of the opinion that the probable outcome of suits existing at September 30, 2003, is not predictable but could have a material impact on the accompanying financial statements. Such impact has currently been estimated to approximate \$721,682.

Risk Management

The State does not carry insurance to cover its potential risks and is thus substantially self-insured for all risks. Management is of the opinion that no material losses have been sustained as a result of this practice.

PUC Loans

As of September 30, 2003, Pohnpei Utilities Corporation, a Component Unit, has drawn \$2,118,767 on a note payable facilitated by an Asian Development Bank loan to the FSM. The loan is ultimately collateralized by a State pledge of Compact of Free Association revenues to the FSM National Government. The State has not imposed collateralization on PUC.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(7) Material Fund Deficits

The following presents material fund deficits as of September 30, 2003. If operations of these funds cannot recover prior losses, the State's General Fund may have to absorb these amounts or a portion thereof.

	<u>Fund Deficit</u>
<u>Major Governmental Funds:</u>	
Special Revenue Funds:	
U.S. Federal Assistance Fund	\$ <u>(158,828)</u>
<u>Nonmajor Governmental Funds:</u>	
Special Revenue Funds:	
Other Federal and Direct Assistance Fund	\$ <u>(61,140)</u>
CFSM State Projects Fund	\$ <u>(37,783)</u>
Early Retirement Fund	\$ <u>(15,613)</u>
Public Land Trust Fund	\$ <u>(48,535)</u>
Capital Projects Fund:	
TTPI CIP	\$ <u>(18,387)</u>

(8) Due to Primary Government

Due to Pohnpei State Government consists of \$2,450,000 borrowed under a medium-term note program and subgranted to Pohnpei Fisheries Corporation, noninterest bearing with repayments not to begin until the Corporation has accumulated retained earnings of at least \$2,000,000 (see note 4). In addition, Pohnpei Fisheries Corporation owes Pohnpei State Government \$979,793 for transfer of notes payable to Caroline Fisheries Corporation with no specific credit term.

As of September 30, 2003, Pohnpei Transportation Authority, a component unit owed Pohnpei State Government's General Fund \$554,762 (see note 4).

(9) Notes Payable

During fiscal year 1997, the State implemented an early retirement program for all eligible public service system employees. This program is funded through a \$4,200,000 loan from the Asian Development Bank (ADB) through the FSM National Government. There is a 1% service charge on the loan, but no interest is charged.

Pursuant to the terms of the financing agreement between the State and the FSM National Government, the State is required to deposit into the Early Retirement Scheme Trust Account (debt service fund) held in the name of the State within the FSM National Government's investment portfolio, 100% of the outstanding principal balance by September 30, 2002. Funds for the repayment of the loan are expected to be derived from annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The loan is to be repaid by the FSM National Government, through accessing the State's debt service fund, in semiannual installments commencing February 2008.

The ADB loan has a grace period of 10 years and no payments commence until February 2008. The future interest payments attendant to the maturing debt is not presented because the ADB loan is an interest free loan.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(9) Notes Payable, Continued

<u>Years Ending September 30,</u>	<u>Principal</u>
2004	\$ -
2005	-
2006	-
2007	-
2008	84,000
2009-2013	420,000
2014-2018	420,000
2019-2023	840,000
2024-2028	840,000
2029-2033	840,000
2034-2038	<u>756,000</u>
	<u>\$ 4,200,000</u>

Notes Payable – Component Units:

Pohnpei Utilities Corporation:

Payable to FSM Development Bank, interest at 9%, collateralized by the Corporation's assignment of restricted investment of \$602,000 to FSM Development Bank \$ 382,987

Amount drawn on a note payable with an available total of \$1,851,000 to the State, facilitated by an Asian Development Bank loan to the FSM, due in semi-annual principal installments commencing October 10, 2007. The loan is ultimately collateralized by a State pledge of Compact of Free Association revenues to the FSM National Government. The State has not imposed collateralization on the Corporation and has waived its rights to receive from PUC 6.82% in interest on the principal sum of the loan withdrawn and outstanding. 2,118,767

Pohnpei Port Authority:

Loan of \$264,600 from the FSM Development Bank, interest at 9%, due in monthly installments of principal and interest of \$5,493, collateralized by a chattel mortgage and an assignment of lease revenue. 12,542

Pohnpei Fisheries Corporation:

Notes payable to Pohnpei Economic Development Authority, uncollateralized and without interest, due in equal monthly installments beginning April 30, 1998 of \$20,000. 40,000

Notes payable to Federated State of Micronesia Development Bank (FSMDB), collateralized by the existing assets of the Corporation, due in monthly installments of \$4,655, with a 9% interest and a term of 4 years beginning June 2003, ending May 2007. 173,813

Notes payable to FSM National Government for amounts received under a conditional grant award, interest at 9% with no specified repayment term. 15,000

Total notes payable \$ 2,743,109

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(9) Notes Payable, Continued

Maturities of this debt are as follows:

<u>Years Ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 187,888	\$ 69,484	\$ 257,372
2005	164,194	50,271	214,465
2006	163,190	34,758	197,948
2007	154,195	23,664	177,859
2008	45,576	21,424	67,000
2009-2013	234,807	100,193	335,000
2014-2018	246,781	88,219	335,000
2019-2023	259,366	75,634	335,000
2024-2028	272,593	62,407	335,000
2029-2033	286,495	48,505	335,000
2034-2038	301,105	33,895	335,000
2039-2043	316,461	18,539	335,000
2044-2046	<u>110,458</u>	<u>3,429</u>	<u>113,887</u>
	<u>\$ 2,743,109</u>	<u>\$ 630,422</u>	<u>\$ 7,573,531</u>

Changes in non-current liabilities for the year ended September 30, 2003, are as follows:

	Balance October 1, 2002	Additions	Reductions	Balance September 30, 2003	Current	Noncurrent
Primary Government:						
ADB Early Retirement Fund	\$ 4,200,000	\$ -	\$ -	\$ 4,200,000	\$ -	\$ 4,200,000
Compensated absences	527,330	272,377	-	799,707	392,125	407,582
Claims and litigation payable	<u>400,000</u>	<u>321,682</u>	-	<u>721,682</u>	-	<u>721,682</u>
	<u>5,127,330</u>	<u>594,059</u>	-	<u>5,721,389</u>	<u>392,125</u>	<u>5,329,264</u>
Component Units:						
Pohnpei Utilities Corporation						
-FSMDB Loan	462,426	-	(79,439)	382,987	94,486	288,501
-ADB Loan	1,651,676	467,091	-	2,118,767	-	2,118,767
Pohnpei Port Authority	66,860	-	(54,318)	12,542	12,542	-
Pohnpei Fisheries Corporation						
-FSMDB Loan		173,813	-	173,813	25,860	147,953
-EDA	40,000	-	-	40,000	40,000	-
-FSM National	<u>15,000</u>	-	-	<u>15,000</u>	<u>15,000</u>	-
	<u>2,235,962</u>	<u>640,904</u>	<u>(133,757)</u>	<u>2,743,109</u>	<u>187,888</u>	<u>2,555,221</u>
	<u>\$ 7,363,292</u>	<u>\$ 1,234,963</u>	<u>\$ (133,757)</u>	<u>\$ 8,464,498</u>	<u>\$ 580,013</u>	<u>\$ 7,884,485</u>

(10) Interfund Receivables and Payables

Receivables and payables between funds reflected as due to/from other funds in the combined balance sheet at September 30, 2003, are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
Compact Capital Projects	General	\$ 2,433,834
Nonmajor governmental funds	General	5,316,800
General	Compact Capital Projects	726,193
General	U.S. Federal Grants	985,616
General	Nonmajor governmental funds	<u>1,039,169</u>
		<u>\$ 10,501,612</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(11) Continuing Appropriations

Continuing appropriations as of September 30, 2003, are summarized as follows:

General Fund

Each fiscal year, the Pohnpei State Legislature appropriates funds for various programs, municipal projects and other projects which are available until fully expended or project completion. \$ 2,669,359

Compact Capital Projects Fund

Each fiscal year, the Pohnpei State Legislature appropriates funds for capital projects and economic development projects. \$ 8,808,783

NonMajor Governmental Funds

Each fiscal year, the Pohnpei State Legislature appropriates funds for various programs and other projects. \$ 1,048,194

(12) Self-Insurance Fund - Component Units

In accordance with section 2(5) of State Law 3L-41-93, an amendment was made to the original enabling legislation for Pohnpei Utilities Corporation (PUC), a component unit - proprietary fund, establishing a self-insurance fund to defray costs of any unforeseen accidents or disasters. The funds are accumulated in a restricted self-insurance fund, held by a trustee, in the name of PUC. No other insurance is maintained by PUC.

Pohnpei Port Authority and Pohnpei Fisheries Corporation purchase insurance to cover workmen's compensation and life insurance risks. Both entities are substantially self-insured for all other risks. Management of both entities are of the opinion that no material losses have been sustained as a result of this practice.

Pohnpei Transportation Authority does not purchase commercial insurance covering potential risks. Management of those entities represent that no material losses have been sustained as a result of this practice during the last three years.

(13) FSM Development Bank Loan Funds

Compact Capital Account funds in an aggregate amount of \$1.7 million were transferred to the control of the FSM Development Bank (FSMDB) (a component unit of the FSM National Government) to be loaned out to borrowers from Pohnpei State mainly for economic development projects. The loan fund is administered by FSMDB in a Trust capacity. All loan decisions are made by management of the State. These loans are not controlled by the State and are not currently recorded in the accompanying general purpose financial statements. As of December 31, 2003 (FSMDB fiscal year end), the outstanding fund balance aggregated \$719,915.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements  
September 30, 2003

(14) Other Payables

The State has recorded liabilities of \$1,612,043 to Municipal Governments for revenue sharing required under the State Constitution, and for other payables to vendors, all of which relate to 1996 and prior years.

