

**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, 2010

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

YEAR ENDED SEPTEMBER 30, 2010

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**FINANCIAL STATEMENTS
YEAR ENDED SEPTEMBER 30, 2010**

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**STATE OF CHUUK
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**INDEPENDENT AUDITORS' REPORT,
FINANCIAL STATEMENTS
AND ADDITIONAL INFORMATION**

YEAR ENDED SEPTEMBER 30, 2010

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 and for the year ended September 30, 2010, 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 opinions on these financial statements based on our audit.

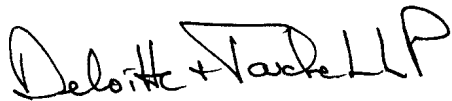
Except as discussed in the following paragraph, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United 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.

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.

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 preceding paragraph, such financial statements, as set forth in Section II of the foregoing table of contents, present fairly, in all material respects, the respective financial position of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk as of September 30, 2010, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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 22, 2011, 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.

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

June 22, 2011

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2010

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, 2010. We encourage readers to consider this information in conjunction with Chuuk State's financial statements, which follow. Fiscal year 2009 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, 2010, Chuuk State's total net assets decreased by \$5.6 million (or 12.2%) from \$45.9 million in the prior year to \$40.3 million. This decrease was primarily the result of Chuuk State assuming the liability of the Asian Development Bank (ADB) Water Supply Loan from the Chuuk Public Utilities Corporation (CPUC) of \$3.6 million and an increase in liabilities resulting from the pass through by the national government of foreign exchange losses on other ADB loans of \$1.2 million.
- During fiscal year 2010, Chuuk State's revenues of \$34.02 million increased from \$31.18 million (up 9.1%) in fiscal year 2009. The increase was attributable to increased revenue sharing proceeds, sales taxes and operating grants. Expenses in fiscal year 2010 of \$36.06 million increased \$4.36 million (or 13.77%) from \$31.70 million in fiscal year 2009. The increase in expenses reflects an increase in education, health and other sector outlays.
- The General Fund deficit decreased \$0.1 million in fiscal year 2010, decreasing from \$8.78 million in the prior year to \$8.68 million. The State's robust general operating revenues reflected a small surplus even after the repayment of ADB principal and interest (\$0.365 million).

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 an 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.

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FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2010

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 State 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 financial 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 Compact Trust Fund.

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 2010, Chuuk State's assets exceeded liabilities by \$40.3 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, 2010, with comparable balances for fiscal year 2009, discloses this relationship.

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Management's Discussion and Analysis
September 30, 2010

	<u>2010</u>	<u>2009</u>
Current and other non-capital assets	\$ 21,080,028	\$ 21,536,392
Capital assets	<u>48,427,808</u>	<u>49,057,775</u>
Total Assets	<u>69,507,836</u>	<u>70,594,167</u>
Long-term liabilities	14,193,647	9,800,192
Other liabilities	<u>15,004,799</u>	<u>14,889,545</u>
Total Liabilities	<u>29,198,446</u>	<u>24,689,737</u>
Net Assets		
Invested in capital assets net of related debt	48,427,808	49,057,775
Restricted	19,598,963	17,875,849
Unrestricted	<u>(27,717,381)</u>	<u>(21,029,194)</u>
Total Net Assets	\$ <u>40,309,390</u>	\$ <u>45,904,430</u>

At the end of fiscal year 2010, Chuuk State's unrestricted assets showed a deficit of \$27.72 million, an increase of \$6.69 million (or 32%). 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. The increase in the 2010 deficit reflects Chuuk State's assumption of a liability for the ADB water supply loan and for increases in long-term loan liabilities as the result of foreign exchange adjustments in SDR amounts of its other ADB loans. Chuuk State will include these amounts in future years' budgets as funding permits.

Net assets decreased \$5.6 million (or 12.2 %) from the prior year. Key elements of the increase and the differences from the prior year are shown in the following schedule:

	<u>2010</u>	<u>2009</u>
Revenues:		
Program Revenues:		
Charges for services	\$ 1,322,279	\$ 1,124,796
Operating grants and contributions	26,263,981	25,864,611
Capital grants and contributions	275,097	-
General Revenues:		
Taxes	5,582,302	4,303,023
Unrestricted investment earnings (losses)	239,016	(122,608)
Other	<u>338,794</u>	<u>5,518</u>
Total revenues	<u>34,021,469</u>	<u>31,175,340</u>

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Management's Discussion and Analysis
September 30, 2010

Expenses:

General government	3,476,244	4,972,322
Health services	9,600,404	7,994,775
Education	14,103,683	12,654,204
Economic development	855,231	434,446
Public safety	1,016,070	848,644
Public works and transportation	2,289,596	2,189,448
Community affairs	13,168	17,211
Boards and commissions	1,710,722	1,591,385
Judiciary	376,633	374,532
Payments to component units	259,454	278,519
Municipal affairs	914,648	271,948
Other	1,366,208	-
Unallocated Interest	<u>80,013</u>	<u>70,470</u>
Total expenses	<u>36,062,074</u>	<u>31,697,904</u>

Special Items:

Forgiveness of Component Unit Debt	<u>3,554,435</u>	<u>-</u>
Total special items	<u>3,554,435</u>	<u>-</u>
Change in net assets	(5,595,040)	(522,564)
Net assets at the beginning of the year	45,904,430	60,656,420
Prior period adjustment	<u>-</u>	<u>(14,229,426)</u>
Net assets at the end of the year	\$ <u>40,309,390</u>	\$ <u>45,904,430</u>

The detail indicates the increase in revenue and expenses in fiscal year 2010, and the significant reduction of net assets primarily from the one-time assumption of the CPUC component unit loan debt.

Revenues of \$34.02 million increased \$2.84 million (or 9.1%) from the prior year's \$31.18 million. The key elements of the increase were increased revenue sharing as the result of greater FSM revenue tax collections, increased local tax collections, and positive investment earnings. Notably, revenue sharing proceeds of \$3.44 million in fiscal year 2010 were up \$.78 million (or 29%) from fiscal year 2009's total of \$2.66 million. Similarly, local revenue collections of \$3.46 million in fiscal 2010 increased \$.69 million (or 25%) from fiscal year 2009's total of \$2.77 million. Both local revenue and revenue sharing proceeds benefited from the increased construction activity in Weno. Additionally, the increase in the local sales tax rate from 5% to 6% in July 2010 also contributed to increased local tax collections.

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

SOURCE OF REVENUE	<u>2010</u>	<u>2009</u>
Compact funding	73.9%	82.0%
Investments	4.0%	(0.1)%
Revenue sharing	10.1%	8.5%
Federal and other grants	0.8%	0.7%
Taxes and fees	10.2%	8.9%
Other	<u>1.0%</u>	<u>0.0%</u>
TOTAL	<u>100.0%</u>	<u>100.0%</u>

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Management's Discussion and Analysis
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Although the increases in both revenue shares passed through to the State and local tax and fee collections reduce the dependency on Compact funding, the predominance of sector funding as 74% of total revenue indicates the importance of sector grant utilization to Chuuk State's overall fiscal picture.

Expenses increased \$4.32 million (up 13.8%), from \$31.7 million in the prior fiscal year to \$36.02 million in fiscal year 2010. Significant increases in fiscal year 2010 were the result of greater utilization of health and education sector grants (up \$1.6 million and \$1.5 million, respectively), increased municipal payments (up \$0.64 million) and new outlays to the infrastructure maintenance fund (\$0.37 million).

The primary reason for the decline in net assets in fiscal year 2010 was the increase in liabilities related to Asian Development Bank loans. In fiscal year 2010, the State entered into an Memorandum of Understanding (MOU) with the Chuuk Public Utility Corporation (CPUC), under the broad auspices of the *Capitalization, Recovery, and Institutional Strengthening Program* (CRISP) report, a multi-lateral institutional agreement to shore-up the CPUC. The MOU established mutual debt forgiveness between CPUC and Chuuk State; the chief feature of which was the permanent assumption by the State from CPUC of the liability for the ADB Water Supply Loan. As of September 30, 2010, the liability assumed by the State was \$3.554 million. Additionally, the FSM national government passed through various foreign exchange losses to the State in the aggregate of \$1.232 million; the net effect of which is to increase Chuuk State's long-term liabilities.

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 2010, Chuuk State's governmental funds reported a combined fund balance of \$6.89 million, which represents a \$0.45 million decrease (or 6.07%) from the \$7.33 million fund balance recorded at the end of fiscal 2009. This decrease is attributable to the excess of Compact sector expenditures over revenues. Of this total combined fund balance, \$26.21 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 (\$8.09 million); 2) to liquidate contracts and purchase orders of the prior period (\$8.83 million) or; 3) to fund specific general fund-related activities (\$9.3 million). These reserved fund balances are off-set by a combined deficit of \$14.6 million, generally unchanged from 2009.

The following table highlights the major expenditure categories:

<u>2010 Expenditure Category</u>	<u>Total ('000's)</u>	<u>% of Total</u>
Personnel	\$ 17,058	49.49%
Travel and training	1,564	4.54%
Scholarships	1,172	3.40%
Books and library materials	1,190	3.45%
Contractual	3,953	11.47%
Vehicles and equipment	1,942	5.63%
Office supplies	1,119	3.25%
ADB loan currency losses	1,232	3.57%
All other categories	<u>5,237</u>	<u>15.19%</u>
Total	\$ <u>34,467</u>	<u>100.00%</u>

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Management's Discussion and Analysis
September 30, 2010

GENERAL FUND BUDGETARY HIGHLIGHTS

In fiscal year 2010, actual revenues of \$7.38 million exceeded budgeted revenues of \$5.73 million by \$1.65 million. Actual expenditures of \$7.45 million were greater than budgetary appropriations of \$5.86 million by \$1.59 million, resulting in an overall deficiency of revenues under expenditures of \$0.07 million. When combined with the transfer out to the infrastructure maintenance fund (\$0.367 million), the net change in unreserved fund deficit on a budgetary basis was a negative \$0.437 million. In accord with the principles of budgetary accounting, the deficit includes encumbrances for which the liquidation has not occurred; without encumbrances there was a small (\$0.1 million) positive change in the general fund deficit.

