

**NATIONAL FISHERIES CORPORATION
FEDERATED STATES OF MICRONESIA**

**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT**

SEPTEMBER 30, 2005 AND 2004

INDEPENDENT AUDITORS' REPORT

The Board of Directors
National Fisheries Corporation:

We were engaged to audit the accompanying statement of net assets of the National Fisheries Corporation (NFC) and subsidiaries, a component unit of the Federated States of Micronesia National Government, 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 NFC's management.

Because of inadequacies in the accounting records, detailed records supporting cash, accounts receivable, inventory, investment, fixed assets, inter-company receivables and payables, accounts payable, and non-operating income, were not available for the audit. We were not able to perform alternative procedures to satisfy ourselves about the amounts at which cash, accounts receivable, inventory, investment, fixed assets, inter-company receivables and payables, accounts payable, lease payable, sales and other income are recorded. Additionally, the aforementioned accounts materially impact the statement of revenues, expenses and changes in net assets.

Financial statements supporting NFC's investment in Micronesia Longline Fishing Company (MLFC), Yap Fishing Corporation, Yap Fresh Tuna, Inc, Chuuk Fresh Tuna, Inc., and Kosrae Sea Venture Inc. at September 30, 2005 and 2004, were not available.

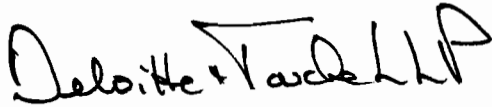
Due to the matters set forth in the second and third paragraphs, we are not in a position to, and we do not express an opinion on the accompanying financial statements.

The accompanying financial statements have been prepared assuming that NFC will continue as a going concern. As discussed in note 7 to the financial statements, NFC has incurred substantial losses from operations. This condition raises substantial doubt about its ability to continue as a going concern.

The Management Discussion and Analysis on pages 3 through 6 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 NFC'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.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements of NFC taken as a whole. The accompanying Combining and Consolidated Schedules for the year ended September 30, 2005 set forth on pages 17-20 are presented for purposes of additional analysis and are not a required part of the basic financial statements of NFC. These schedules are the responsibility of NFC's management. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, due to the matters set forth in the second and third paragraph above, we do not express any form of assurance on the accompanying schedules.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 7, 2007, on our consideration of NFC's internal control over financial reporting and our tests of its compliance with certain 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.

February 7, 2007

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis September 30, 2005 and 2004

This section of the National Fisheries Corporation's (NFC) annual audit report presents the Management's Discussion and Analysis (MD & A) for the fiscal year ended September 30, 2005. MD & A is supplementary information required by the new Government Accounting Standards Board Statement 34 (GASB 34) on reporting model. The preparation of MD & A is the responsibility of the management of NFC, and it is designed to help the readers in understanding the accompanying financial statements and the accompanying notes to the financial statements.

Background

The National Fisheries Corporation is a government owned corporation, created under Public Law No. 3-14 by the 3rd Congress of the Federated States of Micronesia. The main purpose of NFC is to promote the development of the fishing industry in the FSM. NFC is also involved in ancillary activities that support commercial fishery activities. It is for this purpose that NFC initially engaged itself with its subsidiaries; Yap Fresh Tuna Inc. (YFTI), Chuuk Fresh Tuna Inc. (CFTI), Kosrae Sea Ventures Inc. (KSVI) and Micronesia Longline Fishing Co. (MLFC). However, due to the drastic decline in the number of vessels utilizing YFTI and CFTI, NFC was forced to venture into the actual operation of longline fishing vessels, trading of fishing supplies and airfreight business.

Micronesia Longline Fishing Co. (MLFC) being NFC's fishing arm is operating nine longline fishing vessels. Fish catch are shipped via airfreight to Japan for auction on the sashimi market. NFC itself is managing and operating its own fishing vessel, however, its major source of income comes from airfreight business, issuing of permits to foreign fishing companies and trading of baitfish and fishing supplies.

Overview of Fiscal Year 2005

The financial statements presented herein include all of the activities of NFC consisting of Corporate operations, Fishing operations, Airfreight operations, Transshipment operations and Baitfish services. Excluded from the statements are that of Micronesia Longline Fishing Co. (MLFC) and all NFC's subsidiaries namely: YFTI, CFTI, and KSVI. The accounts of NFC are organized as a proprietary fund. Proprietary funds are used by governmental units that are operated in a manner similar to private business enterprises.

NFC's budget is prepared by management with the concurrence of the board of directors. The budget is then forwarded to the President's budget committee which in turn submits it to Congress for approval.

Financial Highlights

NFC started implementing the new financial reporting standards in accordance with Government Accounting Standards Board (GASB) principles in fiscal year 2003. Adopting the GASB principles provide the new financial reporting of the following three basic financial statements:

1. Statement of Net Assets (SNA)

SNA presents what NFC owns (assets), owes (liabilities) and the net assets (the difference between total assets and total liabilities) at the end of fiscal year. The "net assets" is one indicator of the current financial condition of NFC, while the change in net assets is an indicator of whether the overall financial condition has improved or worsened during the year.

The Statement of Net Assets at September 30, 2005 consists of the Corporate, Fishing, Airfreight, Transshipment and Baitfish Services operations of NFC but does not include MLFC. NFC started the non-inclusion of MLFC's financial data in NFC's consolidated financial statement in fiscal year 2004.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis September 30, 2005 and 2004

Comparative Statement of Net Assets at September 30, 2005 and 2004 are summarized below:

	<u>FY 2005</u>	<u>FY 2004</u>	<u>Difference</u>
Assets:			
Current assets	\$ 1,160,215	\$ 1,524,658	\$ (364,443)
Noncurrent asset	<u>895,842</u>	<u>1,107,816</u>	<u>(211,974)</u>
Total assets	<u>\$ 2,056,057</u>	<u>\$ 2,632,474</u>	<u>\$ (576,417)</u>
Liabilities:			
Current liabilities	\$ 4,859,636	\$ 5,360,285	\$ (500,649)
Noncurrent liabilities	-	-	-
Total liabilities	<u>4,859,636</u>	<u>5,360,285</u>	<u>(500,649)</u>
Net assets:			
Invested in capital assets, net of related debts	(803,953)	(591,979)	(211,974)
Unrestricted	<u>(1,999,626)</u>	<u>(2,135,832)</u>	<u>136,206</u>
	<u>(2,803,579)</u>	<u>(2,727,811)</u>	<u>(75,768)</u>
Total liabilities and net assets	<u>\$ 2,056,057</u>	<u>\$ 2,632,474</u>	<u>\$ (576,417)</u>

Assets: Company total assets of \$2.056 Million comprised of \$1.160 Million or 56% current assets and \$896k or 44% fixed assets.

Current assets: The major portion of the \$1.160 Million current assets is in accounts receivable including inter-company receivable, which accounts for \$1.023 Million or 88%. The receivable comprised of net account receivables of \$595k and due from affiliates of \$428k. The remaining 12% of current assets is inventory of \$185k or 16% and cash account of only 1% or \$3k and advances payable of \$51k.

The decline in current assets of \$364k is primarily from the net result of the decrease in cash by \$217k, decrease in receivables by \$233k, and increase in inventory by \$85k.

Noncurrent assets: The total fixed assets of \$401k consists of company property and equipment from fishing operations. In fiscal year 2005, the fixed assets dropped by \$212k or 34%.

Liabilities: NFC's liabilities of \$4.859 Million are all current consisting of \$3.596 Million loan from the National Government or 74% of the total liabilities. The remaining current liabilities are from freight lease of \$992k, other accounts payable of \$122k and intercompany payable of \$149k.

The reduction of current liabilities of \$500k is due to the decrease of accounts payable from transshipment fishing and airfreight operations.

Net Assets: The net assets (deficit) as of September 30, 2005 of \$2.804 Million reflects an increase by \$76k from \$2.728 Million in fiscal year 2004.

2. Summary Statement of Revenues, Expenses and Changes in Net Assets (SRECNA)

The SRECNA provides information on the financial performance for the current fiscal year in terms of revenues and expenses. It presents the operating revenues and expenses and the corresponding net operating results, as well as non-operating revenues and expenses. Below is the comparative summary of SRECNA for fiscal years ended September 30, 2005 and 2004:

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis September 30, 2005 and 2004

	<u>FY 2005</u>	<u>FY 2004</u>	<u>Difference</u>
Sales	\$ 1,375,051	\$ 3,368,967	\$ (1,993,916)
Cost of sales	<u>1,268,726</u>	<u>2,949,014</u>	<u>(1,680,288)</u>
Gross profit	106,325	419,953	(313,628)
Operating expenses	<u>651,738</u>	<u>816,558</u>	(164,820)
Loss from operations	<u>(545,413)</u>	<u>(396,605)</u>	(148,808)
Other income (expense)	<u>469,645</u>	<u>265,130</u>	<u>204,515</u>
Decrease in net assets	\$ <u>(75,768)</u>	\$ <u>(131,475)</u>	\$ <u>55,707</u>

The total sales of \$1.375 Million are from NFC's five main operational activities consisting of airfreight at \$985k, baitfish at \$286k, fishing at \$33k, transshipment at \$63k corporate at \$8k. The components of cost of sales of \$1.269 Million are fuel, airfreight fees, baitfish and supplies, port and transshipment fees, provisioning, and packing materials.