This balance was reversed to income in fiscal year 2004 due to the receipt of an Attorney General opinion that indicates that the State was no longer liable for this obligation.

(15) Reconciliation of Opening Fund Balance

Component Units – Proprietary Fund

Retained earnings, beginning of year, as previously reported	\$ 40,721,767
Inclusion of Pohnpei Fisheries Corporation	(2,604,698)
Inclusion of Pohnpei Transportation Authority	906,514
Inclusion of Economic Development Authority	194,470
Inclusion of Pohnpei Housing Authority	3,785,190
Prior period adjustment relative to depreciation expense recorded by the Pohnpei Port Authority	<u>214,957</u>
Retained earnings, beginning of year, as reported in the accompanying financial statements	\$ <u>43,218,200</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

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**REQUIRED SUPPLEMENTARY INFORMATION-  
OTHER THAN MANAGEMENT'S DISCUSSION AND ANALYSIS**

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**YEAR ENDED SEPTEMBER 30, 2003**

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Revenues, Expenditures and Changes in Unreserved Deficit  
Budget and Actual, Budgetary Basis - General Fund  
Year Ended September 30, 2003

	Budgeted Amount		Actual - Budgetary Basis	Variance Favorable (Unfavorable)
	Original	Final		
Revenues:				
Compact	\$ 11,414,932	\$ 11,414,932	\$ 11,237,118	\$ (177,814)
Local revenues	6,943,000	6,943,000	6,580,162	(362,838)
Net increase (decrease) in the fair value of investments	<u>225,000</u>	<u>225,000</u>	<u>839,435</u>	<u>614,435</u>
Total revenues	<u>18,582,932</u>	<u>18,582,932</u>	<u>18,656,715</u>	<u>73,783</u>
Expenditures:				
General government	4,519,454	4,502,226	8,635,775	(4,133,549)
Health services	3,779,241	3,815,349	3,466,920	348,429
Education	3,362,045	3,532,046	3,411,198	120,848
Public safety	1,060,795	1,060,121	1,026,158	33,963
Resources and development	562,286	504,265	422,831	81,434
Public Works	646,938	646,913	593,277	53,636
Boards, commissions and other external appropriations	863,940	863,940	826,233	37,707
Municipal governments	<u>2,040,000</u>	<u>2,066,753</u>	<u>2,067,245</u>	<u>(492)</u>
Total expenditures, budgetary basis	<u>16,834,699</u>	<u>16,991,613</u>	<u>20,449,637</u>	<u>(3,614,938)</u>
Excess (deficiency) of revenues over (under) expenditures	<u>1,748,233</u>	<u>1,591,319</u>	<u>(1,792,922)</u>	<u>(3,541,155)</u>
Unreserved deficit at beginning of year	(1,833,200)	(1,833,200)	(1,833,200)	-
Other changes in unreserved fund deficit:				
Decrease in reserve for related assets	-	-	4,869,042	4,869,042
Increase in reserve for continuing appropriation	<u>-</u>	<u>-</u>	<u>(2,572,019)</u>	<u>(2,572,019)</u>
Unreserved deficit at end of year	<u>\$ (84,967)</u>	<u>\$ (241,881)</u>	<u>\$ (1,329,099)</u>	<u>\$ (1,244,132)</u>

See accompanying notes to required supplementary information - budgetary reporting.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting  
September 30, 2003

(1) Budgetary Information

The Governor presents to the Pohnpei State Legislature, prior to September 30, proposed budget estimates for the fiscal year commencing October 1. The budget estimates include the overall and total proposed expenditures of the State and the means of financing those expenditures. The Pohnpei State Legislature reviews and approves these estimates making changes, as it deems appropriate. The Appropriation Committee of the Pohnpei State Legislature, during the regular session of the Pohnpei State Legislature, holds public hearings at which time Departments and Offices are required to justify their budget estimates. During the regular session of the Pohnpei State Legislature, an appropriation bill, as required by the Constitution, is introduced and budget estimates are then legally enacted by the Pohnpei State Legislature.

Formal budget integration is employed as a management control device during the year for all funds. The Pohnpei State Legislature has the authority to reprogram budgeted estimates in accordance with the Constitution. All annual appropriations lapse at fiscal year end unless otherwise specified by law. Supplemental appropriations may occur throughout the year. Unexpended encumbrances at each fiscal year end are carried forward until they are expended or canceled without further legislative action. The State does not establish budgets for the operations of its other governmental funds.

Accounting principles used in developing data on a budgetary basis differ from those used in preparing the basic financial statements in conformity with GAAP. Amounts included on the Statement of Revenues, Expenditures, and Changes in Deficit - Budget and Actual - General Fund (which are presented on a non-GAAP budgetary basis) are reconciled to unreserved deficit of the Governmental Fund Balance Sheet within the other changes in unreserved deficit section of that statement.

Encumbrance accounting is employed in governmental funds. For budgetary purposes, the encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP reporting purposes, encumbrances outstanding at year end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be reappropriated and honored during the subsequent fiscal year.

For the year ended September 30, 2003, expenditures of the General Fund exceeded budget at the program area level (i.e., the legal level of budgetary control) as follows:

<u>Program Area</u>	<u>Excess</u>
Office of the Governor	\$ 68,529

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

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**OTHER SUPPLEMENTARY INFORMATION**

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**YEAR ENDED SEPTEMBER 30, 2003**

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account  
Governmental Funds  
Year Ended September 30, 2003

	General	Special Revenue	Capital Projects	Other Governmental Funds	Total
		U.S Federal Grants	Compact Capital Account		
Expenditures:					
Personnel	\$ 11,355,059	\$ 1,235,979	\$ 43,254	\$ 2,600,653	\$ 15,234,945
Travel	210,781	316,509	58,284	131,137	716,711
Capital asset purchases	125,038	345,063	99,253	294,818	864,172
Contractual services, contributions and subsidies	310,724	885,312	2,813,198	1,702,782	5,712,016
Professional services	29,651	2,050	-	-	31,701
Communications	144,311	30,070	-	24,253	198,634
Supplies and materials	266,912	371,111	8,364	659,661	1,306,048
Printing and reproduction	52,278	12,345	6,315	27,214	98,152
Freight	32,312	-	100	-	32,412
Office/house rent/lease	13,200	-	-	-	13,200
Repairs and rental services	78,794	28,896	3,030	18,920	129,640
Housing allowance	35,135	-	-	-	35,135
Meeting allowance	20,345	-	-	-	20,345
Official allowance	115,000	2,050	-	-	117,050
Compensation-nonpayroll	-	396,326	-	-	396,326
Scholarships	-	-	-	357,238	357,238
Utilities	5,057	5,528	-	773,799	784,384
POL	7,296	38,600	497	257,002	303,395
Insurance and fees	48,756	-	-	-	48,756
Dues, memberships and subscriptions	15,131	-	-	-	15,131
Food	173,645	47,016	700	150,358	371,719
Medical referral/Medical services	-	-	-	230,291	230,291
Medical supplies	746,218	1,619	-	-	747,837
Bad debt	2,858,039	-	-	1,088,571	3,946,610
Other	3,725,809	105,501	90,476	326,160	4,247,946
	<u>\$ 20,369,491</u>	<u>\$ 3,823,975</u>	<u>\$ 3,123,471</u>	<u>\$ 8,642,857</u>	<u>\$ 35,959,794</u>

See Accompanying Independent Auditors' Report

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND**

Statement of Revenues, Expenditures by Function and Department and Changes in Fund Balance  
Year Ended September 30, 2003  
(With comparative totals for the year ended September 30, 2002)

	2003	2002
Revenues:		
State taxes and licenses:		
FSM revenue sharing	\$ 4,099,471	\$ 5,219,889
Beer, malt beverages and tobacco	383,553	451,879
Motor vehicle sales tax	102,947	77,671
General merchandise sales tax	1,555,204	1,488,671
Hotel	65,576	63,484
Petroleum and fuel	1,532	367
Use tax	327	-
Others	45,840	68,106
Compact of Free Association:		
Base grant	7,112,100	7,112,100
Inflation adjustment	4,125,018	4,125,018
Net decrease in the fair value of investments		11,237,118
Interest income		839,435
Fines and penalties		-
Public service charges:		13,242
Transportation		292,773
Other		24,186
		54,746
Total revenues	18,656,715	18,656,015
Expenditures:		
General Government:		
Executive and Support	1,954,412	2,455,442
Department of Treasury and Administration	5,162,867	848,250
Legislative operations	1,398,918	1,455,679
Judiciary	314,592	374,592
Public Auditor	205,308	187,291
Total General Government	9,036,097	5,321,254
Department of Education:		
Administration	315,129	293,594
Preschool and elementary	2,972,681	3,718,436
Aid to non-public school	75,000	75,020
PICS supper and weekend meals	-	500
Total Education	3,362,810	4,087,550
Department of Health Services:		
Administration	345,332	306,730
Medical Coordinator-Honolulu	44,714	42,041
Medical services	1,467,846	1,328,965
Dental services	235,885	238,156
Medical supplies	179,823	146,827
Primary health care	372,493	509,091
Hemodialysis	102,085	108,359
Hospital buildings & grounds	55,417	59,921
Hospital food	117,235	109,515
Outer island referral program	(139)	(130)
Health service pharmaceutical supplies	516,048	456,362
Total Health Services	3,436,739	3,305,837
Department of Land and Natural Resources:		
Office of the Director	51,027	37,608
Division of Resource Management & Development	-	(130)
Surveys and mapping	157,404	144,495
Historic and preservation	59,719	57,477
Forestry and marine conservation	121,687	86,693
Management and administration/public land	51,443	44,009
Total Land and Natural Resources	441,280	370,152

