

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2009

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

YEAR ENDED SEPTEMBER 30, 2009

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**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**FINANCIAL STATEMENTS
YEAR ENDED SEPTEMBER 30, 2009**

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**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2009

INDEPENDENT AUDITORS' REPORT

Honorable Wesley Simina
Governor, State of Chuuk
Federated States of Micronesia:

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk (the State) as of September 30, 2009 and the related financial statements of the governmental activities, each major fund, and the aggregate remaining fund information for the year then ended, which collectively comprise the State's basic financial statements as set forth in Section II of the foregoing table of contents. These financial statements are the responsibility of the management of the State. Our responsibility is to express an opinion on the respective financial statements based on our audit.

Except as discussed in the following paragraphs, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

Because of inadequacies in the accounting records, detailed records regarding land in the amount of \$5,885,017 was not substantiated by underlying supporting documentation evidencing the validity of land and related land acquisitions payable for the primary government. Therefore, we are not able to satisfy ourselves about the amounts at which land and related liabilities for the governmental activities and the General Fund are recorded in the accompanying statement of net assets and governmental funds balance sheet at September 30, 2009.

As discussed in Note 9 to the financial statements, the State has not recorded a liability for land leases and other claims payable in the governmental activities and the General Fund and, accordingly, has not recorded an expenditure/expense for the current period change in that liability. Accounting principles generally accepted in the United States of America require that liabilities incurred attributable to services already rendered and that are not contingent upon a specific event that is outside of the control of the State be accrued as liabilities and expenditures/expenses, which would increase the liabilities, decrease net assets, and change the expenses of the governmental activities and increase the liabilities, increase fund deficit, and change the expenditures of the General Fund. The amount by which this departure would affect the liabilities, net assets and expenses of the governmental activities and the liabilities, fund deficit, and expenditures of the General Fund is not reasonably determinable.

We were engaged to audit the financial statements of the Chuuk Public Utility Corporation for the year ended September 30, 2008; however, the system of financial accounting and reporting in operation for the Chuuk Public Utility Corporation for the year ended September 30, 2008 was inadequate. Detailed records regarding inventory, utility plant, accounts payable and accrued expense account balances were not maintained and certain supporting data were not made available for our audit. Therefore we were not able to satisfy ourselves about the account balances presented within the statement of net assets of the aggregate discretely presented component units of the State as of September 30, 2008. The statement of net assets of the aggregate discretely presented component units as of September 30, 2008 enters into the determination of results of operations of the State for the year ended September 30, 2009. The financial activities of the Chuuk Public Utility Corporation are included in the State's basic financial statements as a discretely presented component unit and represent 71% and 82% of the assets and revenues, respectively, of the State's aggregate discretely presented component units.

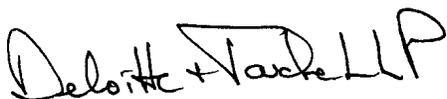
Because of the significance of the matter discussed in the fifth paragraph above, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements of the aggregate discretely presented component units for the year ended September 30, 2009.

In our opinion, except for the effects of not recording a liability for land leases and our inability to examine evidence supporting other claims payable in the governmental activities and the General Fund, as discussed in the fourth paragraph above, and except for the effects of such adjustments, if any, as might have been determined to be necessary had the accounting records been adequate for us to satisfy ourselves about land and related land acquisitions payable recorded for the governmental activities and the General Fund, as discussed in the third paragraph above, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the State as of September 30, 2009 and the changes in its net assets in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 10 to the financial statements, the beginning net assets of the governmental activities has been restated for the correction of an error.

The Management's Discussion and Analysis, on pages 3 through 9, as well as the Schedule of Revenues, Expenditures, and Changes in Deficit - Budget and Actual - General Fund and notes thereto, as set forth in Section III of the foregoing table of contents, are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the management of the State. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 24, 2010, on our consideration of the State's internal control over financial reporting and on 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.



June 24, 2010

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2009

This analysis, prepared by the Department of Administrative Services, Division of Treasury, offers readers of the Chuuk State Government's (Chuuk State) financial statements a narrative overview of the activities of the government for the fiscal year ended September 30, 2009. We encourage readers to consider this information in conjunction with Chuuk State's financial statements, which follow. Fiscal year 2008 comparative information has been included, where appropriate. This analysis is required by the Governmental Accounting Standards Board, (GASB) which provides guidelines on what must be included and excluded from this analysis.

FINANCIAL HIGHLIGHTS

- For the fiscal year ended September 30, 2009, Chuuk State's total net assets decreased by \$0.52 million (or 1.1%) from \$46.43 million in the prior year, as restated, to \$45.91 million. The restatement was the result of an engineering revaluation of the State's infrastructure capital assets to more realistically reflect useful lives; a measure taken to remove the fixed asset qualification on the State's balance sheet.
- During fiscal year 2009, Chuuk State's revenues of \$31.18 million increased from \$24.95 million (up 24.93%) in fiscal year 2008. The increase was attributable to increased revenue sharing proceeds, sales taxes and operating grants. Expenditures in fiscal year 2009 of \$28.99 million also increased by \$2.45 million (or 9.22 %) from \$26.54 million in fiscal year 2008. The increase in expenditures reflects an increase in education sector outlays, primarily the result of a retroactive salary increase for certified teachers.
- The General Fund deficit increased \$0.2 million in fiscal year 2009, increasing from \$8.58 million in the prior year to \$8.78 million. Although the State's general operating budget reflected a small surplus, the repayment of ADB principal and interest (\$0.31 million) and investment losses on its early retirement portfolio (\$0.12 million) eroded the overall fiscal position of the general fund.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to Chuuk State's basic financial statements, Chuuk State's basic financial statements comprise three components: 1) governmental-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains additional required supplementary information in the form of budgetary schedules, which are prepared on the budgetary basis of accounting, and other optional supplementary information, in addition to the basic financial statements themselves, which includes combining statements for governmental funds and component units.

Government-Wide Financial Statements

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

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

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

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Management's Discussion and Analysis
September 30, 2009

The government-wide financial statements of Chuuk State are divided into two categories:

- **Governmental Activities** - Most of Chuuk State's basic services are included here, such as education, health, special appropriations, finance, judiciary, and general administration. Compact sector and other federal grants finance most of these activities.
- **Component Units** - Chuuk State includes the operating results of the Chuuk State Health Care Plan, the Chuuk Public Utility Corporation, and the Chuuk Housing Authority in its report. Although legally separate, these "component units" are important because Chuuk State is financially accountable for them.

Fund Financial Statements

The fund financial statements provide more detailed information about Chuuk State's significant funds. Funds are accounting devices that Chuuk State uses to keep track of specific sources of funding and spending for particular services. The State uses fund accounting to comply with financial and related legal requirements. The fund financial statements present a balance sheet and a statement of revenues, expenditures, and changes in fund balances for its major and aggregated non-major funds.

Most of Chuuk State's basic services are included in governmental funds, which focus on (1) how cash and other financial assets that can be readily converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance Chuuk state programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statement, or on the subsequent page, that explains and reconciles the relationship (or differences) between them.

Chuuk State maintains individual governmental funds, which are categorized as major and non-major. The major funds comprise the General Fund, the Grants Assistance Fund, and the permanent Compact Trust Fund.

Restatement

As discussed above, Chuuk State restated beginning net assets for governmental activities in the amount of \$14.23 million due to a determination that capital assets were overstated. The State engaged outside consultants to perform an engineering study of all principal asset categories in order to eliminate prior audit qualifications on its financial statement. This restatement was in accord with *Government Accounting Standards Board* (GASB) statement No. 34. The result of this study indicated remaining asset useful lives were less than previously estimated resulting in this one-time charge which effectively represents depreciation expense retroactively applied in excess of new infrastructure assets that were capitalized.

Please refer to note 10 to the accompanying financial statements for further discussion on the restatement.

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Management's Discussion and Analysis
September 30, 2009

FINANCIAL ANALYSIS OF CHUUK STATE AS A WHOLE

Net assets may serve over time as a useful indicator of a government's financial position. At the end of fiscal year 2009, Chuuk State's assets exceeded liabilities by \$45.91 million. However, all these net assets are restricted as to the purposes they can be used for or are invested in capital assets. Chuuk State uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although Chuuk State's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. The following summary of Chuuk State's net assets as of September 30, 2009, with comparable balances for fiscal year 2008, discloses this relationship.

	<u>2009</u>	(As Restated) <u>2008</u>
Current and other non-capital assets	\$ 21,536,392	\$ 19,250,209
Capital assets	<u>49,057,775</u>	<u>51,891,364</u>
Total Assets	<u>70,594,167</u>	<u>71,141,573</u>
Long-term liabilities	9,800,192	9,524,505
Other liabilities	<u>14,889,545</u>	<u>15,190,075</u>
Total Liabilities	<u>24,689,737</u>	<u>24,714,580</u>
Net Assets:		
Invested in capital assets, net of related debt	49,057,775	51,891,364
Restricted	17,875,849	17,516,915
Unrestricted	<u>(21,029,194)</u>	<u>(22,981,285)</u>
Total Net Assets	\$ <u>45,904,430</u>	\$ <u>46,426,994</u>

At the end of fiscal year 2009, Chuuk State's unrestricted assets showed a deficit of \$21.03 million, a positive change from prior year balance of \$22.98 million. This deficit is the result of having current and long-term commitments that are greater than currently available resources. Specifically, Chuuk State did not include in past annual budgets the full amounts needed to finance its current liabilities to vendors and others or its long-term liabilities arising from Asian Development Bank (ADB) loans and unused employee leave balances. Chuuk State will include these amounts in future years' budgets as funding permits.

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FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2009

Net assets decreased by \$0.52 million (or 1.1%) from the prior year. Key elements of the decrease and the differences from the prior year are shown in the following schedule:

	<u>2009</u>	(As Restated) <u>2008</u>
Revenues:		
Program revenues:		
Charges for services	\$ 1,124,796	\$ 1,001,670
Operating grants and contributions	25,864,611	20,699,014
General Revenues:		
Taxes	4,303,023	3,837,966
Unrestricted investment earnings (losses)	(122,608)	(787,438)
Other	<u>5,518</u>	<u>202,583</u>
Total revenues	<u>31,175,340</u>	<u>24,953,795</u>
Expenses:		
General government	4,972,322	5,874,817
Health services	7,994,775	7,388,592
Education	12,654,204	9,408,457
Economic development	434,446	360,407
Public safety	848,644	904,667
Public works and transportation	2,189,448	2,059,799
Community affairs	17,211	-
Boards and commissions	1,591,385	1,486,207
Judiciary	374,532	406,764
Payments to component units	278,519	207,125
Municipal affairs	271,948	139,551
Other	<u>70,470</u>	<u>33,761</u>
Total expenses	<u>31,658,435</u>	<u>28,270,147</u>
Special Items:		
Write-off liabilities	<u>-</u>	<u>428,333</u>
Change in net assets	(522,564)	(2,888,019)
Net assets at the beginning of the year, as restated	<u>46,426,994</u>	<u>49,315,013</u>
Net assets at the end of the year	\$ <u>45,904,430</u>	\$ <u>46,426,994</u>

The detail indicates the increases in both revenues and expenses in fiscal year 2009. Revenues of \$31.18 million increased \$6.23 million (or 24.93%) from the prior year's \$24.95 million. The key elements of the increase were more grant drawdowns from higher utilization of sector grants, improved tax collections which increased \$0.465 million (up 12%) from fiscal year 2008, and a \$0.12 million increase (up 12.3%) in collections of charges for services. Both local revenue and revenue sharing proceeds benefited from the increased construction activity in Weno.

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Management's Discussion and Analysis
September 30, 2009

The following table shows a comparison of each revenue component's contribution to total revenues:

SOURCE OF REVENUE	<u>2009</u>	<u>2008</u>
Compact funding	82.0%	74.1%
Investments	(0.1)%	(9.0)%
Revenue sharing	8.5%	9.2%
Federal and other grants	0.7%	14.9%
Taxes and fees	8.9%	10.0%
Other	<u>0.0%</u>	<u>0.8%</u>
TOTAL	<u>100.0%</u>	<u>100.0%</u>

Notwithstanding the increases of taxes and fees, the preponderance of sector funding suggests that the primary way Chuuk State can increase its revenues is to maximize sector grant utilization, thereby increasing related drawdowns.

Expenses increased \$3.39 million (up 11.99%) from \$28.27 million in the prior fiscal year to \$31.66 million. The most notable increase in fiscal year 2009 was in the Education sector where expenses increased 34% to \$12.6 million, up from \$9.4 million in the prior year. In fiscal year 2009, the Chuuk Department of Education enabled a retroactive salary increase for certified teachers as part of a broad program of improving teacher credentials.

The following table highlights the major expense categories:

<u>09 Expenditure Category</u>	<u>Total</u> <u>('000's)</u>	<u>% of</u> <u>Total</u>
Personnel	\$ 15,828	50.00%
Travel and training	1,069	3.38%
Scholarships	1,384	4.37%
Contractual	1,537	4.86%
Medical supplies	1,789	5.65%
All other categories	<u>10,051</u>	<u>31.74%</u>
Total	\$ <u>31,658</u>	<u>100.00%</u>

FINANCIAL ANALYSIS OF CHUUK STATE'S FUNDS

As noted earlier, Chuuk State uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. As of the end of fiscal year 2009, Chuuk State's governmental funds reported a combined fund balance of \$7.33 million, which represents a \$2.7 million increase (or 58.3%) from the \$4.63 million fund balance recorded at the end of fiscal 2008. This increase is attributable to increases in the Compact sector operating and trust fund balances as the result of increased sector drawdowns and trust fund earnings. Of this total combined fund balance, \$21.93 million is reserved to indicate that it is not available for new spending because it has already been committed: 1) to generate income for future operations (\$7.12 million); 2) to liquidate contracts and purchase orders of the prior period (\$5.41 million) or; 3) to fund future specific general fund-related activities (\$9.4 million). These reserved fund balances are off-set by a combined fund deficit of \$14.6 million, a positive decrease of \$1.4 million (or 9.3%) from fiscal year 2008.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2009

GENERAL FUND BUDGETARY HIGHLIGHTS

During fiscal year 2009, there was a \$0.82 million increase in appropriations between the original and final amended budget for General Fund operations. This increase was primarily the result of an increase in Education expenditures of \$0.51 million funded by ADB loan proceeds and debt service expenditures of \$0.31 million funded by restricted investment balances. In fiscal year 2009, actual revenues of \$5.11 million fell short of the budgeted revenues of \$5.48 million by \$0.36 million. Actual budgetary expenditures of \$6.60 million were less than budgetary appropriations of \$6.75 by \$0.15 million, resulting in an overall deficiency of revenues under expenditures of \$0.21 million. Offsetting this general fund deficiency was the drawdown in investment balances to fund current year debt service, which resulted in an overall positive reduction in the deficiency of \$0.13 million and the \$0.42 million gain on the sale of the State's Bank of Guam shares. When combined with the operating deficit, these positive offsets resulted in an overall \$0.34 million decrease in the general fund deficit.