The sales dropped by \$1.994 Million due to significant reduction of airfreight operations by \$1.726 Million. Correspondingly, the reduction of cost of sales is due from reduced consumption of fuel and lesser airfreight fees.

The consolidated total operating expenses for the year is \$652k. Salaries and wages of \$225k or 34% is the highest expense account. The remaining operating expenses include depreciation of \$212k and rent of \$79k, for 33% and 12%, respectively. Other expenses are communication, utilities, repairs and maintenance, office, professional fees, taxes and miscellaneous expenses which account for the remaining 21% of total operating expenses.

The other income of \$469k represents the financial support from FSM National Government and others. The increase of other income is from FSM National Government financial subsidies to the operations of NFC.

3. Summary Statement of Cash Flows (SCF)

SCF presents information about changes in the cash position using the direct method of reporting sources and uses of cash. The direct method reports all major cash inflows and outflows at gross amounts, differentiating these activities into cash flows arising from operating activities, noncapital financing and capital and related financing.

Below is the summary statement of cash flows:

	<u>FY 2005</u>	<u>FY 2004</u>	<u>Difference</u>
From operating activities	\$ (686,772)	\$ 30,161	\$ (716,933)
Provided by noncapital financing activities	100,000	(300,730)	400,730
From capital and related financing activities	<u>369,645</u>	<u>-</u>	<u>369,645</u>
Net decrease in cash and equivalents	\$ (217,127)	\$ (270,569)	\$ 53,442
Cash and equivalents at beginning of year	<u>220,598</u>	<u>491,167</u>	<u>(270,569)</u>
Cash and equivalents at end of year	\$ <u>3,471</u>	\$ <u>220,598</u>	\$ <u>(217,127)</u>

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Management Discussion and Analysis September 30, 2005 and 2004

NFC's SCF for fiscal year 2005 indicates a balance in cash of \$3k. The fiscal year 2005 cash balance is lower by \$217k or 98% compared with fiscal year 2004 of \$220k.

Economic Outlook

The economic outlook for fiscal year 2005 is not different with fiscal year 2004. The substantial losses from its regular operations including investments with Micronesia Longline Fishing Company (MLFC), Kosrae Sea Ventures, Inc. (KSVI), Chuuk Fresh Tuna Inc. (CFTI) and Yap Fresh Tuna Inc. (YFTI) have severely affected NFC's regular operations. These conditions raise substantial doubt about the company's ability to continue as a going concern. Financial assistance from FSM National Government is needed to rehabilitate and to continue the operations of NFC.

Management's Discussion and Analysis for the year ended September 30, 2004 is set forth in NFC's report on the audit of financial statements, which is dated February 7, 2007. That Discussion and Analysis explains the major factors impacting the 2004 financial statements and can be viewed at the Office of the Public Auditor's website at www.fsmpublicauditor.fm.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Consolidated Statement of Net Assets
September 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
<u>ASSETS</u>		
Current assets:		
Cash	\$ 3,471	\$ 220,598
Accounts receivable, net	595,278	742,339
Advances receivable (payable)	(51,325)	10,070
Inventory	184,675	98,944
Due from affiliates, net	428,116	452,707
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Total current assets	1,160,215	1,524,658
Investment	486,855	486,855
Property and equipment, net	408,987	620,961
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	\$ 2,056,057	\$ 2,632,474
	<hr/>	<hr/>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Notes payable	\$ 3,596,149	\$ 3,596,149
Accounts payable	122,394	722,276
Lease payable	992,228	992,228
Accrued liabilities	148,865	49,632
	<hr/>	<hr/>
Total current liabilities	4,859,636	5,360,285
Commitments and contingencies		
Net assets:		
Invested in capital assets, net of related debt	(803,953)	(591,979)
Unrestricted	(1,999,626)	(2,135,832)
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Total net assets	(2,803,579)	(2,727,811)
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	\$ 2,056,057	\$ 2,632,474
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See accompanying notes to consolidated financial statements.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Consolidated Statement of Revenues, Expenses and Changes in Net Assets

Years Ended September 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Sales	\$ 1,375,051	\$ 3,368,967
Cost of sales	<u>1,268,726</u>	<u>2,949,014</u>
Gross profit	<u>106,326</u>	<u>419,953</u>
Operating expenses:		
Salaries and wages	224,570	281,834
Depreciation and amortization	211,975	211,974
Rent	78,678	122,482
Utilities	33,098	34,409
Telephone and communication	25,387	27,754
Payroll and other taxes	22,084	24,919
Travel and entertainment	20,921	18,805
Office expense	15,619	26,386
Representation	9,627	7,366
Repairs and maintenance	4,061	5,944
Contractual services	1,764	6,556
Miscellaneous	<u>3,954</u>	<u>48,129</u>
Total operating expenses	<u>651,738</u>	<u>816,558</u>
Loss from operations	<u>(545,412)</u>	<u>(396,605)</u>
Other income (expense):		
FSM National Government operating subsidy	100,000	-
Other income, net	<u>369,645</u>	<u>265,130</u>
Total other income, net	<u>469,645</u>	<u>265,130</u>
Decrease in net assets	(75,768)	(131,475)
Net assets at beginning of year	<u>(2,727,811)</u>	<u>(2,596,336)</u>
Net assets at end of year	<u><u>\$ (2,803,579)</u></u>	<u><u>\$ (2,727,811)</u></u>

See accompanying notes to consolidated financial statements.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Consolidated Statement 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	\$ 1,583,507	\$ 2,965,880
Cash paid to suppliers and employees	<u>(2,270,279)</u>	<u>(2,935,719)</u>
Net cash (used in) provided by operating activities	<u>(686,772)</u>	<u>30,161</u>
Cash flows from noncapital financing activities:		
FSM National Government operating subsidies	100,000	-
Differences that arise in debt due to the non-inclusion of certain investees' financial statements	-	(2,471,559)
Differences that arise in fixed assets due to the non-inclusion of certain investees' financial statements	-	1,905,699
Interest expense and others	<u>-</u>	<u>265,130</u>
Net cash provided by (used in) noncapital financing activities	<u>100,000</u>	<u>(300,730)</u>
Cash flows from capital and related financing activities:		
Other income	<u>369,645</u>	<u>-</u>
Net cash provided by capital and related financing activities	<u>369,645</u>	<u>-</u>
Net decrease in cash	(217,127)	(270,569)
Cash at beginning of year	<u>220,598</u>	<u>491,167</u>
Cash at end of year	\$ <u><u>3,471</u></u>	\$ <u><u>220,598</u></u>
Reconciliation of loss from operations to cash flows from operating activities:		
Loss from operations	\$ (545,412)	(396,605)
Adjustments to reconcile loss from operations to net cash (used in) provided by operating activities:		
Depreciation and amortization	211,975	211,974
(Increase) decrease in assets:		
Accounts receivable	147,061	(346,961)
Advances receivable, net	61,395	33,254
Inventory	(85,731)	790,119
Due from affiliates	24,591	(100,462)
Prepays and other assets	-	51,907
Increase (decrease) in liabilities:		
Accounts payable	(599,882)	(188,013)
Accrued liabilities	<u>99,231</u>	<u>(25,052)</u>
Net cash (used in) provided by operating activities	\$ <u><u>(686,772)</u></u>	<u><u>30,161</u></u>

See accompanying notes to consolidated financial statements.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements
September 30, 2005 and 2004

(1) Summary of Significant Accounting Policies

Reporting Entity

The National Fisheries Corporation (NFC) was created under FSM Public Law No. 3-14 by the third Congress of the Federated States of Micronesia (FSM).

The purpose of the National Fisheries Corporation is to promote the development of commercial pelagic fisheries and related industries within the Federated States of Micronesia's 200 mile Exclusive Economic Zone. NFC is also involved in ancillary activities that support commercial fishery activities. These activities include technical and infrastructure services, manpower training and other related activities promoting commercial fisheries development.

The NFC is a component unit (proprietary fund type) of the FSM National Government. The financial statements of the NFC are incorporated into those of the FSM National Government. Debts and obligations of the NFC are not obligations of the FSM National Government unless specifically authorized by the FSM National Government. To date, no such authorization has been made.

Basis of Accounting and Basis of Presentation

National Fisheries Corporation operates as a proprietary fund type component unit of the FSM National Government. This fund type is used to account for those operations that are financed and operated in a manner similar to a private business. Because of its fund type, NFC uses the accrual basis of accounting.

Governmental 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 Principle Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. NFC has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectibility of these accounts and prior collection experience. The allowance is established through a provision for uncollectible receivables charged to expense.