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

**GENERAL FUND**

Statement of Revenues, Expenditures by Function and Department and Changes in Fund Balance, Continued  
Year Ended September 30, 2003  
(With comparative totals for the year ended September 30, 2002)

	2003	2002
Expenditures, continued:		
Department of Public Safety:		
Office of Director	82,283	72,131
Division of police and security	744,274	751,769
Correction and rehabilitation	193,905	159,297
Search and rescue	5,298	5,707
	1,025,760	988,904
Total Public Safety		
Boards, Commissions, and Other Appropriations:		
2nd Micronesian Trading Leadership Conference	(64)	39,224
Pohnpei Ethics Commission	140	-
Pohnpei Public Land Trustee	21,561	-
Foreign investment commission	58,983	50,455
Micronesia Legal Services Corporation	38,280	35,280
USDA Rural Development	97,169	96,087
Alms fund	4,694	13,826
Kapinga emergency relief	12,935	20,400
Contract review board	-	5,426
Pohnpei public library	49,464	39,378
Environmental protection agency	151,233	137,255
Pohnpei health care plan board	9,243	-
Planning and zoning committee	13,457	16,859
Economic planning committee	54,625	49,802
Pohnpei broadcasting corporation	145,631	114,317
Sports development program	4,878	18,247
Pohnpei leadership conference	(500)	-
Pohnpei land commission	180,674	162,222
Food relief assistance	-	37,229
Pohnpei Visitors Bureau	59,580	35,590
Pohnpei CHC Tele. Med. Program	-	2,000
Others	-	41
	901,983	873,638
Total Boards, Commissions, and Other Appropriations		
Municipal Governments:		
Kitti	369,449	361,299
Sokehs	368,380	340,962
Madolenihmw	345,011	338,928
Nett	244,889	244,370
Kolonia	226,028	221,043
Uh	209,155	187,545
Pingelap	104,598	110,796
Kapingamarangi	61,025	59,678
Sapwuahfik	52,635	51,524
Mwoakilloa	75,961	45,163
Nukuoro	9,843	38,500
	2,066,974	1,999,808
Total Municipal Governments		
Payments to component units		
Pohnpei State Housing Authority	3,198	95,600
Small Business Guarantee & Finance Corp	70,560	74,843
Pohnpei Economic Development Authority	24,090	21,789
	97,848	192,232
Total component units		
Total expenditures	20,369,491	17,139,375
Excess (deficiency) of revenues over (under) expenditures	(1,712,776)	1,516,640
Fund balance at beginning of year	5,641,341	4,124,701
Fund balance at end of year	\$ 3,928,565	\$ 5,641,341

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Combined Balance Sheet  
Nonmajor Governmental Funds  
September 30, 2003

	<u>Other Special Revenue</u>	<u>Other Debt Services and Capital Projects</u>	<u>Total</u>
<b><u>ASSETS</u></b>			
Investments	\$ 2,592,853	\$ -	\$ 2,592,853
Receivables, net:			
Other governments	493,030	466,189	959,219
Advances	226,406	-	226,406
Interest	3,928	-	3,928
Due from other funds	2,245,120	3,071,680	5,316,800
Inventories	43,100	-	43,100
Restricted assets:			
Investments	-	3,248,887	3,248,887
	<u>                    </u>	<u>                    </u>	<u>                    </u>
Total assets	<u>\$ 5,604,437</u>	<u>\$ 6,786,756</u>	<u>\$ 12,391,193</u>
<b><u>LIABILITIES AND FUND BALANCES</u></b>			
Liabilities:			
Accounts payable	\$ 242,234	\$ 4	\$ 242,238
Other liabilities and accruals	176,241	-	176,241
Due to other funds	1,020,784	18,385	1,039,169
	<u>                    </u>	<u>                    </u>	<u>                    </u>
Total liabilities	<u>1,439,259</u>	<u>18,389</u>	<u>1,457,648</u>
Fund balances:			
Reserved for:			
Related assets	-	3,291,360	3,291,360
Encumbrances	449,333	365,226	814,559
Continuing appropriations	37,175	1,011,019	1,048,194
Compact Special Block	191,236	-	191,236
Other Compact Grants	1,696,269	-	1,696,269
Unreserved, reported in:			
Special revenue funds	1,791,165	-	1,791,165
Capital projects funds	-	2,100,762	2,100,762
	<u>                    </u>	<u>                    </u>	<u>                    </u>
Total fund balances	<u>4,165,178</u>	<u>6,768,367</u>	<u>10,933,545</u>
	<u>                    </u>	<u>                    </u>	<u>                    </u>
Total liabilities and fund balances	<u>\$ 5,604,437</u>	<u>\$ 6,786,756</u>	<u>\$ 12,391,193</u>

See Accompanying Independent Auditors' Report

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Combined Statement of Revenues, Expenditures by Function, and Changes in Fund Balances  
Nonmajor Governmental Funds  
Year Ended September 30, 2003

	<u>Other Special Revenue</u>	<u>Other Debt Services and Capital Projects</u>	<u>Total</u>
Revenues:			
Revenue share taxes	\$ -	\$ 1,521,672	\$ 1,521,672
Compact	3,407,268	-	3,407,268
Compact inflation	541,330	-	541,330
FSM appropriations	173,171	-	173,171
Sales	53,541	-	53,541
Investment earnings	-	315,882	315,882
Other	2,725,802	-	2,725,802
	<hr/>	<hr/>	<hr/>
Total revenues	6,901,112	1,837,554	8,738,666
Expenditures by function:			
Current:			
General government	2,424,881	-	2,424,881
Education	3,260,554	-	3,260,554
Health	764,504	1,418,984	2,183,488
Public Safety	111,017	-	111,017
Public Works	526,537	-	526,537
Boards, Commission, Others	136,380	-	136,380
	<hr/>	<hr/>	<hr/>
Total expenditures	7,223,873	1,418,984	8,642,857
Net change in fund balances	(322,761)	418,570	95,809
Fund balances at the beginning of the year	4,487,939	6,349,797	10,837,736
	<hr/>	<hr/>	<hr/>
Fund balances at the end of the year	<u>\$ 4,165,178</u>	<u>\$ 6,768,367</u>	<u>\$ 10,933,545</u>

See Accompanying Independent Auditors' Report

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Combined Statement of Revenues, Expenditures by Account, and Changes in Fund Balances  
Nonmajor Governmental Funds  
Year Ended September 30, 2003

	Other Special Revenue	Other Debt Services and Capital Projects	Total
Revenues:			
Revenue share taxes	\$ -	\$ 1,521,672	\$ 1,521,672
Compact	3,407,268	-	3,407,268
Compact inflation	541,330	-	541,330
FSM appropriations	173,171	-	173,171
Sales	53,541	-	53,541
Investment earnings	-	315,882	315,882
Other	2,725,802	-	2,725,802
Total revenues	<u>6,901,112</u>	<u>1,837,554</u>	<u>8,738,666</u>
Expenditures by account:			
Personnel	2,600,653	-	2,600,653
Travel	131,137	-	131,137
Capital asset purchases	170,100	124,718	294,818
Contractual services, contributions and subsidies	652,482	1,050,300	1,702,782
Communications	24,253	-	24,253
Supplies and materials	432,981	226,680	659,661
Printing and reproduction	27,143	71	27,214
Repairs and rental services	18,920	-	18,920
Scholarships	357,238	-	357,238
Utilities	773,799	-	773,799
POL	257,002	-	257,002
Food	150,358	-	150,358
Medical referral-Medical services	230,271	20	230,291
Bad debt	1,088,571	-	1,088,571
Other	308,965	17,195	326,160
Total expenditures	<u>7,223,873</u>	<u>1,418,984</u>	<u>8,642,857</u>
Net change in fund balances	(322,761)	418,570	95,809
Fund balances at the beginning of the year	4,487,939	6,349,797	10,837,736
Fund balances at the end of the year	<u>\$ 4,165,178</u>	<u>\$ 6,768,367</u>	<u>\$ 10,933,545</u>

See Accompanying Independent Auditors' Report

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS  
SPECIAL REVENUE FUNDS  
Combining Balance Sheet  
Year Ended September 30, 2003