Chuuk State retains a balanced operating budget but debt financing activities of the State that are not budgeted have negative impacts on overall State operations. In fiscal year 2010, principal and debt service charges on ADB loans of \$0.365 million contributed to the increase in the general fund deficit. Additionally, in fiscal year 2010, the State recorded an expenditure for a U.S. Department of the Interior refund demand of \$0.23 million for which the Chuuk State Legislature did not make an appropriation.

CAPITAL ASSET AND DEBT ADMINISTRATION

Chuuk State's investment in capital assets for the primary government as of September 30, 2010, amounted to \$115.77 million, net of accumulated depreciation of \$67.34 million, leaving a net book value of \$48.43 million. This represents a net decrease of \$0.63 million (or 1%) from fiscal year 2009. Chuuk State recorded nominal additions of \$2.65 million in 2010 primarily from contributions of various equipment from the FSM national government, but current year depreciation charges of \$3.28 million resulted in the net decrease. The table below summarizes Chuuk State's capital assets:

	<u>2010</u>	<u>2009</u>
Land	\$ 17,721,622	\$ 17,686,782
Airport Facilities	12,579,949	13,532,634
Buildings	4,362,601	4,478,405
Seaport Facilities	7,955,163	8,618,093
Vehicles/ Equipment	2,841,410	785,778
Infrastructure	<u>2,967,063</u>	<u>3,956,083</u>
	\$ <u>48,427,808</u>	\$ <u>49,057,775</u>

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

Long-Term Debt

The following schedule shows Chuuk State's non-current liabilities for fiscal year 2010 and comparable amounts for fiscal year 2009.

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Management's Discussion and Analysis
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	<u>2010</u>	<u>2009</u>
ADB Water Supply Loan (1459)	\$ 4,015,325	\$ -
ADB Early Retirement Loan (1520)	5,735,235	5,075,633
ADB Private Sector Reform Program Loan (1873)	717,591	739,840
ADB Private Sector Reform Program Loan (1874)	1,307,601	1,336,896
ADB Basic Social Services Program Loan (1816)	<u>1,146,436</u>	<u>1,268,115</u>
	\$ <u>12,922,188</u>	\$ <u>8,420,484</u>

Long-term debt increased by \$4.5 million (or 53%) in fiscal year 2010 as the net result of (i) forgiveness of CPUC's debt of the water supply loan of \$3.55 million and related foreign exchange adjustments that increased the loan amount by \$0.46 million, (ii) foreign exchange adjustments on the ADB Early Retirement Loan that increased the liability by \$0.77 million, and (iii) principal and interest payments totaling \$0.285 million.

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

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

In fiscal year 2011, Chuuk State continues to have favorable general fund budget variances, with local revenue collections approximately 15% higher year-to-date than comparable periods in fiscal year 2010. General fund appropriations and related expenditures, however, have kept pace with the increased revenue and continue to pose challenges to balanced budgets. Although still rationalizing its budgetary operations in fiscal 2011, required transfer payments to the debt relief fund in fiscal 2011 have had to be postponed. The State still has a large debt overhang to vendors and landowners and any renewed initiatives to pay these old debts will require either the sale of more assets or tighter fiscal discipline. Moreover, although on schedule in the current year with its local matching to the infrastructure maintenance fund (IMF), Chuuk State has \$2 million in arrears from fiscal years 2004-2009 for its IMF transfers for fiscal years 2004-2009 when it made no IMF contributions. It is uncertain how this obligation will be met.

Another recurring problem the State is facing is underutilization of its sector grant funds. At March 31, 2011, the 2010 sector grants expired with approximately \$4.41 million (or 16%) of the \$27.54 million budget unexpended. Although these funds are available to Chuuk State in future periods, the poor planning and management of procurement functions has hampered accomplishment of program objectives and created negative perceptions with the grantor agency and other third parties.

Finally, with 74% of Chuuk State's revenues coming from U.S. Department of the Interior sector grants, the heightened fiscal problems confronting the United States may have negative spillover effects on future sector allotments and grant management issues. In such an environment, Chuuk State's intended course of action will be a renewal of financial reform initiatives, fiscal prudence and improved grant management practices.

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 849, Weno, Chuuk FM 96942

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Net Assets
September 30, 2010

	Primary Government	Component Units
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ 1,942,449	\$ 446,835
Time certificates of deposit	-	252,677
Equity interest in internal investment pool	1,837,273	-
Receivables, net of allowance for uncollectibles	1,985,844	709,650
Inventories	-	129,667
Prepayments	1,358,848	743
Total current assets	7,124,414	1,539,572
Noncurrent assets:		
Restricted assets:		
Investments	11,905,614	-
Investments	2,050,000	-
Capital assets, net of accumulated depreciation	48,427,808	1,485,509
Total noncurrent assets	62,383,422	1,485,509
Total assets	\$ 69,507,836	\$ 3,025,081
<u>LIABILITIES</u>		
Current liabilities:		
Current portion of long-term debt	\$ 362,401	\$ 808,918
Note payable	561,987	-
Accrued interest payable	175,576	-
Accounts payable	4,372,780	116,392
Land acquisition payable	8,783,687	-
Compensated absences payable	450,000	-
Other liabilities and accruals	298,368	1,611,227
Deferred revenues	-	17,693
Total current liabilities	15,004,799	2,554,230
Noncurrent liabilities:		
Noncurrent portion of long-term obligations	12,559,787	75,584
Compensated absences payable, net of current portion	1,633,860	-
Total noncurrent liabilities	14,193,647	75,584
Total liabilities	29,198,446	2,629,814
<u>NET ASSETS</u>		
Invested in capital assets, net of related debt	48,427,808	676,592
Restricted for:		
Nonexpendable:		
Future operations	8,088,435	848,164
Expendable:		
Compact related	6,206,284	-
Debt service	3,947,415	-
Other purposes	1,356,829	-
Unrestricted	(27,717,381)	(1,129,489)
Total net assets	40,309,390	395,267
Total liabilities and net assets	\$ 69,507,836	\$ 3,025,081

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Activities
Year Ended September 30, 2010

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	\$ 3,476,244	\$ 594,341	\$ 1,376,927	\$ -	\$ (1,504,976)	\$ -
Health services	9,600,404	106,366	9,430,125	-	(63,913)	-
Education	14,103,683	-	13,067,980	-	(1,035,703)	-
Economic development	855,231	-	1,250,885	-	395,654	-
Public safety	1,016,070	68,850	174,037	-	(773,183)	-
Public works and transportation	2,289,596	538,742	-	275,097	(1,475,757)	-
Community affairs	13,168	-	-	-	(13,168)	-
Boards and commissions	1,710,722	-	-	-	(1,710,722)	-
Judiciary	376,633	13,980	-	-	(362,653)	-
Payments to component units	259,454	-	-	-	(259,454)	-
Municipal affairs	914,648	-	-	-	(914,648)	-
Future operations	-	-	964,027	-	964,027	-
Other	1,366,208	-	-	-	(1,366,208)	-
Unallocated interest	80,013	-	-	-	(80,013)	-
Total primary government	\$ 36,062,074	\$ 1,322,279	\$ 26,263,981	\$ 275,097	(8,200,717)	-
Component units:						
Chuuk State Health Care Plan	\$ 806,398	\$ 993,047	\$ -	\$ -	-	186,649
Chuuk Public Utility Corporation	4,284,215	3,296,158	-	-	-	(988,057)
Chuuk State Housing Authority	88,302	74,394	-	-	-	(13,908)
Total component units	\$ 5,178,915	\$ 4,363,599	\$ -	\$ -	-	(815,316)
General revenues:						
Taxes:						
Revenue sharing					3,444,182	-
State taxes					2,138,120	-
Unrestricted investment income					239,016	-
Other					338,794	1,805,596
Special item - forgiveness of debt					(3,554,435)	3,554,435
Total general revenues and special items					2,605,677	5,360,031
Change in net assets					(5,595,040)	4,544,715
Net assets at the beginning of the year					45,904,430	(4,149,448)
Net assets at the end of the year					\$ 40,309,390	\$ 395,267

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Balance Sheet
Governmental Funds
September 30, 2010

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
ASSETS					
Cash and cash equivalents	\$ 1,942,449	\$ -	\$ -	\$ -	\$ 1,942,449
Equity interest in internal investment pool	1,837,273	-	-	-	1,837,273
Investments	-	2,050,000	-	-	2,050,000
Receivables, net	1,137,321	848,523	-	-	1,985,844
Prepayments	262,576	1,096,272	-	-	1,358,848
Due from other funds	598,690	4,702,752	-	1,216,227	6,517,669
Restricted assets:					
Investments	3,817,179	-	8,088,435	-	11,905,614
Total assets	<u>\$ 9,595,488</u>	<u>\$ 8,697,547</u>	<u>\$ 8,088,435</u>	<u>\$ 1,216,227</u>	<u>\$ 27,597,697</u>
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accounts payable	\$ 2,539,653	\$ 1,833,127	\$ -	\$ -	\$ 4,372,780
Accrued liabilities	298,368	-	-	-	298,368
Land acquisition payable	8,783,687	-	-	-	8,783,687
Note payable	561,987	-	-	-	561,987
Accrued interest payable	175,576	-	-	-	175,576
Due to other funds	5,918,979	598,690	-	-	6,517,669
Total liabilities	<u>18,278,250</u>	<u>2,431,817</u>	<u>-</u>	<u>-</u>	<u>20,710,067</u>
Fund balances (deficits):					
Reserved for:					
Related assets	-	2,050,000	8,088,435	1,131,480	11,269,915
Encumbrances	537,472	8,295,168	-	-	8,832,640
Continuing appropriations	2,285,249	-	-	-	2,285,249
Debt service	3,817,179	-	-	-	3,817,179
Unreserved:					
General fund	(15,322,662)	-	-	-	(15,322,662)
Special revenue funds	-	(4,079,438)	-	84,747	(3,994,691)
Total fund balances (deficits)	<u>(8,682,762)</u>	<u>6,265,730</u>	<u>8,088,435</u>	<u>1,216,227</u>	<u>6,887,630</u>
Total liabilities and fund balances	<u>\$ 9,595,488</u>	<u>\$ 8,697,547</u>	<u>\$ 8,088,435</u>	<u>\$ 1,216,227</u>	
Amounts reported for governmental activities in the statement of net assets are different because:					
Capital assets used in governmental activities are not financial resources and, therefore, are reported in the funds 48,427,808					
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:					
				(12,922,188)	
				(2,083,860)	
					<u>(15,006,048)</u>
Net assets of governmental activities					<u>\$ 40,309,390</u>