Property and Equipment

Property and equipment are stated at cost or estimated historical cost, less accumulated depreciation. Donated fixed assets are recorded at estimated fair market value at the date received. The provision for depreciation is computed by the straight line method over the estimated useful lives of the assets, ranging from 3 to 15 years depending on the nature of the asset. A singular piece of equipment, vehicles, office equipment, etc. that equals or exceeds \$5,000 is capitalized, except for those assets of the investees, where no set threshold for capitalization of fixed assets has been established.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements
September 30, 2005 and 2004

(1) Summary of Significant Accounting Policies, Continued

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. In accordance with the provisions of Statement of Financial Accounting Standards No. 43, "Accounting for Compensated Absences," no liability is recorded for nonvesting accumulating rights to receive such pay benefits.

Investment and Business Development

NFC, in prior years, has invested in various joint ventures with respective agencies in the four states which are directly involved in the exploitation and development of the FSM's fisheries industry. The NFC involvement in these joint ventures varies in nature.

NFC has previously been directly involved in the management of certain joint ventures through management and marketing agreements entered into with the respective parties. The investment in Kosrae Sea Venture Inc., Chuuk Fresh Tuna Inc.(CFTI), Micronesia Longline Fishing Company (MLFC), and Yap Fishing Corporation are accounted for using the equity method and, accordingly, the carrying values of these investments, with the exception of CFTI, have been reduced to \$0. In 2005 and 2004, financial statements for these joint ventures were not available and, therefore the financial position and results of operation of these joint ventures has not been consolidated with NFC's financial statements.

The investment in Chuuk Fresh Tuna, Inc. is carried at \$486,556. No financial information has been received from this investee and NFC has therefore been unable to determine the carrying value of this investment.

Cash

As of September 30, 2005 and 2004, the carrying amount of the Corporation's total cash and cash equivalents was \$3,471 and \$220,598, and the corresponding bank balance was \$14,532 and \$437,364, respectively. These bank balances are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC). As of September 30, 2005 and 2004, bank deposits in the amount of \$14,532 and \$137,264, respectively were FDIC insured. The Corporation does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized.

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.

Inventory

Inventory of fishing supplies is valued at the lower of cost (first-in, first-out) or market.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements
September 30, 2005 and 2004

(1) Summary of Significant Accounting Policies, Continued

Net Assets

NFC has 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 – Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Disclosures" establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into the following 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.
- Restricted:
 - Nonexpendable – Net assets subject to externally imposed stipulations that require NFC to maintain them permanently. For the year ended September 30, 2005, NFC does not have nonexpendable net assets.
 - Expendable – Net assets whose use by NFC is subject to externally imposed stipulations that can be fulfilled by actions of NFC 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.

New Accounting Principles

In fiscal year 2005, NFC implemented GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3). NFC is of the opinion that the adoption of GASB Statement No. 40, did not materially impact its financial statements. In fiscal year 2006, NFC will be implementing GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. NFC has not evaluated the financial statement impact of the implementation of GASB Statement No. 42.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements
September 30, 2005 and 2004

(2) Accounts Receivable

Accounts receivable are net of an allowance for doubtful accounts as follows:

	<u>2005</u>		
	<u>Gross</u>	<u>Allowance</u>	<u>Net</u>
Trade	\$ 1,199,050	\$ 603,772	\$ 595,278
Due from affiliates	<u>869,536</u>	<u>441,420</u>	<u>428,116</u>
	<u>\$ 2,068,586</u>	<u>\$ 1,045,192</u>	<u>\$ 1,023,394</u>
	<u>2004</u>		
	<u>Gross</u>	<u>Allowance</u>	<u>Net</u>
Trade	\$ 1,414,403	\$ 672,064	\$ 742,339
Due from affiliates	<u>894,127</u>	<u>441,420</u>	<u>452,707</u>
	<u>\$ 2,308,530</u>	<u>\$ 1,113,484</u>	<u>\$ 1,195,046</u>

(3) Related Party Transactions

The Corporation has entered into various transactions with the FSM National Government. Various loans have been obtained from the FSM National Government or the FSM Development Bank, a component unit of the FSM National Government. These loans are disclosed in note 5.

(4) Property and Equipment, Net

Detail of property and equipment, net is as follows:

	<u>Balance at Beginning of Year 2005</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at End of Year 2005</u>
Machinery and equipment	\$ 28,424	\$ -	\$ -	\$ 28,424
Fishing vessels – purchased	543,423	-	-	543,423
Fishing vessels – donated	2,351,454	-	-	2,351,454
Fishing equipment – purchased	89,055	-	-	89,055
Fishing equipment – donated	464,099	-	-	464,099
Office furniture and equipment	208,221	-	-	208,221
Vehicles	<u>12,745</u>	<u>-</u>	<u>-</u>	<u>12,745</u>
	3,697,671	-	-	3,697,671
Less accumulated depreciation	<u>(3,076,710)</u>	<u>(211,974)</u>	<u>-</u>	<u>(3,288,684)</u>
	<u>\$ 620,961</u>	<u>\$ (211,974)</u>	<u>\$ -</u>	<u>\$ 408,987</u>

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements
September 30, 2005 and 2004

(4) Property and Equipment, Net, Continued

	Balance at Beginning of <u>Year 2004</u>	<u>Additions</u>	<u>Deletions</u>	Balance at End of Year 2004
Machinery and equipment	\$ 28,424	\$ -	\$ -	\$ 28,424
Fishing vessels – purchased	3,379,971	-	2,836,548	543,423
Fishing vessels – donated	2,351,454	-		2,351,454
Fishing equipment – purchased	89,055	-		89,055
Fishing equipment – donated	464,099	-		464,099
Office furniture and equipment	248,809	-	40,338	208,221
Warehouse tools and equipment	17,567	-	17,567	-
Vehicles	<u>65,566</u>	<u>-</u>	<u>52,821</u>	<u>12,745</u>
	6,644,945	-	(2,947,274)	3,697,671
Less accumulated depreciation	<u>(3,906,311)</u>	<u>(211,974)</u>	<u>(1,041,575)</u>	<u>(3,076,710)</u>
	<u>\$ 2,738,634</u>	<u>\$ (211,974)</u>	<u>\$(1,905,699)</u>	<u>\$ 620,961</u>

(5) Notes Payable

	Balance at Beginning of <u>Year 2005</u>	<u>Additions</u>	<u>Deletions</u>	Balance at End of Year 2005
National Fisheries Corporation	\$ <u>3,596,149</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>3,596,149</u>
	Balance at Beginning of <u>Year 2004</u>	<u>Additions</u>	<u>Deletions</u>	Balance at End of Year 2004
National Fisheries Corporation	\$ 3,600,000	\$ -	\$ 3,851	\$ 3,596,149
Micronesia Longline Fishing Co.	<u>4,596,907</u>	<u>-</u>	<u>4,596,907</u>	<u>-</u>
	<u>\$ 8,196,907</u>	<u>\$ -</u>	<u>\$4,600,758</u>	<u>\$ 3,596,149</u>

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements
September 30, 2005 and 2004

(5) Notes Payable, Continued

Notes payable of NFC consist of the following at September 30, 2005 and 2004:

	<u>2005</u>	<u>2004</u>
Loan payable to the FSM National Government due in annual installments of \$44,153, non-interest bearing, collateralized by NFC's shares in YFC, with a term of 16 years, beginning March 1994, ending March 2010.	\$ 750,640	\$ 750,640
Loan payable to the FSM National Government due in annual installments of \$86,639, non-interest bearing, with a term of 13 years, beginning July 1994, ending July 2007.	1,212,940	1,212,940
Loan payable to the FSM National Government due in annual installments of \$23,363, non-interest bearing, with a term of 16 years, beginning September 1994, ending September 2010.	397,176	397,176
Loan payable to FSM National Government due in annual installments of \$29,412, non-interest bearing, with a term of 17 years, beginning October 1995, ending October 2011.	500,000	500,000
Loan payable to the FSM National Government due in annual installments of \$5,000, non-interest bearing, with a term of 20 years, beginning April 1995, ending April 2014.	100,000	100,000
Loan payable to the FSM National Government due in annual installments of \$1,962, non-interest bearing, with a term of 20 years, beginning April 1995, ending April 2014.	39,244	39,244
Loan payable to the FSM National Government due in annual installments of \$5,000, non-interest bearing, with a term of 20 years, beginning November 1994, ending April 2013.	100,000	100,000
Loan payable to the FSM National Government with no terms.	500,000	500,000
Unreconciled difference	<u>(3,851)</u>	<u>(3,851)</u>
Total debt of NFC	\$ <u>3,596,149</u>	\$ <u>3,596,149</u>

NFC is in default on its debt issues and therefore, all related debt has been classified as current.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements
September 30, 2005 and 2004

(6) Contingencies

Litigation

NFC is party to several legal proceedings arising from operations. External legal counsel represents that the ultimate outcome of the lawsuits cannot be predicted at this time, therefore, no provision for any related liability is made in the financial statements.

