

**CHUUK STATE HEALTH CARE PLAN  
(A COMPONENT UNIT OF THE STATE OF CHUUK)**

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**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2011 AND 2010**

**CHUUK STATE HEALTH CARE PLAN  
(A COMPONENT UNIT OF THE STATE OF CHUUK)**

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## INDEPENDENT AUDITORS' REPORT

The Board of Trustees  
Chuuk State Health Care Plan

We have audited the accompanying statements of net assets of the Chuuk State Health Care Plan (the "Plan"), a component unit of the State of Chuuk, as of September 30, 2011 and 2010, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

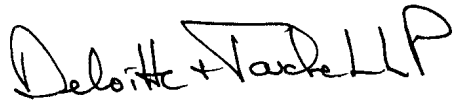
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and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

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Chuuk State Health Care Plan as of September 30, 2011 and 2010, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As stated in note 5, the Plan carries a receivable of \$50,000 from the State of Chuuk and it is not possible to predict when this balance will be collected.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 13, 2012, on our consideration of Chuuk State Health Care Plan'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 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.

The Management's Discussion and Analysis on pages 3 through 8 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Chuuk State Health Care Plan's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

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

June 13, 2012

## **CHUUK STATE HEALTH CARE PLAN**

### **Management's Discussion and Analysis Years Ended September 30, 2011 and 2010**

This analysis, prepared by the management of the Chuuk State Health Care Plan (the "Plan"), offers readers a narrative overview of the activities of the Plan for the fiscal year ended September 30, 2011. We encourage readers to consider this information in conjunction with the Plan's financial statements, which follow. Fiscal year 2010 and 2009 comparative information has been included, where appropriate. This information is required by the Governmental Accounting Standards Board, (GASB), which provides guidelines on what must be included and excluded from the analysis.

There are three financial statements presented: the Balance Sheet; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows.

#### **FINANCIAL HIGHLIGHTS**

- For the fiscal year ended September 30, 2011, the Chuuk State Health Care Plan's net assets increased \$0.25 million (up 29%) from \$0.86 million in the prior year to \$1.11 million. The increase occurred because of increased premium revenues. This is the second increase in net assets since fiscal 2006.
- During fiscal year 2011, the Plan had premium revenues of \$1.176 million compared to \$0.989 million in fiscal year 2010. The \$0.187 million increase (or 19%) was the result of management's rigorous collection of Plan premiums and new premiums from private sector enrollees. Medical claim expenses of \$0.740 million in fiscal year 2011 increased \$0.097 million (or 15%) from \$0.642 million in the prior year. This increase in medical claims expenses reflects the results from the greater plan utilization by enrollees and higher claims expense per patient.
- During fiscal year 2011, the Plan had net income of \$0.232 million compared with net income of \$0.246 million in fiscal year 2010. The Plan paid legal fees during the filing of the case against Pacific International, Inc. (PII) in order to increase premium collections.

#### **THE STATEMENT OF NET ASSETS**

The Statement of Net Assets presents the assets, liabilities and net assets of the Plan as of the fiscal year end and represents a "snapshot" financial statement. The Statement of Net Assets presents end-of-year data concerning assets (current and noncurrent), liabilities (current and noncurrent), and net assets (assets minus liabilities). The difference between current and noncurrent assets and liabilities will be discussed in the footnotes to the financial statements.

From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the operations of the Plan. They are also able to determine how much the Plan owes vendors and others. Finally, the Statement of Net Assets provides a picture of the net assets (assets minus liabilities) that the Plan has available for future expenses by the Plan.

Net assets are divided into two major categories. The first category, invested in capital assets, net of related debt, provides the institution's equity in property, plant and equipment owned by the Plan. The next asset category is restricted assets, which is divided into two categories, nonexpendable and expendable. The corpus of nonexpendable restricted assets is only available for investment purposes; the Plan has no nonexpendable restricted assets. Expendable restricted net assets are available for expenditures by the Plan but must be spent for purposes determined by donors and/or external entities that have place, time or purpose restrictions on the use of the assets. All the Plan assets that are not otherwise invested in capital assets are restricted by law to be used for health care services.

## CHUUK STATE HEALTH CARE PLAN

Management's Discussion and Analysis  
Years Ended September 30, 2011 and 2010

### SUMMARY NET ASSET STATEMENTS (In '000's)

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Assets:			
Current and other assets	\$ 1,194	\$ 872	\$ 652
Capital assets, net	<u>31</u>	<u>25</u>	<u>25</u>
Total assets	\$ <u>1,225</u>	\$ <u>897</u>	\$ <u>677</u>
Liabilities:			
Current liabilities	\$ <u>118</u>	\$ <u>37</u>	\$ <u>85</u>
Net assets:			
Invested in capital assets	31	25	25
Restricted	<u>1,076</u>	<u>835</u>	<u>577</u>
Total net assets	<u>1,107</u>	<u>860</u>	<u>602</u>
Total liabilities and net assets	\$ <u>1,225</u>	\$ <u>897</u>	\$ <u>677</u>

The total assets at the end of fiscal year 2011 of \$1.225 million exceed total liabilities of \$0.118 million, resulting in net assets of \$1.107 million. Of the total assets, \$0.855 million are held in cash, cash equivalents or short-term investments. Another \$0.288 million are in the form of accounts receivable. This contrasts to fiscal year 2010 when \$0.665 million of the total assets were held in cash, cash equivalents or short-term investments and accounts receivables were \$0.156 million. Liabilities of \$0.118 million in fiscal year 2011 compare favorably with the \$0.037 million in fiscal year 2010; up \$0.081 million (or 2.19%).

### STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

Changes in total net assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of the statement is to present the revenues received by the Plan, both operating and non-operating, and the expenses paid by the Plan, operating and non-operating.

Generally speaking, operating revenues are received from income provided by collecting health care premiums from Plan members. Other non-operating revenues are for interest income earning from short-term investments of Plan assets. Operating expenses can be classified as of two types: (i) medical service expenditures provided to eligible enrollees by accredited health care providers, and (ii) other operating expenses necessary to administer the Plan.

## CHUUK STATE HEALTH CARE PLAN

Management's Discussion and Analysis  
Years Ended September 30, 2011 and 2010

### SUMMARY STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS In '000's

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Revenues:			
Premiums	\$ 1,177	\$ 989	\$ 837
Other Revenues	5	4	5
Recovery of premium losses	4	-	-
Claims expenses	<u>(740)</u>	<u>(642)</u>	<u>(756)</u>
Total net revenues	<u>446</u>	<u>351</u>	<u>86</u>
Expenses:			
Other operating expenses	<u>226</u>	<u>179</u>	<u>180</u>
Operating earnings (loss)	220	172	(94)
Non- operating revenues:			
Subsidy from FSM National Government	13	70	-
Interest Income	<u>(1)</u>	<u>4</u>	<u>10</u>
Net income (loss)	232	246	(84)
Capital contribution from FSM National Government	<u>15</u>	<u>12</u>	<u>-</u>
Change in net assets	247	258	(84)
Net assets at beginning of year	<u>860</u>	<u>602</u>	<u>686</u>
Net assets at end of year	\$ <u>1,107</u>	\$ <u>860</u>	\$ <u>602</u>

In fiscal year 2011, the Plan showed positive improvements in virtually every aspect of its financial operations. The Statements of Revenues, Expenses, and Changes in Net Assets reflect \$1.11 million in net assets, with an overall \$0.25 million increase (or 29%) in net assets from the prior year.

Some highlights of the information presented on the Statements of Revenues, Expenses, and Changes in Net Assets are as follows:

## CHUUK STATE HEALTH CARE PLAN

### Management's Discussion and Analysis Years Ended September 30, 2011 and 2010

Premium revenues represent receipts from Plan enrollees. The following table indicates premium revenue activity for fiscal years 2011, 2010 and 2009 for both public and private sector enrollees:

MEMBER COMPOSITION	FY	2011	FY-	2010	FY-	2009
	# ENROLLED @ 9-30-11	PREMIUMS PAID (000's)	# ENROLLED @ 9-30-10	PREMIUMS PAID (000's)	# ENROLLED @ 9-30-09	PREMIUMS PAID (000's)
Public Sector	10,250	\$ 779	10,739	\$ 905	10,177	\$ 761
Private Sector	2,437	397	2,009	84	1,915	76
<b>TOTALS</b>	<b>12,687</b>	<b>\$ 1,176</b>	<b>12,748</b>	<b>\$ 989</b>	<b>12,092</b>	<b>\$ 837</b>

The chart reflects the decline in public sector enrollees in fiscal year 2011, declining from 10,739 in fiscal year 2010 to 10,250 (or 5%) in fiscal year 2011. This is due to the soft landing from the Department of Education while the private sector enrollees in fiscal year 2011 increased from 2,009 in fiscal year 2010 to 2,437 (or 21%) in fiscal year 2011. The enrollment of Pacific International, Inc. and Blue Lagoon Resort & Dive Shop have created a positive climate to recruit new Plan members. This positive trend is the result of management's aggressive collection of prior year accounts receivable and closing loopholes that previously resulted in unpaid premiums

Management's control of claim expenses continues the positive turnaround that commenced in fiscal year 2010. The recurring problem from prior years of medical claim expenses comprising ever larger ratio of Plan premiums, leaving little leftover to cover general and administrative expenses, has been broken as shown in this table reflecting five years of Plan operations:

<u>Fiscal Year</u>	<u>Premiums</u>	<u>Claims Expense</u>	<u>Claims as a % of Premiums</u>
2011	\$ 1,176,426	\$ 739,663	63%
2010	\$ 989,040	\$ 642,557	65%
2009	\$ 837,430	\$ 756,292	90%
2008	\$ 775,114	\$ 758,062	98%
2007	\$ 834,562	\$ 779,597	93%
2006	\$ 872,006	\$ 639,251	73%

Management's promotion of competition among third-party care providers in the Philippines has been a major factor in controlling claims expenses.