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, 2010

	General	Special Revenue	Permanent	Other Governmental Funds	Total
		Grants Assistance	Compact Trust		
Revenues:					
Compact funding	\$ -	\$ 25,135,727	\$ -	\$ -	\$ 25,135,727
Net change in the fair value of investments	239,016	171,500	964,027	-	1,374,543
Federal contributions and other grants	-	97,000	-	170,824	267,824
FSM revenue sharing	3,444,182	-	-	-	3,444,182
State taxes	2,138,120	-	-	-	2,138,120
Fees and charges	1,215,913	-	-	106,366	1,322,279
Other	338,794	-	-	-	338,794
Total revenues	7,376,025	25,404,227	964,027	277,190	34,021,469
Expenditures:					
Current:					
General government	3,346,903	494,999	-	-	3,841,902
Health services	-	9,757,199	-	252,726	10,009,925
Education	106,580	14,183,991	-	-	14,290,571
Economic development	73,743	861,398	-	-	935,141
Public safety	778,311	214,660	-	-	992,971
Public works and transportation	557,115	-	-	65,351	622,466
Community affairs	13,168	-	-	-	13,168
Boards and commissions	200,117	1,510,605	-	-	1,710,722
Judiciary	376,633	-	-	-	376,633
Payments to component units	43,090	216,364	-	-	259,454
Municipal affairs	914,648	-	-	-	914,648
Other	133,857	-	-	-	133,857
Debt service:					
Principal repayment	285,082	-	-	-	285,082
Interest payments	80,013	-	-	-	80,013
Total expenditures	6,909,260	27,239,216	-	318,077	34,466,553
Excess (deficiency) of revenues over (under) expenditures	466,765	(1,834,989)	964,027	(40,887)	(445,084)
Other financing sources (uses):					
Operating transfers in	-	366,466	-	-	366,466
Operating transfers out	(366,466)	-	-	-	(366,466)
Total other financing sources (uses), net	(366,466)	366,466	-	-	-
Net change in fund balances (deficit)	100,299	(1,468,523)	964,027	(40,887)	(445,084)
Fund balances (deficits) at the beginning of the year	(8,783,061)	7,734,253	7,124,408	1,257,114	7,332,714
Fund balances (deficits) at the end of the year	\$ (8,682,762)	\$ 6,265,730	\$ 8,088,435	\$ 1,216,227	\$ 6,887,630

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, 2010

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	\$ (445,084)
<p>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.</p> <p>This is the amount by which depreciation exceeded capital outlays in the current period</p>	
	(629,967)
<p>The net effect of various miscellaneous transactions involving long-term debt is to decrease net assets. For the current year, this amount consists of:</p>	
Forgiveness of debt owed by the Chuuk Public Utilities Corporation.	(3,554,435)
<p>The incurrence 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. For the current year, these amounts consist of:</p>	
Repayment of ADB Loans	285,082
<p>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:</p>	
Change in compensated absences payable	(18,285)
Foreign exchange adjustment in SDR amount for ADB Loans	<u>(1,232,351)</u>
	<u>(1,250,636)</u>
Change in net assets of governmental activities	\$ <u>(5,595,040)</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, 2010**

<u>ASSETS</u>	Chuuk State Health Care Plan	Chuuk Public Utility Corporation	Chuuk State Housing Authority	Total
Current assets:				
Cash and cash equivalents	\$ 412,785	\$ 31,400	\$ 2,650	\$ 446,835
Time certificates of deposit	252,677	-	-	252,677
Receivables, net	155,889	98,516	285,245	539,650
Inventories	-	129,667	-	129,667
Due from primary government	50,000	-	120,000	170,000
Prepayments	743	-	-	743
Total current assets	<u>872,094</u>	<u>259,583</u>	<u>407,895</u>	<u>1,539,572</u>
Noncurrent assets:				
Capital assets, net of accumulated depreciation	<u>26,806</u>	<u>1,373,956</u>	<u>84,747</u>	<u>1,485,509</u>
Total assets	<u>\$ 898,900</u>	<u>\$ 1,633,539</u>	<u>\$ 492,642</u>	<u>\$ 3,025,081</u>
<u>LIABILITIES AND NET ASSETS</u>				
Current liabilities:				
Current portion of long-term debt	\$ -	\$ 808,918	\$ -	\$ 808,918
Accounts payable	20,210	95,764	418	116,392
Accrued liabilities	3,720	1,607,507	-	1,611,227
Deferred income	-	17,693	-	17,693
Total current liabilities	<u>23,930</u>	<u>2,529,882</u>	<u>418</u>	<u>2,554,230</u>
Noncurrent liabilities:				
Noncurrent portion of long-term debt	<u>-</u>	<u>75,584</u>	<u>-</u>	<u>75,584</u>
Total liabilities	<u>23,930</u>	<u>2,605,466</u>	<u>418</u>	<u>2,629,814</u>
Net assets:				
Invested in capital assets, net of related debt	26,806	565,039	84,747	676,592
Restricted	848,164	-	-	848,164
Unrestricted	<u>-</u>	<u>(1,536,966)</u>	<u>407,477</u>	<u>(1,129,489)</u>
Total net assets	<u>874,970</u>	<u>(971,927)</u>	<u>492,224</u>	<u>395,267</u>
Total liabilities and net assets	<u>\$ 898,900</u>	<u>\$ 1,633,539</u>	<u>\$ 492,642</u>	<u>\$ 3,025,081</u>

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, 2010**

	Chuuk State Health Care Plan	Chuuk Public Utility Corporation	Chuuk State Housing Authority	Total
Operating revenues:				
Charges for services	\$ 989,040	\$ 3,290,094	\$ 74,394	\$ 4,353,528
Other	4,007	6,064	-	10,071
Total operating revenues	<u>993,047</u>	<u>3,296,158</u>	<u>74,394</u>	<u>4,363,599</u>
Operating expenses:				
Cost of services	630,908	2,856,154	-	3,487,062
Depreciation	10,112	634,172	18,384	662,668
Administration and general	165,378	793,889	69,918	1,029,185
Total operating expenses	<u>806,398</u>	<u>4,284,215</u>	<u>88,302</u>	<u>5,178,915</u>
Operating income (loss)	<u>186,649</u>	<u>(988,057)</u>	<u>(13,908)</u>	<u>(815,316)</u>
Nonoperating revenues (expenses):				
Other income	82,403	280,961	120,000	483,364
Interest expense	3,937	(90,441)	-	(86,504)
Gain on transfer of liabilities	-	4,963,171	-	4,963,171
Total nonoperating revenues (expenses), net	<u>86,340</u>	<u>5,153,691</u>	<u>120,000</u>	<u>5,360,031</u>
Net income	<u>272,989</u>	<u>4,165,634</u>	<u>106,092</u>	<u>4,544,715</u>
Net assets at the beginning of the year	<u>601,981</u>	<u>(5,137,561)</u>	<u>386,132</u>	<u>(4,149,448)</u>
Net assets at the end of the year	<u>\$ 874,970</u>	<u>\$ (971,927)</u>	<u>\$ 492,224</u>	<u>\$ 395,267</u>

See accompanying notes to basic financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(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, 2010

(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, 2010

(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, 2010

(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, 2010

(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 \$19,598,963 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, 2010

(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

Government-Wide Financial Statements:

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.

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.

Governmental Fund Financial Statements:

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.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

Governmental Fund Financial Statements, Continued:

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. Federal grants and assistance awards made on the basis of entitlement periods are recorded as revenue when available and entitlement occurs which is generally within 12 months of the end of the current fiscal period. 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.

Component Unit Financial Statements:

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, 2010

(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, 2010

(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 \$3,817,179. Furthermore, investments recorded in the Compact Trust Fund of \$8,088,435 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, 2010

(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, 2010

(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, 2010, 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	-	-	-	1,131,480	1,131,480
Restricted assets:					
Investments	-	-	<u>8,088,435</u>	-	<u>8,088,435</u>
	<u>\$ -</u>	<u>\$ 2,050,000</u>	<u>\$ 8,088,435</u>	<u>\$ 1,131,480</u>	<u>\$ 11,269,915</u>

The continuing appropriations within the General Fund include \$2,285,249 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, 2010

(1) Summary of Significant Accounting Policies, Continued

R. New Accounting Standards

During fiscal year 2010, the State implemented the following pronouncements:

- GASB 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.
- GASB 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.
- GASB 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.
- GASB Statement No. 58, *Accounting and Financial Reporting for Chapter 9 Bankruptcies*, which provides guidance for governments that have petitioned for protection from creditors by filing for bankruptcy under Chapter 9 of the United States Bankruptcy Code, and establishes requirements for recognizing and measuring the effects of the bankruptcy process on assets and liabilities, and for classifying changes in those items and related costs.