Chuuk State retains a balanced operating budget but increasingly investment and debt financing activities of the State can have negative impacts on overall State operations. In fiscal year 2009, general fund negative changes in the fair value of investments of \$0.12 million and principal and debt service charges of \$0.31 million both contributed to the increase in the general fund deficit.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

Chuuk State's capital asset balances were restated in fiscal year 2009; a project undertaken because not all infrastructure assets were on its fixed asset register and the historical cost values reported in prior years for other capital assets were not supported by available documentation. Chuuk State's restated investment in capital assets for the primary government as of September 30, 2009, amounted to \$113.13 million, net of accumulated depreciation of \$64.07 million, leaving a net book value of \$49.06 million. This represents a net decrease of \$2.83 million (or 5.5%) from the fiscal year 2008 restated amount. The table below summarizes Chuuk State's capital assets by category, net of accumulated depreciation:

	<u>2009</u>	(As Restated) <u>2008</u>
Land	\$ 17,686,782	\$ 17,686,782
Airport Facilities	13,532,634	14,485,319
Buildings	4,478,405	4,523,949
Seaport Facilities	8,618,093	9,281,023
Vehicles / Other Equipment	785,777	969,186
Infrastructure	<u>3,956,084</u>	<u>4,945,105</u>
	\$ <u>49,057,775</u>	\$ <u>51,891,364</u>

Additional information on Chuuk State's capital assets can be found in Note 5 to the accompanying financial statements.

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September 30, 2009

Long-Term Debt

The following schedule shows Chuuk State's outstanding long-term debt for fiscal year 2009 and comparable amounts for fiscal year 2008.

	<u>2009</u>	<u>2008</u>
ADB Early Retirement Loan (1520)	\$ 5,075,633	\$ 5,181,633
ADB Private Sector Reform Program Loan (1873)	739,840	739,840
ADB Private Sector Reform Program Loan (1874)	1,336,896	866,110
ADB Basic Social Services Program Loan (1816)	<u>1,268,115</u>	<u>1,359,665</u>
	\$ <u>8,420,484</u>	\$ <u>8,147,248</u>

Long-term debt increased by \$0.27 million (or 3.35%) in fiscal year 2009 as the result of loan drawdowns of \$0.51 million on ADB Loan Numbers 1816 and 1874, net of repayment on the Early Retirement (Loan Number 1520) and BSSP (Loan Number 1816) loans. In fiscal year 2009, the State received the final proceeds under the Private Sector Loan program, increasing the outstanding loan amount by \$0.47 million. No new additions to existing ADB loans or other long-term debt are planned by the State so gradual reductions in long-term debt are expected in fiscal year 2010 and beyond.

Additional information on Chuuk State's long-term debt obligations can be found in Notes 7 and 8 to the accompanying financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

Local revenue collections in Chuuk State are showing robust growth in fiscal year 2010 with final projections expected at around \$6.0 million \pm 10%. This does not include any gains or losses from State investments. Not including these investment losses, fiscal year 2010 general fund revenue totals are on track to exceed fiscal year's 2009 total by 14.6%. This increase reflects the revenue flows from the road construction activity in the State as well as increased audit efforts by the Tax & Revenue division. These increased revenues have allowed the State to increase funding to certain programs that had seen shortfalls in prior years, notably matching funds for infrastructure maintenance and prior year contributions for tax refunds. The State has become current with its income tax refunds in fiscal year 2010 by settling all arrears and distributing refund checks to all eligible taxpayers. Finally, in fiscal year 2010 Chuuk State is progressing on a broad range of fiscal initiatives that bode well for improved financial position and operating results: an eminent domain law was enacted and is being supported by sector grant funding; debt relief measures continue as old liabilities are paid down and improvements are being made in Ed sector grant utilization.

CONTACTING CHUUK STATE'S FINANCIAL MANAGEMENT

The financial report is designed to provide our citizens, taxpayers, customers, and investments and creditors, a general overview of Chuuk State's finances to demonstrate its accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Director, Office of Administrative Services, P.O. Box 189, Weno, Chuuk FM 96942.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Net Assets
September 30, 2009

	Primary Government	Component Units
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ 669,389	\$ 317,250
Time certificates of deposit	-	252,677
Equity interest in internal investment pool	2,442,115	-
Receivables, net of allowance for uncollectibles	2,752,626	828,530
Inventories	-	141,094
Prepayments	2,126,939	842
Total current assets	7,991,069	1,540,393
Noncurrent assets:		
Restricted assets:		
Investments	11,071,823	-
Investments	2,473,500	-
Capital assets, net of accumulated depreciation	49,057,775	2,138,262
Total noncurrent assets	62,603,098	2,138,262
Total assets	\$ 70,594,167	\$ 3,678,655
<u>LIABILITIES</u>		
Current liabilities:		
Current portion of long-term debt	\$ 235,867	\$ 992,392
Note payable	561,987	-
Accounts payable	4,326,216	159,390
Land acquisition payable	8,628,545	-
Compensated absences payable	450,000	-
Other liabilities and accruals	686,930	3,237,667
Deferred revenues	-	67,693
Total current liabilities	14,889,545	4,457,142
Noncurrent liabilities:		
Noncurrent portion of long-term obligations	8,184,617	3,370,961
Compensated absences payable, net of current portion	1,615,575	-
Total noncurrent liabilities	9,800,192	3,370,961
Total liabilities	24,689,737	7,828,103
<u>NET ASSETS</u>		
Invested in capital assets, net of related debt	49,057,775	(2,225,091)
Restricted for:		
Nonexpendable:		
Future operations	7,124,408	576,891
Expendable:		
Compact related	5,546,912	-
Debt service	3,947,415	-
Other purposes	1,257,114	-
Unrestricted	(21,029,194)	(2,501,248)
Total net assets	45,904,430	(4,149,448)
Total liabilities and net assets	\$ 70,594,167	\$ 3,678,655

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Activities
Year Ended September 30, 2009

Functions/Programs	Program Revenues				Net (Expenses) Revenues and Changes in Net Assets	
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government	Component Units
Primary government:						
Governmental activities:						
General government	\$ 4,972,322	\$ 344,326	\$ 1,906,199	\$ -	\$ (2,721,797)	\$ -
Health services	7,994,775	197,336	10,372,347	-	2,574,908	-
Education	12,654,204	-	11,698,790	-	(955,414)	-
Economic development	434,446	-	229,500	-	(204,946)	-
Public safety	848,644	56,643	98,188	-	(693,813)	-
Public works and transportation	2,189,448	513,694	-	-	(1,675,754)	-
Community affairs	17,211	-	-	-	(17,211)	-
Boards and commissions	1,591,385	-	1,233,408	-	(357,977)	-
Judiciary	374,532	12,797	-	-	(361,735)	-
Payments to component units	278,519	-	234,680	-	(43,839)	-
Municipal affairs	271,948	-	-	-	(271,948)	-
Future operations	-	-	91,499	-	91,499	-
Unallocated interest	70,470	-	-	-	(70,470)	-
Total primary government	\$ 31,697,904	\$ 1,124,796	\$ 25,864,611	\$ -	(4,708,497)	-
Component units:						
Chuuk State Health Care Plan	\$ 936,647	\$ 842,203	\$ -	\$ -	-	(94,444)
Chuuk Public Utility Corporation	5,437,735	4,059,093	-	-	-	(1,378,642)
Chuuk State Housing Authority	745,135	78,959	-	-	-	(666,176)
Total component units	\$ 7,119,517	\$ 4,980,255	\$ -	\$ -	-	(2,139,262)
General revenues:						
Taxes:						
Revenue sharing					2,660,821	-
State taxes					1,642,202	-
Unrestricted investment losses					(122,608)	-
Other					5,518	10,315
Total general revenues					4,185,933	10,315
Change in net assets					(522,564)	(2,128,947)
Net assets at the beginning of the year, as previously reported					60,656,420	(2,020,501)
Prior-period adjustment (Note 10)					(14,229,426)	-
Net assets at the beginning of the year, as restated					46,426,994	(2,020,501)
Net assets at the end of the year					\$ 45,904,430	\$ (4,149,448)

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Balance Sheet
Governmental Funds
September 30, 2009

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
<u>ASSETS</u>					
Cash and cash equivalents	\$ 669,389	\$ -	\$ -	\$ -	\$ 669,389
Equity interest in internal investment pool	2,442,115	-	-	-	2,442,115
Investments	423,500	2,050,000	-	-	2,473,500
Receivables, net	605,853	2,146,773	-	-	2,752,626
Prepayments	228,958	1,897,981	-	-	2,126,939
Due from other funds	2,029,121	4,599,750	-	1,257,114	7,885,985
Restricted assets:					
Investments	3,947,415	-	7,124,408	-	11,071,823
Total assets	\$ 10,346,351	\$ 10,694,504	\$ 7,124,408	\$ 1,257,114	\$ 29,422,377
<u>LIABILITIES AND FUND BALANCES</u>					
Liabilities:					
Accounts payable	\$ 3,395,086	\$ 931,130	\$ -	\$ -	\$ 4,326,216
Accrued liabilities	686,930	-	-	-	686,930
Land acquisition payable	8,628,545	-	-	-	8,628,545
Note payable	561,987	-	-	-	561,987
Due to other funds	5,856,864	2,029,121	-	-	7,885,985
Total liabilities	19,129,412	2,960,251	-	-	22,089,663
Fund balances (deficits):					
Reserved for:					
Related assets	-	2,050,000	7,124,408	1,196,831	10,371,239
Encumbrances	352,103	5,061,654	-	-	5,413,757
Continuing appropriations	2,196,255	-	-	-	2,196,255
Debt service	3,947,415	-	-	-	3,947,415
Unreserved:					
General fund	(15,278,834)	-	-	-	(15,278,834)
Special revenue funds	-	622,599	-	60,283	682,882
Total fund balances (deficits)	(8,783,061)	7,734,253	7,124,408	1,257,114	7,332,714
Total liabilities and fund balances	\$ 10,346,351	\$ 10,694,504	\$ 7,124,408	\$ 1,257,114	
Amounts reported for governmental activities in the statement of net assets are different because:					
Capital assets used in governmental activities are not financial resources and, therefore, are reported in the funds					49,057,775
Long-term liabilities, including loans payable, are not due and payable in the current period and, therefore, are not reported in the funds. The liabilities include:					
Long-term obligations				(8,420,484)	
Compensated absences				(2,065,575)	
					(10,486,059)
Net assets of governmental activities					\$ 45,904,430

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures, and Changes in Fund Balances (Deficits)
Governmental Funds
Year Ended September 30, 2009

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
Revenues:					
Compact funding	\$ -	\$ 25,570,114	\$ -	\$ -	\$ 25,570,114
Net change in the fair value of investments	(122,608)	-	91,499	-	(31,109)
CFSM grants	-	43,962	-	-	43,962
Federal contributions and other grants	-	-	-	159,036	159,036
FSM revenue sharing	2,660,821	-	-	-	2,660,821
State taxes	1,642,202	-	-	-	1,642,202
Fees and charges	927,460	-	-	197,336	1,124,796
Other	5,518	-	-	-	5,518
Total revenues	<u>5,113,393</u>	<u>25,614,076</u>	<u>91,499</u>	<u>356,372</u>	<u>31,175,340</u>
Expenditures:					
Current:					
General government	3,017,684	642,969	-	-	3,660,653
Health services	-	7,783,556	-	296,089	8,079,645
Education	536,471	12,041,625	-	-	12,578,096
Economic development	72,610	389,228	-	-	461,838
Public safety	721,657	98,188	-	-	819,845
Public works and transportation	524,275	-	-	-	524,275
Community affairs	17,211	-	-	-	17,211
Boards and commissions	341,129	1,250,256	-	-	1,591,385
Judiciary	374,532	-	-	-	374,532
Payments to component units	43,839	234,680	-	-	278,519
Municipal affairs	271,948	-	-	-	271,948
Other	19,642	-	-	-	19,642
Debt service:					
Principal repayment	240,623	-	-	-	240,623
Interest payments	70,470	-	-	-	70,470
Total expenditures	<u>6,252,091</u>	<u>22,440,502</u>	<u>-</u>	<u>296,089</u>	<u>28,988,682</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(1,138,698)</u>	<u>3,173,574</u>	<u>91,499</u>	<u>60,283</u>	<u>2,186,658</u>
Other financing sources (uses):					
Proceeds from issuance of long-term debt	513,859	-	-	-	513,859
Operating transfers in	423,500	-	-	-	423,500
Operating transfers out	-	(423,500)	-	-	(423,500)
Total other financing sources (uses), net	<u>937,359</u>	<u>(423,500)</u>	<u>-</u>	<u>-</u>	<u>513,859</u>
Net change in fund balances (deficit)	<u>(201,339)</u>	<u>2,750,074</u>	<u>91,499</u>	<u>60,283</u>	<u>2,700,517</u>
Fund balances (deficits) at the beginning of the year	<u>(8,581,722)</u>	<u>4,984,179</u>	<u>7,032,909</u>	<u>1,196,831</u>	<u>4,632,197</u>
Fund balances (deficits) at the end of the year	<u>\$ (8,783,061)</u>	<u>\$ 7,734,253</u>	<u>\$ 7,124,408</u>	<u>\$ 1,257,114</u>	<u>\$ 7,332,714</u>

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Reconciliation of the Statement of Revenues, Expenditures,
and Changes in Fund Balances of Governmental Funds
to the Statement of Activities
Year Ended September 30, 2009