(7) Going Concern

NFC has incurred substantial losses from operations. This condition raises substantial doubt about the Corporation's ability to continue as a going concern. NFC, as a component unit of the FSM National Government, is dependent on the FSM National Government for its cash flows.

(8) Risk Management

National Fisheries Corporation is substantially self-insured for all risks. Management is of the opinion that no material losses have been sustained as a result of this practice.

NATIONAL FISHERIES CORPORATION (NFC) AND SUBSIDIARIES

Combining Statements of Net Assets - NFC
September 30, 2005

<u>ASSETS</u>	<u>Corporate</u>	<u>Fishing Operations</u>	<u>Airfreight Operations</u>	<u>Transshipment Operations</u>	<u>Baitfish Services</u>	<u>Total</u>
Current assets:						
Cash	\$ 3,488	\$ 912	\$ 3,327	\$ (5,805)	1,549	\$ 3,471
Accounts receivable, net	5,954	27,027	(109,090)	369,543	301,844	595,278
Advances receivable, net	4,233	395	8,618	(64,571)	-	(51,325)
Inventory	-	-	152,527	-	32,148	184,675
Due from affiliates	2,974	75	157,244	102,236	165,587	428,116
Intercompany receivable, net	<u>2,083</u>	<u>(228,457)</u>	<u> </u>	<u>(8,453)</u>	<u>89,395</u>	<u>(145,432)</u>
Total current assets	18,732	(200,048)	212,626	392,950	590,523	1,014,783
Investments	486,855	-	-	-	-	486,855
Fixed assets, net	<u>-</u>	<u>404,762</u>	<u>-</u>	<u>-</u>	<u>4,225</u>	<u>408,987</u>
	<u>\$ 505,587</u>	<u>\$ 204,714</u>	<u>\$ 212,626</u>	<u>\$ 392,950</u>	<u>\$ 594,748</u>	<u>\$ 1,910,625</u>
 <u>LIABILITIES AND NET ASSETS</u>						
Current liabilities:						
Current portion of notes payable	\$ 1,783,210	\$ 1,312,939	\$ 500,000	\$ -	\$ -	\$ 3,596,149
Accounts payable	45,599	(226,243)	273,294	(9,657)	39,401	122,394
Lease payable	-	-	992,228	-	-	992,228
Accrued liabilities	<u>(710)</u>	<u>3,488</u>	<u>243</u>	<u>412</u>	<u>-</u>	<u>3,433</u>
Total liabilities	<u>1,828,099</u>	<u>1,090,184</u>	<u>1,765,765</u>	<u>(9,245)</u>	<u>39,401</u>	<u>4,714,204</u>
Net assets:						
Unrestricted	<u>(1,322,512)</u>	<u>(885,470)</u>	<u>(1,553,139)</u>	<u>402,195</u>	<u>555,347</u>	<u>(2,803,579)</u>
Total net assets	<u>(1,322,512)</u>	<u>(885,470)</u>	<u>(1,553,139)</u>	<u>402,195</u>	<u>555,347</u>	<u>(2,803,579)</u>
	<u>\$ 505,587</u>	<u>\$ 204,714</u>	<u>\$ 212,626</u>	<u>\$ 392,950</u>	<u>\$ 594,748</u>	<u>\$ 1,910,625</u>

See accompanying independent auditors' report.

NATIONAL FISHERIES CORPORATION (NFC) AND SUBSIDIARIES

Combining Statement of Revenues, Expenses and Changes in Net Assets - NFC
Year Ended September 30, 2005

	<u>Corporate</u>	<u>Fishing Operations</u>	<u>Airfreight Operations</u>	<u>Transshipment Operations</u>	<u>Baitfish Services</u>	<u>Total</u>
Sales	\$ 7,758	\$ 32,657	\$ 985,125	\$ 63,462	\$ 286,049	\$ 1,375,051
Cost of sales	<u>-</u>	<u>67,421</u>	<u>991,154</u>	<u>-</u>	<u>210,150</u>	<u>1,268,726</u>
Gross profit (loss)	<u>7,758</u>	<u>(34,764)</u>	<u>(6,030)</u>	<u>63,462</u>	<u>75,899</u>	<u>106,326</u>
Operating expenses:						
Depreciation and amortization	-	211,975	-	-	-	211,975
Salaries and wages	37,525	30,550	110,630	45,865	-	224,570
Rent	11,130	6,651	40,297	8,000	12,600	78,678
Telephone and communication	13,561	-	9,726	1,500	600	25,387
Travel and entertainment	6,225	4,873	3,496	6,327	-	20,921
Utilities	3,885	-	4,320	800	24,093	33,098
Payroll and other taxes	3,963	3,351	11,696	3,074	-	22,084
Repairs and maintenance	-	4,061	-	-	-	4,061
Office expense	1,057	35	11,746	2,706	75	15,619
Representation	6,344	-	1,815	1,467	-	9,627
Contractual services	-	-	1,150	614	-	1,764
Miscellaneous	<u>2,243</u>	<u>2,600</u>	<u>12,109</u>	<u>(13,537)</u>	<u>539</u>	<u>3,954</u>
Total operating expenses	<u>85,933</u>	<u>264,096</u>	<u>206,985</u>	<u>56,817</u>	<u>37,907</u>	<u>651,738</u>
Operating income (loss)	<u>(78,175)</u>	<u>(298,860)</u>	<u>(213,015)</u>	<u>6,646</u>	<u>37,992</u>	<u>(545,412)</u>
Other income (expense):						
FSM appropriation	-	-	100,000	-	-	100,000
Other income (expense), net	<u>69,339</u>	<u>326,432</u>	<u>(147,824)</u>	<u>249,904</u>	<u>(128,206)</u>	<u>369,645</u>
Total other income (expense), net	<u>69,339</u>	<u>326,432</u>	<u>(47,824)</u>	<u>249,904</u>	<u>(128,206)</u>	<u>469,645</u>
Decrease in net assets	(8,836)	27,572	(260,839)	256,550	(90,215)	(75,768)
Net assets at beginning of year	<u>(1,313,676)</u>	<u>(913,042)</u>	<u>(1,292,300)</u>	<u>145,645</u>	<u>645,562</u>	<u>(2,727,811)</u>
Net assets at end of year	\$ <u><u>(1,322,512)</u></u>	\$ <u><u>(885,470)</u></u>	\$ <u><u>(1,553,139)</u></u>	\$ <u><u>402,195</u></u>	\$ <u><u>555,347</u></u>	\$ <u><u>(2,803,579)</u></u>

See accompanying independent auditors' report.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Consolidating Statement of Net Assets
September 30, 2005

ASSETS	National Fisheries Corporation	Micronesia Longline Fishing Co., Inc.	Combined Balance	Consolidating Entries		Consolidated Balance
				Debit	Credit	
Current assets:						
Cash	\$ 3,471	\$ -	\$ 3,471	\$ -	\$ -	\$ 3,471
Accounts receivable, net	595,278	-	595,278	-	-	595,278
Advances receivable, net	(51,325)	-	(51,325)	-	-	(51,325)
Inventory	184,675	-	184,675	-	-	184,675
Due from affiliates	428,116	-	428,116	-	-	428,116
Intercompany receivables, net	(145,432)	-	(145,432)	145,432	-	-
Total current assets	1,014,783	-	1,014,783	145,432	-	1,160,215
Investments	486,855	-	486,855	-	-	486,855
Fixed assets, net	408,987	-	408,987	-	-	408,987
	<u>\$ 1,910,625</u>	<u>\$ -</u>	<u>\$ 1,910,625</u>	<u>\$ 145,432</u>	<u>\$ -</u>	<u>\$ 2,056,057</u>
<u>LIABILITIES AND NET ASSETS</u>						
Liabilities:						
Current portion of notes payable	\$ 3,596,149	\$ -	\$ 3,596,149	\$ -	\$ -	\$ 3,596,149
Accounts payable	122,394	-	122,394	-	-	122,394
Lease payable	992,228	-	992,228	-	-	992,228
Accrued liabilities and others	3,433	-	3,433	-	145,432	148,865
Total liabilities	4,714,204	-	4,714,204	-	145,432	4,859,636
Net assets:						
Investment in fixed assets	-	-	-	803,953	-	(803,953)
Unrestricted	(2,803,579)	-	(2,803,579)	-	803,953	(1,999,626)
Total net assets	(2,803,579)	-	(2,803,579)	803,953	803,953	(2,803,579)
	<u>\$ 1,910,625</u>	<u>\$ -</u>	<u>\$ 1,910,625</u>	<u>\$ 803,953</u>	<u>\$ 949,385</u>	<u>\$ 2,056,057</u>

See accompanying independent auditors' report.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

Consolidating Statement of Revenues, Expenses and Changes in Net Assets
Year Ended September 30, 2005

