

**POHNPEI STATE HOUSING AUTHORITY  
(A COMPONENT UNIT OF THE STATE OF POHNPEI)**

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**FINANCIAL STATEMENTS  
AND INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2009 AND 2008**

## **INDEPENDENT AUDITORS' REPORT**

Board of Directors  
Pohnpei State Housing Authority:

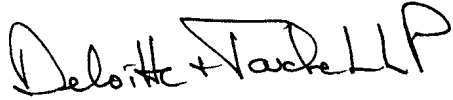
We have audited the accompanying statements of net assets of the Pohnpei State Housing Authority (the Authority), a component unit of the State of Pohnpei, as of September 30, 2009 and 2008 and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Pohnpei State Housing Authority as of September 30, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended in conformity with the accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 6 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Authority's management. 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 January 6, 2010, on our consideration of the Authority'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 read in conjunction with this report in considering the results of our audit.

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

January 6, 2010

**POHNPEI STATE HOUSING AUTHORITY  
(A COMPONENT UNIT OF THE STATE OF POHNPEI)**

Management's Discussion and Analysis  
September 30, 2009 and 2008

Our discussion and analysis of the Pohnpei State Housing Authority's financial performance provides an overview of the Authority's financial activities for the fiscal year ended September 30, 2009. Please read it in conjunction with the Authority's financial statements, which follows this section.

Financial Highlights

- For fiscal year ended September 30, 2009, the Authority's total operating revenues decreased by \$4,041 or 2% from prior year.
- During the year, the Authority's total expenses decreased by \$45,113 or 27% from prior year.
- During the year, the Authority recorded a net recovery of loan losses in the amount of \$1,053,136.
- For fiscal year 2009, the Authority collected an aggregate amount of \$166,665 representing actual interest paid by customers on loans.
- During the year, a board resolution was made for the Authority to pay from the Escrow Account the accelerated amounts due to USDA Rural Development. There were payments made to USDA in a total amount of \$562,765. This caused an increase in the liability to the primary government.

Overview of the Financial Statements

The financial statements presented herein include all of the activities of the Authority. Included in this report are the statement of net assets and the statement of revenues, expenses, and changes in net assets. These financial statements present the complete financial picture of the Authority from the economic measurement focus substantially using the accrual basis of accounting. It can be read from these statements whether the Authority is solvent, liquid, stable or profitable.

The Authority operates on an annual budget appropriated by the Legislature, which is accounted for by the Pohnpei State Department of Treasury.

Financial Analysis

Net Assets:

The statement of net assets presents the financial position or condition of the Authority and it shows the information on all of the authority's assets and liabilities, with the difference between the two reported as net assets. This financial statement communicates the lending ability of the Authority through the turn over of its receivables. The passage of time and/or increases or decreases in net assets may serve as a usual indicator whether the financial position of the Authority is improving or deteriorating.

**POHNPEI STATE HOUSING AUTHORITY  
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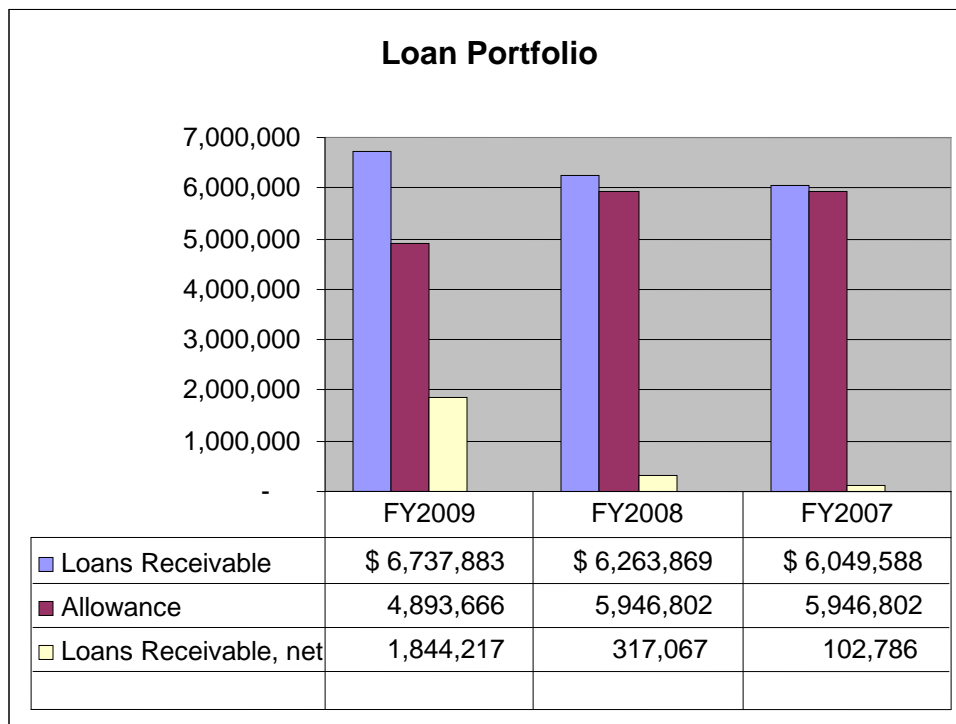
Management's Discussion and Analysis  
September 30, 2009 and 2008