Amounts reported for governmental activities in the statement of activities are different from changes in fund balances because:

Net change in fund balances - total governmental funds	\$ 2,700,517
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlays in the current period	(2,833,589)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. For the current year, these activities consist of:	
Change in compensated absences payable	(116,256)
The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction has any effect on net assets. This amount is the net effect of these differences in the treatment of long-term debt and related items	<u>(233,767)</u>
Change in net assets of governmental activities	\$ <u><u>(522,564)</u></u>

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**DISCRETELY PRESENTED COMPONENT UNITS
Combining Statement of Net Assets
September 30, 2009**

<u>ASSETS</u>	<u>Chuuk State Health Care Plan</u>	<u>Chuuk Public Utility Corporation</u>	<u>Chuuk State Housing Authority</u>	<u>Total</u>
Current assets:				
Cash and cash equivalents	\$ 310,849	\$ 4,664	\$ 1,737	\$ 317,250
Time certificates of deposit	252,677	-	-	252,677
Receivables, net	87,284	459,564	281,682	828,530
Inventories	-	141,094	-	141,094
Prepayments	842	-	-	842
	<hr/>	<hr/>	<hr/>	<hr/>
Total current assets	651,652	605,322	283,419	1,540,393
Noncurrent assets:				
Capital assets, net of accumulated depreciation	25,090	2,010,041	103,131	2,138,262
	<hr/>	<hr/>	<hr/>	<hr/>
Total assets	\$ 676,742	\$ 2,615,363	\$ 386,550	\$ 3,678,655
	<hr/>	<hr/>	<hr/>	<hr/>
<u>LIABILITIES AND NET ASSETS</u>				
Current liabilities:				
Current portion of long-term debt	\$ -	\$ 992,392	\$ -	\$ 992,392
Accounts payable	74,761	84,211	418	159,390
Accrued liabilities	-	3,237,667	-	3,237,667
Deferred income	-	67,693	-	67,693
	<hr/>	<hr/>	<hr/>	<hr/>
Total current liabilities	74,761	4,381,963	418	4,457,142
Noncurrent liabilities:				
Noncurrent portion of long-term debt	-	3,370,961	-	3,370,961
	<hr/>	<hr/>	<hr/>	<hr/>
Total liabilities	74,761	7,752,924	418	7,828,103
	<hr/>	<hr/>	<hr/>	<hr/>
Net assets:				
Invested in capital assets, net of related debt	25,090	(2,353,312)	103,131	(2,225,091)
Restricted	576,891	-	-	576,891
Unrestricted	-	(2,784,249)	283,001	(2,501,248)
	<hr/>	<hr/>	<hr/>	<hr/>
Total net assets	601,981	(5,137,561)	386,132	(4,149,448)
	<hr/>	<hr/>	<hr/>	<hr/>
Total liabilities and net assets	\$ 676,742	\$ 2,615,363	\$ 386,550	\$ 3,678,655
	<hr/>	<hr/>	<hr/>	<hr/>

See accompanying notes to basic financial statements

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**DISCRETELY PRESENTED COMPONENT UNITS
Combining Statement of Revenues, Expenses, and Changes in Net Assets
Year Ended September 30, 2009**

	Chuuk State Health Care Plan	Chuuk Public Utility Corporation	Chuuk State Housing Authority	Total
Operating revenues:				
Charges for services	\$ 837,430	\$ 4,059,093	\$ -	\$ 4,896,523
Other	4,773	-	78,959	83,732
Total operating revenues	<u>842,203</u>	<u>4,059,093</u>	<u>78,959</u>	<u>4,980,255</u>
Operating expenses:				
Cost of services	756,292	2,758,465	-	3,514,757
Depreciation	9,418	951,295	18,383	979,096
Administration and general	170,937	1,489,326	726,752	2,387,015
Total operating expenses	<u>936,647</u>	<u>5,199,086</u>	<u>745,135</u>	<u>6,880,868</u>
Operating loss	<u>(94,444)</u>	<u>(1,139,993)</u>	<u>(666,176)</u>	<u>(1,900,613)</u>
Nonoperating revenues (expenses):				
Other income	10,277	38	-	10,315
Interest expense	-	(238,649)	-	(238,649)
Total nonoperating revenues (expenses), net	<u>10,277</u>	<u>(238,611)</u>	<u>-</u>	<u>(228,334)</u>
Net loss	(84,167)	(1,378,604)	(666,176)	(2,128,947)
Net assets at the beginning of the year	686,148	(3,758,957)	1,052,308	(2,020,501)
Net assets at the end of the year	<u>\$ 601,981</u>	<u>\$ (5,137,561)</u>	<u>\$ 386,132</u>	<u>\$ (4,149,448)</u>

See accompanying notes to basic financial statements

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies

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

A. Reporting Entity

The State is one of the four states that make up the Federated States of Micronesia (FSM), along with the states of Kosrae, Pohnpei and Yap. The State is a constitutional government comprised of three branches: the Legislative Branch, consisting of the Senate (10 members elected for a term of four years by qualified voters of their respective election districts with the President of the Senate as its highest officer) and the House of Representatives (28 members elected for a term of two years by qualified voters of their respective election districts with the Speaker as its highest officer); the Executive Branch, headed by the Governor and Lt. Governor who are primarily responsible for executing the laws and administering state government services; and the Judiciary Branch made up of the State Supreme Court, which consists of a Chief Justice and four Associate Justices, such inferior courts that may be created by law, and the municipal courts.

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

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

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

Blended component units are entities that are legally separate from the State, but are so related to the State that they are, in substance, the same as the State or entities providing services entirely or almost entirely to the State. The State has not identified any entities that should be so blended.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

i. Discretely Presented Component Units

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

Chuuk State Housing Authority (CSHA): CSHA was created by Chuuk State Law (CSL) No. 3-30 and is responsible for monitoring the U.S. Department of Housing and Urban Development Section 8 and CDBG housing renovation loan programs. Additionally, CSHA monitors the GLF loan fund of the State which provides low cost housing loans to the general public. CSHA is governed by a five-member Board of Directors appointed by the Governor subject to the advice and consent of the Legislature.

Chuuk Public Utility Corporation (CPUC): CPUC was created by CSL No. 3-97-05 and is responsible for providing electrical services to the public through the operation and the maintenance of the State's electrical power system. CPUC is governed by a five-member Board of Directors appointed by the Governor subject to the advice and consent of the Legislature.

Chuuk State Health Care Plan (CSHCP): CSHCP was established under CSL No. 2-94-06 for the purpose of establishing a financial system to provide universal coverage of an essential level of health care for all eligible enrollees and to create a means for collection of health care premiums for additional coverage.

The State's component units, departments, and funds that are separately audited issue their own financial statements. These statements may be obtained by directly contacting the various entities or obtaining them directly from the Office of the Public Auditor at the following address:

P.O. Box 760
Weno, Chuuk, FSM 96942

ii. Omitted Governmental Funds

The following funds are considered to be nonmajor governmental funds of the State but are not included in the accompanying basic financial statements due to absence of account balances and financial activities. The omission of these funds is not considered material to either the nonmajor other governmental funds or the governmental activities reporting units:

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

ii. Omitted Governmental Funds, Continued

Development Authorities - The Northern Namoneas Economic Development Authority, the Southern Namoneas Development Authority, the Inner Faichuk Social and Economic Development Authority, the Outer Faichuk Development Authority, the Faichuk Transportation and Economic Development Authority, the Hall Islands Economic Development Authority, the Pattiw Islands Development Authority, and the Witto Resources and Development Authority. These development authorities were established to identify the development needs and promote economic development within the various municipalities, in coordination and cooperation with the State and the FSM National Government.

Chuuk Visitors Bureau (CVB) Fund - This fund was created by CSL No. 6-39 and is responsible for improving and developing the State's tourism industry. CVB is governed by a nine-member Board of Directors, five of whom are appointed by the Governor subject to the advice and consent of the Legislature and the remaining four of whom are appointed by the President and Speaker of the Legislature.

Representation Fund: This fund was established under CSL No. 3-95-09 for the use of members of the State Legislature to provide assistance to constituents' legitimate emergencies, educational, and civic needs not met by other appropriations.

Chuuk State Legislature Entertainment Fund: This fund was established under Title 21, Section 751 of the Truk District Code (TDC), for the use by the Legislature to entertain guests or other distinguished persons living in or visiting the State.

Legislature Emergency Fund: This fund was established under Truk District Law (TDL) No. 21-1 to defray salaries of personnel of the Legislature and office expenses of the Legislature during a period of time between the close of a fiscal year and the signing into law of an appropriation for salaries and expenses of the Legislature office and staff for the next succeeding fiscal year.

Chuuk State Travel Fund: This fund was established under TDL No. 22-27 to enable members of the Legislature, Magistrates of municipalities, members of municipal councils, and other leaders in the State to travel outside of the State for the purposes of attending functions prescribed by the enabling legislation.

Association of Pacific Island Legislatures Fund: This fund was established under TDL No. 24-9 for the purpose of funding donations or membership fees to the Association of Pacific Island Legislatures.

Municipal Operations and Projects Fund: This fund was established under TDL No. 25-23 for the purpose of funding operational expenses of municipalities in the State, and providing funds for municipal projects and programs.

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

ii. Omitted Governmental Funds, Continued

Fire Disaster Relief Fund: This fund was established under 7 TDC Section 51 for the purpose of providing relief to persons suffering loss or damage to homes or furnishings as a result of accidental fires.

Economic Development Loan Fund: This fund was established under 13 TDC Section 1 for the purpose of providing loans to any private citizen of the State or any Chuukese corporation or cooperative, wishing to begin, operate, or improve business operations in the State.

Chuuk Farmers', Fishermen's, and Handicrafts Fair Fund: This fund was established under TDL No. 23-28 for the purpose of paying for supplies, materials, prizes and other expenses incurred in the preparation for and holding of the Chuuk Farmers', Fishermen and Handicrafts Fair.

Chuuk State Local Farmers Revolving Fund: This fund was established under TDL No. 21-25 for the purpose of purchasing agricultural supplies, livestock, feeds, assorted tools and other materials, for the use of local farmers in the State.

Chuuk State Hospital Transportation Fund: This fund was established under TDL No. 22-32 for the purpose of transporting patients of the State, who require periodic medical treatment and care, to the Chuuk State Hospital, to provide return transportation to their homes after treatment at the Chuuk State Hospital, and to provide for each of these patients a one dollar and fifty cents (\$1.50) noon meal during such travel, treatment and care.

iii. Omitted Component Units

The following component units have been omitted from the basic financial statements due to the lack of available financial information. The omission of these component units is not considered material to the aggregate discretely presented component unit reporting unit:

Chuuk State Coconut Authority (CSCA): CSCA was created by TSL No. 1-1-12 and is responsible for the manufacturing, processing, buying, collecting, marketing, selling, exporting and dealing with, in general, all products derived from the coconut tree. CSCA is governed by a five-member Board of Directors appointed by the Governor subject to the advice and consent of the Legislature.

Chuuk Public Fisheries Corporation (CPFC): CPFC was created by CSL No. 5-99-22 and is responsible for promoting the development of pelagic fisheries and related industries for the economic benefit of the people of the State. CPFC is governed by a five-member Board of Directors, which comprises of the Director of the Department of Marine Resources, the Director of the Department of Commerce and Industry, one member who is appointed by the Governor representing the Chamber of Commerce, and two members who are appointed by the President and the Speaker.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements

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

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

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

- Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt that are attributed to the acquisition, construction or improvement of those assets.
- Restricted net assets - nonexpendable consists of permanent funds in which donors or other outside sources have stipulated that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to the principal.
- Restricted net assets - expendable consists of resources in which the State is legally or contractually obligated to spend resources in accordance with restrictions either externally imposed by creditors, grantors, contributors, and the like, or imposed by law.
- Unrestricted net assets consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, (for example, internally restricted), to indicate that management does not consider them to be available for general operations.

The government-wide Statement of Net Assets reports \$17,875,849 of restricted net assets, of which \$1,257,114 is restricted by enabling legislation.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements, Continued

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

C. Fund Financial Statements

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

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

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

D. Measurement Focus and Basis of Accounting

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

Significant revenues susceptible to accrual include income and gross revenue taxes, federal grants, federal reimbursements and other reimbursements for use of materials and services. Miscellaneous revenues from other financing sources are recognized when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available. Expenditures generally are recorded in the period in which the related fund liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

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

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

The State reports the following governmental fund types:

i. General Fund

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

ii. Special Revenue Funds

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

iii. Capital Projects Funds

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

iv. Permanent Fund

This fund accounts for resources that are legally restricted to the extent that only earnings, and not principal, may be used to support programs for the benefit of the government.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

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

Grants Assistance Fund, a Governmental Fund Type - Special Revenue Fund. This fund accounts for funds received under sector grants pursuant to the amended Compact of Free Association; all financial transactions of federally assisted funds, which are subgranted to the State, as well as other direct federal grants that the State received from the United States government, and foreign assistance grants.

Section 215 Compact Trust, a Governmental Fund Type - Permanent Fund, accounts for the State's contributions to the Trust Fund established in accordance with Section 215 of the Compact of Free Association, as amended, to provide for an additional source of revenue for the government budget that will be needed to substitute for the absence of Compact of Free Association funding.

E. Reporting Standards

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

F. Cash and Cash Equivalents and Time Certificates of Deposit

Cash and cash equivalents include cash held in demand accounts as well as short-term investments in U.S. Treasury obligations with a maturity date within three months of the date acquired by the State. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified on the statement of net assets/balance sheet.

G. Investments

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

H. Receivables

In general, tax revenue is recognized on the government-wide financial statements when assessed or levied and on the governmental fund financial statements to the extent that it is both measurable and available. Receivables are stated net of estimated allowances for uncollectible accounts. Federal receivables include those funds which are earned, primarily from FSM National Government administered federal grants, which have yet to be reimbursed by the applicable grantor.

Receivables of the primary government are primarily due from businesses and individuals residing in the State. The State establishes an allowance for doubtful accounts receivable based on the credit risk of specific customers, historical trends and other information.

I. Prepaid Items

Certain payments made to vendors or persons for services reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and governmental fund financial statements.