	National Fisheries Corporation	Micronesia Longline Fishing Co., Inc.	Combined Balance	Consolidating Entries		Consolidated Balance
				Debit	Credit	
Sales	\$ 1,375,051	\$ -	\$ 1,375,051	\$ -	\$ -	\$ 1,375,051
Cost of Sales	<u>1,268,726</u>	<u>-</u>	<u>1,268,726</u>	<u>-</u>	<u>-</u>	<u>1,268,726</u>
Gross profit	<u>106,326</u>	<u>-</u>	<u>106,326</u>	<u>-</u>	<u>-</u>	<u>106,326</u>
Operating Expenses:						
Depreciation and amortization	211,975	-	211,975	-	-	211,975
Salaries and wages	224,570	-	224,570	-	-	224,570
Rent	78,678	-	78,678	-	-	78,678
Telephone and communication	25,387	-	25,387	-	-	25,387
Travel and entertainment	20,921	-	20,921	-	-	20,921
Utilities	33,098	-	33,098	-	-	33,098
Payroll and other taxes	22,084	-	22,084	-	-	22,084
Repairs and maintenance	4,061	-	4,061	-	-	4,061
Office expense	15,619	-	15,619	-	-	15,619
Representation	9,627	-	9,627	-	-	9,627
Contractual services	1,764	-	1,764	-	-	1,764
Miscellaneous	<u>3,954</u>	<u>-</u>	<u>3,954</u>	<u>-</u>	<u>-</u>	<u>3,954</u>
Total operating expenses	<u>651,738</u>	<u>-</u>	<u>651,738</u>	<u>-</u>	<u>-</u>	<u>651,738</u>
Operating loss	<u>(545,412)</u>	<u>-</u>	<u>(545,412)</u>	<u>-</u>	<u>-</u>	<u>(545,412)</u>
Other income (expense):						
FSM appropriation	100,000	-	100,000	-	-	100,000
Other income (expenses), net	<u>369,645</u>	<u>-</u>	<u>369,645</u>	<u>-</u>	<u>-</u>	<u>369,645</u>
Total other income (expense), net	<u>469,645</u>	<u>-</u>	<u>469,645</u>	<u>-</u>	<u>-</u>	<u>469,645</u>
Increase (decrease) in net assets	(75,768)	-	(75,768)	-	-	(75,768)
Total net assets at beginning of year	<u>(2,727,811)</u>	<u>-</u>	<u>(2,727,811)</u>	<u>-</u>	<u>-</u>	<u>(2,727,811)</u>
Total net assets at end of year	<u>\$ (2,803,579)</u>	<u>\$ -</u>	<u>\$ (2,803,579)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (2,803,579)</u>

See accompanying independent auditors' report.

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

The Board of Directors
National Fisheries Corporation:

We were engaged to audit the financial statements of the National Fisheries Corporation (NFC), as of and for the year ended September 30, 2005, and have issued our report thereon dated February 7, 2007, which stated that the scope of our work was not sufficient to enable us to express, and we did not express, an opinion on the financial statements due to: of inadequacies in the accounting records, detailed records regarding cash, accounts receivable, intercompany receivables and payables, inventory, investment, fixed assets, accounts payable, lease payable, sales, and non-operating income related supporting data were not available for the audit.

Internal Control Over Financial Reporting

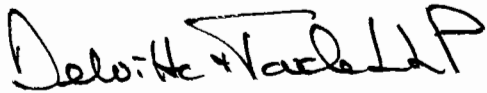
In planning and performing our audit, we considered NFC's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, 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 NFC'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 as items 2005-1 through 2005-22.

A material weakness is a reportable 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 caused by error or fraud 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 believe finding numbers 2005-1, 2005-3, 2005-5, 2005-8 through 2005-10, 2005-12, 2005-15, 2005-21 and 2005-22 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether NFC'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 Board of Directors and management of NFC, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than these specified parties.

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

February 7, 2007

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Absence of Investee's Financial Statements

Finding No. 2005-1

Criteria: Adequate documentation, i.e. investee's audited financial statements, should be available to support amounts reported in the financial statements.

Condition: Financial statements supporting NFC's investment in Chuuk Fresh Tuna, Inc. are not available for inspection.

Cause: The cause of this condition is that financial statements from the investee have not been provided.

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

Prior Year Status: This condition has been reported in prior year audits.

Recommendation: We recommend that management ensure that its investees provide audited financial statements on an annual basis.

Auditee Response: CFTI has already phased out its operations prior to fiscal year 2005. The absence of appropriate staffs to assist in the audit makes it impossible for NFC to get audited financial statements from CFTI. NFC plans to ask FSM government to fund a separate audit for all its subsidiary companies.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Receivables

Finding No. 2005-2

Criteria: Adequate documentation, including subsidiary ledgers, should be available to support amounts and items reported in the financial statements.

Condition: No subsidiary ledger supporting \$ 14,646 of recorded advances was available for inspection.

<u>Division</u>	<u>Acct. #</u>	<u>Description</u>	
Airfreight Operation	1230	Advances - Empl.	\$ 8,618
Comm. Fishing	1230	Advance-Employee	395
Baitfish	1230	Advances - Employee	1,400
Corporate Office	1225	Advances Rec. - Travel	919
Corporate Office	1230	Advance - Employee	<u>3,314</u>
		Total	\$ <u>14,646</u>

NFC was not able to provide the rationale for \$16,737 of recorded suspense accounts. A subsidiary ledger supporting this amount was not available for inspection.

<u>Division</u>	<u>Acct. #</u>	<u>Description</u>	
Comm_fishing	2700	Suspense	\$ 75
Baitfish	2700	Suspense	<u>16,662</u>
		Total	\$ <u>16,737</u>

Cause: The root cause of the weakness is that a subsidiary ledger was not maintained.

Effect: As a result of this condition, advances of \$ 14,646 are deemed uncollectible due to the absence of a subsidiary ledger. Also, there is a potential material misstatement of the financial statements.

Recommendation: We recommend that NFC ensure maintenance of all subsidiary ledgers to support amounts reported in the financial statements.

Auditee Response: We concur with the finding and already included this finding with other problems that were reported to NFC Board of Directors regarding missing records, files and documents. The new management of NFC will ensure that this finding will not occur in fiscal year 2006.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Receivables, Continued

Finding No. 2005-3

Criteria: Amounts reported in the financial statements should agree with subsidiary records.

Condition: The total of trade receivables and due from affiliates per the general ledger does not agree with the provided aging schedule.

<u>Division</u>	<u>Per books</u>	<u>Per aging</u>	<u>Variance</u>
Airfreight	\$ 667,877	\$ 649,963	\$ 17,913
Baitfish	675,556	747,751	(72,195)
Comm fishing	65,562	6,734	58,828
Corporate	8,928	-	8,928
Transshipment	633,926	75,677	558,249

Cause: The root cause of the weakness is that subsidiary records, i.e. aging schedules, are not reconciled with the general ledger.

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

Recommendation: We recommend that NFC ensure that subsidiary records reconcile with the general ledger and that the reconciliation occurs periodically throughout the year.

Auditee Response: NFC is in the process of performing reconciliations of general ledger with subsidiary ledger and will continue it as part of the current accounting procedures and practices to ensure reporting of correct and accurate accounts in the financial statements.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Receivables, Continued

Finding No. 2005-4

Criteria: Amounts reported in the financial statements should both reasonable and valid.

Condition: NFC recorded an allowance of \$64,374 for bad debts potentially arising from advances. However, we noted that the advance account reflects a negative balance of \$197.

<u>Division</u>	<u>Acct. #</u>	<u>Description</u>	<u>Per book</u>
Transshipment	1230	Advances Employee	(197)
Transshipment	1298	Allowance for Bad Debts - Advances	(64,374)

Cause: The root cause of the weakness is that inadequate reconciliation efforts have been applied to the financial statements.

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

Recommendation: We recommend that NFC ensure that the allowance for doubtful accounts is reasonably and correctly calculated.

Auditee Response: The new management and accounting office could not justify why this finding exist. However, we will take corrective measures and prepare the necessary analysis of this account and make the appropriate correcting entries to ensure proper recording of transactions.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Fixed Assets

Finding No. 2005-5

Criteria: Adequate documentation, including subsidiary records, should be available to support amounts and items reported in the financial statements.

Condition: Subsidiary records, i.e. the fixed asset register, supporting \$ 408,987 of net fixed assets were not available for inspection.