The following table summarizes the changes in net assets for FY2009, FY2008 and FY2007.

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Current assets	\$ 2,148,453	\$ 366,867	\$ 242,510
Capital assets, net	<u>9,203</u>	<u>10,381</u>	<u>11,216</u>
Total assets	\$ <u>2,157,656</u>	\$ <u>377,248</u>	\$ <u>253,726</u>
Current liabilities	\$ <u>593,309</u>	\$ <u>31,481</u>	\$ <u>13,986</u>
Net assets:			
Invested in capital assets	9,203	10,381	11,216
Restricted	<u>1,555,144</u>	<u>335,386</u>	<u>228,524</u>
Total net assets	<u>1,564,347</u>	<u>345,767</u>	<u>239,740</u>
Total liabilities and net assets	\$ <u>2,157,656</u>	\$ <u>377,248</u>	\$ <u>253,726</u>

Total net assets increased by \$1,218,580 or 352% during fiscal year 2009 compared to prior year. Assets, other than capital, increased by \$1,781,586 or 486% while capital assets decreased by \$1,178 or 11% and total liabilities increased by \$561,828 or 1,785%. Liabilities increased primarily due to the aforementioned liabilities due to the Primary Government arising from the USDA Rural Development escrow account transaction.

Following is a graphical presentation showing the 3-year trend in the loan portfolio of PSHA:



**POHNPEI STATE HOUSING AUTHORITY**  
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Management's Discussion and Analysis  
September 30, 2009 and 2008

Changes in Net Assets:

The statement of revenues, expenses, and changes in net assets shows the results of operation of the Authority. It reports the revenues earned and expenses incurred and it indicates the effect on the net assets of the Authority.

For the year ended September 30, 2009, net assets of the Authority changed as follows with comparison from prior years:

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Operating revenues:			
Interest and fees on loans	\$ 169,675	\$ 160,382	\$ 147,971
Other	<u>4,679</u>	<u>18,013</u>	<u>1,533</u>
	<u>174,354</u>	<u>178,395</u>	<u>149,504</u>
Net recovery of loan losses	1,053,136	-	-
Provision for loan losses	<u>-</u>	<u>-</u>	<u>(1,959,809)</u>
Operating expenses:			
Salaries	93,876	96,395	94,029
Utilities	4,950	5,799	6,149
Depreciation	4,385	5,467	4,906
Communication	3,960	2,248	1,172
Repairs and maintenance	2,110	2,557	4,182
Supplies and materials	2,092	2,884	3,419
Contractual services	2,060	39,324	33,152
Bad debts	490	5,043	109,953
Transportation and travel	-	2,308	8,632
Miscellaneous and others	<u>10,676</u>	<u>7,687</u>	<u>6,519</u>
Total operating expenses	<u>124,599</u>	<u>169,712</u>	<u>272,113</u>
Operating income (loss)	1,102,891	8,683	(2,082,418)
Nonoperating revenues:			
Operating subsidy from primary government	<u>115,689</u>	<u>97,344</u>	<u>93,231</u>
Change in net assets	\$ <u>1,218,580</u>	\$ <u>106,027</u>	\$ <u>(1,989,187)</u>

The result of the Authority's operations for the year ended September 30, 2009 is a favorable variance in the change in net assets of \$1,218,580 from the prior year.