J. Interfund Receivables/Payables

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

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

K. Restricted Assets

Certain assets of the primary government are classified as restricted assets because their use is completely restricted through loan agreements or enabling legislation. Specifically, the State has collateralized Asian Development Bank loan proceeds and earnings for the Chuuk State Early Retirement Scheme with investments recorded in the General Fund of \$3,947,415. Furthermore, investments recorded in the Compact Trust Fund of \$7,124,408 are restricted in that they are not available to be used in current operations.

L. Capital Assets

Capital assets, which include property, plant, equipment and infrastructure (e.g. roads, bridges, ramps and other similar items), are reported in the governmental activity column of the government-wide financial statements.

Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at fair market value at the date of donation.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

L. Capital Assets, Continued

The State currently holds no title to land. Singular pieces of machinery and equipment, other than vehicles, that equal or exceed \$50,000 are capitalized. Buildings and infrastructure projects with a cost that equals or exceeds \$100,000 are capitalized. The costs of normal maintenance and repairs that do not add to the value of assets or materially extend asset lives are not capitalized.

Capital assets of the primary government and the discretely presented component units are depreciated using the straight-line method over their estimated useful lives, with a full year's depreciation charged in the year of acquisition and disposal, regardless of date. Estimated useful lives are as follows:

Buildings	40 - 50 years
Infrastructure	25 - 50 years
Facilities	3 - 40 years
Machinery and equipment	3 - 25 years
Furniture and fixtures	3 - 10 years

M. Interfund/Intrafund Transactions

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

N. Compensated Absences

It is the government's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. There is no liability for unpaid accumulated sick leave since the government does not have a policy to pay any amounts when employees separate from service with the government. All vacation pay is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements. Annual leave accumulates at the rate of one working day per bi-weekly pay period.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

O. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. The unreserved fund balances for the governmental funds represent the amount available for budgeting future operations. The reserve for related assets as of September 30, 2009, is represented by the following assets:

	<u>General</u>	<u>Grants Assistance</u>	<u>Compact Trust</u>	<u>Other Governmental Funds</u>	<u>Totals</u>
Investments	\$ -	\$ 2,050,000	\$ -	\$ -	\$ 2,050,000
Due from other funds	-	-	-	1,196,831	1,196,831
Restricted assets:					
Investments	-	-	7,124,408	-	7,124,408
	<u>\$ -</u>	<u>\$ 2,050,000</u>	<u>\$ 7,124,408</u>	<u>\$ 1,196,831</u>	<u>\$ 10,371,239</u>

The continuing appropriations within the General Fund include \$2,196,255 set aside for future payments of the Chuuk State Legislature Building Complex and for future payments for Chuuk Municipal capital projects.

P. Risk Financing

The State is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. It is the policy of the primary government not to purchase commercial insurance for the risks of loss to which it is exposed. Instead, the State management believes it is more economical to manage its risks internally. In the event of claim settlements and judgments, the State reports all of its risk management activities in its General Fund. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. No losses have occurred as a result of these risks in any of the past three fiscal years.

Q. Estimates

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

R. New Accounting Standards

During fiscal year 2009, the State implemented the following pronouncements:

- GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which establishes standards for the measurement, recognition, and display of other postemployment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers.
- GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, which provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation.
- GASB Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, which improves the quality of financial reporting by requiring endowments to report their land and other real estate investments at fair value, creating consistency in reporting among similar entities that exist to invest resources for the purpose of generating income.
- GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which improves financial reporting by contributing to the GASB's efforts to codify all GAAP for state and local governments so that they derive from a single source.
- GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*, which incorporates accounting and financial reporting guidance previously only contained in the American Institute of Certified Public Accountants (AICPA) auditing literature into the GASB's accounting and financial reporting literature for state and local governments, and addresses three issues from the AICPA's literature - related party transactions, going concern considerations, and subsequent events.

The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

In June 2007, GASB issued statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, which addresses whether and when intangible assets should be considered capital assets for financial reporting purposes. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(1) Summary of Significant Accounting Policies, Continued

R. New Accounting Standards, Continued

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which is intended to improve how state and local governments report information about derivative instruments - financial arrangements used by governments to manage specific risks or make investments - in their financial statements. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In December 2008, GASB issued Technical Bulletin No. 2008-1, *Determining the Annual Required Contribution Adjustment for Postemployment Benefits*, which clarifies the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, for calculating the annual required contribution (ARC) adjustment. The provisions of this statement are effective for periods beginning after December 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In March 2009, GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The provisions of this statement are effective for periods beginning after June 15, 2010. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

S. Total Columns

Total columns are presented primarily to facilitate financial analysis. The Management's Discussion and Analysis includes certain prior year summarized comparative information in total. Such information does not include sufficient detail to constitute a full comparative presentation. Accordingly, such information should be read in conjunction with the State's financial statements for the year ended September 30, 2008 from which summarized information was derived.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(2) Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

The State pools cash resources of its various funds in order to facilitate the management of cash. Unless otherwise required by law, interest income received on pooled cash accrues to the General Fund. Cash and cash equivalents applicable to a particular fund are readily identifiable. The State has invested the majority of its excess Compact Funds in a pooled investment fund which is managed under the control of the Federated Development Authority, an entity comprised of the FSM National Government and its four component states. Investment income originating from the pool accrues to the General Fund.

The deposit and investment policies of the State are governed by State legislation. The Treasurer is responsible for ensuring that deposits of the General Fund are maintained in commercial checking or savings accounts of any financial institution whose assets are at least \$1 billion and whose deposits are subject to Federal Deposit Insurance Corporation (FDIC) insurance. The Governor is responsible for the investment of any monies of the State that are deemed not necessary for immediate use.

The Federated Development Authority has selected investment managers who are given authority to buy and sell securities. These investment managers may invest in stocks, bonds and cash equivalents, for which minimum standards of quality of such investments at the time of purchase shall be as follows:

- i. Cash equivalents - the investment manager may engage in all normally accepted short-term investment practices including, but not limited to U.S. Treasury and government agency securities, bankers acceptances, certificates of deposit, commercial paper and repurchase agreements using any of the foregoing as collateral. The following restrictions apply: (1) Commercial paper must be rated A-1/P-1 or higher by Standard & Poor Corporation and Moody's Investor Services; and (2) Certificates of deposit must be from FDIC insured banks or FSLIC insured savings and loan associations, both of which must have assets in excess of \$2 billion. Deposits in smaller institutions are acceptable, but must not exceed the amount of the insurance, unless collateralized by U.S. Treasury obligations at 102%.
- ii. Stocks - A "B" rating by a national rating service. Non-rated stocks, such as banks or insurance companies, must be equal in quality or higher.
- iii. Bonds - Confined to issues rated "A" or higher by a national rating service, except in the case of U.S. Treasury or government agency obligations which are not rated.

The equity portfolio shall be diversified among issues and industry classifications. No more than 25% of the equity portfolio may be invested in any single classification, as described by the Standard and Poor 500 Index, unless prior approval is received from the Secretary of Finance.

No investment may be made in a single corporate entity which exceeds 5% of the total assets of the fund at the time of purchase without prior approval of the Secretary of Finance.

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2009

(2) Deposits and Investments, Continued

A. Deposits

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1 - Deposits that are federally insured or collateralized with securities held by the State or its agent in the State's name;

Category 2 - Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the State's name; or

Category 3 - Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in the State's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the State's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The State does not have a deposit policy for custodial credit risk or foreign currency risk.

As of September 30, 2009, the carrying amount of the primary government's total cash and cash equivalents were \$669,389 and the corresponding bank balances were \$1,933,336, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2009, bank deposits in the amount of \$500,000 were FDIC insured. The State does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

As of September 30, 2009, the carrying amount and corresponding bank balance amount of the discretely presented component units' total cash and cash equivalents and time certificates of deposit was \$569,927 and the corresponding bank balance was \$575,282, which were maintained in financial institutions subject to FDIC insurance. As of September 30, 2009, bank deposits in the amount of \$470,466 were FDIC insured. The component units do not require collateralization of their cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Therefore, these deposits are exposed to custodial credit risk.

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2009

(2) Deposits and Investments, Continued

B. Investments

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

Category 1 - Investments that are insured or registered, or securities held by the State or its agent in the State's name;

Category 2 - Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in the State's name; or

Category 3 - Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the State's name.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

As of September 30, 2009, the State's investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	\$ 1,332,000
Other investments:	
Domestic equities	9,474,683
Cash management account	<u>265,140</u>
	<u>9,739,823</u>
	\$ <u>11,071,823</u>

As of September 30, 2009, the General Fund has an Automated Cash Management account with the Bank of Hawaii in the amount of \$2,442,115.

As of September 30, 2009, the General Fund holds 0.01% of the shares of the Bank of Guam carried at cost in the amount of \$423,500. Furthermore, the Grants Assistance Fund holds 16% of the shares of the Bank of the Federated States of Micronesia in the amount of \$1,500,000, 4.8% of the shares of the Pacific Islands Development Bank in the amount of \$250,000, and 1% of the shares of the FSM Development Bank in the amount of \$300,000. As the fair market value of these investments is not readily available, such have been recorded at cost.

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. With the exception of investments in U.S. government securities, which are explicitly or implicitly guaranteed by the United States government, all other investments must be rated in accordance with the State's investment policy.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(2) Deposits and Investments, Continued

B. Investments, Continued

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the State will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The State's investments are held and administered by trustees. Based on negotiated trust and custody contracts, all of these investments were held in the State's name by the State's custodial financial institutions at September 30, 2009.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the State. As of September 30, 2009, the State did not hold an investment in any one issuer that represented more than 5% of the State's total investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The State does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

As of September 30, 2009, the State's fixed income securities, including their Moody's Investors Service credit ratings, had the following maturities:

Investment Type	Rating Type	Maturity (in years)				Total
		Current	1-5	6-10	Over	
U.S Treasury Obligations	Aaa	\$ -	\$ 118,338	\$ 75,497	\$ 71,647	\$ 265,482
U.S. Government Agency Obligations:						
Federal Home Loan Bank	Aaa	-	-	-	21,320	21,320
Federal Farm Credit Bank	Aaa	-	28,678	-	-	28,678
Federal Home Loan Mortgage Corporation	Aaa	19,146	45,790	9,500	238,755	313,191
Federal National Mortgage Association	Aaa	-	22,990	14,330	213,133	250,453
Government National Mortgage Association	Aaa	-	-	-	7,365	7,365
Tennessee Valley Authority	Aaa	-	-	-	11,502	11,502
Corporate notes and bonds	Aaa	-	14,186	14,763	-	28,949
Corporate notes and bonds	Aa1	-	34,097	24,047	-	58,144
Corporate notes and bonds	Aa2	-	43,904	-	21,035	64,939
Corporate notes and bonds	A1	-	-	10,507	54,900	65,407
Corporate notes and bonds	A2	-	25,590	24,708	-	50,298
Corporate notes and bonds	A3	-	19,216	-	12,898	32,114
Corporate notes and bonds	Baa1	-	39,223	48,088	-	87,311
Corporate notes and bonds	Baa2	-	7,804	-	7,317	15,121
Corporate notes and bonds	Baa3	-	-	-	31,726	31,726
Grand Total		\$ <u>19,146</u>	\$ <u>399,816</u>	\$ <u>221,440</u>	\$ <u>691,598</u>	\$ <u>1,332,000</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(3) Receivables

Primary Government

Receivables as of September 30, 2009, for the primary government's individual major funds and nonmajor funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	<u>General</u>	<u>Grants Assistance</u>	<u>Total</u>
Receivables:			
FSM National Government	\$ 911,115	\$ 2,146,773	\$ 3,057,888
Less: allowance for uncollectible Accounts	(305,262)	-	(305,262)
Net receivables	\$ <u>605,853</u>	\$ <u>2,146,773</u>	\$ <u>2,752,626</u>

Discretely Presented Component Units

Chuuk State Health Care Plan

Receivables as of September 30, 2009, for the Chuuk State Health Care Plan in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

General	\$ 134,394
Less: allowance for uncollectible accounts	<u>(47,110)</u>
Net receivables	\$ <u>87,284</u>

Chuuk Public Utilities Corporation

Receivables as of September 30, 2009, for the Chuuk Public Utilities Corporation in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

General	\$ 1,934,371
Less: allowance for uncollectible accounts	<u>(1,474,807)</u>
Net receivables	\$ <u>459,564</u>

Chuuk State Housing Authority

Receivables as of September 30, 2009, for the Chuuk State Housing Authority in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

Receivables:	
General	\$ 252,231
Loans	<u>1,828,739</u>
	2,080,970
Less: allowance for uncollectible accounts	<u>(1,799,288)</u>
Net receivables	\$ <u>281,682</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(4) Interfund Receivables and Payables

Receivables and payables between funds reflected as due to/from other funds in the combined balance sheet at September 30, 2009, are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
Grants Assistance	General	\$ 4,599,750
General	Grants Assistance	2,029,121
Nonmajor governmental funds	General	<u>1,257,114</u>
		<u>\$ 7,885,985</u>

Interfund receivables not expected to be repaid within the next twelve months are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
Nonmajor governmental funds: Chuuk Airport Authority	General	<u>\$ 1,196,831</u>

(5) Fixed Assets

Capital asset activities of the primary government for the year ended September 30, 2009, are as follows:

	Balance October <u>1, 2008</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2009</u>
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 17,686,782	\$ -	\$ -	\$ 17,686,782
Capital assets, being depreciated:				
Airport facilities	38,107,415	-	-	38,107,415
Buildings	9,934,604	174,013	-	10,108,617
Seaport facilities	26,517,208	-	-	26,517,208
Vehicles and other equipment	5,713,015	156,823	-	5,869,838
Infrastructure	<u>14,835,315</u>	<u>-</u>	<u>-</u>	<u>14,835,315</u>
	<u>95,107,557</u>	<u>330,836</u>	<u>-</u>	<u>95,438,393</u>
Less accumulated depreciation for:				
Airport facilities	(23,622,096)	(952,685)	-	(24,574,781)
Buildings	(5,410,655)	(219,557)	-	(5,630,212)
Seaport facilities	(17,236,185)	(662,930)	-	(17,899,115)
Vehicles and other equipment	(4,743,829)	(340,232)	-	(5,084,061)
Infrastructure	<u>(9,890,210)</u>	<u>(989,021)</u>	<u>-</u>	<u>(10,879,231)</u>
	<u>(60,902,975)</u>	<u>(3,164,425)</u>	<u>-</u>	<u>(64,067,400)</u>
	<u>34,204,582</u>	<u>(2,833,589)</u>	<u>-</u>	<u>31,370,993</u>
	<u>\$ 51,891,364</u>	<u>\$ (2,833,589)</u>	<u>\$ -</u>	<u>\$ 49,057,775</u>

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2009

(5) Fixed Assets, Continued

Depreciation expense was charged to functions/programs of the primary government's governmental activities as follows:

General government	\$ 1,215,595
Health services	151,592
Education	103,266
Public safety	28,799
Public works and transportation	<u>1,665,173</u>
	\$ <u>3,164,425</u>

(6) Short-Term Debt

Primary Government

Note payable to the FSM National Government, payable in quarterly installments of \$416,667, non-interest bearing with a service charge of 1% per annum, due on September 30, 2001. \$ 561,987

No activity in short-term debt of the primary government occurred during the year ended September 30, 2009.