	Special Block Grant Section 221(b)	Compact Other Grants	Non US Assistance	CFSM State Projects	Agriculture Revolving	SVAP Revolving	Airport Operations	Recycling Revolving	Pave Road Maintenance	Medical Supplies Revolving	Health Care Premiums	V6AH Revolving	Environ. Quality	Early Retirement	Special Police Fee	Fishing Fines	Public Lands Trust Fund	Total
<b>ASSETS</b>																		
Investments	\$ 823,856	\$ 1,768,997	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,592,853
Receivables, net:																		
Other governments	-	347,448	14,150	131,432	-	-	-	-	-	-	-	-	-	-	-	-	-	493,030
Advances	3,003	54,995	67,858	85,052	-	-	2,142	-	-	-	-	1,546	1,134	-	-	-	10,676	226,406
Interest	-	-	-	3,928	-	-	-	-	-	-	-	-	-	-	-	-	-	3,928
Due from other funds	-	-	-	-	37,511	11,133	20,131	22,944	627,381	99,439	733,991	12,217	1,793	-	38,632	639,948	-	2,245,120
Inventory	-	-	-	-	43,100	-	-	-	-	-	-	-	-	-	-	-	-	43,100
Total assets	<u>\$ 826,859</u>	<u>\$ 2,171,440</u>	<u>\$ 82,008</u>	<u>\$ 220,412</u>	<u>\$ 80,611</u>	<u>\$ 11,133</u>	<u>\$ 22,273</u>	<u>\$ 22,944</u>	<u>\$ 627,381</u>	<u>\$ 99,439</u>	<u>\$ 733,991</u>	<u>\$ 13,763</u>	<u>\$ 2,927</u>	<u>\$ -</u>	<u>\$ 38,632</u>	<u>\$ 639,948</u>	<u>\$ 10,676</u>	<u>\$ 5,604,437</u>
<b>LIABILITIES AND FUND BALANCES</b>																		
<b>(DEFICITS)</b>																		
Liabilities:																		
Accounts payable	\$ 30,286	\$ 158,579	\$ 15,677	\$ 14,330	\$ 743	\$ 1,899	\$ -	\$ 45	\$ -	\$ 20,653	\$ -	\$ 22	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 242,234
Other liabilities and accruals	43,361	134,816	-	(1,936)	-	-	-	-	-	-	-	-	-	-	-	-	-	176,241
Due to other funds	481,407	91,281	127,471	245,801	-	-	-	-	-	-	-	-	-	15,613	-	-	59,211	1,020,784
Total liabilities	<u>555,054</u>	<u>384,676</u>	<u>143,148</u>	<u>258,195</u>	<u>743</u>	<u>1,899</u>	<u>-</u>	<u>45</u>	<u>-</u>	<u>20,653</u>	<u>-</u>	<u>22</u>	<u>-</u>	<u>15,613</u>	<u>-</u>	<u>-</u>	<u>59,211</u>	<u>1,439,259</u>
Fund balances (deficits):																		
Reserved for:																		
Encumbrances	80,569	90,495	1,488	183,891	11,254	1,170	-	-	18,045	44,378	-	9,064	1,668	-	-	5,086	2,225	449,333
Continuing appropriations	-	-	-	-	-	-	-	-	37,175	-	-	-	-	-	-	-	-	37,175
Compact Special Block	191,236	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	191,236
Compact Other Grants	-	1,696,269	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1,696,269
Unreserved (deficit)	-	-	(62,628)	(221,674)	68,614	8,064	22,273	22,899	572,161	34,408	733,991	4,677	1,259	(15,613)	38,632	634,862	(50,760)	1,791,165
Total fund balances (deficits)	<u>271,805</u>	<u>1,786,764</u>	<u>(61,140)</u>	<u>(37,783)</u>	<u>79,868</u>	<u>9,234</u>	<u>22,273</u>	<u>22,899</u>	<u>627,381</u>	<u>78,786</u>	<u>733,991</u>	<u>13,741</u>	<u>2,927</u>	<u>(15,613)</u>	<u>38,632</u>	<u>639,948</u>	<u>(48,535)</u>	<u>4,165,178</u>
Total liabilities and fund balances	<u>\$ 826,859</u>	<u>\$ 2,171,440</u>	<u>\$ 82,008</u>	<u>\$ 220,412</u>	<u>\$ 80,611</u>	<u>\$ 11,133</u>	<u>\$ 22,273</u>	<u>\$ 22,944</u>	<u>\$ 627,381</u>	<u>\$ 99,439</u>	<u>\$ 733,991</u>	<u>\$ 13,763</u>	<u>\$ 2,927</u>	<u>\$ -</u>	<u>\$ 38,632</u>	<u>\$ 639,948</u>	<u>\$ 10,676</u>	<u>\$ 5,604,437</u>

See Accompanying Independent Auditors' Report

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS  
SPECIAL REVENUE FUNDS**  
Combining Statement of Revenues, Expenditures By Function, and Changes in Fund Balances (Deficits)  
Year Ended September 30, 2003

	Special Block Grant Section 221(b)	Compact Other Grants	Non U.S. Assistance	CFSM State Projects	Agriculture Revolving	SVAP Revolving	Airport Operations	Recycling Revolving	Pave Road Maintenance	Medical Supplies Revolving	Health Care Premiums	V6AH Revolving	Environ. Quality	Early Retirement	Special Police Fee	Fishing Fines	Public Land Trust Fund	Total
<b>Revenues:</b>																		
Compact	\$ 1,890,000	\$ 1,517,268	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,407,268
Compact Inflation	-	541,330	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	541,330
FSM appropriations	-	-	-	173,171	-	-	-	-	-	-	-	-	-	-	-	-	-	173,171
Sales	-	-	-	-	28,400	5,270	-	-	-	-	-	19,871	-	-	-	-	-	53,541
Other	-	50	172,029	-	-	-	-	-	249,420	277,844	130,175	-	3,500	-	44,756	725,000	1,123,028	2,725,802
<b>Total revenues</b>	<b>1,890,000</b>	<b>2,058,648</b>	<b>172,029</b>	<b>173,171</b>	<b>28,400</b>	<b>5,270</b>	<b>-</b>	<b>-</b>	<b>249,420</b>	<b>277,844</b>	<b>130,175</b>	<b>19,871</b>	<b>3,500</b>	<b>-</b>	<b>44,756</b>	<b>725,000</b>	<b>1,123,028</b>	<b>6,901,112</b>
<b>Expenditures by function:</b>																		
<b>Current:</b>																		
General government	-	1,069,526	41,920	72,434	23,341	9,224	-	-	-	-	-	20,929	9,102	4,782	-	85,052	1,088,571	2,424,881
Education	2,799,495	355,575	105,484	-	-	-	-	-	-	-	-	-	-	-	-	-	-	3,260,554
Health	37,161	430,596	24,625	-	-	-	-	-	-	272,122	-	-	-	-	-	-	-	764,504
Public Safety	-	-	-	24,822	-	-	-	-	-	-	-	-	-	-	86,195	-	-	111,017
Public Works	-	250,000	-	75,915	-	-	-	-	200,622	-	-	-	-	-	-	-	-	526,537
Boards, Commissions, Others	-	136,380	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	136,380
<b>Total expenditures</b>	<b>2,836,656</b>	<b>2,242,077</b>	<b>172,029</b>	<b>173,171</b>	<b>23,341</b>	<b>9,224</b>	<b>-</b>	<b>-</b>	<b>200,622</b>	<b>272,122</b>	<b>-</b>	<b>20,929</b>	<b>9,102</b>	<b>4,782</b>	<b>86,195</b>	<b>85,052</b>	<b>1,088,571</b>	<b>7,223,873</b>
Net change in fund balances (deficit)	(946,656)	(183,429)	-	-	5,059	(3,954)	-	-	48,798	5,722	130,175	(1,058)	(5,602)	(4,782)	(41,439)	639,948	34,457	(322,761)
<b>Fund balances (deficits) at the beginning</b>																		
of the year	1,218,461	1,970,193	(61,140)	(37,783)	74,809	13,188	22,273	22,899	578,583	73,064	603,816	14,799	8,529	(10,831)	80,071	-	(82,992)	4,487,939
<b>Fund balances (deficits) at the end of the year</b>	<b>\$ 271,805</b>	<b>\$ 1,786,764</b>	<b>\$ (61,140)</b>	<b>\$ (37,783)</b>	<b>\$ 79,868</b>	<b>\$ 9,234</b>	<b>\$ 22,273</b>	<b>\$ 22,899</b>	<b>\$ 627,381</b>	<b>\$ 78,786</b>	<b>\$ 733,991</b>	<b>\$ 13,741</b>	<b>\$ 2,927</b>	<b>\$ (15,613)</b>	<b>\$ 38,632</b>	<b>\$ 639,948</b>	<b>\$ (48,535)</b>	<b>\$ 4,165,178</b>

See Accompanying Independent Auditors' Report

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS  
SPECIAL REVENUE FUNDS  
Combining Statement of Revenues, Expenditures By Account, and Changes in Fund Balances (Deficits)  
Year Ended September 30, 2003**