<u>Acct. #</u>	<u>Description</u>		
1705	Office Furniture & Eqpmnt.	\$	37,072
1715	Fishing Vessel		543,423
1720	Fishing Equipment		89,055
1730	Fishing Vessels Donated		2,351,454
175031	Acc. Depr.-NFC Kosrae		(65,210)
175033	Acc. Depr.-NFC Waab		(479,002)
175035	Acc. Depr.-NFC Chuuk		(670,561)
175037	Acc. Depr.-NFC Pohnpei		(670,560)
175039	Acc. Depr.-NFC Cpt. Honda		(604,782)
1760	Accum Depreciation		<u>(126,127)</u>
	Total – Comm-fishing	\$	<u>404,762</u>

<u>Acct. #</u>	<u>Description</u>		
1705	Office Fur. & Eqpmnt.	\$	1,595
1707	Machineries & Eqpmnt.		13,749
1760	Accum. Depreciation		<u>(11,119)</u>
	Total - Baitfish	\$	<u>4,225</u>

Cause: The root cause of the condition is that subsidiary records are not maintained in a correct manner.

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

Recommendation: We recommend that NFC ensure that subsidiary records are properly maintained.

Auditee Response: Missing records is the main cause for this finding and the actual reason for these missing files is still being sought. The previous accounting system was adequate and former staffs were capable however the records were not properly maintained and there was no proper turn-over of records and files to new staffs. We will try to locate the records and make the report accordingly.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Depreciation Expense

Finding No. 2005-6

Criteria: Depreciation expense should be accurately calculated and recorded.

Condition: For 4 of 5 (80%) samples tested, depreciation expense was incorrectly calculated.

Asset Description	Per DTT	Per NFC	Variance
Depr. - Kosrae	\$ 36,228	\$ 32,605	\$ 3,623
Depr. - Waab	36,228	32,605	3,623
Depr. - Chuuk	49,921	44,921	5,000
Depr. - PNI	49,921	44,921	<u>5,000</u>
		Total	\$ <u>17,245</u>

Cause: The root cause of the weakness is an incorrect calculation of depreciation expense.

Effect: The effect of this condition is a misstatement of depreciation expense of \$ 17,245.

Recommendation: We recommend that NFC ensure that accurate calculations of depreciation expense are performed.

Auditee Response: We have corrected the depreciation calculation of all NFC major equipments including fishing vessels in fiscal year 2006. The cause of the finding may be due to lack of capability of staff that did the calculations for fiscal year 2005. In fiscal year 2006, NFC has hired an accountant to ensure accuracy of calculating depreciation. Additional staff is also being considered by NFC to assist the accountant in handling the accounting activities of NFC.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Intercompany Transactions

Finding No. 2005-7

Criteria: NFC should ensure that intercompany transactions are properly reconciled and eliminated from the consolidated financial statements.

Condition: Intercompany receivables and payables net to an out-of-balance condition of \$7,095 and inadequate documentation exists to support the manner in which this amount should be corrected.

Cause: The cause of this condition is because of the numerous general ledgers kept to account for NFC's activities, inter-fund receivable/payable and income/expense out-of balance conditions continue to occur.

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

Prior Year Status: This condition was reported in the National Fisheries Corporation audits for fiscal years 1997, 1998, 1999, 2000, 2001, 2002, and 2004.

Recommendation: We recommend that NFC maintain only one general ledger for Corporate, Fishing, Air-freight, Baitfish, Transshipment, and Chartered Boat divisions to mitigate the risk of having inter-company receivable/payable and income/expense out-of-balance conditions.

Auditee Response: We concur with this finding which had been cited in previous years. The analysis of inter-company receivable/payable is in process. After the appropriate analysis, adjusting entries will be made to maintain one consolidated general ledger accounts for all the operations of NFC.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Liabilities

Finding No. 2005-8

Criteria: Amounts reported in the financial statements should agree with subsidiary records.

Condition: Based on the following analysis, payables per the general ledger do not agree with applicable aging schedules.

<u>Division</u>	<u>Per g/l</u>	<u>Per aging</u>	<u>diff</u>
Airfreight operations	\$ (273,294)	\$ (262,333)	\$ (10,961)
Baitfish	(39,401)	(37,878)	(1,523)
Comm fishing	226,243	(19,130)	245,373
Corporate	(45,599)	(80,056)	34,457
Transshipment	9,657	(85,342)	94,999

Cause: The root cause of the weakness is that subsidiary records, i.e. aging schedules, are not periodically reconciled with the general ledger.

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

Recommendation: We recommend that NFC periodically ensure that subsidiary records reconcile with the general ledger.

Auditee Response: We agree with the recommendation and in the process of analyzing and undertaking regular reconciliations of the general ledger with subsidiary ledgers and schedules starting fiscal year 2006.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Other Income

Finding No. 2005-9

Criteria: Adequate documentation, including subsidiary records, should be available to support amounts and items reported in the financial statements.

Condition: Subsidiary records supporting \$ 14,817 of other income are not available for inspection.

<u>Division</u>	<u>#</u>	<u>Description</u>	<u>Amount</u>
AF_operation	9120	Other Income	\$ 3,580
Comm_fishing	9090	Misc. Income	(341)
Corporate	3900	Miscellaneous Income	(17,700)
Corporate	9090	Miscellaneous Income	(356)
		Total	\$ (14,817)

Documentation supporting \$100,000 of cargo subsidy (revenue account) are not available for inspection.

<u>Division</u>	<u>#</u>	<u>Description</u>	<u>Amount</u>
AF_operation	9140	Cargo Subsidy	\$ (100,000)

Subsidiary records supporting the following account balances are not available for inspection.

<u>Division</u>	<u>#</u>	<u>Description</u>	<u>Amount</u>
AF_operation	9910	Prior Period Expense	\$ (5,335)
AF_operation	9920	Interco. Inc. / Exp.	149,580
Comm_fishing	9200	Gain Sales of Assets	(2,000)
Comm_fishing	9920	Intercompany Inc./Exp.	(324,091)
Corporate	9200	Gain on Sale of Fix Asset	(42,000)
Corporate	9920	Interco. Income /Expense	(7,053)
Baitfish	9920	Intercompany Inc./Exp.	128,206
Transshipment	9090	Miscellaneous Income	(203,503)
Transshipment	9200	Gain Sales on Fixed Assets	(99,975)
Transshipment	9920	Intercompany Inc./Exp.	53,574
		Total	\$ (352,597)

Cause: The root cause of the weakness is that subsidiary records are not correctly maintained.

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

Recommendation: We recommend that NFC ensure appropriate maintenance of all subsidiary ledgers to support amounts reported in the financial statements.

Auditee Response: We concur with the finding. For fiscal year 2006, all transactions relating to other income are duly supported by documents and available for inspection.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Revenue

Finding No. 2005-10

Criteria: Adequate documentation, including subsidiary records/ledgers, should be available to support amounts and items reported in the financial statements.

Condition: Subsidiary records/ledgers, i.e. accounts receivable consolidated G/L transfers control report, supporting \$ 95,269 of operating revenues, were not available for inspection.

<u>Division</u>	<u>Account #</u>	<u>Description</u>	<u>Transaction date per detail TB</u>	<u>Amount</u>
Baitfish Supplies & Services	3500	Fish grading	2/29/2004	\$ 1,750
Baitfish Supplies & Services	3851	Sales - Baitfish/PNI	2/29/2004	15,714
Baitfish Supplies & Services	3861	Sales - C/Boxes-PNI	2/29/2004	17,415
Baitfish Supplies & Services	3861	Sales - C/Boxes-PNI	4/30/2004	14,228
Baitfish Supplies & Services	3871	Sales - Gel Ice - PNI	2/29/2004	3,162
Baitfish Supplies & Services	3871	Sales - Gel Ice - PNI	4/30/2004	2,558
Airfreight Operation	3101	PNI Tuna Flt. Charges	8/31/2004	<u>40,442</u>
		Total		\$ <u>95,269</u>

Cause: The root cause of the weakness is that subsidiary ledgers are not maintained.

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

Recommendation: We recommend that NFC ensure maintenance of all subsidiary ledgers to support amounts reported in the financial statements.

Auditee Response: We concur with the finding and agree with the recommendation. For fiscal year 2006, all operating revenues are duly supported by documents and available for inspection.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Management Fees

Finding No. 2005-11

Criteria: Amounts reported in the financial statements should be valid.

Condition: The management contracts for Kosrae Sea Venture, Inc. and Ettal Municipal Government terminated on April 22, 1998 and January, 20, 1999, respectively. The termination of the contract with Ettal Municipal Government was acknowledged by NFC's lawyer in a memo to Ettal Investment Corporation dated October 5, 2000. However, management fees for these contracts continued to be recorded throughout fiscal year 2005.

Cause: The root cause of this condition is an inadequate review of underlying source documentation.

Effect: Revenue of some \$7,758 was recorded in error.

Recommendation: We recommend that NFC ensure that all amounts reported in the financial statements are valid.

Auditee Response: The management contract was extended again but was not formalized into a written agreement. NFC continued to manage the vessels until early part of fiscal year 2006 when Ettal finally took their vessel. KSVI is in the process of terminating the contract and in taking possession of their vessel.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Cash

Finding No. 2005-12

Criteria: Amounts reported in the financial statements should agree with subsidiary records.

Condition: The cash balance per the general ledger does not agree with the underlying bank reconciliation.