(7) Long-Term Obligations

Primary Government

Asian Development Bank (ADB Loans):

The State implemented an Early Retirement Scheme (ERS) in which employees holding certain nonessential positions as identified by the State were retired early with a payout of the equivalent of two-years' wages. This ERS program is funded by a \$5,300,000 loan from the ADB (Loan Number 1520 (SF)) through the FSM National Government, non-interest bearing with a service charge of 1% per annum on the amount of the loan withdrawn from the Loan Account. The activities of the ERS Program are recorded in the General Fund.

The ADB loan has a grace period of ten years with the first payment due in February 2008 and the last payment in August 2037. However, pursuant to the terms of the Financing Agreement between the State and the FSM National Government, the State is required to deposit into the ERS Trust account held in the name of the State within the FSM National Government investment portfolio, 100% of the outstanding principal balance by September 30, 2002.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(7) Long-Term Obligations, Continued

Primary Government, Continued

Asian Development Bank (ADB Loans, Continued):

Funds for the repayment of the ERS loan are expected to be derived from the annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The Financing Agreement requires the State to continue to appropriate salaries for the abolished positions and deposit the appropriate funds into the ERS Trust Account. These funds had not been deposited to the Trust Account as of September 30, 2009. As of September 30, 2009, the amount outstanding against this loan was \$5,075,633. This amount has been identified as future debt service payments and is included in the General Fund reserve for debt service of which \$3,947,415 is actually deposited in an investment account held jointly with the FSM National Government. That investment account is restricted for the repayment of this debt and other ADB related debt set forth below.

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government program loans with ADB (Loan Number 1816 FSM (SF)) for the purpose of funding the Basic Social Services Project, with interest at 1% to 1.5% per annum. The principal payments shall be made semiannually commencing February 1, 2009, with a maturity date of August 1, 2032. As of September 30, 2009, the balance payable on this loan amounted to \$1,268,115.

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government Program Loans with ADB (Loan Number 1873 (SF) and Loan Number 1874 FSM (SF)) for the purpose of promoting private sector development in Chuuk, with interest at 1% to 1.5% per annum. The principal payments shall be made in 32 equal semi-annual payments with the first payment due on May 15, 2010 and the last payment on November 15, 2025. As of September 30, 2009, the balances payable on these loans amounted to \$739,840 and \$1,336,896, respectively.

Annual debt service requirements to maturity for principal and interest are as follows:

<u>Year Ending</u> <u>September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 235,867	\$ 100,793	\$ 336,660
2011	252,665	97,532	350,197
2012	252,665	94,271	346,936
2013	252,665	89,952	342,617
2014	273,812	86,479	360,291
2015-2019	1,570,205	375,963	1,946,168
2020-2024	1,908,569	264,331	2,172,900
2025-2029	1,769,908	149,703	1,919,611
2030-2034	1,243,792	58,842	1,302,634
2035-2037	<u>660,336</u>	<u>6,344</u>	<u>666,680</u>
	<u>\$ 8,420,484</u>	<u>\$ 1,324,210</u>	<u>\$ 9,744,694</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(7) Long-Term Obligations, Continued

Discretely Presented Component Units

Chuuk Public Utilities Corporation

Note payable to a commercial bank, 90 day terms, interest at prime plus 2% on a \$150,000 line of credit. The loan is collateralized by a bank deposit and security interest in fixed assets, accounts receivable and inventories. \$ 81,921

Note payable to the FSM Development Bank, interest at 9%, due in monthly installments of \$4,000. The loan is collateralized by major machinery, equipment and assignment of income. 731,260

Note payable to the FSM National Government, interest at 6.82%, due in semi-annual installments commencing August 1, 2007. 3,550,172

\$ 4,363,353

Annual debt service requirements to maturity for principal and interest are as follows:

<u>September 30,</u>	<u>Principal</u>	<u>Year ending Interest</u>	<u>Total</u>
2010	\$ 992,392	\$ 180,965	\$ 1,173,357
2011	59,737	176,891	236,628
2012	59,737	172,816	232,553
2013	59,737	168,742	228,479
2014	59,737	164,668	224,405
2015-2019	547,640	745,251	1,292,891
2020-2024	796,595	499,081	1,295,676
2025-2029	796,595	227,441	1,024,036
2030-2032	<u>991,183</u>	<u>17,715</u>	<u>1,008,898</u>
	<u>\$ 4,363,353</u>	<u>\$ 2,353,570</u>	<u>\$ 6,716,923</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2009

(8) Changes in Long-Term Obligations

Primary Government

Long-term liabilities will be liquidated in the future from governmental funds. During the year ended September 30, 2009, the following changes occurred in liabilities reported as part of the primary government's long-term liabilities in the statement of net assets:

	Balance October 1, 30, 2008	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2009	Due Within One Year
Loan payable:					
ADB loans:					
Loan 1520	\$ 5,181,633	\$ -	\$ (106,000)	\$ 5,075,633	\$ 106,000
Loan 1816	1,359,665	43,073	(134,623)	1,268,115	129,867
Loan 1873	739,840	-	-	739,840	-
Loan 1874	<u>866,110</u>	<u>470,786</u>	<u>-</u>	<u>1,336,896</u>	<u>-</u>
	8,147,248	513,859	(240,623)	8,420,484	235,867
Other:					
Compensated absences	<u>1,949,319</u>	<u>438,356</u>	<u>(322,100)</u>	<u>2,065,575</u>	<u>450,000</u>
	<u>\$ 10,096,567</u>	<u>\$ 952,215</u>	<u>\$ (562,723)</u>	<u>\$ 10,486,059</u>	<u>\$ 685,867</u>

Discretely Presented Component Units

During the year ended September 30, 2009, the following changes occurred in liabilities reported as part of the component unit's long-term liabilities in the statement of net assets:

	Balance October 1, 2008	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2009	Due Within One Year
Loans payable	<u>\$ 4,461,972</u>	<u>\$ -</u>	<u>\$ (98,619)</u>	<u>\$ 4,363,353</u>	<u>\$ 992,392</u>

(9) Contingencies

Sick Leave

It is the policy of the State to record expenditures for sick leave when leave is actually taken. Sick leave is compensated time for absence during working hours arising from employee illness or injury. The estimated accumulated amount of unused sick leave as of September 30, 2009 is \$4,379,659.

Insurance Coverage

The State does not maintain insurance coverage for a significant amount of fixed assets. In the event of a catastrophe, the State may be self-insured to a material extent.

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2009

(9) Contingencies, Continued

Federal Grants

The State participates in a number of federally assisted grant programs. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Cumulative questioned costs of \$1,097,349 relating to fiscal years 2003 through 2009 have been set forth in the State's Single Audit Report for the year ended September 30, 2009. The ultimate disposition of these questioned costs can be determined only by final action of the respective grantor agencies. Therefore, no provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

Litigation

The State is a party to various legal proceedings. However, the State is currently negotiating with judgment creditors to arrive at settlement amounts favorable to both parties. Claims must be adjudicated and are not recognized as current liabilities of the State as they cannot be paid without an underlying appropriation from the State Legislature and a corresponding allotment from the Executive Branch. No appropriation currently exists to finance these judgments. The State's Attorney General indicates that pending land lease cases and other claims against the State exist at September 30, 2009 in an amount that is material to the financial statements. Due to an inability to predict the ultimate outcome of these matters, no provision for these liabilities has been made in the accompanying financial statements.

Delinquent Taxes

The State is delinquent in remitting certain social security and withholding taxes. Management is of the opinion that no significant penalties or interest will arise from this matter and that if any such changes occur, they will be accounted for prospectively.

Loan Guarantee

The State has guaranteed repayment of a note payable of Chuuk Public Utility Corporation (CPUC) to the Asian Development Bank. The loan additionally passed through the FSM National Government. At September 30, 2009, the loan balance recorded by CPUC is \$3,550,172.

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2009

(9) Contingencies, Continued

General Fund Financial Position

The State's General Fund has sustained recurring operating deficits and has an unreserved fund deficit of \$15,278,834 at September 30, 2009. In addition, at September 30, 2009, the primary government's current liabilities exceed current assets by \$6,898,476.

Management of the State has entered into a memorandum of understanding with the FSM National Government to outline reform measures to address the deficit. The plan includes the following:

- The State will sell off its stock holdings or investments.
- The State is considering the sale of the Chuuk State Medical Referral House in Honolulu.
- The State will adopt measures to control General Fund expenditures. Such include moratorium of hiring, salary increases and other spending, such as travel.
- The State agreed to work to balance its proposed budgets.
- The State will work to restructure its government to include restructuring the Chuuk Legislature into a unicameral legislature.

Management of the State believes that the actions above will provide the State the opportunity to continue the process of reducing the General Fund deficit position.

(10) Restatement

Subsequent to the issuance of the State's 2008 financial statements, management of the State determined that capital asset balances were overstated by \$22,850,737, net of accumulated depreciation of \$8,621,311. As a result of this determination, beginning net assets of the governmental activities has been restated by \$14,229,426.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2009

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Revenues, Expenditures and Changes in Deficit
Budget and Actual - General Fund
Year Ended September 30, 2009

	Budgeted Amounts		Actual - Budgetary Basis (see Note 1)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues:				
Local revenues	\$ 5,060,674	\$ 5,060,674	\$ 5,236,001	\$ 175,327
Net change in fair value of investments	-	-	(122,608)	(122,608)
Total revenues	<u>5,060,674</u>	<u>5,060,674</u>	<u>5,113,393</u>	<u>52,719</u>
Expenditures:				
Current:				
General government	2,873,705	2,873,705	3,139,856	(266,151)
Education	132,350	646,209	536,471	109,738
Economic development	137,333	137,333	74,335	62,998
Health services	3,375	3,375	-	3,375
Public safety	771,733	771,733	729,886	41,847
Public works and transportation	616,193	616,193	540,258	75,935
Community affairs	137,756	137,756	17,211	120,545
Boards and commissions	406,226	406,226	364,304	41,922
Judiciary	408,626	408,626	380,634	27,992
Payments to component units	49,172	49,172	43,839	5,333
Municipal affairs	353,177	353,177	446,665	(93,488)
Other	36,220	36,220	19,642	16,578
Debt service	-	311,093	311,093	-
Total expenditures	<u>5,925,866</u>	<u>6,750,818</u>	<u>6,604,194</u>	<u>146,624</u>
Deficiency of revenues under expenditures	<u>(865,192)</u>	<u>(1,690,144)</u>	<u>(1,490,801)</u>	<u>199,343</u>
Other financing sources:				
Proceeds from issuance of long-term debt	-	513,859	513,859	-
Operating transfers in	-	-	423,500	423,500
Total other financing sources	<u>-</u>	<u>513,859</u>	<u>937,359</u>	<u>423,500</u>
Net change in deficit	<u>(865,192)</u>	<u>(1,176,285)</u>	<u>(553,442)</u>	<u>622,843</u>
Other changes in unreserved deficit				
Decrease in reserve for debt service	-	311,093	443,132	132,039
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes	447,946	447,946	447,946	-
Unreserved deficit at the beginning of the year	<u>(15,616,470)</u>	<u>(15,616,470)</u>	<u>(15,616,470)</u>	<u>-</u>
Unreserved deficit at the end of the year	<u>\$ (16,033,716)</u>	<u>\$ (16,033,716)</u>	<u>\$ (15,278,834)</u>	<u>\$ 754,882</u>

See accompanying notes to required supplementary information - budgetary reporting.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting
September 30, 2009

(1) Budgetary Information

An annual appropriated budget is adopted by the State’s Legislature for the General Fund and Compact Programs through an Appropriations Act. However, additional appropriations and budget modifications occur throughout the year. The majority of unencumbered appropriations lapse as of year end unless specifically extended by the State’s Legislature. Budgets for special revenue funds, except the Compact Program Fund, are not included in the annual Appropriations Act. Accordingly, a budget to actual presentation for special revenue funds, except the Compact Program Fund, is not required or presented. Project-length financial plans are generally adopted for all capital project funds.

Encumbrance accounting is utilized for budgetary control purposes. Encumbrances outstanding at year-end are reported as reservations of fund balance and will be funded as expenditures in the ensuing year. Encumbrances remain as reservations of fund balance until becoming expended or canceled. If an encumbrance is subsequently canceled, the funds revert to the applicable unreserved fund balance unless otherwise required by law.

Budgetary expenditures, which are on a basis other than GAAP, represent current charges against appropriations; current charges consist of all current year liquidated and unliquidated encumbrances. Budgetary expenditures are therefore determined by subtracting both current year liquidations of prior year encumbrances and unliquidated prior year encumbrances from the combined total of current year. When reviewed in relation to respective budgets, budgetary expenditures provide the principal means of evaluating current year operating performance and management stewardship. Amounts included on the Statement of Revenues, Expenditures, and Changes in Deficit - Budget and Actual - General Fund (which are presented on a non-GAAP budgetary basis) are reconciled to unreserved deficit of the Combined Balance Sheet within the other charges in unreserved deficit section of that statement.