	Special Block Grant Section 221(b)	Compact Other Grants	Non U.S. Assistance	CFSM State Projects	Agriculture Revolving	SVAP Revolving	Airport Operations	Recycling Revolving	Pave Road Maintenance	Medical Supplies Revolving	Health Care Premiums	V6AH Revolving	Environ. Quality	Early Retirement	Special Police Fee	Fishing Fines	Public Land Trust Fund	Total
<b>Revenues:</b>																		
Compact	\$ 1,890,000	\$ 1,517,268	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,407,268
Compact Inflation	-	541,330	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	541,330
FSM appropriations	-	-	-	173,171	-	-	-	-	-	-	-	-	-	-	-	-	-	173,171
Sales	-	-	-	-	28,400	5,270	-	-	-	-	-	19,871	-	-	-	-	-	53,541
Other	-	50	172,029	-	-	-	-	-	249,420	277,844	130,175	-	3,500	-	44,756	725,000	1,123,028	2,725,802
<b>Total revenues</b>	<b>1,890,000</b>	<b>2,058,648</b>	<b>172,029</b>	<b>173,171</b>	<b>28,400</b>	<b>5,270</b>	<b>-</b>	<b>-</b>	<b>249,420</b>	<b>277,844</b>	<b>130,175</b>	<b>19,871</b>	<b>3,500</b>	<b>-</b>	<b>44,756</b>	<b>725,000</b>	<b>1,123,028</b>	<b>6,901,112</b>
<b>Expenditures by account:</b>																		
Personnel	2,452,228	-	22,539	125,886	-	-	-	-	-	-	-	-	-	-	-	-	-	2,600,653
Travel	12,202	107,378	720	6,531	-	-	-	-	-	-	-	-	-	-	-	4,306	-	131,137
Capital asset purchases	-	-	20,727	12,267	2,091	1,403	-	-	-	-	-	8,038	4,952	-	82,432	38,190	-	170,100
Contractual services, contributions and subsidies	11,126	394,415	10,216	6,467	-	-	-	-	200,622	-	-	1,804	-	-	-	27,832	-	652,482
Communications	8,958	-	-	4,020	-	-	-	-	-	-	-	2,427	-	-	-	8,848	-	24,253
Supplies and materials	44,798	1,340	69,213	12,110	17,167	7,732	-	-	-	272,122	-	5,001	2,402	-	-	1,096	-	432,981
Printing and reproduction	-	-	25,567	-	-	-	-	-	-	-	-	-	1,576	-	-	-	-	27,143
Repairs and rental services	15,872	-	1,538	(103)	201	-	-	-	-	-	-	1,412	-	-	-	-	-	18,920
Scholarships	-	352,575	-	4,663	-	-	-	-	-	-	-	-	-	-	-	-	-	357,238
Utilities	-	759,615	14,184	-	-	-	-	-	-	-	-	-	-	-	-	-	-	773,799
POL	-	257,156	-	(326)	-	-	-	-	-	-	-	-	172	-	-	-	-	257,002
Food	146,473	-	4,324	(459)	-	-	-	-	-	-	-	20	-	-	-	-	-	150,358
Medical referral-Medical Services	-	230,271	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	230,271
Bad debt expense	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1,088,571	1,088,571
Other	144,999	139,327	3,001	2,115	3,882	89	-	-	-	-	-	2,227	-	4,782	3,763	4,780	-	308,965
<b>Total expenditures</b>	<b>2,836,656</b>	<b>2,242,077</b>	<b>172,029</b>	<b>173,171</b>	<b>23,341</b>	<b>9,224</b>	<b>-</b>	<b>-</b>	<b>200,622</b>	<b>272,122</b>	<b>-</b>	<b>20,929</b>	<b>9,102</b>	<b>4,782</b>	<b>86,195</b>	<b>85,052</b>	<b>1,088,571</b>	<b>7,223,873</b>
<b>Net change in fund balances (deficit)</b>	<b>(946,656)</b>	<b>(183,429)</b>	<b>-</b>	<b>-</b>	<b>5,059</b>	<b>(3,954)</b>	<b>-</b>	<b>-</b>	<b>48,798</b>	<b>5,722</b>	<b>130,175</b>	<b>(1,058)</b>	<b>(5,602)</b>	<b>(4,782)</b>	<b>(41,439)</b>	<b>639,948</b>	<b>34,457</b>	<b>(322,761)</b>
<b>Fund balances (deficits) at beginning of year</b>	<b>1,218,461</b>	<b>1,970,193</b>	<b>(61,140)</b>	<b>(37,783)</b>	<b>74,809</b>	<b>13,188</b>	<b>22,273</b>	<b>22,899</b>	<b>578,583</b>	<b>73,064</b>	<b>603,816</b>	<b>14,799</b>	<b>8,529</b>	<b>(10,831)</b>	<b>80,071</b>	<b>-</b>	<b>(82,992)</b>	<b>4,487,939</b>
<b>Fund balances (deficits) at end of year</b>	<b>\$ 271,805</b>	<b>\$ 1,786,764</b>	<b>\$ (61,140)</b>	<b>\$ (37,783)</b>	<b>\$ 79,868</b>	<b>\$ 9,234</b>	<b>\$ 22,273</b>	<b>\$ 22,899</b>	<b>\$ 627,381</b>	<b>\$ 78,786</b>	<b>\$ 733,991</b>	<b>\$ 13,741</b>	<b>\$ 2,927</b>	<b>\$ (15,613)</b>	<b>\$ 38,632</b>	<b>\$ 639,948</b>	<b>\$ (48,535)</b>	<b>\$ 4,165,178</b>

See Accompanying Independent Auditors' Report

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS - DEBT SERVICE AND CAPITAL PROJECTS FUNDS  
Combining Balance Sheet  
September 30, 2003

	Debt Services Fund	Capital Projects Fund Health and Education	OIA Capital Projects	Total
<b><u>ASSETS</u></b>				
Receivables, net:				
Other governments	\$ -	\$ 466,189	\$ -	\$ 466,189
Due from other funds	42,473	3,029,207	-	3,071,680
Restricted assets:				
Investments	3,248,887	-	-	3,248,887
	\$ 3,291,360	\$ 3,495,396	\$ -	\$ 6,786,756
 <b><u>LIABILITIES AND FUND BALANCES (DEFICITS)</u></b>				
Liabilities:				
Accounts payable	\$ -	\$ 2	\$ 2	\$ 4
Due to other funds	-	-	18,385	18,385
Total liabilities	-	2	18,387	18,389
Fund balances (deficits):				
Reserved for:				
Related assets	3,291,360	-	-	3,291,360
Encumbrances	-	364,492	734	365,226
Continuing appropriations	-	1,011,019	-	1,011,019
Unreserved	-	2,119,883	(19,121)	2,100,762
Total fund balances (deficits)	3,291,360	3,495,394	(18,387)	6,768,367
Total liabilities and fund balances	\$ 3,291,360	\$ 3,495,396	\$ -	\$ 6,786,756

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS - DEBT SERVICE AND CAPITAL PROJECTS FUNDS  
Combining Statement of Expenditures by Function, and Changes in Fund Balances (Deficit)  
Year Ended September 30, 2003

	Debt Services Fund	Capital Projects Fund Health and Education	OIA Capital Projects	Total
Revenues:				
Revenue share taxes	\$ -	\$ 1,521,672	\$ -	\$ 1,521,672
Investment earnings	315,882	-	-	315,882
Total revenues	315,882	1,521,672	-	1,837,554
Expenditures by function:				
Health	-	1,418,984	-	1,418,984
Total expenditures	-	1,418,984	-	1,418,984
Net change in fund balances (deficit)	315,882	102,688	-	418,570
Fund balances (deficit) at the beginning of the year	2,975,478	3,392,706	(18,387)	6,349,797
Fund balances (deficit) at the end of the year	\$ 3,291,360	\$ 3,495,394	\$ (18,387)	\$ 6,768,367

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS - DEBT SERVICE AND CAPITAL PROJECTS FUNDS  
Combining Statement of Expenditures by Account, and Changes in Fund Balances (Deficit)  
Year Ended September 30, 2003

	Debt Services Fund	Capital Projects Fund		Total
		Health and Education	OIA Capital Projects	
Revenues:				
Revenue share taxes	\$ -	\$ 1,521,672	\$ -	\$ 1,521,672
Investment earnings	315,882	-	-	315,882
<b>Total revenues</b>	<b>315,882</b>	<b>1,521,672</b>	<b>-</b>	<b>1,837,554</b>
Expenditures by account:				
Capital asset purchases	-	124,718	-	124,718
Contractual services, contributions and subsidies	-	1,050,300	-	1,050,300
Supplies and materials	-	226,680	-	226,680
Printing and reproduction	-	71	-	71
Food	-	20	-	20
Other	-	17,195	-	17,195
<b>Total expenditures</b>	<b>-</b>	<b>1,418,984</b>	<b>-</b>	<b>1,418,984</b>
Net change in fund balances (deficit)	315,882	102,688	-	418,570
Fund balances (deficit) at the beginning of the year	2,975,478	3,392,706	(18,387)	6,349,797
Fund balances (deficit) at the end of the year	<u>\$ 3,291,360</u>	<u>\$ 3,495,394</u>	<u>\$ (18,387)</u>	<u>\$ 6,768,367</u>

See Accompanying Independent Auditors' Report.

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

Honorable Johnny P. David  
Governor, State of Pohnpei  
Federated States of Micronesia:

We have audited the financial statements of the State of Pohnpei as of and for the year ended September 30, 2003, and have issued our report thereon dated September 30, 2005, which report was qualified due to 1) the inadequacy of accounting records regarding advances recorded within the aggregate remaining fund information and reserves for encumbrances recorded within each major fund and the aggregate remaining fund information; 2) our inability to determine the propriety of certain accounts payable and related expenses of the Pohnpei Port Authority; and 3) the inclusion of unaudited financial statements of the Pohnpei Economic Development Authority, the Pohnpei State Housing Authority, and the Pohnpei Transportation Authority. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

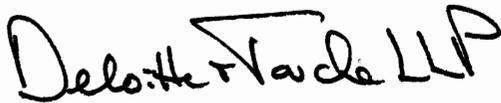
In planning and performing our audit, we considered the State of Pohnpei's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial 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 State of Pohnpei'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 (pages 71 through 82) as items 2003-4 through 2003-10.

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 2003-6 and 2003-7 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Pohnpei'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 no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

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

A handwritten signature in black ink that reads "Deloitte Touche LLP". The signature is written in a cursive, flowing style.

September 30, 2005

**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 Johnny P. David  
Governor, State of Pohnpei  
Federated States of Micronesia:

Compliance

We have audited the compliance of the State of Pohnpei 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, 2003. The State of Pohnpei's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs (pages 71 through 82). 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 Pohnpei's management. Our responsibility is to express an opinion on the State of Pohnpei'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; 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 Pohnpei'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 Pohnpei's compliance with those requirements.