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

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 has not evaluated the effect that the implementation of this statement will have on the financial statements of the State.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(1) Summary of Significant Accounting Policies, Continued

R. New Accounting Standards, Continued

In December 2009, GASB issued Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which amends Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and addresses issues related to measurement of OPEB obligations by certain employers participating in agent multiple-employer OPEB plans. The provisions of Statement 57 related to the use and reporting of the alternative measurement method are effective immediately. The provisions related to the frequency and timing of measurements are effective for actuarial valuations first used to report funded status information in OPEB plan financial statements for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In June 2010, GASB issued Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting of certain financial instruments and external investment pools. The provisions of this statement are effective for periods beginning after June 15, 2010. Management has not evaluated the effect that the implementation of this statement will have 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, 2009 from which summarized information was derived.

(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.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(2) Deposits and Investments, Continued

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.

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.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(2) Deposits and Investments, Continued

A. Deposits, Continued

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, 2010, the carrying amount of the primary government's total cash and cash equivalents were \$1,942,449 and the corresponding bank balances were \$4,215,496, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2010, 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, 2010, the carrying amount of the discretely presented component units' total cash and cash equivalents and time certificates of deposit was \$699,512 and the corresponding bank balances were \$650,695, which were maintained in financial institutions subject to FDIC insurance. As of September 30, 2010, bank deposits in the amount of \$496,130 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.

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.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(2) Deposits and Investments, Continued

B. Investments, Continued

As of September 30, 2010, the State's investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	\$ 1,267,887
Other investments:	
Domestic equities	10,442,443
Cash management account	<u>195,284</u>
	\$ <u>11,905,614</u>

As of September 30, 2010, the General Fund has an Automated Cash Management account with the Bank of Hawaii in the amount of \$1,837,273.

As of September 30, 2010, 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.

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, 2010.

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, 2010, 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.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(2) Deposits and Investments, Continued

B. Investments, Continued

As of September 30, 2010, the State's fixed income securities, including their Moody's Investors Service credit ratings, had the following maturities:

Investment Type	Investment Maturities (In Years)					Credit Ratings
	Fair Value	Current	1-5	6-10	Over 10	
U.S. Treasury Notes and Bonds	\$ 303,614	\$ -	\$ 170,861	\$ 69,099	\$ 63,654	Aaa/AAA
U.S. Government Agency Obligations:						
Federal Home Loan Mortgage Corporation	270,955	-	8,025	31,509	231,421	AAA
Government National Mortgage Association	30,017	-	-	-	30,017	AAA
Federal National Mortgage Association	161,384	-	-	15,703	145,681	AAA
Tennessee Valley Authority	12,484	-	-	-	12,484	AAA
Housing Urban Development	21,836	-	21,836	-	-	No rating
Municipal Obligations	7,538	-	-	-	7,538	Aa1
Municipal Obligations	4,476	-	-	-	4,476	Aa2
Corporate Bonds	37,416	-	14,831	-	22,585	Aaa/AAA
Corporate Bonds	15,996	-	-	15,996	-	Aa1/AA+
Corporate Bonds	65,177	21,620	-	25,817	17,740	Aa2/AA
Corporate Bonds	11,334	-	-	11,334	-	Aa3/AA-
Corporate Bonds	49,837	-	-	-	49,837	A1/A+
Corporate Bonds	49,241	-	22,994	26,247	-	A2/A
Corporate Bonds	39,304	-	16,901	-	22,403	A3/A-
Corporate Bonds	117,388	-	81,690	28,338	7,360	Baa1/BBB+
Corporate Bonds	16,025	-	16,025	-	-	Baa2/BBB
Corporate Bonds	53,865	-	43,070	10,795	-	No rating
Grand total	<u>\$1,267,887</u>	<u>\$21,620</u>	<u>\$396,233</u>	<u>\$234,838</u>	<u>\$615,196</u>	

(3) Receivables

Primary Government

Receivables as of September 30, 2010, for the primary government's individual major funds and nonmajor funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	General	Grants Assistance	Total
Receivables:			
General receivables	\$ 46,843	\$ 66,837	\$ 113,680
FSM National Government	<u>1,608,626</u>	<u>781,686</u>	<u>2,390,312</u>
	1,655,469	848,523	2,503,992
Less: allowance for uncollectible Accounts	<u>(518,148)</u>	<u>-</u>	<u>(518,148)</u>
Net receivables	<u>\$1,137,321</u>	<u>\$ 848,523</u>	<u>\$1,985,844</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(3) Receivables, Continued

Discretely Presented Component Units

Chuuk State Health Care Plan

Receivables as of September 30, 2010, for the Chuuk State Health Care Plan in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

General	\$ 202,999
Less: allowance for uncollectible accounts	<u>(47,110)</u>
Net receivables	\$ <u>155,889</u>

Chuuk Public Utilities Corporation

Receivables as of September 30, 2010, for the Chuuk Public Utilities Corporation in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

General	\$ 1,486,465
Other	<u>6,452</u>
	1,492,917
Less: allowance for uncollectible accounts	<u>(1,394,401)</u>
Net receivables	\$ <u>98,516</u>

Chuuk State Housing Authority

Receivables as of September 30, 2010, for the Chuuk State Housing Authority in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

Receivables:	
Loans	\$ 2,182,301
Less: allowance for uncollectible accounts	<u>(1,897,056)</u>
Net receivables	\$ <u>285,245</u>

(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, 2010, are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
Grants Assistance	General	\$ 4,702,752
General	Grants Assistance	598,690
Nonmajor governmental funds	General	<u>1,216,227</u>
		\$ <u>6,517,669</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(4) Interfund Receivables and Payables, Continued

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>1,131,480</u>

(5) Fixed Assets

Capital asset activities of the primary government for the year ended September 30, 2010, are as follows:

	<u>Balance October 1, 2009</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance September 30, 2010</u>
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 17,686,782	\$ 34,840	\$ -	\$ 17,721,622
Capital assets, being depreciated:				
Airport facilities	38,107,415	-	-	38,107,415
Buildings	10,108,617	106,413	-	10,215,030
Seaport facilities	26,517,208	-	-	26,517,208
Vehicles and other equipment	5,869,838	2,505,533	-	8,375,371
Infrastructure	<u>14,835,315</u>	<u>-</u>	<u>-</u>	<u>14,835,315</u>
	<u>95,438,393</u>	<u>2,611,946</u>	<u>-</u>	<u>98,050,339</u>
Less accumulated depreciation for:				
Airport facilities	(24,574,781)	(952,685)	-	(25,527,466)
Buildings	(5,630,212)	(222,217)	-	(5,852,429)
Seaport facilities	(17,899,115)	(662,930)	-	(18,562,045)
Vehicles and other equipment	(5,084,061)	(449,900)	-	(5,533,961)
Infrastructure	<u>(10,879,231)</u>	<u>(989,021)</u>	<u>-</u>	<u>(11,868,252)</u>
	<u>(64,067,400)</u>	<u>(3,276,753)</u>	<u>-</u>	<u>(67,344,153)</u>
	<u>31,370,993</u>	<u>(664,807)</u>	<u>-</u>	<u>30,706,186</u>
	<u>\$ 49,057,775</u>	<u>\$ (629,967)</u>	<u>\$ -</u>	<u>\$ 48,427,808</u>

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

General government	\$ 1,241,561
Health services	210,110
Education	134,853
Public safety	23,099
Public works and transportation	<u>1,667,130</u>
	<u>\$ 3,276,753</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(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, 2010.

(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.

Funds for the repayment of the ADB 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 appropriated funds into the ERS Trust Account. These funds had not been deposited to the Trust Account as of September 30, 2010. As of September 30, 2010, the amount outstanding against this loan was \$5,735,235. Of the required \$5,300,000 identified for future debt service payments, \$3,817,179 is 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 Loan 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. Principal payments shall be made semiannually commencing February 1, 2009, with a maturity date of August 1, 2032. As of September 30, 2010, the balance payable on this loan amounted to \$1,146,436.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(7) Long-Term Obligations, Continued

Primary Government, Continued

Asian Development Bank (ADB) Loans, Continued:

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. 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, 2010, the balances payable on these loans amounted to \$717,591 and \$1,307,601, respectively.

On December 21, 2010, the Chuuk Public Utilities Corporation (CPUC) and the State agreed through memorandum of understanding to offset certain claims and transferred certain debt between CPUC and the State. The transferred debt was the FSM National Government Program Loan with ADB (Loan Number 1459 (SF)), totaling \$3,554,435, for water wells and electric construction purposes, with interest at 1% to 1.5% per annum. Principal payments shall be made semiannually commencing August 1, 2007, with a maturity date of August 1, 2036. The State has elected to record this transaction during the year ended September 30, 2010, which, in essence, represents forgiveness of debt owed by CPUC to the State and, accordingly, has been presented as a special item in the accompanying financial statements. As of September 30, 2010, the balance payable on this loan amounted to \$4,015,325.