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

For the year ended September 30, 2009, expenditures of the General Fund exceeded budget at the program area level (i.e., legal level of budgetary control as follows):

<u>Program Area</u>	<u>Excess</u>
Department of Treasury	\$ 339,568
Chuuk Recreation Board	\$ 14,253
Environmental Protection Agency	\$ 3,000
Payments to municipalities	\$ 93,488
Farmers Home Administration	\$ 9,897

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting
September 30, 2009

(2) Reconciliation - GAAP and Budgetary Bases of Accounting

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

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

Net change in fund deficit	\$ (201,339)
Encumbrances	<u>(352,103)</u>
Net change in unreserved fund deficit	\$ <u>(553,442)</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

OTHER SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2009

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account
Governmental Funds
Year Ended September 30, 2009

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
Expenditures:					
Salaries and wages					
Regular	\$ 3,596,185	\$ 10,174,978	\$ -	\$ -	\$ 13,771,163
Overtime	83,060	497,937	-	-	580,997
Fringe benefits	392,435	1,083,577	-	-	1,476,012
Travel and transportation	194,377	365,718	-	10,962	571,057
Books and library materials	-	309,054	-	-	309,054
Communications	24,397	119,331	-	-	143,728
Dues, membership, and subscriptions	-	6,960	-	-	6,960
Food stuffs	47,791	620,548	-	-	668,339
Port charges	280	20,019	-	16,487	36,786
Capital outlays	513,861	-	-	-	513,861
Office supplies and materials	43,959	934,681	-	68,596	1,047,236
POL	167,088	283,158	-	-	450,246
Printing and reproduction	28,150	39,578	-	-	67,728
Rental services	10,536	103,656	-	24,800	138,992
Repairs and maintenance	1,736	589,196	-	6,730	597,662
Utilities	110,326	888,117	-	-	998,443
Goods and services	5,921	1,213	-	-	7,134
Subsidies and contributions	3,494	232,457	-	-	235,951
Medical referrals	-	106,145	-	-	106,145
Medical supplies	-	1,754,526	-	34,850	1,789,376
Contractual services	48,181	1,213,291	-	37,071	1,298,543
Professional services	1,500	218,931	-	18,000	238,431
Retirement contributions	945	-	-	50,318	51,263
Scholarships and allowances	399,680	978,850	-	5,238	1,383,768
Training	-	497,644	-	-	497,644
Insurance	-	91,700	-	-	91,700
Leased housing, buildings and land	41,000	248,740	-	-	289,740
Equipment	50,144	1,053,117	-	23,037	1,126,298
Principal repayment	240,623	-	-	-	240,623
Interest payments	70,470	-	-	-	70,470
Miscellaneous	136,483	7,380	-	-	143,863
	<u>\$ 6,212,622</u>	<u>\$ 22,440,502</u>	<u>\$ -</u>	<u>\$ 296,089</u>	<u>\$ 28,949,213</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GENERAL FUND

September 30, 2009

The general fund is used to account for resources traditionally associated with government which are not required legally or by sound financial management to be accounted for in another fund. The United States Compact of Free Association current account and inflation adjustment funds associated with the current account are accounted for in this fund in addition to local taxes and other revenues.

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function, and Changes in Deficit
General Fund
Year Ended September 30, 2009
(with comparative totals for the year ended September 30, 2008)

	2009	2008
Revenues:		
FSM revenue sharing	\$ 2,660,821	\$ 2,306,567
State taxes:		
Sales tax	1,114,512	983,773
Hotel	153,744	142,948
Tobacco	75,161	98,309
Alcoholic beverages	110,329	118,653
Delinquent tax collections	64,206	75,257
Other excise taxes	124,250	112,459
	1,642,202	1,531,399
Fees and charges:		
Licenses and permits	288,424	254,695
Leases and other rentals	125,342	55,872
	413,766	310,567
Departmental charges:		
Transportation collections	513,694	625,017
Net change in the fair value of investments	(122,608)	(787,438)
Other revenues	5,518	202,583
Total revenues	5,113,393	4,188,695
Expenditures:		
Current:		
General government:		
Office of the Governor	493,584	529,975
State Legislature	1,736,646	1,571,213
Department of Planning and Statistics	23,956	-
Department of Treasury	763,498	281,160
	3,017,684	2,382,348
Education:		
Department of Education	536,471	554,958
Economic development:		
Department of Agriculture	37,935	46,535
Department of Marine Resources	34,675	84,784
	72,610	131,319
Health services	-	554,958
Public safety:		
Office of the Attorney General	194,188	200,487
Department of Public Safety	527,469	548,560
	721,657	749,047
Public works and transportation:		
Department of Transportation	524,275	761,162
Community affairs:		
Department of Public Affairs	17,211	-

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function, and Changes in Deficit, Continued
General Fund
Year Ended September 30, 2009
(with comparative totals for the year ended September 30, 2008)

	2009	2008
Expenditures, continued:		
Current, continued:		
Boards and commissions:		
Chuuk Recreation Board	14,253	16,401
Land Commission	83,038	88,720
Environmental Protection Agency	3,000	4,423
Election Commission	240,838	80,626
	341,129	190,170
Judiciary:		
State Court	374,532	406,764
Payments to component units:		
Chuuk State Housing Authority	43,839	-
Municipal affairs:		
Payments to municipalities	271,948	139,551
Other:		
Small Business Development Center	-	354
Farmers Home Administration	17,147	17,269
Red Cross	-	3,680
Peace Corps	2,495	6,300
Other	-	6,157
	19,642	33,760
Debt service:		
Principal repayment	240,623	-
Interest payment	70,470	-
	311,093	-
Total expenditures	6,252,091	5,904,037
Deficiency of revenues under expenditures	(1,138,698)	(1,715,342)
Other financing sources:		
Proceeds from issuance of long-term debt	513,859	1,322,649
Operating transfers in	423,500	3,499,999
Total other financing sources	937,359	4,822,648
Special items:		
Write off of liabilities	-	428,333
Total other financing sources	-	428,333
Net change in deficit	(201,339)	3,535,639
Deficit at the beginning of the year	(8,581,722)	(12,117,361)
Deficit at the end of the year	\$ (8,783,061)	\$ (8,581,722)

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures and Changes in Deficit
Budget and Actual - General Fund
Year Ended September 30, 2009

	Budgeted Amounts		Actual Budgetary Basis (see Note 1)	Variance with Final Budget Positive/(Negative)
	Original	Final		
Revenues:				
Local revenues	\$ 5,060,674	\$ 5,060,674	\$ 5,236,001	\$ 175,327
Net change in fair value of investments	-	-	(122,608)	(122,608)
	<u>5,060,674</u>	<u>5,060,674</u>	<u>5,113,393</u>	<u>52,719</u>
Total revenues				
Expenditures:				
Current:				
General government:				
Office of the Governor	540,900	540,900	503,734	37,166
State Legislature	1,855,847	1,855,847	1,846,879	8,968
Department of Planning and Statistics	53,028	53,028	53,745	27,283
Department of Treasury	423,930	423,930	763,498	(339,568)
	<u>2,873,705</u>	<u>2,873,705</u>	<u>3,139,856</u>	<u>(266,151)</u>
Education:				
Department of Education	132,350	646,209	536,471	109,738
Economic development:				
Department of Agriculture	39,555	39,555	37,935	1,620
Department of Marine Resources	44,432	44,432	36,400	8,032
Historic preservation	12,073	12,073	-	12,073
Department of Commerce and Industry	41,273	41,273	-	41,273
	<u>137,333</u>	<u>137,333</u>	<u>74,335</u>	<u>62,998</u>
Health services:				
Department of Health Services	3,375	3,375	-	3,375
Public safety:				
Office of the Attorney General	210,208	210,208	202,417	7,791
Department of Public Safety	561,525	561,525	527,469	34,056
	<u>771,733</u>	<u>771,733</u>	<u>729,886</u>	<u>41,847</u>
Public works and transportation:				
Department of Transportation	616,193	616,193	540,258	75,935
Community affairs:				
Department of Public Affairs	137,756	137,756	17,211	120,545
Boards and commissions:				
Chuuk Recreation Board	-	-	14,253	(14,253)
Land Commission	88,387	88,387	83,038	5,349
Environmental Protection Agency	-	-	3,000	(3,000)
Election Commission	316,482	316,482	262,656	53,826
Mortlocks Commission	1,357	1,357	1,357	-
	<u>406,226</u>	<u>406,226</u>	<u>364,304</u>	<u>41,922</u>
Judiciary:				
State Court	408,626	408,626	380,634	27,992
Payments to component units:				
Chuuk State Housing Authority	49,172	49,172	43,839	5,333
Municipal affairs:				
Payments to municipalities	353,177	353,177	446,665	(93,488)
Other:				
Farmers Home Administration	7,250	7,250	17,147	(9,897)
Peace Corps	2,500	2,500	2,495	5
Other	26,470	26,470	-	26,470
	<u>36,220</u>	<u>36,220</u>	<u>19,642</u>	<u>16,578</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures and Changes in Deficit
Budget and Actual - General Fund, Continued
Year Ended September 30, 2009

	Budgeted Amounts		Actual Budgetary Basis (see Note 1)	Variance with Final Budget Positive/(Negative)
	Original	Final		
Debt service:				
Principal repayment	-	240,623	240,623	-
Interest payments	-	70,470	70,470	-
	-	311,093	311,093	-
Total expenditures	5,925,866	6,750,818	6,604,194	146,624
Deficiency of revenues under expenditures	(865,192)	(1,690,144)	(1,490,801)	199,343
Other financing sources:				
Proceeds from issuance of long-term debt	-	513,859	513,859	-
Operating transfers in	-	-	423,500	423,500
Total other financing sources	-	513,859	937,359	423,500
Special items:				
Write off of liabilities	-	-	-	-
Net change in deficit	(865,192)	(1,176,285)	(553,442)	622,843
Other changes in unreserved deficit:				
Decrease in reserve for debt service	-	311,093	443,132	132,039
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes	447,946	447,946	447,946	-
Unreserved deficit at the beginning of the year	(15,616,470)	(15,616,470)	(15,616,470)	-
Unreserved deficit at the end of the year	\$ (16,033,716)	\$ (16,033,716)	\$ (15,278,834)	\$ 754,882

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS - SPECIAL REVENUE FUNDS

September 30, 2009

Special revenue funds are used to account for specific revenues that are legally restricted for particular purposes. A brief discussion of the State's Nonmajor Governmental Funds - Special Revenue Funds as of September 30, 2009, follows:

Chuuk Airport Authority Fund

This fund accounts for certain funds received by the Airport Authority for the maintenance of Chuuk Airport. In fiscal year 2007, the requirement to deposit fees related to airport collections into the revolving fund was repealed but the remaining fund balance may still be used to expend on airport maintenance.

CFSM Grants Fund

This fund accounts for activities received from FSM congressional appropriations utilized by the State to finance general governmental operations.

Compact Other Grants Fund

This fund accounts for the following funds received under the Compact of Free Association:

Compact Section 212 - Special Development Assistance Fund: This grant is restricted for special development assistance and is granted under the Compact of Free Association with the United States.

Compact 214(c) - Energy Grant Fund: This fund accounts for funds, granted under the Compact of Free Association with the United States, specifically restricted for energy programs.

Compact 216 (a)(2) Health and Medical Fund: This fund accounts for funds granted under the Compact of Free Association with the United States, specifically restricted for health and medical programs including referrals to hospital and treatment centers.

Compact Section 216(a)(3) Scholarship Fund: This fund accounts for funds granted under the Compact of Free Association with the United States to the FSM National Government which are subgranted to the State and are specifically restricted for educational scholarships at U.S. and Micronesian higher education institutions.

Compact Special Block Grant Section 221 (b) Fund

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

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS

Combining Balance Sheet
September 30, 2009

	<u>Chuuk Airport Authority</u>	<u>Hospital Revolving</u>	<u>Total</u>
<u>ASSETS</u>			
Due from other funds	\$ 1,196,831	\$ 60,283	\$ 1,257,114
<u>FUND BALANCES</u>			
Fund balances:			
Reserved for:			
Related assets	\$ 1,196,831	\$ -	\$ 1,196,831
Unreserved	<u>-</u>	<u>60,283</u>	<u>60,283</u>
	<u>\$ 1,196,831</u>	<u>\$ 60,283</u>	<u>\$ 1,257,114</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Statement of Revenues, Expenditures By Function, and Changes in Fund Balances
Year Ended September 30, 2009

	<u>Chuuk Airport Authority</u>	<u>Hospital Revolving</u>	<u>Total</u>
Revenues:			
Federal contributions and other grants	\$ -	\$ 159,036	\$ 159,036
Fees and charges	<u>-</u>	<u>197,336</u>	<u>197,336</u>
Total revenues	<u>-</u>	<u>356,372</u>	<u>356,372</u>
Expenditures by function:			
Current:			
Health services	<u>-</u>	<u>296,089</u>	<u>296,089</u>
Total expenditures	<u>-</u>	<u>296,089</u>	<u>296,089</u>
Net change in fund balances	-	60,283	60,283
Fund balance at the beginning of the year	<u>1,196,831</u>	<u>-</u>	<u>1,196,831</u>
Fund balance at the end of the year	<u>\$ 1,196,831</u>	<u>\$ 60,283</u>	<u>\$ 1,257,114</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Statement of Revenues, Expenditures By Account, and Changes in Fund Balances
Year Ended September 30, 2009

	<u>Chuuk Airport Authority</u>	<u>Hospital Revolving</u>	<u>Total</u>
Revenues:			
Federal contributions and other grants	\$ -	\$ 159,036	\$ 159,036
Fees and charges	-	197,336	197,336
Total revenues	<u>-</u>	<u>356,372</u>	<u>356,372</u>
Expenditures by account:			
Travel and transportation	-	10,962	10,962
Port charges	-	16,487	16,487
Office supplies and materials	-	68,596	68,596
Rental services	-	24,800	24,800
Repairs and maintenance	-	6,730	6,730
Medical supplies	-	34,850	34,850
Contractual services	-	37,071	37,071
Professional services	-	18,000	18,000
Retirement contributions	-	50,318	50,318
Scholarships and allowances	-	5,238	5,238
Equipment	-	23,037	23,037
Total expenditures	<u>-</u>	<u>296,089</u>	<u>296,089</u>
Net change in fund balances	-	60,283	60,283
Fund balance at the beginning of the year	<u>1,196,831</u>	<u>-</u>	<u>1,196,831</u>
Fund balance at the end of the year	<u>\$ 1,196,831</u>	<u>\$ 60,283</u>	<u>\$ 1,257,114</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Balance Sheet
September 30, 2009