<u>Acct #</u>	<u>Description</u>	<u>Per bank recon</u>	<u>Per book</u>	<u>Difference</u>
1020	CIB BOG (Chk.)	\$128,364	\$(36,286)	\$164,650

Cause: The root cause of the condition is that subsidiary records, i.e. bank reconciliations, are not reconciled with the general ledger on a timely basis. Reconciling items should be recorded in a timely manner and unknown variances thoroughly investigated.

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

Recommendation: We recommend that subsidiary records be timely reconciled with the general ledger and that variances be investigated and disposed of in a timely manner.

Auditee Response: We agree with the recommendation and in the process of analyzing and undertaking regular bank reconciliations for fiscal year 2006.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Inventory

Finding No. 2005-13

Criteria: The number of inventory items contained in final inventory lists should agree with actual counts conducted.

Condition: Of three samples tested, one item had variances. The quantities initially counted and observed varied with quantities on the final inventory report as follows.

	a	b	c	d	a-c	b-d
	Agreed upon <u>count</u>	Total \$ <u>Value</u>	Qty per Final Inventory <u>List</u>	\$ Value per Final <u>Inventory</u>	Quantity <u>Variance</u>	\$ Value <u>Variance</u>
1 Rain Coats	267	265.20	27	275.40	(1)	(10.20)

Cause: The root cause of the weakness is a lack of proper inventory record keeping.

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

Recommendation: We recommend that NFC ensure that inventory records are reconciled with general ledger balances and be properly maintained.

Auditee Response: We concur and agree with the finding and recommendation. The correction is in progress for fiscal year 2006 and updating of inventory count and accounts will be handled to reflect the correct balance of inventory based on the physical count.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Missing Invoices

Finding No. 2005-14

Criteria: Inventories bought and accounted for should be supported by invoices.

Condition: For 3 of 3 (100%) of samples, no invoices could be provided to support the inventory cost.

Per Final Inventory Listing

	<u>Description</u>	<u>Unit</u>	<u>Qty</u>	<u>Unit Cost</u>	<u>Extension</u>
1	Brush Steel OVL	brush	15	\$ 1.34	\$ 20.07
2	Cutter Wire 18MM	H wire	70	6.35	444.50
3	BF MOR Shine	Moruaji Shine	1398	12.70	17,754.60

Cause: The root cause of the weakness is a lack of control over recordkeeping.

Effect: The effect of this condition is a potential misstatement of inventory as there is no record of the purchase of the item.

Recommendation: We recommend that National Fisheries Corporation exercise more stringent adherence to existing document policies to prevent the disappearance of necessary supporting documentation

Auditee Response: Poor record keeping was a problem in prior years but it is now corrected as part of the new management accounting procedures and system. Files and records for fiscal year 2006 are kept intact and available for inspection to support the recorded transactions.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Other Income

Finding No. 2005-15

Criteria: Adequate documentation, including subsidiary records, should be available to support amounts and items reported in the financial statements.

Condition: Subsidiary records supporting \$170,018 of other income are not available for inspection.

<u>Acct #</u>	<u>Description</u>	<u>Per book</u>
9120	Other Income	\$ 12,932
9920	Intercompany Inc./Exp.	53,000
3900	Miscellaneous Income	14,862
9090	Miscellaneous Income	2,700
9090	Miscellaneous Income	86,524

Additionally documentation supporting \$152,368 of cargo subsidy (revenue account) is not available for inspection.

Cause: The root cause of the weakness is that subsidiary records are not maintained.

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

Recommendation: We recommend that NFC ensure maintenance of all subsidiary ledgers to support amounts reported in the financial statements.

Auditee Response: We concur with the finding and recommendation. For fiscal year 2006, all transactions relating to other income are duly supported by documents and available for inspection.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Cash

Finding No. 2005-16

Criteria: Amounts reported in the financial statements should agree with subsidiary records.

Condition: The cash balance per the general ledger does not agree with the underlying bank reconciliation.

<u>Division</u>	<u>Acct #</u>	<u>Description</u>	<u>\$</u> <u>Per book</u>	<u>Per bank</u> <u>recon</u>	<u>\$</u> <u>Variance</u>
Transshipment	1019	CIB BOG (PNI)	(1,872)	0	(1,872)

Cause: The root cause of the condition is that subsidiary records, i.e. bank reconciliations, are not reconciled with the general ledger on a timely basis. Reconciling items should be recorded in a timely manner and unknown variances thoroughly investigated.

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

Recommendation: We recommend that subsidiary records be timely reconciled with the general ledger and variances be investigated and disposed of in a timely manner.

Auditee Response: We agree with the finding and recommendation, and in the process of analyzing and undertaking regular bank reconciliations for fiscal year 2006.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Inventory

Finding No. 2005-17

Criteria: The number of inventory items contained in final inventory lists should agree with actual counts conducted.

Condition: Of five samples tested, four items (80%) reflected variances. The quantities initially counted and observed varied with quantities on the final inventory report as follows.

	a	b	c	d	a-c	b-d
	Agreed upon count	Total \$ Value	Qty per Final Inventory List	\$ Value per Final Inventory	Quantity Variance	\$ Value Variance
<u>Sheet to Floor</u>						
1 Boxes Renolith	957.00	0.00	-	-	957.00	0.00
2 Box Sea Pak	3,024.00	30,075.62	37.00	367.99	2,987.00	29,707.63
<u>Floor to Sheet</u>						
1 130x1000 Rope BR3.5 x	6.00	88.51	30.00	442.56	(24.00)	(354.05)
2 1200	16.00	1,760.00	9.00	990.00	7.00	770.00

Cause: The root cause of the weakness is a lack of inventory record keeping.

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

Recommendation: We recommend that NFC ensure that inventory records are reconciled with general ledger balances.

Auditee Response: We concur and agree with the finding and recommendation. The correction is in progress in fiscal year 2006 and updating of inventory count and accounts will be handled to reflect the correct balance of inventory based on the physical count.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Inventory

Finding No. 2005-18

Criteria: Amounts reported in the financial statements should agree with subsidiary records.

Condition: The inventory per the general ledger does not agree with the provided subsidiary record, i.e. inventory valuation report.

<u>Division</u>	<u>Per G/L</u>	<u>Per detailed schedule</u>	<u>Variance</u>
Baitfish	\$ 30,747	\$ 71,905	\$ (41,158)

Cause: The root cause of the weakness is that subsidiary records, i.e. the inventory valuation report, are not reconciled with the general ledger.

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

Recommendation: We recommend that NFC ensure that subsidiary records reconcile with the general ledger and that the reconciliation occurs periodically throughout the year.

Auditee Response: As stated in finding 13 and 17, we concur and agree with the finding and recommendation relating to inventory. The correction is in progress in fiscal year 2006 and updating of inventory count and accounts will be handled to reflect the correct balances of inventory based on the physical count.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Missing Invoices

Finding No. 2005-19

Criteria: Inventories bought and accounted for should be supported by invoices.

Condition: For one of four items tested, no invoices could be provided to support the price.

<u>Sel'n</u>	<u>Description</u>	<u>unit</u>	<u>Per Final Inventory Listing</u>			<u>Per Vendor's Invoice</u>	
			<u>Qty</u>	<u>Unit Cost</u>	<u>Extension</u>	<u>Vendor</u>	<u>Invoice #</u>
1	Presser-Hand730	Hand Presser - 730MM	3	\$ 220.00	\$ 660.00	n/a	No invoice provided

Cause: The root cause of the weakness is a lack of control over recordkeeping.

Effect: The effect of this condition is a potential misstatement of inventory as there is no record of the purchase of the item.

Recommendation: We recommend that National Fisheries Corporation exercise more stringent adherence to existing document policies to prevent the disappearance of necessary supporting documentation.

Auditee Response: Again we agree with the finding and recommendation, and we have the same response relating to missing invoice as stated in finding 2005-14.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Unsupported Revenue

Finding No. 2005-20

Criteria: Adequate source documentation should be available to support amounts and items reported in the financial statements.

Condition: For 47 of 47 (100%) samples tested, NFC could not provide the cash receipts, bank validated deposit slips and/or bank statements, and sales invoices. As such, we could not ensure the completeness and validity of the recorded amounts. Also, we could not determine if amounts collected were accordingly deposited to the bank.