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

<u>Year Ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2011	\$ 362,401	\$ 146,286	\$ 508,687
2012	362,401	141,894	504,295
2013	368,955	138,289	507,244
2014	368,955	133,798	502,753
2015	368,955	129,308	498,263
2016-2020	2,558,846	567,866	3,126,712
2021-2025	2,889,434	410,330	3,299,764
2026-2030	2,681,443	251,385	2,932,828
2031-2035	2,419,250	106,635	2,525,885
2036-2039	<u>541,548</u>	<u>9,133</u>	<u>550,681</u>
	<u>\$ 12,922,188</u>	<u>\$ 2,034,924</u>	<u>\$ 14,957,112</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(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. 726,997

\$ 808,918

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>
2011	\$ <u>808,918</u>	\$ <u>283,742</u>	\$ <u>1,092,660</u>

(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, 2010, the following changes occurred in liabilities reported as part of the primary government's long-term liabilities in the statement of net assets:

	<u>Balance October 1, 30, 2009</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2010</u>	<u>Due Within One Year</u>
Loans payable:					
ADB loans:					
Loan 1459	\$ -	\$ 4,015,325	\$ -	\$ 4,015,325	\$ 87,141
Loan 1520	5,075,633	771,461	(111,859)	5,735,235	121,656
Loan 1816	1,268,115	-	(121,679)	1,146,436	52,004
Loan 1873	739,840	-	(22,249)	717,591	46,220
Loan 1874	<u>1,336,896</u>	<u>-</u>	<u>(29,295)</u>	<u>1,307,601</u>	<u>55,380</u>
	8,420,484	4,786,786	(285,082)	12,922,188	362,401
Other:					
Compensated absences	<u>2,065,575</u>	<u>476,461</u>	<u>(458,176)</u>	<u>2,083,860</u>	<u>450,000</u>
	<u>\$10,486,059</u>	<u>\$ 5,263,247</u>	<u>\$ (743,258)</u>	<u>\$15,006,048</u>	<u>\$ 812,401</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(8) Changes in Long-Term Obligations, Continued

Primary Government, Continued

Included in the net additions is a foreign exchange adjustment due to a change in the SDR calculation of \$460,890 and \$771,461 for ADB Loan Number 1459 and 1520, respectively, which was passed through by the FSM National Government, and resulted in an increase in the outstanding loans payable to the FSM National Government.

Discretely Presented Component Units

During the year ended September 30, 2010, 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, <u>2009</u>	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2010	<u>Due Within One Year</u>
Loans payable:					
CPUC	\$ 4,363,353	\$ -	\$ (3,554,435)	\$ 808,918	\$ 808,918
Annual leave	<u>103,478</u>	<u>54,493</u>	<u>(48,700)</u>	<u>109,271</u>	<u>33,687</u>
	<u>\$ 4,466,831</u>	<u>\$ 54,493</u>	<u>\$ (3,603,135)</u>	<u>\$ 918,189</u>	<u>\$ 842,605</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, 2010 is \$4,572,573.

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.

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. The ultimate disposition of questioned costs can be determined only by final action of the respective grantor agencies. No provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

(9) Contingencies, Continued

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, 2010 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.

General Fund Financial Position

The State's General Fund has sustained recurring operating deficits and has an unreserved fund deficit of \$15,322,662 at September 30, 2010. In addition, at September 30, 2010, the primary government's current liabilities exceed current assets by \$7,880,385.

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.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2010

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**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2010

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Revenues, Expenditures and Changes in Deficit
Budget and Actual - General Fund
Year Ended September 30, 2010

	<u>Budgeted Amounts</u>		Actual - Budgetary Basis (see Note 1)	Variance with Final Budget - Positive (Negative)
	<u>Original</u>	<u>Final</u>		
Revenues:				
Local revenues	\$ 5,641,381	\$ 5,725,741	\$ 7,137,009	\$ 1,411,268
Net change in fair value of investments	-	-	239,016	239,016
Total revenues	<u>5,641,381</u>	<u>5,725,741</u>	<u>7,376,025</u>	<u>1,650,284</u>
Expenditures:				
Current:				
General government	3,151,841	3,178,397	3,590,122	(411,725)
Education	-	-	110,327	(110,327)
Economic development	75,756	86,000	75,468	10,532
Public safety	871,431	871,431	788,716	82,715
Public works and transportation	644,417	614,746	610,335	4,411
Community affairs	-	-	13,168	(13,168)
Boards and commissions	193,273	193,273	252,588	(59,315)
Judiciary	416,261	373,426	379,481	(6,055)
Payments to component units	42,322	42,322	43,352	(1,030)
Municipal affairs	354,717	354,717	1,083,083	(728,366)
Other	27,000	147,066	134,997	12,069
Debt service	-	-	365,095	(365,095)
Total expenditures	<u>5,777,018</u>	<u>5,861,378</u>	<u>7,446,732</u>	<u>(1,585,354)</u>
Deficiency of revenues under expenditures	<u>(135,637)</u>	<u>(135,637)</u>	<u>(70,707)</u>	<u>64,930</u>
Other financing uses:				
Operating transfers out	<u>(216,466)</u>	<u>(216,466)</u>	<u>(366,466)</u>	<u>(150,000)</u>
Total other financing uses	<u>(216,466)</u>	<u>(216,466)</u>	<u>(366,466)</u>	<u>(150,000)</u>
Net change in deficit	<u>(352,103)</u>	<u>(352,103)</u>	<u>(437,173)</u>	<u>(85,070)</u>
Other changes in unreserved deficit				
Decrease in reserve for debt service	-	-	130,236	130,236
Increase in reserve for continuing appropriations	-	-	(88,994)	(88,994)
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	-	-	352,103	352,103
Unreserved deficit at the beginning of the year	<u>(15,278,834)</u>	<u>(15,278,834)</u>	<u>(15,278,834)</u>	<u>-</u>
Unreserved deficit at the end of the year	<u>\$ (15,630,937)</u>	<u>\$ (15,630,937)</u>	<u>\$ (15,322,662)</u>	<u>\$ 308,275</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, 2010

(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, 2010, 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 Administrative Services	\$ 347,567
Office of the Governor	\$ 126,921
Payments to municipalities	\$ 728,366
Department of Planning and Statistics	\$ 6,711
Election Commission	\$ 71,228
Guandong Proviencie	\$ 13,948
Department of Education	\$ 110,327
Department of Public Affairs	\$ 13,168
State Court	\$ 6,055
Chuuk State Housing Authority	\$ 1,030
Goodwill Games	\$ 19,986

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting
September 30, 2010

(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	\$ 100,299
Encumbrances	<u>(537,472)</u>
Net change in unreserved fund deficit	\$ <u>(437,173)</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

OTHER SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2010

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account
Governmental Funds
Year Ended September 30, 2010

	Special Revenue		Permanent		Other Governmental Funds	Total
	General	Grants Assistance	Compact Trust			
Expenditures:						
Salaries and wages						
Regular	\$ 3,811,540	\$ 10,933,919	\$ -	\$ -	\$ -	\$ 14,745,459
Overtime	131,838	616,185	-	-	-	748,023
Fringe benefits	395,999	1,168,224	-	-	-	1,564,223
Travel and transportation	320,727	823,802	-	45,858	-	1,190,387
Books and library materials	-	400,403	-	-	-	400,403
Communications	41,680	93,746	-	-	-	135,426
Dues, membership, and subscriptions	-	4,836	-	-	-	4,836
Food stuffs	26,540	541,304	-	-	-	567,844
Port charges	503	20,120	-	4,964	-	25,587
Office supplies and materials	52,731	1,046,270	-	20,411	-	1,119,412
POL	111,163	601,971	-	3,449	-	716,583
Printing and reproduction	25,572	14,199	-	-	-	39,771
Rental services	21,484	54,211	-	56,574	-	132,269
Repairs and maintenance	5,306	357,005	-	10,930	-	373,241
Constructional materials	1,692	366,048	-	-	-	367,740
Utilities	73,229	841,361	-	74,762	-	989,352
Goods and services	25,561	12,130	-	7,122	-	44,813
Subsidies and contributions	3,000	198,571	-	-	-	201,571
Medical referrals	-	499,784	-	-	-	499,784
Medical supplies	-	2,088,295	-	2,331	-	2,090,626
Contractual services	8,330	1,841,354	-	12,207	-	1,861,891
Professional services	3,000	285,827	-	-	-	288,827
Housing allowance	25,800	54,500	-	-	-	80,300
Compensation non-payroll	3,120	3,000	-	-	-	6,120
Allowance	13,559	-	-	-	-	13,559
Educational allowance	-	4,400	-	-	-	4,400
Scholarships and allowances	-	1,110,813	-	61,333	-	1,172,146
Training	26,900	554,330	-	-	-	581,230
Official allowance	409,901	-	-	-	-	409,901
Meeting fees and allowance	15,870	2,475	-	-	-	18,345
Representation allowance	100,945	-	-	-	-	100,945
Insurance	-	111,257	-	-	-	111,257
Leased housing, buildings and land	26,000	335,600	-	-	-	361,600
Bank charges	1,703	-	-	-	-	1,703
Equipment	31,107	1,540,056	-	7,901	-	1,579,064
Furniture and fixtures	1,025	348,363	-	10,235	-	359,623
Vehicles	33,265	329,577	-	-	-	362,842
Land	-	34,840	-	-	-	34,840
Principal repayment	285,082	-	-	-	-	285,082
Interest payments	80,013	-	-	-	-	80,013
Payout to municipalities	604,983	-	-	-	-	604,983
Miscellaneous	190,092	440	-	-	-	190,532
	<u>\$ 6,909,260</u>	<u>\$ 27,239,216</u>	<u>\$ -</u>	<u>\$ 318,077</u>	<u>\$ -</u>	<u>\$ 34,466,553</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GENERAL FUND

September 30, 2010

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, 2010
(with comparative totals for the year ended September 30, 2009)

