

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

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**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

## INDEPENDENT AUDITORS' REPORT

Chairman  
Board of Directors  
Federated States of Micronesia  
Coconut Development Authority:

We have audited the accompanying statements of net assets of Federated States of Micronesia Coconut Development Authority (the Authority), a component unit of the National Government of the Federated States of Micronesia, as of September 30, 2005 and 2004, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Authority as of September 30, 2005 and 2004, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Management Discussion and Analysis on pages 3-5 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Authority's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurements and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 12, 2006 on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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

September 12, 2006

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Management Discussion and Analysis  
Year Ended September 30, 2005

This section of the FSM Coconut Development Authority (the Authority's) annual financial report presents our discussion and analysis of the Authority's financial performance for the year ended September 30, 2005.

The Federated States of Micronesia Coconut Development Authority (the Authority) was established in 1981 by Public Law 1-156 and incorporated as Chapter Two, Title 22 of the Code of the Federated States of Micronesia. The purpose of the Authority is to manufacture, process, buy, collect, market, sell, export, inspect, improve the quality, and deal with, in general, all products derived from the coconut tree. The Authority has the additional responsibility to establish prices to producers or sellers of coconut products in the Federated States of Micronesia, to collect and receive all monies derived from the sales of coconut products and to stabilize the price of these products. The Authority is a component unit of the Federated States of Micronesia National Government.

The affairs of the Authority are managed by a five-member board, consisting of representatives of the four FSM states and the FSM National Government. Daily operations of the Authority is delegated to a general manager, who is hired by and serves at the pleasure of the Board.

The operation of the Authority is funded by annual appropriations from the FSM Congress. The purchase of copra is funded by copra subsidy appropriations from the FSM Congress and revenues generated through sales of copra and coconut by-products.

The Authority's fiscal year 2005 annual copra subsidy was only \$75,000 with an additional \$50,000 supplemental during the fiscal year. With the continuous instability of the world prices in the world market, the copra subsidy plays an important role in maintaining a stable price for the producers. If there is going to be a further reduction of the copra subsidy in fiscal 2006 the nation can expect a reduction of the copra price which will affect those people whose livelihood depends on the revenue from the copra.

The Authority has also experienced a drastic decline in the production of copra over the years. The Authority's peak production of 5,788 s/tons in 1985 has gone down steadily over the years and under the current year dropped to only 190 s/tons.

Following are the production of copra in s/tons within the past 20 years:

1986 .....	607 s/tons	1996 .....	717 s/tons
1987 .....	1,774 s/tons	1997 .....	510 s/tons
1988 .....	2,175 s/tons	1998 .....	928 s/tons
1989 .....	1,140 s/tons	1999 .....	548 s/tons
1990 .....	2,305 s/tons	2000 .....	757 s/tons
1991 .....	982 s/tons	2001 .....	529 s/tons
1992 .....	242 s/tons	2002 .....	754 s/tons
1993 .....	633 s/tons	2003 .....	583 s/tons
1994 .....	909 s/tons	2004 .....	600 s/tons
1995 .....	1,210 s/tons	2005 .....	190 s/tons



**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Management Discussion and Analysis  
Year Ended September 30, 2005

**Financial Highlights**

The initial copra subsidy remains at the level of \$75,000.

The operation cost for the Authority, which is provided under appropriation from the FSM Congress, has not gone through any drastic change. The Authority continues to maintain its operation at a minimal level to meet the objective of minimizing the operating cost of the Government.

**Plan of Action for 2006**

The Authority will maintain the following course of action plans for the industry:

1. Re-examine the budget and make straightforward assessment of its expenses to minimize its operation costs.
2. Promote accountability of the Authority's records.
3. Advocate teamwork in the current operations to accomplish efficiency and enhance employee moral
4. Stop all non essential expenses and promote cost saving measures
5. Aggressive collection of receivables
6. Venture into development of other high value added coconut products.