Division	Account #	Reference #	\$ Amount
Airfreight Operation	3101	300390	16,368
Airfreight Operation	3101		25,762
Airfreight Operation	3101	300390-300391	21,757
Airfreight Operation	3101		68,215
Airfreight Operation	3101	300383	21,134
Airfreight Operation	3101	300373	9,300
Airfreight Operation	3101	300358	18,804
Airfreight Operation	3101	300351	20,631
Airfreight Operation	3101	300331	7,510
Airfreight Operation	3101	300302	3,905
Airfreight Operation	3101	300294	20,007
Airfreight Operation	3101	300260	16,074
Airfreight Operation	3501	JE-10003	20,142
Airfreight Operation	3501	JE-01001	1,000
Airfreight Operation	3501	GUM-0512	800
Airfreight Operation	3502	GUM-1223	7,692
Airfreight Operation	3505	300375	4,486
Airfreight Operation	3599	300385	1,470
Airfreight Operation	3101	300283	23,139
Airfreight Operation	3101	300296	20,842
Airfreight Operation	3101	300320	21,828
Airfreight Operation	3101	300329	24,421
Airfreight Operation	3101	300341	28,494
Airfreight Operation	3501	JE-03002	20,794
Airfreight Operation	3101	300270	10,758
Airfreight Operation	3101	300311	11,093
Airfreight Operation	3101	300382	3,628
Airfreight Operation	3101	300396	14,712
Airfreight Operation	3101	300363	12,538
Airfreight Operation	3101	GUM-0128	2,652
Airfreight Operation	3501	GUM-0708	2,413
Airfreight Operation	3501	GUM-0318	2,961
Airfreight Operation	3505		4,863
Airfreight Operation	3599		7,300
Baitfish Supplies & Services	3851	212068	5,400
Baitfish Supplies & Services	3851	212178	6,300

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Unsupported Revenue, Continued

Finding No. 2005-20, Continued

Baitfish Supplies & Services	3851	212232	3,600
Baitfish Supplies & Services	3861	212091	1,035
Baitfish Supplies & Services	3881	212094	1,438
Baitfish Supplies & Services	3881	212049	4,860
Baitfish Supplies & Services	3851	212089	5,040
Baitfish Supplies & Services	3851	212163	8,100
Baitfish Supplies & Services	3861	212185	3,240
Commercial Fishing	301039	CR080504	11,996
Commercial Fishing	301039	CR080505	6,540
Transshipment	3829	JE-09018	24,700
Transshipment	3829	JE-09016	<u>18,200</u>
		Total	\$ <u>597,941</u>

Cause: The root cause of the weakness is lack of control over recordkeeping.

Effect: The effect of this condition is a potential material misstatement of the financial statements. Moreover, due to the absence of cash receipts and bank validated deposit slips, the risk of misappropriation of cash collected appears to be high.

Recommendation: We recommend that more stringent documentation policies be considered to prevent the disappearance of underlying documentation.

Auditee Response: We concur with the finding and agree with the recommendation. The nature of the cited samples seems legitimate and regular revenue transactions of NFC. However, files and records could not be located for inspection during the audit. We do consider this problem as a serious matter to be reported to the NFC Board of Directors for corrective action. For fiscal year 2006, all operating revenues are duly supported by documents and available for inspection.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Unsupported Expenditures – Cost of Sales, Administrative Expenses

Finding No. 2005-21

Criteria: Adequate source documentation must be available to support amounts and items reported.

Condition: For 47 of 114 (41%) samples tested, NFC was not able to provide the underlying documentation, i.e. vendor invoice, contracts, or any related documentation, to support the recorded expenditures.

<u>Sl'n</u>	<u>Division</u>	<u>Acct. #</u>	<u>Acct. name</u>	<u>Reference #</u>	<u>\$ Amount</u>
1	Airfreight Operations	4160	Charter fees	2637	26,606.00
2	Airfreight Operations	4160	Charter fees	2726	26,765.00
3	Airfreight Operations	4160	Charter fees	3077	26,924.00
4	Airfreight Operations	4160	Charter fees	3846	26,924.00
5	Airfreight Operations	4160	Charter fees	4081	30,315.25
6	Airfreight Operations	4160	Charter fees	4264	30,907.00
7	Airfreight Operations	4150	Freight Forwarding	AE040068	6,342.50
8	Airfreight Operations	4150	Freight Forwarding	AE030080	1,146.20
9	Airfreight Operations	4150	Freight Forwarding	AEIVNRTO	8,697.25
10	Airfreight Operations	4150	Freight Forwarding	AE040038	4,479.60
11	Airfreight Operations	4159	Ground Handling	NFC-02-0	1,650.00
12	Airfreight Operations	4160	Charter fees	3812	13,285.50
13	Airfreight Operations	4160	Charter fees	3863	17,360.86
14	Airfreight Operations	4160	Charter fees	MFV 0804	17,147.65
15	Airfreight Operations	4162	Cargo Handling expense	GUM-1371	4,422.85
16	Airfreight Operations	4162	Cargo Handling expense	GUM-1551	1,150.00
17	Airfreight Operations	4162	Cargo Handling expense	GUM-1719	3,059.00
18	Airfreight Operations	4165	Landing fees	5725-IN	2,100.00
19	Airfreight Operations	5008	Salaries & wages	JE - 08008	986.21
20	Airfreight Operations	5008	Salaries & wages		4,609.49
21	Airfreight Operations	5008	Salaries & wages		4,715.87
22	Airfreight Operations	5008	Salaries & wages		4,435.10
23	Airfreight Operations	7608	Rent expense	JE-09010	1,164.38
24	Airfreight Operations	7400	Communications	GUM-1684	463.84
25	Airfreight Operations	7200	Office expense	JE-09008	5,334.85
26	Airfreight Operations	7101	Packing materials	1057	2,160.00
27	Baitfish Supplies & Services	4501	Inventory- Baitfish	JE-010401	27,137.50
28	Baitfish Supplies & Services	4502	Inventory- Baitfish	JE-090401	24,237.50
29	Baitfish Supplies & Services	4503	Inventory- Baitfish	JE-090409	30,362.50
30	Baitfish Supplies & Services	4501	COS - Inventory Baitfish	JE-110302	23,362.50
31	Baitfish Supplies & Services	4501	COS - Inventory Baitfish	JE-030401	6,537.50
32	Baitfish Supplies & Services	4501	COS - Inventory Baitfish	JE-050408	18,875.00
33	Baitfish Supplies & Services	4501	COS - Inventory Baitfish	JE-090413	10,437.50
34	Baitfish Supplies & Services	4601	COS - Inventory Boxes	JE-110306	13,185.35
35	Baitfish Supplies & Services	4601	COS - Inventory Boxes	JE-120302	19,107.84
36	Baitfish Supplies & Services	4601	COS - Inventory Boxes	JE-030402	10,595.12
37	Baitfish Supplies & Services	4601	COS - Inventory Boxes	JE-090402	10,731.36
38	Baitfish Supplies & Services	4801	COS - Inventory F/Gears	JE-030404	2,692.51
39	Baitfish Supplies & Services	8705	Utilities	15105900	2,080.20
40	Baitfish Supplies & Services	7600	Off/ House rental	RENT-04/	600.00
41	Corporate Operation	5005	Salaries - NFC	MEMO DAT	6,229.44
42	Corporate Operation	5005	Salaries - NFC	Leave Co	8,653.86
43	Corporate Operation	7600	Rent - NFC	HA-11/20	600.00
44	Commercial Fishing	502599	Salaries-Admin	40 hrs. - CA	442.31

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Unsupported Expenditures – Cost of Sales, Administrative Expenses, Continued

Finding No. 2005-21, Continued

<u>Sl'n</u>	<u>Division</u>	<u>Acct. #</u>	<u>Acct. name</u>	<u>Reference #</u>	<u>\$ Amount</u>
45	Transshipment Operation	5005	Salaries - NFC	Payroll	2,375.00
46	Transshipment Operation	5005	Salaries - NFC	Payroll	1,629.34
47	Transshipment Operation	7550	C/Boxes-Freight & Handling	299889	17,024.00

Cause: The root cause of the weakness is lack of control over recordkeeping.

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

Recommendation: We recommend that more stringent documentation policies be considered to prevent the disappearance of underlying documentation.

Auditee Response: Again we agree with the finding and recommendation. As stated in our response to previous findings, NFC will ensure that documents are available on file for inspection to support the recording of the reported amounts in the financial statements. For fiscal year 2006, all supporting documents of the recorded expenditures are kept intact and available for inspection.

NATIONAL FISHERIES CORPORATION AND SUBSIDIARIES

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

Leases Payable

Finding No. 2005-22

Criteria: Items and amounts reported in the financial statements should be valid.

Condition: We attempted to confirm the \$992,228 lease payable recorded by NFC. However, the confirmation letter we sent to the vendor was returned noting the vendor's mailing address was incorrect.

<u>Division</u>	<u>Acct. #</u>	<u>Description</u>	<u>Amount</u>
Airfreight Operation	2600	Lease payable	\$ (992,228)

Cause: The root cause of the condition is that relevant information about the entity's vendor was not properly updated, i.e. mailing address.

Effect: It is possible that this liability is no longer valid as we have not been made aware of any collections attempt by the vendor and we did not note anything related to this matter in the letter from legal counsel.

Recommendation: We recommend that NFC management investigate this matter and determine if the recorded amount is still valid.

Auditee Response: The recorded amount is valid and a written note from APA management is forthcoming. Management is in the process of negotiation with APA on the resolution of this account.