	2010	2009
Revenues:		
FSM revenue sharing	\$ 3,444,182	\$ 2,660,821
State taxes:		
Sales tax	1,531,990	1,114,512
Hotel	46,157	153,744
Tobacco	142,133	75,161
Alcoholic beverages	171,367	110,329
Delinquent tax collections	125,563	64,206
Other excise taxes	120,910	124,250
	2,138,120	1,642,202
Fees and charges:		
Licenses and permits	548,159	288,424
Leases and other rentals	129,012	125,342
	677,171	413,766
Departmental charges:		
Transportation collections	538,742	513,694
Net change in the fair value of investments	239,016	(122,608)
Other revenues	338,794	5,518
Total revenues	7,376,025	5,113,393
Expenditures:		
Current:		
General government:		
Office of the Governor	361,311	493,584
State Legislature	2,044,548	1,736,646
Department of Planning and Statistics	6,711	23,956
Department of Administrative Services	934,333	763,498
	3,346,903	3,017,684
Education:		
Department of Education	106,580	536,471
Economic development:		
Department of Agriculture	39,064	37,935
Department of Marine Resources	34,679	34,675
	73,743	72,610
Public safety:		
Office of the Attorney General	191,339	194,188
Department of Public Safety	586,972	527,469
	778,311	721,657
Public works and transportation:		
Department of Transportation	557,115	524,275
Community affairs:		
Department of Public Affairs	13,168	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, 2010
(with comparative totals for the year ended September 30, 2009)

	2010	2009
Expenditures, continued:		
Current, continued:		
Boards and commissions:		
Chuuk Recreation Board	14,253	14,253
Land Commission	75,669	83,038
Environmental Protection Agency	-	3,000
Election Commission	110,195	240,838
	200,117	341,129
Judiciary:		
State Court	376,633	374,532
Payments to component units:		
Chuuk State Housing Authority	43,090	43,839
Municipal affairs:		
Payments to municipalities	914,648	271,948
Other:		
Farmers Home Administration	24,134	17,147
Peace Corps	3,000	2,495
Micro Games	53,929	-
Goodwill games	19,986	-
Guandong Province	32,808	-
	133,857	19,642
Debt service:		
Principal repayment	285,082	240,623
Interest payment	80,013	70,470
	365,095	311,093
Total expenditures	6,909,260	6,252,091
Excess (deficiency) of revenues over (under) expenditures	466,765	(1,138,698)
Other financing sources (uses):		
Proceeds from issuance of long-term debt	-	513,859
Operating transfers out	(366,466)	-
Operating transfers in	-	423,500
Total other financing sources (uses), net	(366,466)	937,359
Net change in deficit	100,299	(201,339)
Deficit at the beginning of the year	(8,783,061)	(8,581,722)
Deficit at the end of the year	\$ (8,682,762)	\$ (8,783,061)

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, 2010

	Budgeted Amounts		Actual	Variance with
	Original	Final	Budgetary Basis (see Note 1)	Final Budget Positive/(Negative)
Revenues:				
Local revenues	\$ 5,641,381	\$ 5,725,741	\$ 7,137,009	\$ 1,411,268
Net change in fair value of investments	-	-	239,016	239,016
Total revenues	5,641,381	5,725,741	7,376,025	1,650,284
Expenditures:				
Current:				
General government:				
Office of the Governor	320,062	335,062	461,983	(126,921)
State Legislature	2,112,185	2,123,741	2,120,892	2,849
Department of Planning and Statistics	-	-	6,711	(6,711)
Department of Administrative Services	719,594	719,594	1,000,536	(280,942)
	<u>3,151,841</u>	<u>3,178,397</u>	<u>3,590,122</u>	<u>(411,725)</u>
Education:				
Department of Education	-	-	110,327	(110,327)
Economic development:				
Department of Agriculture	39,555	49,799	39,064	10,735
Department of Marine Resources	36,201	36,201	36,404	(203)
	<u>75,756</u>	<u>86,000</u>	<u>75,468</u>	<u>10,532</u>
Public safety:				
Office of the Attorney General	240,164	240,164	198,241	41,923
Department of Public Safety	631,267	631,267	590,475	40,792
	<u>871,431</u>	<u>871,431</u>	<u>788,716</u>	<u>82,715</u>
Public works and transportation:				
Department of Transportation	644,417	614,746	610,335	4,411
Community affairs:				
Department of Public Affairs	-	-	13,168	(13,168)
Boards and commissions:				
Chuuk Recreation Board	14,324	14,324	14,253	71
Land Commission	88,511	88,511	76,669	11,842
Election Commission	89,081	89,081	160,309	(71,228)
Mortlocks Commission	1,357	1,357	1,357	-
	<u>193,273</u>	<u>193,273</u>	<u>252,588</u>	<u>(59,315)</u>
Judiciary:				
State Court	416,261	373,426	379,481	(6,055)
Payments to component units:				
Chuuk State Housing Authority	42,322	42,322	43,352	(1,030)
Municipal affairs:				
Payments to municipalities	354,717	354,717	1,083,083	(728,366)
Other:				
Farmers Home Administration	24,000	24,000	24,134	(134)
Peace Corps	3,000	3,000	3,000	-
Micro Games	-	55,066	53,929	1,137
Goodwill Games	-	-	19,986	(19,986)
Guandong Province	-	20,000	33,948	(13,948)
China Travel	-	45,000	-	45,000
	<u>27,000</u>	<u>147,066</u>	<u>134,997</u>	<u>12,069</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, 2010

	Budgeted Amounts		Actual Budgetary Basis (see Note 1)	Variance with Final Budget Positive/(Negative)
	Original	Final		
Debt service:				
Principal repayment	-	-	285,082	(285,082)
Interest payments	-	-	80,013	(80,013)
	-	-	365,095	(365,095)
Total expenditures	5,777,018	5,861,378	7,446,732	(1,585,354)
Deficiency of revenues under expenditures	(135,637)	(135,637)	(70,707)	64,930
Other financing uses:				
Operating transfers out	(216,466)	(216,466)	(366,466)	(150,000)
Total other financing uses	(216,466)	(216,466)	(366,466)	(150,000)
Net change in deficit	(352,103)	(352,103)	(437,173)	(85,070)
Other changes in unreserved deficit:				
Decrease in reserve for debt service	-	-	130,236	130,236
Increase in reserve for continuing appropriations	-	-	(88,994)	(88,994)
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	-	-	352,103	352,103
Unreserved deficit at the beginning of the year	(15,278,834)	(15,278,834)	(15,278,834)	-
Unreserved deficit at the end of the year	\$ (15,630,937)	\$ (15,630,937)	\$ (15,322,662)	\$ 308,275

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS - SPECIAL REVENUE FUNDS

September 30, 2010

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, 2010, 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, 2010

	<u>Chuuk Airport Authority</u>	<u>Hospital Revolving</u>	<u>Total</u>
<u>ASSETS</u>			
Due from other funds	\$ 1,131,480	\$ 84,747	\$ 1,216,227
<u>FUND BALANCES</u>			
Fund balances:			
Reserved for:			
Related assets	\$ 1,131,480	\$ -	\$ 1,131,480
Unreserved	<u>-</u>	<u>84,747</u>	<u>84,747</u>
	<u>\$ 1,131,480</u>	<u>\$ 84,747</u>	<u>\$ 1,216,227</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, 2010

	<u>Chuuk Airport Authority</u>	<u>Hospital Revolving</u>	<u>Total</u>
Revenues:			
Federal contributions and other grants	\$ -	\$ 170,824	\$ 170,824
Fees and charges	-	106,366	106,366
Total revenues	<u>-</u>	<u>277,190</u>	<u>277,190</u>
Expenditures by function:			
Current:			
Health services	-	252,726	252,726
Public Works and Transportation	65,351	-	65,351
Total expenditures	<u>65,351</u>	<u>252,726</u>	<u>318,077</u>
Net change in fund balances	(65,351)	24,464	(40,887)
Fund balance at the beginning of the year	<u>1,196,831</u>	<u>60,283</u>	<u>1,257,114</u>
Fund balance at the end of the year	<u>\$ 1,131,480</u>	<u>\$ 84,747</u>	<u>\$ 1,216,227</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, 2010

	Chuuk Airport Authority	Hospital Revolving	Total
	<u> </u>	<u> </u>	<u> </u>
Revenues:			
Federal contributions and other grants	\$ -	\$ 170,824	\$ 170,824
Fees and charges	-	106,366	106,366
Total revenues	<u>-</u>	<u>277,190</u>	<u>277,190</u>
Expenditures by account:			
Travel and transportation	-	45,858	45,858
Port charges	-	4,964	4,964
Office supplies and materials	-	20,411	20,411
POL	-	3,449	3,449
Rental services	-	56,574	56,574
Repairs and maintenance	-	10,930	10,930
Medical supplies	-	2,331	2,331
Utilities	65,351	9,411	74,762
Miscellaneous goods	-	7,122	7,122
Contractual services	-	12,207	12,207
Meeting allowances	-	61,333	61,333
Equipment	-	7,901	7,901
Furniture and fixtures	-	10,235	10,235
Total expenditures	<u>65,351</u>	<u>252,726</u>	<u>318,077</u>
Net change in fund balances	(65,351)	24,464	(40,887)
Fund balance at the beginning of the year	<u>1,196,831</u>	<u>60,283</u>	<u>1,257,114</u>
Fund balance at the end of the year	<u>\$ 1,131,480</u>	<u>\$ 84,747</u>	<u>\$ 1,216,227</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Balance Sheet
September 30, 2010