Capital Assets and Debt Administration

Please see note 4 for additional information concerning capital assets. The Authority does not have long-term debt.

**POHNPEI STATE HOUSING AUTHORITY  
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Management's Discussion and Analysis  
September 30, 2009 and 2008

Management's Discussion and Analysis for the year ended September 30, 2008 is set forth in the Authority's report on the audit of financial statements, which is dated May 12, 2009. That Discussion and Analysis explains the major factors impacting the 2008 financial statements and can be viewed at the Office of the Public Auditor's website at [www.fsmpublicauditor.fm](http://www.fsmpublicauditor.fm).

Economic Outlook

The going forward plan of the Authority is to first go after collection at a more aggressive level to reduce loans receivable to an acceptable level before seeking outside funding assistance like a soft loan from banks, domestic or offshore, or seeking such assistance from state or national governments by way of stimulus package. The Authority could not start with funding request without a down to bottom efforts on collection and the financials will be looked at should funding assistance is pursued. This is going to be a process and will take some time to be there at plans. The Authority is also in the process of lending to best customers with shortest loan term and increase of loan fees as well.

Contacting the Authority's Financial Management

This Management's Discussion and Analysis is designed to provide our citizens, taxpayers, customers, creditors, and other interested parties, with a general overview of the Pohnpei State Housing Authority's finances and to demonstrate the Authority's accountability for the appropriations it receives. Questions concerning any of the information provided in this discussion and analysis or requests for additional information should be addressed to the Executive Director, Pohnpei State Housing Authority P.O. Box 1109 Kolonia, Pohnpei, FM 96941, or call (691) 320-4225 or (691) 320-2582.

**POHNPEI STATE HOUSING AUTHORITY**  
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Statements of Net Assets  
September 30, 2009 and 2008

<u>ASSETS</u>	<u>2009</u>	<u>2008</u>
Cash	\$ 255,001	\$ 32,001
Employee advances, net of an allowance for doubtful accounts of \$217,819 in 2009 and \$218,096 in 2008	-	-
Due from primary government	36,032	17,728
Loans receivable, net	1,844,217	317,067
Interest receivable	13,160	-
Prepays	43	71
Property and equipment, net	<u>9,203</u>	<u>10,381</u>
	<u>\$ 2,157,656</u>	<u>\$ 377,248</u>

LIABILITIES AND NET ASSETS

Liabilities:		
Accrued liabilities	\$ 13,576	\$ 31,481
Due to primary government	<u>579,733</u>	<u>-</u>
Total liabilities	<u>593,309</u>	<u>31,481</u>
Commitments and contingencies		
Net assets:		
Invested in capital assets	9,203	10,381
Restricted	<u>1,555,144</u>	<u>335,386</u>
Total net assets	<u>1,564,347</u>	<u>345,767</u>
	<u>\$ 2,157,656</u>	<u>\$ 377,248</u>

See accompanying notes to financial statements.



**POHNPEI STATE HOUSING AUTHORITY**  
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Statements of Revenues, Expenses and Changes in Net Assets  
Years Ended September 30, 2009 and 2008

	2009	2008
Operating revenues:		
Interest and fees on loans	\$ 169,675	\$ 160,382
Other	4,679	18,013
Total operating revenues	174,354	178,395
Net recovery of loan losses	1,053,136	-
Operating expenses:		
Salaries	93,876	96,395
Utilities	4,950	5,799
Depreciation	4,385	5,467
Communication	3,960	2,248
Repairs and maintenance	2,110	2,557
Supplies and materials	2,092	2,884
Contractual services	2,060	39,324
Bad debts	490	5,043
Transportation and travel	-	2,308
Miscellaneous and others	10,676	7,687
Total operating expenses	124,599	169,712
Operating income	1,102,891	8,683
Nonoperating revenues:		
Operating subsidy from primary government	115,689	97,344
Total nonoperating revenues	115,689	97,344
Change in net assets	1,218,580	106,027
Net assets at beginning of year	345,767	239,740
Net assets at end of year	\$ 1,564,347	\$ 345,767

See accompanying notes to financial statements.