As described in items 2003-1, 2003-2 and 2003-9, in the accompanying Schedule of Findings and Questioned Costs, the State of Pohnpei did not comply with requirements regarding procurement and suspension and debarment applicable to the Hospital Renovation Grant (CFDA #15.875); allowable costs/cost principles that are applicable to its Compact of Free Association, Section 211(a)(2) Capital Account (CFDA #15.875); and requirements regarding equipment and real property management for all Federal programs. Compliance with such requirements is necessary, in our opinion, for the State of Pohnpei to comply with requirements applicable to its federal award programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the State of Pohnpei 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, 2003.

## Internal Control Over Compliance

The management of the State of Pohnpei is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the State of Pohnpei'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.

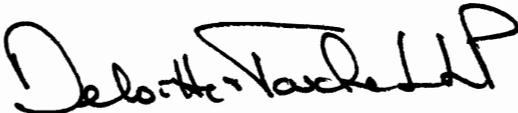
We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the State of Pohnpei's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 2003-1, 2003-2 and 2003-9.

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 the 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 none of the reportable conditions described above to be material weaknesses.

## Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of the State of Pohnpei as of and for the year ended September 30, 2003, and have issued our report thereon dated September 30, 2005, which report was qualified due to 1) the inadequacy of accounting records regarding advances recorded within the aggregate remaining fund information and reserves for encumbrances recorded within each major fund and the aggregate remaining fund information; 2) our inability to determine the propriety of certain accounts payable and related expenses of the Pohnpei Port Authority; and 3) the inclusion of unaudited financial statements of the Pohnpei Economic Development Authority, the Pohnpei State Housing Authority, and the Pohnpei Transportation Authority. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards (pages 62 through 67) is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of the management of the State of Pohnpei. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary due to the inadequacy of accounting records regarding advances, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

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



September 30, 2005

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Expenditures of Federal Awards, by Grantor  
Year Ended September 30, 2003

Agency/Program	CFDA#	Expenditures
U.S. Department of Agriculture		\$ 70,342
U.S. Department of the Interior		19,714,235
U.S. Department of Labor		524,064
Federal Emergency Management Agency		17,659
U.S. Department of Education		2,441,904
U.S. Department of Health and Human Services		495,093
 GRAND TOTAL		 <u>\$ 23,263,297</u>

Note: All awards are received in a subgrantee capacity through the FSM National Government, except for the following, which are received directly from the grantor agencies:

U.S. Department of Education:		
Freely Associated States Educational Grants	84.256A	
Twenty-First Century Community Learning Center	84.287	
Vocational Education Improvement Program	84.994	

Reconciliation to the basic financial statements:

U.S. Federal Grants Fund (page 14)	\$ 3,823,975
Compact Capital Projects Fund (page 14)	3,123,471
Compact Special Block Grant Section 221(b) Fund (page 52)	2,836,656
Compact Other Grants Fund (page 52)	2,242,077
Compact Current Account	<u>11,237,118</u>
	<u>\$ 23,263,297</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards  
Year Ended September 30, 2003

<u>Agency/Program</u>	<u>CFDA#</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF AGRICULTURE		
Cooperative Forestry Assistance	10.664	\$ <u>70,342</u>
U.S. DEPARTMENT OF AGRICULTURE TOTAL		\$ <u><u>70,342</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Year Ended September 30, 2003

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF THE INTERIOR		
Economic, Social and Political Development of the Territories and the Freely Associated States:	15.875	
Compact Current Account		\$ 11,237,118
Compact Capital Improvement Projects		3,123,471
Compact Energy Grants		1,069,526
Compact Health and Medical Grants		430,596
Compact Scholarship Grants		352,575
Compact Special Block Grants		2,836,656
Compact Special Development Grants		389,380
Technical Assistance:		
Hospital Renovation		123,510
Survey and Mapping		85,599
Y2K Remediation		44,342
Historic Preservation Fund Grants-In-Aid	15.904	<u>21,462</u>
U.S. DEPARTMENT OF THE INTERIOR TOTAL		<u><u>\$ 19,714,235</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Year Ended September 30, 2003

<u>Agency/Program</u>	<u>CFDA#</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF LABOR		
Job Training Partnership Act	17.250	\$ (962)
WIA Administration	17.255	42,712
WIA Adult Program	17.258	131,250
WIA Youth Activities	17.259	116,626
WIA Dislocated Worker	17.260	<u>234,438</u>
U.S. DEPARTMENT OF LABOR TOTAL		\$ <u><u>524,064</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Year Ended September 30, 2003

<u>Agency/Program</u>	<u>CFDA#</u>	<u>Expenditures</u>
FEDERAL EMERGENCY MANAGEMENT AGENCY		
Public Assistance Projects	83.516	\$ <u>17,659</u>
FEDERAL EMERGENCY MANAGEMENT AGENCY TOTAL		\$ <u><u>17,659</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Year Ended September 30, 2003

<u>Agency/Program</u>	<u>CFDA#</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF EDUCATION		
Special Education - Grants to States	84.027	\$ 1,049,343
Freely Associated Educational Grants	84.256A	446,608
Goals 2000	84.276	594
Twenty-First Century Community Learning Center	84.287	836,878
Vocational Education Improvement Program	84.994	<u>108,481</u>
U.S. DEPARTMENT OF EDUCATION TOTAL		<u><u>\$ 2,441,904</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Year Ended September 30, 2003

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES		
CDC Project Grants and Cooperative Agreements for Tuberculosis		
Control Programs	93.116	\$ 23,124
Hansen's Disease National Ambulatory Care Program	93.215	1,070
Family Planning - Services	93.217	46,219
Community Health Centers	93.224	99,423
Immunization Grants	93.268	66,180
CDC & Prevention-Investigations & Technical Assistance	93.283	7,828
HIV Care Project	93.917	2,960
HIV Prevention Activities-Health Department Based	93.940	9,285
Block Grants for Prevention and Treatment of Substance Abuse		
(Prevention and Treatment (SAPT) Block Grant)	93.959	123,756
Preventive Health Services - Sexually Transmitted Diseases		
Control Grants	93.977	9,684
Cooperative Agreements for State-Based Diabetes Control		
Programs and Evaluation of Surveillance Systems	93.988	10,296
Maternal and Child Health Services Block Grant to the States	93.994	<u>95,268</u>
 U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES TOTAL		 \$ <u><u>495,093</u></u>
 GRAND TOTAL		 \$ <u><u>23,263,297</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards  
Year Ended September 30, 2003

1. Scope of Review

The State of Pohnpei is one of the four States of the Federated States of Micronesia. 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 Single Audit.

A. Programs Subject to Single Audit

Schedules of expenditures of federal awards are presented for each federal program related to the following agencies:

- 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
- 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 accrual basis of accounting.

B. Reporting Entity

The State of Pohnpei, for purposes of the basic 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."

C. Subgrantees

Certain program funds are passed through the State to subgrantee organizations. The Schedule of Expenditures of Federal Awards does not contain separate schedules disclosing how the subgrantee outside of the State's control utilizes these funds.

D. Indirect Cost Allocation

The State does not receive any indirect cost allocation and does not charge indirect costs against federal programs.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards  
Year Ended September 30, 2003

3. Discretely Presented Component Units

The State of Pohnpei's component units separately satisfy the requirements of OMB Circular A-133. The following presents information concerning the respective component units.

Pohnpei Utilities Corporation

The Pohnpei Utilities Corporation is the recipient of various pass-through funds from State of Pohnpei. No material instances of noncompliance or questioned costs are presented in its audit reports. Following is the Schedule of Expenditures of Federal Awards for Pohnpei Utilities Corporation:

<u>Grantor</u>	<u>CFDA #</u>	<u>Total Authorization</u>	<u>Prior Years Expenditures</u>	<u>2003 Expenditures</u>	<u>Total Program Expenditures</u>
U.S. Department of the Interior:					
Office of Territorial and International Affairs:					
Operations and Maintenance Improvement					
Programs (OMIP):	15.875				
Pohnpei Power Generation and Distribution -					
Sixth Year – Apprenticeship training		\$ 60,000	\$ 52,345	\$ 7,655	\$ 60,000
Continuation of Prepaid Meter Program		250,000	250,000	-	250,000
Utility Development 2001		117,668	50,393	42,420	92,813
OMIP Bench		562,500	234,826	205,897	440,723
HR Development 2003		<u>12,500</u>	<u>-</u>	<u>7,380</u>	<u>7,380</u>
		<u>\$ 1,002,668</u>	<u>\$ 587,564</u>	<u>\$ 263,352</u>	<u>\$ 850,916</u>

The Schedule of Expenditures of Federal Awards for Pohnpei Utilities Corporation is prepared on the accrual basis of accounting.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Programs Selected For  
Audit in Accordance with OMB Circular A-133  
Year Ended September 30, 2003