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Statements of Net Assets  
September 30, 2005 and 2004

<u>ASSETS</u>	<u>2005</u>	<u>2004</u>
Current assets:		
Cash and equivalents	\$ 75,271	\$ 7,230
Copra buyers' revolving fund, net	22,550	22,550
Accounts receivable, net	1,560	2,358
Prepayments	1,362	1,362
Copra bags inventory	14,125	18,463
Copra inventory, net	<u>76,901</u>	<u>69,438</u>
Total current assets	191,769	121,401
Property, plant and equipment, net	<u>252,888</u>	<u>238,794</u>
	<u>\$ 444,657</u>	<u>\$ 360,195</u>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Accounts payable	\$ 5,997	\$ 21,604
Accrued payroll and others	3,673	2,538
Customer deposits	<u>2,000</u>	<u>2,000</u>
Total current liabilities	<u>11,670</u>	<u>26,142</u>
Contingency		
Net assets:		
Invested in capital assets, net of related debt	252,888	238,794
Unrestricted	<u>180,099</u>	<u>95,259</u>
Total net assets	<u>432,987</u>	<u>334,053</u>
	<u>\$ 444,657</u>	<u>\$ 360,195</u>

See accompanying notes to financial statements.

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Statements of Revenues, Expenses, and Changes in Net Assets  
Years Ended September 30, 2005 and 2004

	2005	2004
Copra sales	\$ 85,196	\$ 114,666
Cost of copra sold	(37,687)	(259,329)
Gross profit (loss)	47,509	(144,663)
Operating expenses:		
Personnel services	84,263	80,493
Depreciation	44,135	46,221
Consumables and others	29,932	21,257
Inventory shrinkage	29,110	18,060
Contractual services	22,160	22,244
Damaged bags expense	18,819	6,552
Travel	13,400	13,981
Bad debts	-	23,457
Ocean freight	-	7,501
Stevedoring	-	5,480
Handling	-	3,644
Miscellaneous	15,621	18,915
Total expenses	257,440	267,805
Loss from operations	(209,931)	(412,468)
Nonoperating revenues (expenses), net:		
Operating grants and subsidies	282,565	215,534
Miscellaneous income	26,300	25,815
Total nonoperating revenues	308,865	241,349
Change in net assets	98,934	(171,119)
Net assets at beginning of year	334,053	505,172
Net assets at end of year	\$ 432,987	\$ 334,053

See accompanying notes to financial statements.



**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Statements of Cash Flows  
Years Ended September 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Cash received from customers	\$ 112,294	\$ 136,409
Cash paid to employees	(83,125)	(80,763)
Cash paid to suppliers	<u>(185,464)</u>	<u>(287,115)</u>
Net cash used for operating activities	<u>(156,295)</u>	<u>(231,469)</u>
Cash flows from noncapital financing activities:		
Congress of the FSM operating appropriations	<u>282,565</u>	<u>215,534</u>
Cash flows from capital and related financing activities:		
Acquisition of property, plant and equipment	<u>(58,229)</u>	<u>(9,292)</u>
Change in cash	68,041	(25,228)
Cash and equivalents at beginning of year	<u>7,230</u>	<u>32,457</u>
Cash and equivalents at end of year	<u>\$ 75,271</u>	<u>\$ 7,229</u>
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (209,931)	\$ (412,468)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	44,135	46,221
Bad debts	-	23,457
Inventory shrinkage expense	29,110	18,060
Others	26,300	25,815
Change in accounts receivable	798	(4,072)
Change in inventory and prepayments	(32,235)	59,557
Change in accounts payable	(15,608)	12,231
Change in accrued payroll and others	<u>1,136</u>	<u>(270)</u>
Net cash used for operating activities	<u>\$ (156,295)</u>	<u>\$ (231,469)</u>

See accompanying notes to financial statements.

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Notes to Financial Statements  
September 30, 2005 and 2004

(1) Summary of Significant Accounting Policies

A. Reporting Entity

The Federated States of Micronesia Coconut Development Authority (the Authority) was established in 1981 by Public Law 1-145, as amended by Public Law 2-8, and incorporated as Chapter Two, Title 22 of the Code of the Federated States of Micronesia. The purpose of the Authority is to manufacture, process, buy, collect, market, sell, export, inspect, improve the quality, and deal with, in general, all products derived from the coconut tree. The Authority has the additional responsibility to establish prices to producers or sellers of coconut products in the Federated States of Micronesia, to collect and receive all monies derived from the sales of coconut products, and to stabilize the price of these products. The Authority is a component unit of the National Government of the Federated States of Micronesia.

The affairs of the Authority are managed by a five-member board, consisting of representatives of the four FSM states and the FSM National Government. Daily operations of the Authority are delegated to a general manager, who is hired by and serves at the pleasure of the board.