**POHNPEI STATE HOUSING AUTHORITY**  
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Statements of Cash Flow  
Years Ended September 30, 2009 and 2008

	2009	2008
Cash flows from operating activities:		
Cash received from customers	\$ 144,804	\$ 182,793
Cash paid to suppliers for goods and services	(45,024)	(62,807)
Cash paid to employees	(93,752)	(100,158)
Net cash provided by operating activities	6,028	19,828
Cash flows from noncapital activities:		
Operating subsidy received from primary government	97,385	107,696
Cash flows from capital and related activities:		
Acquisition of fixed assets	(3,207)	(4,632)
Cash flows from investing activities:		
Loan originations and principal collections, net	122,794	(202,218)
Net change in cash	223,000	(79,326)
Cash at beginning of year	32,001	111,327
Cash at end of year	\$ 255,001	\$ 32,001
Cash flows from operating activities:		
Operating income	\$ 1,102,891	\$ 8,683
Adjustments to reconcile operating income to net cash provided by operating activities:		
Bad debts	490	5,043
Depreciation	4,385	5,467
Net recovery of loan losses	(1,053,136)	-
Decrease (increase) in assets:		
Interest receivable	(13,160)	-
Employee advances	-	(4,797)
Prepays	28	-
Due from primary government, net	(17,565)	-
Increase (decrease) in liabilities:		
Accrued liabilities	(17,905)	5,432
Net cash provided by operating activities	\$ 6,028	\$ 19,828

Summary schedule of non-cash activities:

During the year ended September 30, 2009, the Authority recorded \$581,711 of loans granted under the USDA Rural loan program and recorded a liability due to Pohnpei State, the primary government, in the same amount.

See accompanying notes to financial statements.

**POHNPEI STATE HOUSING AUTHORITY**  
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Notes to Financial Statements  
September 30, 2009 and 2008

(1) Organization and Summary of Significant Accounting Policies

Organization

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

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

The Authority's financial statements are incorporated into the financial statements of the Pohnpei State Government as a component unit.

Basis of Accounting

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America as applicable to governmental entities, specifically proprietary funds. Governmental Accounting Standards Board (GASB) Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting," requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principle Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Authority has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments: Omnibus*, and modified by Statement No. 38, *Certain Financial Statement Note Disclosures*, establishes financial reporting standards for governmental entities which require that management's discussion and analysis of the financial activities be included with the basic financial statements and notes and modifies certain other financial statement disclosure requirements.

To conform to the requirements of GASB Statement 34, retained earnings are presented in the following net asset categories:

- Invested in capital assets; capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- Restricted:
  - Nonexpendable – Net assets subject to externally imposed stipulations that require the Authority to maintain them permanently.

**POHNPEI STATE HOUSING AUTHORITY  
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Notes to Financial Statements  
September 30, 2009 and 2008

(1) Organization and Summary of Significant Accounting Policies, Continued

Basis of Accounting, Continued

- Expendable – Net assets whose use by the Authority is subject to externally imposed stipulations that can be fulfilled by actions of the Authority pursuant to those stipulations or that expire by the passage of time.
- Unrestricted; net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

All of the Authority assets are restricted for loan programs.

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of the fund are included in the statements of net assets. Proprietary fund operating statements present increases and decreases in net assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Authority considers interest income and costs that are directly related to lending operations to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

Net Assets

Net assets represent the residual interest in the Authority's assets after liabilities are deducted and consist of three sections: invested in capital assets, net of related debt; restricted and unrestricted. Net assets classified as invested in capital assets net of debt, include capital assets, restricted and unrestricted, net of accumulated depreciation and reduced by outstanding debt net of debt service reserve. Net assets are reported as restricted when constraints are imposed by third parties or enabling legislation. The Authority's restricted assets are expendable. All other net assets are unrestricted.

Budget

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

**POHNPEI STATE HOUSING AUTHORITY**  
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Notes to Financial Statements  
September 30, 2009 and 2008

(1) Organization and Summary of Significant Accounting Policies, Continued

Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses.

Cash

Custodial credit risk is the risk that in the event of a bank failure, the Authority'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 Authority does not have a deposit policy for custodial credit risk.

For the purposes of the statements of net assets and cash flows, cash is defined as cash in checking accounts, savings accounts and cash on hand. As of September 30, 2009 and 2008, cash was \$255,001 and \$32,001, respectively, which approximated corresponding bank balances maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2009 and 2008, bank deposits were fully FDIC insured.