<u>Grantor</u> <u>Program Title</u>	<u>CFDA No.</u>	<u>2003</u> <u>Fiscal Year</u> <u>Expenditures</u>
<u>U.S. Department of the Interior</u>		
Compact of Free Association:		
Section 211(A)(2) Capital Account	15.875	\$ 3,123,471
Section 216(A)(2) Compact Health & Medical	15.875	430,596
Section 212 Compact Special Development	15.875	389,380
Section 216(A)(3) Compact Scholarship	15.875	<u>352,575</u>
Total Major Programs Under CFDA # 15.875, excluding Compact Section 211 (A) Current Account expenditures		4,296,022
Hospital Renovation	15.875	<u>123,510</u>
Total Major Programs Under U.S. Department of the Interior		<u>4,419,532</u>
<u>U.S. Department of Education</u>		
Special Education Program	84.027	1,049,343
TFAS Educational Grant	84.256A	<u>446,608</u>
Total Major Programs Under U.S. Department of Education		<u>1,495,951</u>
<u>U.S. Department of Labor</u>		
WIA Cluster	17.258, 17.259 and 17.260	<u>482,314</u>
Total Major Programs Under U.S. Department of Labor		<u>482,314</u>
<u>U.S. Department of Health &amp; Human Services</u>		
Substance Abuse Program	93.959	<u>123,756</u>
Total Major Programs Under U.S. Department of Health & Human Services		<u>123,756</u>
Total U.S. Federal program expenditures selected, excluding Compact Section 211 (A) Current Account expenditures		\$ <u>6,521,553</u>
Total U.S. Federal program expenditures, excluding Compact Section 211 (A) Current Account expenditures		\$ <u>11,015,347</u>
% of total U.S. Federal expenditures covered by major programs, excluding Compact Section 211 (A) Current Account expenditures		<u>59%</u>

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs  
Year Ended September 30, 2003

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

1. The Independent Auditors' Report on the financial statements expressed a qualified opinion due to 1) the inadequacy of accounting records regarding advances recorded within the aggregate remaining fund information and reserves for encumbrances recorded within each major fund and the aggregate remaining fund information; 2) our inability to determine the propriety of certain accounts payable and related expenses of the Pohnpei Port Authority; and 3) the inclusion of unaudited financial statements of the Pohnpei Economic Development Authority, the Pohnpei State Housing Authority, and the Pohnpei Transportation Authority.
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 not disclosed by the audit.
4. Reportable conditions in internal control over compliance with requirements applicable to major federal award programs were identified, none of which are considered to be material weaknesses.
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	15.875
U.S. Department of the Interior – Hospital Renovation	15.875
U.S. Department of Education – Special Education Program	84.027
U.S. Department of Education - TFAS Educational Grant	84.256A
U.S. Department of Labor – WIA Cluster	17.258, 17.259 and 17.260
U.S. Department of Health & Human Services – Substance Abuse	93.959

8. A threshold of \$360,785 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>
2003-4	Bank reconciliation	\$ -
2003-5	Encumbrance	\$ -
2003-6	Travel Advance	\$ -
2003-7	General Receivables	\$ -
2003-8	Travel Advance	\$ -
2003-9	Equipment and Real Property Management	\$ -
2003-10	Insufficient Fund Bank Charges	\$ -

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

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

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>
2003-1	Procurement and Suspension and Debarment	\$ -
2003-2	Allowable Costs/Cost Principles	-
2003-9	Equipment and Real Property Management	-

**Part IV - Local Findings and Questioned Cost Section**

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>
2003-3	Unfunded Expenditures	\$ -
2003-4	Bank Reconciliation	-
2003-5	Encumbrance	-
2003-6	Travel Advance	-
2003-7	General Receivables	-
2003-8	Travel Advances	-
2003-9	Equipment and Real Property Management	-
2003-10	Insufficient Fund Bank Charges	-

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Federal Award Findings and Questioned Costs Section

Finding No.: 2003-1  
CFDA No.: 15.875 – Hospital Renovation Grant  
Grantor Agency: U.S. Department of the Interior  
Program/Area: Procurement and Suspension and Debarment  
Questioned Costs: \$0

Criteria: Federal procurement standards require that any procurement greater than the threshold be conducted in a manner providing full and open competition.

Condition: We found 4 instances from a sample of 7 transactions aggregating \$119,491 (out of a total population of \$123,510) where Pohnpei State did not follow applicable competitive procurement requirements.

<u>Contract</u>	<u>Voucher No.</u>	<u>Amount</u>	
C2060401	781169	17,157	Federal competitive bidding was superseded by a local procurement guideline disqualifying any bidder with unfinished construction work with the government from bidding
C2060401	782471	10,343	Federal competitive bidding was superseded by a local procurement guideline disqualifying any bidder with unfinished construction work with the government from bidding
C2060401	V30160	29,067	Federal competitive bidding was superseded by a local procurement guideline disqualifying any bidder with unfinished construction work with the government from bidding
C2060401	V30194	19,698	Federal competitive bidding was superseded by a local procurement guideline disqualifying any bidder with unfinished construction work with the government from bidding

Cause: The cause of this condition is that local procurement guidelines were used to limit competition since, as a result of the local guideline, only one submitting vendor qualified for the work.

Effect: The effect of this condition is noncompliance with federal procurement standards. However, no questioned costs result from this finding as the grantor agency has accepted the underlying costs as meeting grant intent.

Recommendation: We recommend that management ensure compliance with competitive procurement requirements.

Auditee Response and Corrective Action: The grantor agency resolved the questioned costs and therefore no other action is required. The Department of Treasury and Administration will ensure that the grantor agency's recommendation to follow the applicable competitive procurement will be strictly implemented. The Chief of Finance will provide copy of the grantor agency's letter to the Head of the Office of Transportation and Infrastructure for proper implementation of the competitive bidding.

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FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Federal Award Findings and Questioned Costs Section

Finding No.: 2003-2  
CFDA No.: 15.875 – Compact of Free Association, Section 211(a), Capital Account  
Grantor Agency: U.S. Department of the Interior  
Program/Area: Allowable Costs/Cost Principles  
Questioned Costs: \$0

Criteria: Compact funds should be expended in accordance with underlying terms and conditions of the treaty.

Condition: We were not able to determine how the following disbursement qualifies as a capital improvement project as such appears to be of a general operating nature.

<u>Doc. No.</u>	<u>Amount</u>	<u>Account</u>
V30259	\$80,000	6122-8399 Payment to U.S Farmer's Home for delinquent personal loans charged as miscellaneous expense

Cause: The cause of this condition is that adequate documentation was not prepared to justify this expenditure as Compact Capital account related.

Effect: The effect of the above condition does not result in questioned costs since, in fiscal year 2004, as the Compact Capital Projects Fund was reimbursed by the General Fund in the amount of \$80,000.

Recommendation: We recommend that Pohnpei State Government ensure adherence to the criteria.

Auditee Response and Corrective Action Plan: The Department of Treasury and Administration will ensure that compact funds will be expended in accordance with the terms and condition of the Compact. This will be a continuous task for the Chief of Finance.

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FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Local Findings Section

Finding No.: 2003-3  
Area: Unfunded Expenditures

Criteria: State law requires that all expenditures should be authorized by legislative appropriations.

Condition: Our review of the FY 03 Expenditure Fund Status Report revealed that one program area exceeded spending authorized by law.

<u>Office</u>	<u>Appropriation</u>	<u>Expenditure</u>	<u>Variance</u>
Office of the Governor	\$446,707	\$515,236	\$ (68,529)

Cause: The cause of the above condition is that the Executive Branch requested an appropriation in accordance with local laws to ratify costs incurred in typhoon preparation proceedings. A formal appropriation request was made to the Legislature, but no formal response from the Legislature appears to have occurred.

Effect: The effect of this condition is an apparent expenditure of local funds in excess of appropriated balances.

Recommendation: We recommend that the Executive Branch communicate with the Legislature and determine whether a set amount of transfer authority could be utilized by the Executive Branch to cover typhoon preparation costs.

Auditee Response and Corrective Action Plan: We note that Article 13, section 9 of the Pohnpei Constitution authorizes the Governor to “declare a state of emergency and issue appropriate decrees, to preserve the public peace, health, or safety, at a time of extreme emergency caused by civil disturbance, epidemic, natural disaster or immediate threat of war.” Implementation of this authority would necessarily, in almost all cases, warrant expenditure of public funds to achieve the constitutional mandate. However, we agree with the Auditor’s finding that all expenditures should be duly authorized by law. We also agree with the recommendation that we initiate discussion with the legislature with a view to providing the executive with authority to use funds up to a certain limit to prepare for emergency situations. The Legal Advisor of the Department of Treasury will prepare a draft bill to the Legislature no later than November 2005 to accomplish the recommendation stated above. Similarly, a draft bill will be re-submitted requesting for appropriation for the variance noted in the finding.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Financial Statements Findings Section

Finding No.: 2003-4  
Area: Bank Reconciliation

Criteria: A functioning system of internal control requires all cash accounts be reconciled with bank statements on a monthly and on a timely basis.

Condition: During the twelve months ended September 30, 2003, accurate bank reconciliations were not performed.

Cause: The cause of the above condition is that a one-sided bank reconciliation was performed at the end of each month. Material adjustments were required as of year-end to reconcile the cash balances with the book balances.

Effect: The effect of this condition is that during fiscal year 2003, inaccurate internal financial information resulted. However, we note that management corrected this situation in 2004 and monthly bank reconciliations are now occurring.

Recommendation: Management should ensure that bank reconciliations, reconciling the cash book balances to the book balances, are prepared each month.

Auditee Response and Corrective Action Plan: Currently, bank reconciliations are being performed and will be continuously performed monthly. The Chief of Finance is task to ensure that the bank reconciliations are performed on a timely basis.

**STATE OF POHNPEI  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Financial Statements Findings Section

Finding No.: 2003-5  
Area: Encumbrance

Criteria: Pohnpei State should ensure that outstanding encumbrances are evaluated on a monthly basis to determine whether the underlying encumbrance continues to be valid.