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
<u>ASSETS</u>											
Investments	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,050,000	\$ 2,050,000
Receivables:											
FSM National Government	10,125	26,145	73,297	16,058	1,133,721	843,465	-	-	43,962	-	2,146,773
Prepayments	89,560	1,782,556	-	-	15,465	10,400	-	-	-	-	1,897,981
Due from other funds	2,563,792	1,596,891	-	113,754	-	-	109,458	178,583	-	37,272	4,599,750
Due from component units	-	-	-	-	-	-	-	-	-	-	-
	<u>\$ 2,663,477</u>	<u>\$ 3,405,592</u>	<u>\$ 73,297</u>	<u>\$ 129,812</u>	<u>\$ 1,149,186</u>	<u>\$ 853,865</u>	<u>\$ 109,458</u>	<u>\$ 178,583</u>	<u>\$ 43,962</u>	<u>\$ 2,087,272</u>	<u>\$ 6,094,754</u>
<u>LIABILITIES AND FUND BALANCES (DEFICITS)</u>											
Liabilities:											
Accounts payable	\$ 185,279	\$ 450,704	\$ 19,418	\$ 15,986	\$ 6,984	\$ 87,318	\$ 96,939	\$ 50,851	\$ 17,651	\$ -	\$ 931,130
Due to other funds	-	-	53,879	-	1,142,202	766,547	-	-	66,493	-	2,029,121
Total liabilities	<u>185,279</u>	<u>450,704</u>	<u>73,297</u>	<u>15,986</u>	<u>1,149,186</u>	<u>853,865</u>	<u>96,939</u>	<u>50,851</u>	<u>84,144</u>	<u>-</u>	<u>2,960,251</u>
Fund balances:											
Reserved for:											
Related assets	-	-	-	-	-	-	-	-	-	2,050,000	2,050,000
Encumbrances	2,158,471	2,238,125	35,467	32,881	46,806	497,899	39,009	-	12,996	-	5,061,654
Unreserved	319,727	716,763	(35,467)	80,945	(46,806)	(497,899)	(26,490)	127,732	(53,178)	37,272	622,599
Total fund balances (deficits)	<u>2,478,198</u>	<u>2,954,888</u>	<u>-</u>	<u>113,826</u>	<u>-</u>	<u>-</u>	<u>12,519</u>	<u>127,732</u>	<u>(40,182)</u>	<u>2,087,272</u>	<u>7,734,253</u>
Total liabilities and fund balances (deficits)	<u>\$ 2,663,477</u>	<u>\$ 3,405,592</u>	<u>\$ 73,297</u>	<u>\$ 129,812</u>	<u>\$ 1,149,186</u>	<u>\$ 853,865</u>	<u>\$ 109,458</u>	<u>\$ 178,583</u>	<u>\$ 43,962</u>	<u>\$ 2,087,272</u>	<u>\$ 10,694,504</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances (Deficits)
Year Ended September 30, 2009

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
Revenues:											
Compact funding	\$ 8,391,216	\$ 10,215,534	\$ 214,981	\$ 353,000	\$ 1,894,444	\$ 4,500,939	\$ -	\$ -	\$ -	\$ -	\$ 25,570,114
CFSM grants	-	-	-	-	-	-	-	-	43,962	-	43,962
Total revenues	<u>8,391,216</u>	<u>10,215,534</u>	<u>214,981</u>	<u>353,000</u>	<u>1,894,444</u>	<u>4,500,939</u>	<u>-</u>	<u>-</u>	<u>43,962</u>	<u>-</u>	<u>25,614,076</u>
Expenditures by function:											
Current:											
General government	-	-	-	-	642,969	-	-	-	-	-	642,969
Health services	-	7,783,556	-	-	-	-	-	-	-	-	7,783,556
Education	8,018,950	-	-	-	-	4,022,675	-	-	-	-	12,041,625
Economic development	-	-	133,220	256,008	-	-	-	-	-	-	389,228
Public safety	-	-	-	-	54,226	-	-	-	43,962	-	98,188
Boards and commissions	960,908	-	165,848	123,500	-	-	-	-	-	-	1,250,256
Payment to component units	232,457	2,223	-	-	-	-	-	-	-	-	234,680
Total expenditures	<u>9,212,315</u>	<u>7,785,779</u>	<u>299,068</u>	<u>379,508</u>	<u>697,195</u>	<u>4,022,675</u>	<u>-</u>	<u>-</u>	<u>43,962</u>	<u>-</u>	<u>22,440,502</u>
Excess (deficiency) of revenues over (under) expenditures	(821,099)	2,429,755	(84,087)	(26,508)	1,197,249	478,264	-	-	-	-	3,173,574
Other financing uses:											
Operating transfers out	-	-	-	-	-	-	-	-	-	(423,500)	(423,500)
Net change in fund balances (deficits)	<u>(821,099)</u>	<u>2,429,755</u>	<u>(84,087)</u>	<u>(26,508)</u>	<u>1,197,249</u>	<u>478,264</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(423,500)</u>	<u>2,750,074</u>
Fund balances (deficits) at the beginning of the year	3,299,297	525,133	84,087	140,334	(1,197,249)	(478,264)	12,519	127,732	(40,182)	2,510,772	4,984,179
Fund balances (deficits) at the end of the year	<u>\$ 2,478,198</u>	<u>\$ 2,954,888</u>	<u>\$ -</u>	<u>\$ 113,826</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 12,519</u>	<u>\$ 127,732</u>	<u>\$ (40,182)</u>	<u>\$ 2,087,272</u>	<u>\$ 7,734,253</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances (Deficits)
Year Ended September 30, 2009

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
Revenues:											
Compact funding	\$ 8,391,216	\$ 10,215,534	\$ 214,981	\$ 353,000	\$ 1,894,444	\$ 4,500,939	\$ -	\$ -	\$ -	\$ -	\$ 25,570,114
CFSM grants	-	-	-	-	-	-	-	-	43,962	-	43,962
Total revenues	<u>8,391,216</u>	<u>10,215,534</u>	<u>214,981</u>	<u>353,000</u>	<u>1,894,444</u>	<u>4,500,939</u>	<u>-</u>	<u>-</u>	<u>43,962</u>	<u>-</u>	<u>25,614,076</u>
Expenditures by account:											
Salaries and wages:											
Regular	5,450,802	2,461,170	165,723	149,934	226,531	1,720,818	-	-	-	-	10,174,978
Overtime	13,035	483,633	-	-	-	1,269	-	-	-	-	497,937
Fringe benefits	547,362	299,494	18,494	8,393	23,152	186,682	-	-	-	-	1,083,577
Travel and transportation	38,269	80,547	8,352	18,023	28,967	188,167	-	-	3,393	-	365,718
Books and library materials	306,820	-	-	-	-	2,234	-	-	-	-	309,054
Communications	25,255	23,190	10,455	15,441	11,725	29,648	-	-	3,617	-	119,331
Dues, memberships, and subscriptions	-	4,546	-	290	2,124	-	-	-	-	-	6,960
Food stuffs	260,165	226,738	-	-	-	129,318	-	-	4,327	-	620,548
Port charges	7,600	8,636	2,088	1,285	-	410	-	-	-	-	20,019
Office supplies and materials	319,321	109,476	24,526	16,624	40,589	410,569	-	-	13,576	-	934,681
POL	89,705	72,824	9,314	9,372	2,149	93,599	-	-	6,195	-	283,158
Printing and reproduction	10,822	3,412	-	6,433	-	18,911	-	-	-	-	39,578
Rental services	65,015	3,032	7,463	3,125	915	24,106	-	-	-	-	103,656
Repairs and maintenance	217,297	275,419	2,892	10,612	700	82,276	-	-	-	-	589,196
Utilities	93,498	741,417	9,899	7,132	8,550	27,621	-	-	-	-	888,117
Goods and services	114	924	-	175	-	-	-	-	-	-	1,213
Subsidies and contributions	232,457	-	-	-	-	-	-	-	-	-	232,457
Medical referrals	-	106,145	-	-	-	-	-	-	-	-	106,145
Medical supplies	-	1,743,902	-	-	-	10,624	-	-	-	-	1,754,526
Contractual services	377,149	452,964	15,260	88,175	96,563	181,143	-	-	2,037	-	1,213,291
Professional services	18,000	-	-	-	200,931	-	-	-	-	-	218,931
Scholarships and allowances	918,400	60,000	450	-	-	-	-	-	-	-	978,850
Training	70,000	27,160	-	784	6,000	393,700	-	-	-	-	497,644
Insurance	-	-	-	1,200	-	90,500	-	-	-	-	91,700
Leased housing, buildings and land	-	93,000	-	13,200	28,200	114,340	-	-	-	-	248,740
Equipment	151,229	503,161	24,152	29,310	17,708	316,740	-	-	10,817	-	1,053,117
Miscellaneous	-	4,989	-	-	2,391	-	-	-	-	-	7,380
Total expenditures	<u>9,212,315</u>	<u>7,785,779</u>	<u>299,068</u>	<u>379,508</u>	<u>697,195</u>	<u>4,022,675</u>	<u>-</u>	<u>-</u>	<u>43,962</u>	<u>-</u>	<u>22,440,502</u>
Excess (deficiency) of revenues over (under) expenditures	(821,099)	2,429,755	(84,087)	(26,508)	1,197,249	478,264	-	-	-	-	3,173,574
Other financing uses:											
Operating transfers out	-	-	-	-	-	-	-	-	-	(423,500)	(423,500)
Net change in fund balances (deficits)	(821,099)	2,429,755	(84,087)	(26,508)	1,197,249	478,264	-	-	-	(423,500)	2,750,074
Fund balances (deficits) at the beginning of the year	<u>3,299,297</u>	<u>525,133</u>	<u>84,087</u>	<u>140,334</u>	<u>(1,197,249)</u>	<u>(478,264)</u>	<u>12,519</u>	<u>127,732</u>	<u>(40,182)</u>	<u>2,510,772</u>	<u>4,984,179</u>
Fund balances (deficits) at the end of the year	<u>\$ 2,478,198</u>	<u>\$ 2,954,888</u>	<u>\$ -</u>	<u>\$ 113,826</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 12,519</u>	<u>\$ 127,732</u>	<u>\$ (40,182)</u>	<u>\$ 2,087,272</u>	<u>\$ 7,734,253</u>

See Accompanying Independent Auditors' Report.

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

Honorable Wesley Simina
Governor, State of Chuuk
Federated States of Micronesia:

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk (the State) as of and for the year ended September 30, 2009, which collectively comprise the State of Chuuk's basic financial statements and have issued our report thereon dated June 24, 2010, which report was qualified with respect to: 1) a liability for land leases and other claims payable in the governmental activities and the General Fund; and 2) the inadequacy of accounting records for land and related land acquisitions payable recorded for the governmental activities and the General Fund, and 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 of the aggregate discretely presented component units for the year ended September 30, 2009. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

For purposes of this report, our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants, and other matters did not include the Chuuk State Health Care Plan, the Chuuk Public Utility Corporation, and the Chuuk State Housing Authority, which were all audited by us. We have issued separate reports on our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters for these entities. The findings, if any, included in those reports are not included herein.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the State's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the State's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs (pages 70 through 76) as items 2009-03 through 2009-05 to be significant deficiencies in internal control over financial reporting.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that the significant deficiencies described above are material weaknesses.

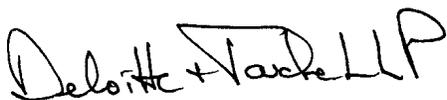
Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the State in a separate letter June 24, 2010.

The State's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the State's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the management of the State, the Honorable Members of the Chuuk State Legislature, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.



June 24, 2010

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 AND ON THE
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

Honorable Wesley Simina
Governor, State of Chuuk
Federated States of Micronesia:

Compliance

We have audited the compliance of the State of Chuuk (the State) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended September 30, 2009. The State's major federal program is identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (pages 70 through 76). Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the State's management. Our responsibility is to express an opinion on the State's compliance based on our audit.

As discussed in Note 2b to the Schedule of Expenditures of Federal Awards, the State's basic financial statements include the operations of certain entities whose federal awards are not included in the Schedule of Expenditures of Federal Awards for the year ended September 30, 2009. Our audit, described below, did not include the operations of the entities identified in Note 2b as these entities conducted separate audits in accordance with OMB Circular A-133, if required.

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

As described in items 2009-01 and 2009-02 in the accompanying Schedule of Findings and Questioned Costs, the State did not comply with requirements regarding equipment and real property management, and special tests and provisions that are applicable to its Compact of Free Association Sector Grants (CFDA # 15.875) major program. Compliance with such requirements is necessary, in our opinion, for the State to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the State complied, in all material respects, with the requirements referred to above that are applicable to its Compact of Free Association Sector Grants (CFDA # 15.875) major program for the year ended September 30, 2009.

Internal Control Over Compliance

The management of the State is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the State internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the State internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies and others that we consider to be material weaknesses.

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 2009-01 and 2009-02 to be significant deficiencies.

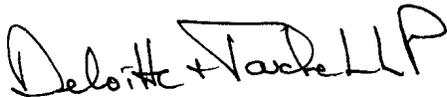
A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We consider the significant deficiencies described above to be material weaknesses.

The State's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the State's responses and, accordingly, we express no opinion on them.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk (the State) as of and for the year ended September 30, 2009, and have issued our report thereon dated June 24, 2010, which report was qualified with respect to: 1) a liability for land leases and other claims payable in the governmental activities and the General Fund; and 2) the inadequacy of accounting records for land and related land acquisitions payable recorded for the governmental activities and the General Fund, and 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 of the aggregate discretely presented component units for the year ended September 30, 2009. The accompanying Schedule of Expenditures of Federal Awards (pages 65 through 66) is presented for the purpose of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of the management of the State. Because the scope of our work was not sufficient to enable us to express, and we did not express, an opinion on the statement of activities for the governmental activities, and the governmental funds statement of revenues, expenditures, and changes in fund balances (deficits), we do not express an opinion on the Schedule of Expenditures of Federal Awards.

This report is intended solely for the information and use of the management of the State, the Honorable Members of the Chuuk State Legislature, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and others within the entity 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.