Property and Equipment

Property and equipment are stated at cost. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the respective assets, which range from three to ten years. The Authority capitalizes all fixed assets, irrespective of value, that have estimated useful lives of more than one year.

Compensated Absences

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

New Accounting Standards

During fiscal year 2009, the Authority 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.

**POHNPEI STATE HOUSING AUTHORITY**  
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Notes to Financial Statements  
September 30, 2009 and 2008

(1) Summary of Significant Accounting Policies

New Accounting Standards, Continued

- 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 Authority.

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 Authority.

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 Authority.

**POHNPEI STATE HOUSING AUTHORITY  
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Notes to Financial Statements  
September 30, 2009 and 2008

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

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 Authority.

(2) Due From Primary Government

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

(3) Loans Receivable

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

The PSHA loans derive from the capital contributions of Compact of Free Association Capital Account Funds - Capital Projects by Pohnpei State to fund the Housing Development Loan Fund. The HPG loans are from a grant extended by the United States Department of Agriculture (USDA) Rural Development through the Housing and Community Facilities Program. Loans are stated at face value, net of an allowance for loan losses. The allowance represents an amount which, in management's judgment, will be adequate to absorb possible losses on existing loans that may become uncollectible. Management's judgment in determining the adequacy of the allowance is based on evaluations of the collectibility of loans. The allowance for loan losses are reported based on certain assumptions pertaining to the Authority's periodic review and evaluation of the loan portfolio, which is subject to change. Due to uncertainties inherent in the estimations and assumptions process, it is at least reasonably possible that changes in the estimates and assumptions in the near term would be material to the financial statements. A summary of loans receivable as of September 30, 2009 and 2008, are presented below:

	<u>2009</u>	<u>2008</u>
Pohnpei State Housing Authority loans	\$ 5,732,972	\$ 5,832,557
HPG loans	423,200	431,312
USDA Rural Development loans	<u>581,711</u>	<u>-</u>
	6,737,883	6,263,869
Less allowance for loan losses	<u>(4,893,666)</u>	<u>(5,946,802)</u>
Loans receivable, net	<u>\$ 1,844,217</u>	<u>\$ 317,067</u>

All loans other than USDA Rural Development, are at fixed rates (substantially 4.5%) and the loan terms range from 3 to 25 years. The USDA Rural Development loans are non-interest bearing.

During the year ended September 30, 2009, the State of Pohnpei transferred to the Authority certain USDA Rural Development loans which the State had guaranteed. The Authority will bear responsibility for collection and returning the collections to Pohnpei State Government.

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

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Notes to Financial Statements  
September 30, 2009 and 2008

(4) Property and Equipment

Capital asset activity for the years ended September 30, 2009 and 2008, was as follows:

	Estimated Useful Life	2009			Balance at September 30, 2009
		Balance at October 1, 2008	Additions	Deletions	
Building	10 years	\$ 26,061	\$ -	\$ -	\$ 26,061
Machinery and equipment	3-5 year	163,335	-	-	163,335
Other equipment	2 years	<u>8,684</u>	<u>515</u>	<u>-</u>	<u>9,199</u>
		198,080	515	-	198,595
Less accumulated depreciation		<u>(187,699)</u>	<u>(4,385)</u>	<u>-</u>	<u>(192,084)</u>
		<u>10,381</u>	<u>(3,870)</u>	<u>-</u>	<u>6,511</u>
Construction in progress		<u>-</u>	<u>2,692</u>	<u>-</u>	<u>2,692</u>
		\$ <u>10,381</u>	\$ <u>(1,178)</u>	\$ <u>-</u>	\$ <u>9,203</u>
2008					
	Estimated Useful Life	Balance at October 1, 2007	Additions	Deletions	Balance at September 30, 2008
Building	10 years	\$ 26,061	\$ -	\$ -	\$ 26,061
Machinery and equipment	3-5 year	160,343	2,992	-	163,335
Other equipment	2 years	<u>7,044</u>	<u>1,640</u>	<u>-</u>	<u>8,684</u>
		193,448	4,632	-	198,080
Less accumulated depreciation		<u>(182,232)</u>	<u>(5,467)</u>	<u>-</u>	<u>(187,699)</u>
		\$ <u>11,216</u>	\$ <u>(835)</u>	\$ <u>-</u>	\$ <u>10,381</u>

(5) Commitments and Contingencies

Loan Commitments

The Authority has loan commitments to borrowers aggregating \$1,032,700 and \$1,099,700 as of September 30, 2009 and 2008. These loan commitments represent the remaining balances of approved loans for borrower housing projects.