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	Infrastructure	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	113,575	-	10,739	-	-	657,372	-	-	-	-	-	781,686
Advances	5,565	9,106	2,940	4,803	1,141	42,003	-	-	-	1,279	-	66,837
Prepayments	479,196	345,998	16,740	5,175	236,620	12,543	-	-	-	-	-	1,096,272
Due from other funds	-	2,825,509	13,495	221,446	503,926	-	641,563	109,458	178,583	-	208,772	4,702,752
	<u>\$ 598,336</u>	<u>\$ 3,180,613</u>	<u>\$ 43,914</u>	<u>\$ 231,424</u>	<u>\$ 741,687</u>	<u>\$ 711,918</u>	<u>\$ 641,563</u>	<u>\$ 109,458</u>	<u>\$ 178,583</u>	<u>\$ 1,279</u>	<u>\$ 2,258,772</u>	<u>\$ 8,697,547</u>
<u>LIABILITIES AND FUND BALANCES (DEFICITS)</u>												
Liabilities:												
Accounts payable	\$ 489,999	\$ 740,233	\$ 43,914	\$ 75,100	\$ 32,442	\$ 291,262	\$ -	\$ 96,939	\$ 50,851	\$ 12,387	\$ -	\$ 1,833,127
Due to other funds	108,337	-	-	-	-	420,656	-	-	-	69,697	-	598,690
Total liabilities	<u>598,336</u>	<u>740,233</u>	<u>43,914</u>	<u>75,100</u>	<u>32,442</u>	<u>711,918</u>	<u>-</u>	<u>96,939</u>	<u>50,851</u>	<u>82,084</u>	<u>-</u>	<u>2,431,817</u>
Fund balances:												
Reserved for:												
Related assets	-	-	-	-	-	-	-	-	-	-	2,050,000	2,050,000
Encumbrances	2,587,102	2,238,450	106,456	155,788	2,487,515	660,293	-	39,009	-	20,555	-	8,295,168
Unreserved	<u>(2,587,102)</u>	<u>201,930</u>	<u>(106,456)</u>	<u>536</u>	<u>(1,778,270)</u>	<u>(660,293)</u>	<u>641,563</u>	<u>(26,490)</u>	<u>127,732</u>	<u>(101,360)</u>	<u>208,772</u>	<u>(4,079,438)</u>
Total fund balances (deficits)	<u>-</u>	<u>2,440,380</u>	<u>-</u>	<u>156,324</u>	<u>709,245</u>	<u>-</u>	<u>641,563</u>	<u>12,519</u>	<u>127,732</u>	<u>(80,805)</u>	<u>2,258,772</u>	<u>6,265,730</u>
Total liabilities and fund balances (deficits)	<u>\$ 598,336</u>	<u>\$ 3,180,613</u>	<u>\$ 43,914</u>	<u>\$ 231,424</u>	<u>\$ 741,687</u>	<u>\$ 711,918</u>	<u>\$ 641,563</u>	<u>\$ 109,458</u>	<u>\$ 178,583</u>	<u>\$ 1,279</u>	<u>\$ 2,258,772</u>	<u>\$ 8,697,547</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, 2010

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	Infrastructure	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
Revenues:												
Compact funding	\$ 8,650,719	\$ 9,259,301	\$ 524,728	\$ 726,157	\$ 1,282,464	\$ 4,417,261	\$ 275,097	\$ -	\$ -	\$ -	\$ -	\$ 25,135,727
Federal and other grants	-	-	-	-	-	-	-	-	97,000	-	-	97,000
Investment earnings	-	-	-	-	-	-	-	-	-	-	171,500	171,500
Total revenues	<u>8,650,719</u>	<u>9,259,301</u>	<u>524,728</u>	<u>726,157</u>	<u>1,282,464</u>	<u>4,417,261</u>	<u>275,097</u>	<u>-</u>	<u>97,000</u>	<u>-</u>	<u>171,500</u>	<u>25,404,227</u>
Expenditures by function:												
Current:												
General government	-	-	-	-	397,999	-	-	-	97,000	-	-	494,999
Health services	-	9,757,199	-	-	-	-	-	-	-	-	-	9,757,199
Education	9,766,730	-	-	-	-	4,417,261	-	-	-	-	-	14,183,991
Economic development	-	-	351,949	509,449	-	-	-	-	-	-	-	861,398
Public safety	-	-	-	-	174,037	-	-	-	-	40,623	-	214,660
Boards and commissions	1,163,616	-	172,779	174,210	-	-	-	-	-	-	-	1,510,605
Payment to component units	198,571	16,610	-	-	1,183	-	-	-	-	-	-	216,364
Total expenditures	<u>11,128,917</u>	<u>9,773,809</u>	<u>524,728</u>	<u>683,659</u>	<u>573,219</u>	<u>4,417,261</u>	<u>-</u>	<u>-</u>	<u>97,000</u>	<u>40,623</u>	<u>-</u>	<u>27,239,216</u>
Excess (deficiency) of revenues over (under) expenditures	(2,478,198)	(514,508)	-	42,498	709,245	-	275,097	-	-	(40,623)	171,500	(1,834,989)
Other financing uses:												
Operating transfers out	-	-	-	-	-	-	366,466	-	-	-	-	366,466
Net change in fund balances (deficits)	(2,478,198)	(514,508)	-	42,498	709,245	-	641,563	-	-	(40,623)	171,500	(1,468,523)
Fund balances (deficits) at the beginning of the year	2,478,198	2,954,888	-	113,826	-	-	-	12,519	127,732	(40,182)	2,087,272	7,734,253
Fund balances (deficits) at the end of the year	<u>\$ -</u>	<u>\$ 2,440,380</u>	<u>\$ -</u>	<u>\$ 156,324</u>	<u>\$ 709,245</u>	<u>\$ -</u>	<u>\$ 641,563</u>	<u>\$ 12,519</u>	<u>\$ 127,732</u>	<u>\$ (80,805)</u>	<u>\$ 2,258,772</u>	<u>\$ 6,265,730</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, 2010

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	Infrastructure	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
Revenues:												
Compact funding	\$ 8,650,719	\$ 9,259,301	\$ 524,728	\$ 726,157	\$ 1,282,464	\$ 4,417,261	\$ 275,097	\$ -	\$ -	\$ -	\$ -	\$ 25,135,727
Federal and other grants	-	-	-	-	-	-	-	-	97,000	-	-	97,000
Investment earnings	-	-	-	-	-	-	-	-	-	-	171,500	171,500
Total revenues	<u>8,650,719</u>	<u>9,259,301</u>	<u>524,728</u>	<u>726,157</u>	<u>1,282,464</u>	<u>4,417,261</u>	<u>275,097</u>	<u>-</u>	<u>97,000</u>	<u>-</u>	<u>171,500</u>	<u>25,404,227</u>
Expenditures by account:												
Salaries and wages:												
Regular	6,403,741	2,747,411	194,471	207,421	-	1,380,875	-	-	-	-	-	10,933,919
Overtime	16,065	595,745	3,197	924	-	254	-	-	-	-	-	616,185
Fringe benefits	644,444	319,595	20,027	25,409	9,222	149,527	-	-	-	-	-	1,168,224
Travel and transportation	56,795	132,452	33,165	84,882	16,026	495,745	-	-	-	4,737	-	823,802
Books and library materials	400,403	-	-	-	-	-	-	-	-	-	-	400,403
Communications	27,072	9,516	5,272	8,192	15,980	25,658	-	-	-	2,056	-	93,746
Dues, memberships, and subscriptions	100	4,546	130	-	-	60	-	-	-	-	-	4,836
Food stuffs	161,431	223,858	453	1,236	1,336	151,178	-	-	-	1,812	-	541,304
Port charges	10,925	-	1,244	1,913	2,266	3,772	-	-	-	-	-	20,120
Office supplies and materials	456,514	158,533	64,365	42,245	33,311	274,430	-	-	-	16,872	-	1,046,270
POL	127,422	296,141	36,051	23,291	3,981	106,877	-	-	-	8,208	-	601,971
Printing and reproduction	420	5,427	763	3	255	7,331	-	-	-	-	-	14,199
Rental services	9,118	5,235	5,802	7	146	33,903	-	-	-	-	-	54,211
Repairs and maintenance	103,795	154,313	12,895	6,323	1,723	74,105	-	-	-	3,851	-	357,005
Construction materials	297,714	-	4,890	21,774	-	41,670	-	-	-	-	-	366,048
Utilities	150,190	624,580	11,500	12,969	7,679	34,443	-	-	-	-	-	841,361
Goods and services	3,289	2,004	5,255	958	624	-	-	-	-	-	-	12,130
Subsidies and contributions	198,571	-	-	-	-	-	-	-	-	-	-	198,571
Medical referrals	-	499,784	-	-	-	-	-	-	-	-	-	499,784
Medical supplies	-	2,088,295	-	-	-	-	-	-	-	-	-	2,088,295
Contractual services	401,958	377,302	33,457	149,935	119,494	756,719	-	-	-	2,489	-	1,841,354
Professional services	500	-	6,000	-	258,477	20,850	-	-	-	-	-	285,827
Housing allowance	-	54,500	-	-	-	-	-	-	-	-	-	54,500
Educational allowance	4,400	-	-	-	-	-	-	-	-	-	-	4,400
Scholarships and allowances	1,110,813	-	-	-	-	-	-	-	-	-	-	1,110,813
Fees and meeting allowances	2,475	-	-	-	-	-	-	-	-	-	-	2,475
Training	-	30,330	-	27,900	4,160	491,940	-	-	-	-	-	554,330
Insurance	-	5,007	-	1,200	-	105,050	-	-	-	-	-	111,257
Leased housing, buildings and land	27,500	115,300	450	14,400	31,650	146,300	-	-	-	-	-	335,600
Compensation non-payroll	-	3,000	-	-	-	-	-	-	-	-	-	3,000
Equipment	300,449	1,031,060	35,410	12,958	41,050	22,129	-	97,000	-	-	-	1,540,056
Furniture and fixtures	210,113	59,784	5,121	10,394	1,488	60,865	-	-	-	598	-	348,363
Vehicles	2,700	195,251	44,810	29,325	23,911	33,580	-	-	-	-	-	329,577
Land	-	34,840	-	-	-	-	-	-	-	-	-	34,840
Miscellaneous	-	-	-	-	440	-	-	-	-	-	-	440
Total expenditures	<u>11,128,917</u>	<u>9,773,809</u>	<u>524,728</u>	<u>683,659</u>	<u>573,219</u>	<u>4,417,261</u>	<u>-</u>	<u>-</u>	<u>97,000</u>	<u>40,623</u>	<u>-</u>	<u>27,239,216</u>
Excess (deficiency) of revenues over (under) expenditures	(2,478,198)	(514,508)	-	42,498	709,245	-	275,097	-	-	(40,623)	171,500	(1,834,989)
Other financing sources:												
Operating transfers in	-	-	-	-	-	-	366,466	-	-	-	-	366,466
Net change in fund balances (deficits)	(2,478,198)	(514,508)	-	42,498	709,245	-	641,563	-	-	(40,623)	171,500	(1,468,523)
Fund balances (deficits) at the beginning of the year	<u>2,478,198</u>	<u>2,954,888</u>	<u>-</u>	<u>113,826</u>	<u>-</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>
Fund balances (deficits) at the end of the year	\$ -	\$ 2,440,380	\$ -	\$ 156,324	\$ 709,245	\$ -	\$ 641,563	\$ 12,519	\$ 127,732	\$ (80,805)	\$ 2,258,772	\$ 6,265,730

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 as of and for the year ended September 30, 2010, which collectively comprise the State of Chuuk's basic financial statements and have issued our report thereon dated June 22, 2011, which report was qualified with respect to a liability for land leases and other claims payable in the governmental activities and the General Fund. 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 discretely presented component units, 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 of Chuuk'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 of Chuuk's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the State of Chuuk'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 was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs (pages 70 through 72), we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as item 2010-2 to be a material weakness.