June 24, 2010

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Expenditures of Federal Awards, by Grantor
Year Ended September 30, 2009

<u>Agency/Program</u>	<u>Expenditures</u>
U.S. Department of the Interior	\$ <u>22,396,540</u>
GRAND TOTAL	\$ <u><u>22,396,540</u></u>
Reconciliation to the basic financial statements:	
Grants Assistance Fund	\$ 22,440,502
Less: CFSM Grants	<u>43,962</u>
	\$ <u><u>22,396,540</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2009

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF THE INTERIOR		
Economic, Social and Political Development of the Territories:		
Compact Sector Grants - Capacity Building Sector		\$ 697,195
Compact Sector Grants - Education Sector		9,212,315
Supplemental Education Grant		4,022,675
Compact Sector Grants - Environment Sector		299,068
Compact Sector Grants - Health Sector		7,785,779
Compact Sector Grants - Private Sector Development		<u>379,508</u>
Total Compact Sector Grants Fund	15.875	<u>22,396,540</u>
U.S. DEPARTMENT OF THE INTERIOR TOTAL		<u><u>\$ 22,396,540</u></u>

Note: The above grants are received in a subrecipient capacity through the FSM National Government.

See accompanying notes to schedule of expenditures of federal awards.

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2009

1. Scope of Audit

The State is one of the four States of the Federated States of Micronesia. All significant operations of the State are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior has been designated as the State's cognizant agency for Single Audit.

A. Programs Subject to Single Audit

Schedules of Expenditures of Federal Awards are presented for each federal program related to the following agencies:

- U.S. Department of the Interior

2. Summary of Significant Accounting Policies

A. Basis of Accounting

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

B. Reporting Entity

For purposes of complying with The Single Audit Act of 1984, as amended in 1996, the State's reporting entity is defined in Note 1A to its September 30, 2009 basic financial statements; and all of the discretely presented component units are excluded. Accordingly, the accompanying Schedule of Expenditures of Federal Awards presents the federal award programs administered by the State, as defined above, for the year ended September 30, 2009.

C. Subgrantees

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

D. Indirect Cost Allocation

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2009

2. Summary of Significant Accounting Policies, Continued

E. CFDA #15.875

CFDA #15.875 represents the Office of Insular Affairs (OIA), U. S. Department of the Interior. Funding from this source is subject to varying rules and regulations since OIA administers the Compact of Free Association, which is a treaty, and is not a federal program. The Compact is comprised of various funded programs, each with separate compliance requirements. To maximize audit coverage of OIA funding, the OIG has recommended that programs administered under CFDA #15.875 be grouped by like compliance requirements and such groupings be separately evaluated as major programs.

3. Component Units

The State's component units are to separately satisfy the requirements of OMB Circular A-133. The following presents information concerning component units, which are to separately satisfy their A-133 requirements.

Chuuk Public Utility Corporation

The Chuuk Public Utility Corporation, (CPUC), a discretely presented component unit, is the recipient of various pass-through funds from Chuuk State and direct grants from the U.S. Department of the Interior. The CPUC is to separately satisfy its 2009 reporting responsibilities under the Single Audit Act.

Chuuk State Housing Authority

The Chuuk State Housing Authority (CSHA), a discretely presented component unit, is the recipient of various pass-through funds from Chuuk State and certain direct grants.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Programs Selected For
Audit in Accordance with OMB Circular A-133
Year Ended September 30, 2009

<u>Grantor</u> <u>Program Title</u>	<u>CFDA No.</u>	<u>2009</u> <u>Fiscal Year</u> <u>Expenditures</u>
<u>U.S. Department of the Interior</u>		
Compact of Free Association:		
Compact Sector Grants	15.875	\$ <u>22,396,540</u>
Total U.S. Federal program expenditures		\$ <u>22,396,540</u>
% of total U.S. Federal expenditures covered by major programs		<u>100%</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs
Year Ended September 30, 2009

Part I - Summary of Auditors' Results

- | | |
|---|-----------------------|
| 1. Type of auditors' report issued:
Internal control over financial reporting: | Qualified; Disclaimer |
| 2. Material weakness(es) identified? | Yes |
| 3. Significant deficiency(ies) identified that is not considered to be a material weakness? | None reported |
| 4. Noncompliance material to the financial statements noted? | No |

Federal Awards

Internal control over major programs:

- | | |
|---|-----------|
| 5. Material weakness(es) identified? | Yes |
| 6. Significant deficiency(ies) identified that is not considered to be a material weakness? | No |
| 7. Type of auditors' report issued on compliance for major programs: | Qualified |
| 8. Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? | Yes |
| 9. The State's major programs were as follows: | |

<u>CFDA Number</u>	<u>Federal Program</u>	
15.875	U.S. Department of the Interior – Compact of Free Association – Sector Grants	

- | | |
|--|-----------|
| 10. Dollar threshold used to distinguish between Type A and Type B Programs, as those terms are defined in OMB Circular A-133: | \$671,896 |
| 11. The State qualified as a low-risk auditee, as that term is defined in OMB Circular A-133? | No |

Part II - Financial Statement Findings Section

<u>Reference #</u>	<u>Findings</u>
2009-3	Land Lease Payable
2009-4	Land Acquisitions
2009-5	Outstanding Checks

Part III - Federal Award Findings and Questioned Cost Section

<u>Reference #</u>	<u>CFDA #</u>	<u>Findings</u>	<u>Questioned Costs</u>
2009-01	15.875	Special Tests and Provisions	\$ -
2009-02	15.875	Equipment and Real Property Management	\$ -

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2009

Finding No.: 2009-01
Grantor Agency: U.S. Department of the Interior
CFDA Program: 15.875 Compact of Free Association
Grant Number: Compact Sector Grants
Requirement: Special Tests and Provisions
Questioned Costs: \$0

Criteria: Article VI, Section 1(j)(14) of the Fiscal Procedures Agreement (FPA) states that all contracts paid with funds provided pursuant to the Compact, as amended, shall contain the following provisions: (i) for contracts in excess of \$100,000 - administrative, contractual, or legal remedies in instances where contractors violate or breach contract terms, and the provision of such sanctions and penalties as appropriate; (ii) for contracts in excess of \$100,000 - termination for cause and for convenience by the Grantee or Sub-Grantee including the manner by which it will be effected and the basis for settlement; (iii) compliance with the local statutes regarding kickbacks and corrupt practices; (iv) access by the FSM National Government and its Sub-Grantees, the Government of the United States, or any of their duly authorized representatives to any books, documents, papers, and records of the contractor which are directly pertinent to that specific Contract for the purpose of making audit, examination, excerpts, and transcriptions; (v) retention of all required records for three years after Grantees or Sub-Grantees make final payments and all other pending matters are closed; and (vi) compliance with all applicable standards, orders, or requirements issued under local environmental laws.

Condition:

For 12 (or 5%) of 204 transactions tested, the underlying contract lacks applicable contract provisions required by the Fiscal Procedures Agreement.

<u>Transaction Date</u>	<u>Oblig. #</u>
3/11/2009	21843
1/7/2009	17534
2/4/2009	20619
03/25/09	25773
03/31/09	24947
04/08/09	25076
04/13/09	22501
06/12/09	26177
06/05/09	24409
04/24/09	24331
05/25/09	25103
07/13/09	27544

Cause: There appears to be weak internal controls over ensuring that required provisions are contained in contracts.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2009

Finding No.: 2009-01, Continued
Grantor Agency: U.S. Department of the Interior
CFDA Program: 15.875 Compact of Free Association
Grant Number: Compact Sector Grants
Requirement: Special Tests and Provisions
Questioned Costs: \$0

Effect: The condition may result in potential noncompliance with applicable compliance requirements and a potential misstatement of expenditures may exist. However no questioned cost result from this matter as the underlying contracts were otherwise executed in accordance with governing standards.

Recommendation: The State should strengthen controls over ensuring compliance with applicable Compact Fiscal Procedures.

Auditee Response and Corrective Action Plan: We agree with the finding and recommendation. Although the Office of the Attorney General and relevant departments have already been instructed to include such provisions, we will specifically list those clauses that need to be inserted for a particular department's inclusion and assist them in using adequate contract templates for sector funds.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2009

Finding No.: 2009-02
Grantor Agency: U.S. Department of the Interior
CFDA Program: 15.875 Compact of Free Association
Grant Number: Compact Sector Grants
Requirement: Equipment and Real Property Management
Questioned Cost: \$0

Criteria: Management should periodically review asset maintenance activities to ensure compliance with program objectives and requirements.

Condition: No documented procedures are in currently in place to ensure that fixed assets are periodically reviewed for asset maintenance.

Cause: There appears to be a weakness in internal controls over ensuring that fixed assets are periodically maintained.

Effect: The expected life of fixed assets may be lessened. However, no questioned costs result from this finding as no specific instances came to our attention in fiscal year 2009 of unnecessary expenditures that occurred due to this condition.

Prior Year Status: Noncompliance with maintenance of fixed assets was reported as a finding in the fiscal years 2006-2008 single audits.

Recommendation: We recommend that the State strengthen internal controls to ensure that periodic reviews are performed to ensure that asset maintenance activities are documented and monitored.

Auditee Response and Corrective Action: We agree with the finding and recommendation. In fiscal 2009 management revalued its infrastructure and building assets and performed a physical inventory to properly reflect all of Chuuk State's fixed assets on its fixed asset register. Departments receiving sector funding will be instructed to maintain equipment and vehicle files to ensure full compliance with Article VI, 1, f (4) of the Fiscal Procedures Agreement, including adequate maintenance.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2009

Finding No. 2009-03
Area: Land Leases Payable

Criteria: A functioning system of internal control requires that subsidiary ledgers be supported by underlying supporting documentation such as vendor invoices, contracts, agreements, etc.

Condition: For 37 of 64 land leases payable tested, no supporting documentation such as an executed lease agreement was available for inspection.

Cause: The cause of this condition is that the management is still searching for the documentation.

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

Recommendation: The State should set a timetable and obtain technical assistance to assist in resolution of the abovementioned matters.

Auditee Response and Correction Action: The sample of 64 was for land *acquisition* contracts, not land *lease* contracts. By the end of audit field work there were only 2 of the 64 land acquisition contracts still missing. Throughout fiscal year 2009 and now in fiscal year 2010, Chuuk DAS management has been obtaining and making an electronic archive of heretofore missing land acquisition contracts. Temporary contract workers have been hired to assist with this task. Since all the contracts that have been obtained, and related payments, substantiate the balances carried on the State's FY-09 fixed asset register and balance sheet, we feel the balances included therein accurately reflect the State's financial position with respect to land acquisitions. We will continue to track down and verify with State records copies of the remaining 20 contracts missing from the entire population of 100+ land parcels acquired.

At this time, Chuuk land lease payable liability cannot be substantiated. We agree with the recommendation that assistance needs to be obtained to sort out the liability. Complicating factors in determining the State's Land leases payables are Municipal transactions that have not been recorded in the State's records, lack of contract documents because of the fire at land offices in 2002, the delinquent status of most leases, and an unknown number of existing leases and settlement agreements. Chuuk DAS now has the temporary staff available to undertake this project and work for completion before the end of fiscal year 2010.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2009

Finding No. 2009-04
Area: Land Acquisitions

Criteria: The State should be able to support the carrying value of land acquired and should be able to determine amounts that it owes for past due rent and for future scheduled rent commitments.

Condition: The Department of Administrative Services (DAS) assumed the responsibility in fiscal year 2009 for building the detail of land acquisitions and of the status of leases in order to support balances contained in the financial statements. DAS has made good strides in compiling this data but certain land acquisition agreements and various leases have not been locatable and therefore, this effort is not yet completed.

Cause: The cause of this condition is the fire that destroyed the prior Land Management office and the manner in which airport land acquisition agreements have not been controlled.

Effect: The effect of this condition is that the State's financial statements are not yet presented in accordance with accounting principles generally accepted in the United States of America.

Recommendation: We recommend that DAS continue in its efforts to build this information and we are pleased with the current levels of improvement that have been demonstrated.

Auditee Response and Corrective Action: We agree with the finding and recommendation. DAS now has two temporary staff working to obtain copies of remaining land acquisition and lease contracts and its goal is to have this project completed by September 30, 2010. These will be used to adjust its liabilities for land transactions.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2009

Finding No. 2009-05
Area: Outstanding Checks

Criteria: Outstanding checks per bank reconciliations should be subject to review to ensure that the items continue to represent outstanding items.

Condition: The State is currently assessing its outstanding checks and this matter has not yet been fully completed.

Cause: There are substantial numbers of outstanding checks and while this assessment is ongoing, it is not expected to be completed until fiscal year 2010.

Effect: The effect of this matter is not currently expected to have a material impact on the financial statements.

Recommendation: We recommend that the State continue its assessment and that such be concluded in 2010.

Auditee Response and Correction Action Plan: We agree with the finding and recommendation. All outstanding checks will be verified by the end of fiscal 2010 and a determination made which are valid and which can be written off.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Resolution of Prior Years' Findings and Questioned Costs
Year Ended September 30, 2009

For the year ended September 30, 2009, the following questioned costs were noted and prior questioned costs resolved:

	Questioned Costs Set Forth in Prior Audit Report <u>2008</u>	Questioned Costs Resolved During Fiscal Year <u>2009</u>	Unresolved Questioned Costs at <u>September 30, 2009</u>
Unresolved Questioned Costs FY 03	\$ 122,029	\$ -	\$ 122,029
Unresolved Questioned Costs FY 04	47,999	(38,546) ⁽³⁾	9,453
Unresolved Questioned Costs FY 06	958,987	(958,987) ⁽¹⁾	-
Unresolved Questioned Costs FY 07	915,802	(3,084) ⁽²⁾	912,718
Unresolved Questioned Costs FY 08	<u>11,519</u>	<u>-</u>	<u>11,519</u>
	<u>\$ 2,056,336</u>	<u>\$ (1,000,617)</u>	1,055,719
Questioned Costs FY 09			<u>-</u>
			<u>\$ 1,055,719</u>

(1) During the fiscal year ended September 30, 2009, certain questioned costs, aggregating \$958,987, were resolved by the FSM National Government.

(2) During the fiscal year ended September 30, 2009, the State refunded \$3,084 to the grantor agency.

(3) Per U.S. Department of Education resolution letter.