Litigation

The Authority is party to two legal proceedings. The Attorney General of the Pohnpei State Government is of the opinion that the probable outcome of such cases existing at September 30, 2009, is not predictable. No provision for any liability has been made in the accompanying financial statements because management believes that no unfavorable outcome is likely to occur.

(6) Risk Management

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



**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**

Board of Directors  
Pohnpei State Housing Authority:

We have audited the financial statements of the Pohnpei State Housing Authority (the Authority), as of and for the year ended September 30, 2009, and have issued our report thereon dated January 6, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority'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 accounting principles generally accepted in the United States of America 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 Responses as items 2009-1 and 2009-2 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 material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

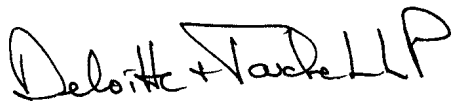
Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose 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 Authority'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*.

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

This report is intended solely for the information and use of the Board of Directors, management, 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.

January 6, 2010

# POHNPEI STATE HOUSING AUTHORITY

## Schedule of Findings and Responses Year Ended September 30, 2009

### **Finding 2009-1: Receipts**

Criteria: All cash receipts should be banked in a timely manner.

Condition: We obtained a schedule of employee advances and noted that there are additional advances in the total amount of \$489 to an employee from loan collections, which were initially recorded as deposits in transit in fiscal year 2008. Furthermore, the advances have not been paid back to the Authority.

Cause: The cause of this condition is internal control weakness over the cash receipts cycle.

Effect: The effect of this condition is potential misappropriation of cash.

Recommendation: We recommend that all cash receipts be banked in a timely manner and should not be advanced to employees.

Prior Year Status: Lack of cash receipts being banked in a timely manner was reported as a finding in the audit of the Authority for fiscal year 2008.

Auditee Response and Corrective Action Plan: Again, this is something of the past and AG office needs and must do something about this. This is already one year pending and appearing again on audit.

I wish something could come out of AG office before next audit. Otherwise, same finding will remain popping out. Per current control, this weakness is under control from repeating itself.

## POHNPEI STATE HOUSING AUTHORITY

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2009

### **Finding 2009-2: Employee Advances**

Criteria: Policies and procedures should be in place to promote timely collection of employee advances.

Condition: Employee advances are not being paid back per payment schedule, and \$217,819 still remains uncollected at year end.

Cause: Set procedures are not in place to monitor and enforce collection of employee advances.

Effect: Excessively aged employee advance balances increase the likelihood of large balances becoming uncollectible.

Recommendation: We recommend that management actively pursue collection of employee advances.

Prior Year Status: Lack of timely collection of employee advances was reported as a finding in the audit of the Authority for fiscal year 2008.

Auditee Response and Corrective Action Plan: I responded to this on last audit. This was submitted to AG office after last audit and still pending until now for investigation and prosecution. Per follow up, pending with Pohnpei State Police detective and white collar crime task force. Beyond me, how much longer this will take to be solved.

Current internal control on financial handling of PSHA would not allow weakness of this sort/type.

I seek AG's handling hoping for setting precedent and/or cautionary measures. However, things are slower than expected.

**POHNPEI STATE HOUSING AUTHORITY**

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

Questioned Costs

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

	Questioned Costs Set Forth in 2008 Audit <u>Report</u>	Questioned Costs Resolved in Fiscal Year <u>2009</u>	Questioned Costs at <u>September 30, 2009</u>
	\$ 18,424	\$ 18,424*	\$ -
Questioned Costs per the 2009 Audit Report	-	-	<u>-</u>
			<u>\$ -</u>

\* The questioned costs pertain to fiscal year 1999. The Authority elected to apply the two-year rule in fiscal year 2009 to resolve the questioned costs.

Prior Year Findings

The status of unresolved prior year findings is disclosed within the Schedule of Findings and Responses section (pages 18 and 19) of this report.