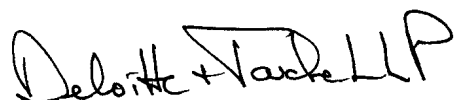
Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Chuuk'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 of Chuuk in a separate letter dated June 22, 2011.

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

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is stylized and appears to be written in a cursive or semi-cursive font.

June 22, 2011

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON 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 State of Chuuk's compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on the State of Chuuk's major federal program for the year ended September 30, 2010. The State of Chuuk'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 72). Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the State of Chuuk's management. Our responsibility is to express an opinion on the State of Chuuk's compliance based on our audit.

As discussed in Note 2b to the Schedule of Expenditures of Federal Awards, the State of Chuuk'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, 2010. 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; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of Chuuk'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 of Chuuk's compliance with those requirements.

As described in item 2010-1 in the accompanying Schedule of Findings and Questioned Costs, the State of Chuuk did not comply with requirements regarding equipment and real property management that is applicable to its Economic, Social and Political Development of the Territories - Compact of Free Association Sector Grants (CFDA # 15.875) major program. Compliance with such requirements is necessary, in our opinion, for the State of Chuuk to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the State of Chuuk complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major program for the year ended September 30, 2010.

Internal Control Over Compliance

Management of the State of Chuuk is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the State of Chuuk's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 of Chuuk's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses.

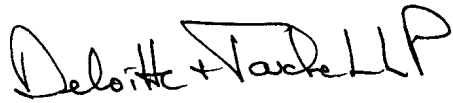
A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item 2010-1 to be a material weakness.

The State of Chuuk'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 of Chuuk'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 as of and for the year ended September 30, 2010, and have issued our report thereon dated June 22, 2011, which report was qualified with respect to a liability for land leases and other claims payable in the governmental activities and the General Fund. Our audit was performed for the purpose of forming our opinions on the financial statements that collectively comprise the State of Chuuk's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards (pages 65 and 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 of Chuuk. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

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

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

June 22, 2011

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Expenditures of Federal Awards, by Grantor
Year Ended September 30, 2010

<u>Agency/Program</u>	<u>Expenditures</u>
U.S. Department of the Interior	\$ <u>27,101,593</u>
GRAND TOTAL	\$ <u><u>27,101,593</u></u>
Reconciliation to the basic financial statements:	
Grants Assistance Fund	\$ 27,239,216
Less: CFSM Grants	40,622
Non-US Grants	<u>97,000</u>
	\$ <u><u>27,101,594</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, 2010

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF THE INTERIOR		
Economic, Social and Political Development of the Territories:		
Compact Sector Grants - Capacity Building Sector		\$ 573,219
Compact Sector Grants - Education Sector		11,128,917
Supplemental Education Grant		4,417,261
Compact Sector Grants - Environment Sector		524,728
Compact Sector Grants - Health Sector		9,773,809
Compact Sector Grants - Private Sector Development		<u>683,659</u>
Total Compact Sector Grants Fund	15.875	<u>27,101,593</u>
U.S. DEPARTMENT OF THE INTERIOR TOTAL		<u>\$ 27,101,593</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, 2010

1. Scope of Audit

The State of Chuuk (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 agency:

- 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, 2010 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, 2010.

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, 2010

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 2010 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, 2010

<u>Program Title</u>	<u>Fiscal Year CFDA No.</u>	2010 <u>Expenditures</u>
<u>U.S. Department of the Interior</u>		
Compact of Free Association:		
Compact Sector Grants	15.875	\$ <u>27,101,593</u>
Total U.S. Federal program expenditures		\$ <u>27,101,593</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, 2010

Part I - Summary of Auditors' Results

Financial Statements

- | | |
|--|---------------|
| 1. Type of auditors' report issued: | Qualified |
| Internal control over financial reporting: | |
| 2. Material weakness(es) identified? | Yes |
| 3. Significant deficiency(ies) identified? | None reported |
| 4. Noncompliance material to financial statements noted? | No |

Federal Awards

- | | | | | | |
|---|---|------------------------|--------|---|--|
| Internal control over major programs: | | | | | |
| 5. Material weakness(es) identified? | Yes | | | | |
| 6. Significant deficiency(ies) identified? | None reported | | | | |
| 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. Identification of major programs: | | | | | |
| <table style="border-collapse: collapse; width: 100%;"> <tr> <td style="border-bottom: 1px solid black; width: 25%;"><u>CFDA Number</u></td> <td style="border-bottom: 1px solid black; width: 75%;"><u>Federal Program</u></td> </tr> <tr> <td>15.875</td> <td>Economic, Social and Political Development of the Territories – Compact of Free Association Sector Grants</td> </tr> </table> | <u>CFDA Number</u> | <u>Federal Program</u> | 15.875 | Economic, Social and Political Development of the Territories – Compact of Free Association Sector Grants | |
| <u>CFDA Number</u> | <u>Federal Program</u> | | | | |
| 15.875 | Economic, Social and Political Development of the Territories – Compact of Free Association Sector Grants | | | | |
| 10. Dollar threshold used to distinguish between Type A and Type B Programs: | \$813,048 | | | | |
| 11. Auditee qualified as a low-risk auditee? | No | | | | |

Part II - Financial Statement Findings Section

<u>Reference #</u>	<u>Findings</u>
2010-2	Daily Cash Collections

Part III - Federal Award Findings and Questioned Cost Section

<u>Reference #</u>	<u>CFDA #</u>	<u>Findings</u>	<u>Questioned Costs</u>
2010-1	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, 2010

Finding No.: 2010-1
Grantor Agency: U.S. Department of the Interior
CFDA Program: 15.875 Economic, Social and Political Development of the Territories
Grant Number: Compact of Free Association 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 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 2010 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 2006-2009 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. Procurement and supply will conduct physical inventory of all accountable and capitalized fixed assets and required all departments receiving compact sector and other U.S. Federal Funds for purchased of fixed assets to prepare maintenance plan for their vehicles, equipments and real property.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2010

Finding No.: 2010-2
Area: Revenue

Criteria: A functioning system of internal control requires that the total of daily cash receipts equal the amount banked. Variances due to insufficient fund checks should be recorded as a receivable.

Condition: Of 59 items tested, we found eight instances where total collections for the day do not equal the amount banked due to a condition of insufficient funds provided by payors.

Cause: The cause of this condition is an internal control weakness.

Effect: A potential unrecorded tax receivable from customers exists as a result of this matter.

Recommendation: We recommend that the State ensure that collections are recorded correctly.

Auditee Response and Corrective Action: We agree with the finding and recommendation. The additional amount deposited in the instances cited pertain to insufficient fund checks that are being redeposited after initially not clearing. In most cases these checks were deposited to the NSF payee's bank of origin rather than to the State's general depository account. In those cases a separate deposit slip is prepared for the alternate bank. We note, however, that there is no duplicate recording of revenue or cash in these instances.

Management believes it has good control over NSF checks and routinely follows up with the payee's to insure they are ultimately collected. In fiscal year 2011 a written procedure will be prepared to address the redeposit and accounting for NSF checks by Tax&Revenue and Treasury personnel.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Unresolved Prior Year Findings and Questioned Costs
Year Ended September 30, 2010

Questioned Costs

For the year ended September 30, 2010, the following questioned costs were noted and prior questioned costs resolved:

	Questioned Costs Set Forth in Prior Audit Report <u>2009</u>	Questioned Costs Resolved During Fiscal Year <u>2010</u>	Unresolved Questioned Costs at <u>September 30, 2010</u>
Unresolved Questioned Costs FY 03	\$ 122,029	\$ (122,029) ⁽²⁾	\$ -
Unresolved Questioned Costs FY 04	9,453	(9,453) ⁽²⁾	-
Unresolved Questioned Costs FY 07	912,718	(912,718) ⁽¹⁾	-
Unresolved Questioned Costs FY 08	<u>11,519</u>	<u>(11,519) ⁽¹⁾</u>	<u>-</u>
	<u>\$ 1,055,719</u>	<u>\$ (1,055,719)</u>	-
Questioned Costs FY 10			<u>-</u>
			<u>\$ -</u>

Unresolved Findings

The status of unresolved findings is discussed in the Schedule of Findings and Questioned Costs section of this report (pages 70 through 72).

Resolved Questioned Costs

- (1) Questioned costs resolved during fiscal year 2010 are per a resolution letter signed by the Acting Chairman of the FSM Questioned Costs Review Committee.
- (2) Questioned costs resolved during fiscal year 2010 are per the State exercising the two-year rule per OMB Circular A-133 Section .315(b)(4).