Condition: Numerous encumbrances were not liquidated and dated as far back as 1998. In addition, we found encumbrances were still outstanding as of September 30, 2003 totaling \$567,395, where the corresponding travel advance no longer existed in the travel advance subsidiary ledger.

Cause: The major cause of the above condition is the lack of reconciliation of outstanding encumbrances.

Effect: The effect of this condition is a qualification of the 2003 financial statements. However, management has shown us that this matter was corrected in fiscal year 2004 and the effects of such correction have been recorded in the 2004 financial statements.

Recommendation: The encumbrance subsidiary ledger should be reviewed on a periodic basis and encumbrances related to travel advances should be matched with the travel advance subsidiary ledger.

Auditee Response and Corrective Action Plan: Encumbrances are being reviewed monthly and adjustments are being made to correctly state the encumbrance ledger. The Head of the Fund Certification and Accounts Payable Section of the Department of Treasury will consistently make the reviews of the encumbrances as well as makes adjustments to the record; as appropriate.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Financial Statements Findings Section

Finding No.: 2003-6  
Area: Travel Advance

Criteria: Details of travel advance should be maintained to support general ledger balances.

Condition: Details of travel advance for nonmajor governmental funds amounting to \$220,364 at September 30, 2003 were not available.

Cause: The cause of this condition is that the general ledger was not reconciled with the subsidiary ledger.

Effect: The effect of this condition is a qualification of the opinion upon the 2003 financial statements. We note that management corrected this matter in the 2004 financial statements, which reflect the necessary adjustments to affect correction.

Prior Year Status: This finding was brought to management's attention in the 2002 Single Audit Report.

Recommendation: We recommend that the Finance Office ensure adherence to the criteria.

Auditee Response and Corrective Action Plan: As already stated, in fiscal year 2004 travel advances and other general ledger accounts are being reconciled monthly. Again, the Head of the Fund Certification and Accounts Payable Section of the Department of Treasury & Administration will continue to strive hard to come up with the schedule of travel advances prior to fiscal year 2003 no later than December 31, 2005.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Financial Statements Findings Section

Finding No.: 2003-7  
Area: General Receivables

Criteria: Money owed to Pohnpei State Government should be collected in a timely manner.

Condition: Taxes and leases of \$2,034,915 owed to the State as of September 30, 2003 have been outstanding for a number of years. This amount does not reconcile with the schedule submitted by the Revenue Department.

Cause: The cause of this condition is that the difference between the two sets of records has not been reconciled.

Effect: The effect of this condition is a negative impact on cash flows from operations.

Prior Year Status: This finding was brought to management's attention in the 2000, 2001 and 2002 Single Audit Reports.

Recommendation: We recommend that Pohnpei State pursue the collection of funds owed through legal means. Better correspondence with other departments should also result from this condition.

Auditee Response and Corrective Action Plan: The Revenue Division is committed in its effort to collect all accounts receivables, particularly the state taxes and land leases. Regarding taxes, except for collection action that is ongoing in almost all the receivables, majority of the accounts have installment plan in place and some are being litigated in court. As for the leases, the Division is working with the department of Land to recover all outstanding leases. Appropriate notices for payment are regularly sent to the leaseholders and public announcement on the radio has been made encouraging lessees to made prompt payment. The Chief of Revenue Division will continue to pursue recovery action in court for the delinquent accounts. In addition, the Division is now working with the Division of Finance to perform periodic reconciliation of the revenue accounts to ensure the accurate recording of state taxes.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Financial Statements Findings Section

Finding No.: 2003-8  
Area: Travel Advances

Criteria: Pohnpei State should ensure that travel advances are cleared in a timely manner.

Condition: It is evident that travel advances are not cleared in a timely manner.

Cause: The cause of this condition is that follow up measures are not undertaken to ensure that travelers file travel vouchers in a timely manner.

Effect: The effect of this condition is a potential overstatement of this condition is that travel advances are not cleared in a timely manner, which indicates that expenditures are understated. This is especially important for reimbursable grants since the State does not recover its cash advanced from grantor agencies.

Recommendation: The State should ensure that travel vouchers are filed in a timely manner. If vouchers are not timely filed, payroll deductions should automatically commence.

Auditee Response and Corrective Action Plan: The Pohnpei State's Financial Management Regulations are amended to address this issue. The travel authorization (TA) form will be modified also to authorize automatic payroll deductions from traveler's salary in the event of the traveler's failure to file the travel voucher in a timely manner. The amendment will be effected by the Department of Treasury in fiscal year 2006.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Financial Statements Findings Section

Finding No.: 2003-9  
Area: Equipment and Real Property Management

Criteria: A functioning system of internal control requires that a summary schedule of fixed asset details be produced by the automated fixed asset subsystem, and be further classified by major asset category.

Condition: During the twelve months ended September 30, 2003, a summarization of assets data from the automated fixed assets subsystem was not updated. Additionally, a physical inventory of property was not performed as required by the Common Rule.

Cause: The cause of this condition is a lack of periodic update of the fixed asset subsystem.

Effect: The effect of this condition is that noncompliance with the Common Rule occurred in 2003 and the State did not have a functioning fixed asset system during that year. However, during fiscal year 2004, the Finance Division was able to reconcile its fixed asset subsystem, conduct the required inventory and produce required reports.

Recommendation: We recommend that the Finance Office continue to ensure that the fixed assets subsystem is updated on a regular basis.

Auditee Response and Corrective Action Plan: The Procurement and Property Accountability staff will continue to update the fixed assets master file to ensure that all fixed assets are recorded and properly valued particularly infrastructure in order to meet the GASB 34 requirement in fiscal year 2007.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Financial Statements Findings Section

Finding No.: 2003-10  
Area: Insufficient Fund Bank Charges

Criteria: A functioning system of internal control requires timely resolution of bank reconciling items.

Condition: Pohnpei State had to record \$21,000 in bank charges as a result of unidentified charges made by the bank.

Cause: The cause of this condition is untimely resolution of bank reconciling items.

Effect: The effect of this condition is potential unauthorized use of public funds.

Recommendation: We recommend that the Finance Office perform timely bank reconciliations and that all reconciling items be timely recorded in the financial statements.

Auditee Response and Corrective Action Plan: The above charge was debited by the bank in December 2002 and was noted in the FY 03 bank reconciliation which was performed from June 2004 through September 2004. Currently, all bank reconciliations are being performed monthly. The Chief of Finance is monitoring the daily cash balance and in constant coordination with the Bank Reconciliation Staffs to ensure that bank charges due to insufficient funds are avoided.

**STATE OF POHNPEI  
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Summary Schedule of Prior Audit Federal Findings and Questioned Costs  
Year Ended September 30, 2003

The following is a summary of unresolved questioned costs of the State of Pohnpei as of September 30, 2003:

	Questioned Costs Set Forth in Prior Audit Report <u>2002</u>	Questioned Costs Resolved in Fiscal Year <u>2003</u>	Questioned Costs at September 30, 2003
Unresolved Questioned Costs FY 96	\$ 15,182	\$ -	\$ 15,182
Unresolved Questioned Costs FY 98	24,000	-	24,000
Unresolved Questioned Costs FY 99	39,439	-	39,439
Unresolved Questioned Costs FY 00	12,375	-	12,375
Unresolved Questioned Costs FY 01	74,332	74,332[1]	-
Unresolved Questioned Costs FY 02	<u>842,896</u>	<u>703,228</u> [2][3][4]	<u>139,668</u>
	\$ <u>1,008,224</u>	\$ <u>777,560</u>	\$ <u>230,664</u>

- [1] The pass-through entity, the FSM National Government, has evaluated the Pohnpei State Attorney General's opinion relating to Finding 2001-2 and concluded that \$74,332 relating to fuel or operations is an allowable use of Compact Energy funds.
- [2] The pass-through entity, the FSM National Government, has evaluated documentation provided by Pohnpei State in FY03 relating to Finding 2002-02 and concluded that farm machinery acquired in FY02 amounting to \$13,385 was necessary and reasonable for the Special Education Program.
- [3] The pass-through entity, the FSM National Government, through the Secretary of Justice, has opined that \$677,995 of dry-docking expenses is an allowable use of Compact Capital funds.
- [4] The pass-through entity, the FSM National Government, has reviewed a journal voucher transferring \$11,848 from the Compact Capital Projects fund to the General fund and concluded that Finding 2002-6 is adequately resolved through the transfer of these expenditures.

Unresolved federal findings for fiscal year 1999:

<u>Page No.</u>	<u>Finding No.</u>	<u>Description</u>
74	99-2	Allowable Costs/Costs Principles
77	99-4	Allowable Costs/Costs Principles-Questionable Use of Compact Funds
78	99-5	Subrecipient Monitoring – PSHA
81	99-7	Compact Capital Fund – Allowable Costs/Cost Principles

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Summary Schedule of Prior Audits Findings and Questioned Costs, Continued  
Year Ended September 30, 2003

Unresolved federal findings for fiscal year 2000:

<u>Page No.</u>	<u>Finding No.</u>	<u>Description</u>
72	2000-2	Allowable Costs/Costs Principles
74	2000-4	Allowable Costs/Costs Principles
75	2000-5	Allowable Costs/Costs Principles

Unresolved federal findings for fiscal year 2002:

<u>Page No.</u>	<u>Finding No.</u>	<u>Description</u>
68	2002-3	Allowable Costs/Cost Principles
69	2002-4	Procurement
70	2002-5	Allowable Costs/Cost Principles