The operation of the Authority is funded by annual appropriations from the FSM Congress. The purchase of coconut products is funded by copra subsidy appropriations from the FSM Congress and revenues generated through sales of copra.

The financial statements of the Authority have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. Government Accounting Standards Board (GASB) Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting", requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Authority has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

For the year ended September 30, 2003, the Authority adopted GASB Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments" (GASB 34) as amended by GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments", and GASB Statement No. 38, "Certain Financial Statement Note Disclosures," and applied those standards on a retroactive basis. GASB Statement Nos. 34, 37 and 38 establish standards for external financial reporting for state and local governments and require that resources be classified for accounting and reporting purposes into the following four net asset categories:

- Invested in capital assets, net of related debt:  
Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Notes to Financial Statements  
September 30, 2005 and 2004

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

• Restricted:

- Nonexpendable – Net assets subject to externally imposed stipulations that require the Authority to maintain them permanently. For the years ended September 30, 2005 and 2004, the Authority does not have nonexpendable restricted net assets.
- Expendable – Net assets whose use by the Authority is subject to externally imposed stipulations that can be fulfilled by actions of the Authority pursuant to those stipulations or that expire by the passage of time.

• Unrestricted:

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

B. Fund Structure and Basis of Accounting

The accounts of the Authority are organized in the same manner as a proprietary fund-component unit. A proprietary fund is used by governmental units that are operated in a manner similar to private business enterprises. The purpose of a proprietary fund is to provide periodic determination of revenues, expenses and net income, with maintenance of capital. Proprietary funds are accounted for on the flow of economic resources measurement focus, whereby all assets and liabilities associated with the operations of the funds are included on the balance sheet. This is in contrast to "governmental" fund type accounting, which has a measurement focus on the sources and uses of funds, and includes only current assets and current liabilities on the balance sheet.

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

C. Cash and Equivalents

For the purposes of the statements of net assets and of cash flows, cash and equivalents are defined as cash in checking accounts and certificates of deposit with initial maturities of ninety days or less. There are no significant differences between cash balances per book and per bank.

D. Management Estimates

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



**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Notes to Financial Statements  
September 30, 2005 and 2004

(1) Summary of Significant Accounting Policies, Continued

F. Inventory, Continued

Ending copra inventory at September 30, 2005 and 2004 is valued at estimated realizable market value.

The inventory of bags is recorded at cost. Provision for damaged bags and deterioration in value of usable bags is made at the end of each fiscal year.

G. Property, Plant and Equipment

Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation expense is calculated by the straight-line method over the estimated useful lives of the assets.

H. New Accounting Standards

For fiscal year 2006, the Authority will be implementing GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. The Authority has not yet evaluated the financial statement impact of GASB Statement No. 42.

(I) Reclassifications

Certain reclassifications have been made to the 2004 financial statements to correspond to the 2005 presentation.

(2) Property, Plant and Equipment

Fixed assets movement for the years ended September 30, 2005 and 2004, are as follows:

	<u>Estimated Useful Life</u>	<u>October 1, 2004</u>	<u>Additions</u>	<u>Retirements</u>	<u>September 30, 2005</u>
Buildings	20 years	\$ 255,524	\$ -	\$ -	\$ 255,524
Equipment	5-10 years	188,488	5,742	(360)	193,870
Vehicles	5 years	31,642	3,711	-	35,353
Furniture and fixtures	5-10 years	6,422	-	-	6,422
Leasehold improvements	20 years	11,255	-	-	11,255
Water tank	10 years	7,589	-	-	7,589
Equipment in transit		-	48,776	-	48,776
		500,920	58,229	(360)	558,789
Less accumulated depreciation		(262,126)	(44,135)	360	(305,901)
		<u>\$ 238,794</u>	<u>\$ 14,094</u>	<u>\$ -</u>	<u>\$ 252,888</u>
	<u>Estimated Useful Life</u>	<u>October 1, 2003</u>	<u>Additions</u>	<u>Retirements</u>	<u>September 30, 2004</u>
Buildings	20 years	\$ 255,524	\$ -	\$ -	\$ 255,524
Equipment	5-10 years	179,196	9,292	-	188,488
Vehicles	5 years	31,642	-	-	31,642
Furniture and fixtures	5-10 years	6,422	-	-	6,422
Leasehold improvements	20 years	11,255	-	-	11,255
Water tank	10 years	7,589	-	-	7,589
		491,628	9,292	-	500,920
Less accumulated depreciation		(215,905)	(46,221)	-	(262,126)
		<u>\$ 275,723</u>	<u>\$ (36,929)</u>	<u>\$ -</u>	<u>\$ 238,794</u>

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Notes to Financial Statements  
September 30, 2005 and 2004

**(3) Grants and Subsidies**

During the years ended September 30, 2005 and 2004, the Authority recognized grants and contributions from FSM Congressional appropriations as follows:

	<u>2005</u>	<u>2004</u>
Copra subsidy funds	\$ 125,000	\$ 100,000
Operational grants:		
Administrative expenses	<u>157,565</u>	<u>115,534</u>
Total grants and subsidies	\$ <u>282,565</u>	\$ <u>215,534</u>

**(4) Risk Management**

The Authority purchases insurance to cover risks associated with its warehouses and buildings. As of September 30, 2005, the Authority's warehouses and buildings were insured for coverage of \$131,500. Furthermore, the contents (equipment and stock) held at the warehouses and buildings were insured for coverage of \$240,000. The Authority is self insured for all other risks.

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

Chairman  
Board of Directors  
Federated States of Micronesia  
Coconut Development Authority:

We have audited the financial statements of Federated States of Micronesia Coconut Development Authority (the Authority), as of and for the year ended September 30, 2005, and have issued our report thereon dated September 12, 2006. 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 of the financial statements of the Authority for the year ended September 30, 2005, we considered its internal control in order to determine our auditing procedures for the purpose of expressing an 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 operations of the internal control over financial reporting that, in our judgment, could adversely affect the Authority's ability to record, process, summarize and report financial data consistent with assertions of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 2005-01 through 2005-02.

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 over financial reporting that might be material weaknesses. However, we consider none of the reportable conditions described above to be a material weakness.

Compliance

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not the 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 Board of Directors and management of the Authority and is not intended to be and should not be used by anyone other than those specified parties.

*Deloitte + Stark LLP*

September 12, 2006



**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Schedule of Findings and Questioned Costs  
Year Ended September 30, 2005

Finding No. 2005-1

Criteria: Policies and procedures should be in place to promote timely collection of trade accounts receivable.

Condition: Trade accounts receivable balances from some customers have been outstanding for over one year. Credit sales to one of these customers, Pohnpei Coconut Products, continued to be made during FY 2005, despite the outstanding receivable balance.

Cause: Set procedures are not in place to monitor and enforce collection of trade accounts receivable. In addition, management has been reluctant to cut off sales to major customers (primarily Pohnpei Coconut Products).

Effect: Excessively aged accounts receivable balances increase the likelihood of large balances becoming uncollectible.

Recommendation: We recommend that management actively pursue collection of accounts receivable over 90 days. If management does not believe these amounts will be recovered, these accounts should be written off.

Prior Year Status: This condition was reported as an internal control finding in the audit of the Authority for the year ended September 30, 2002, 2003 and 2004.

Auditee Response and Corrective Action Plan: The Authority continued to make attempts to collect on the Receivables. The Authority feels old accounts are very important to be collected and will continue to make attempts to collect. The Authority will determine in the next audit period which of those old accounts can not be collected and will recommend to be written off in the next audit. As for PCPI, there is still hope that we could recover their debt in small installment. Their new project in coconut bio-diesel is a promising project and may become a turning point in the recovering their debts.

**FEDERATED STATES OF MICRONESIA  
COCONUT DEVELOPMENT AUTHORITY**

Schedule of Findings and Questioned Costs  
Year Ended September 30, 2005

Finding No.: 2005-2  
Area: Payable

Criteria: Policies and procedures should be in place to promote accurate reconciliation of trade accounts payables.

Condition: The entity has a number of payables in its subsidiary ledger for which no supporting documentation is on hand. In addition, payables were on the ledger which have been paid.

Cause: These payables were written off to miscellaneous revenue.

Effect: An overstatement of payables resulted from this condition. However, management proposed adjustments to write-off these balances during the audit process.

Recommendation: We recommend that accounts payable be supported by adequate documentation and are regularly reviewed to ensure amounts that have been paid are appropriately recorded.

Auditee Response and Corrective Action Plan: The Authority will pay close attention to its payable to make sure adequate supporting documents are in place to support its payables.