In fiscal year 2011, operating expenses of \$0.226 million increased from \$0.179 million incurred in the prior year. Legal fees spent during the filing of the case against Pacific International, Inc. (PII) resulted in a court judgment in favor of the Plan. Even with rising Plan enrollments, operating expenses are controlled within net revenues because of stringent control of Plan operating expenses by management oversight and Board policies.



## CHUUK STATE HEALTH CARE PLAN

Management's Discussion and Analysis  
Years Ended September 30, 2011 and 2010

### STATEMENT OF CASH FLOWS

The final statement presented by the Chuuk State Health Care Plan is the Statement of Cash Flows. The Statement of Cash Flows presents detailed information about the cash activity during the year. The statement is divided into four parts. The first part deals with operating cash flows from noncapital financing activities of the Plan. The second section reflects cash flows from capital and related financing activities. This section deals with the cash used for the acquisition and construction of capital and related items. The third section reflects the cash flows from investing activities and shows the purchases, proceeds and interest received from investing activities. The fourth section reconciles the net cash used in operating activities to operating income or loss reflected on the Statement of Revenues, Expenses, and Changes in Net Assets.

#### SUMMARY STATEMENT OF CASH FLOWS (In '000's)

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Cash provided by (used in):			
Operating activities	\$ 177	\$ 28	\$ (59)
Capital and noncapital related financing activities	13	70	-
Investing activities	<u>(96)</u>	<u>4</u>	<u>207</u>
Net change in cash and cash equivalents	94	102	148
Cash and cash equivalents, beginning of year	<u>413</u>	<u>311</u>	<u>163</u>
Cash and cash equivalents, end of year	\$ <u>507</u>	\$ <u>413</u>	\$ <u>311</u>

The table indicates that cash and cash equivalents increased \$0.1 million in fiscal 2011, from \$0.41 million in fiscal 2010 to \$0.51 million in the current year. Notably, for the second time since fiscal 2006, operating activities provided positive cash flow as the Plan staunched the cash outflows from operating losses that had eroded the Plan's cash position in prior fiscal years. Supplementing these results in fiscal 2011 was a \$13 thousand subsidy from the FSM National Government.

Management's Discussion and Analysis for the year ended September 30, 2010 is set forth in the Plan's report on the audit of financial statements, which is dated June 20, 2011. That Discussion and Analysis explains the major factors impacting the 2010 financial statements and can be obtained via the Office of the Public Auditor's website at [www.fsmopa.fm](http://www.fsmopa.fm).

### CAPITAL ASSET AND DEBT ADMINISTRATION

The Plan's net investment in capital assets of \$31 thousand at fiscal 2011 year end increased from fiscal year 2010 of \$25 thousand.

The Plan has no debt and there are no foreseen circumstances that would affect the Plan's access to future capital financing.

Further information on the Plan's capital assets can be found in note 4 to the financial statements.

# **CHUUK STATE HEALTH CARE PLAN**

Management's Discussion and Analysis  
Years Ended September 30, 2011 and 2010

## **ECONOMIC OUTLOOK**

In fiscal year 2011, Plan management will continue its focus on collecting accounts receivables, increasing Plan enrollments, and reducing medical claim and other operating expenses. Plan management will specifically focus on collecting multi-year delinquent premiums of the CPUC as that entity takes steps to rationalize its operations. Additionally, aggressive targeting of private sector firms for new enrollments will continue in fiscal 2011 as the construction sector fuels a wave of private sector growth in Chuuk State. Finally, the Plan has relocated its offices to Chuuk State Hospital in fiscal 2010; a move that will allow closer scrutiny of medical referrals with State personnel and save on rental expense.

## **CONTACTING THE CHUUK STATE HEALTH CARE PLAN'S MANAGEMENT**

This financial report is designed to provide our citizens, Plan enrollees, accredited health care providers, and other users of our financial information, a general overview of the Plan'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 Executive Director, Chuuk State Health Care Plan; P.O Box 1679; Weno, Chuuk; FM 96942.

# CHUUK STATE HEALTH CARE PLAN

## Statements of Net Assets September 30, 2011 and 2010

<u>ASSETS</u>	<u>2011</u>	<u>2010</u>
Current assets:		
Cash and cash equivalents	\$ 507,015	\$ 412,785
Short-term investments	348,011	252,677
Premiums receivable, net of an allowance for doubtful premiums of \$42,872 in 2011 and \$47,110 in 2010	280,252	148,627
Other receivables	8,473	7,262
Other assets	-	743
Total current assets	<u>1,143,751</u>	<u>822,094</u>
Due from the State of Chuuk	50,000	50,000
Property and equipment, net	<u>30,718</u>	<u>24,757</u>
Total assets	<u><u>\$ 1,224,469</u></u>	<u><u>\$ 896,851</u></u>
 <u>LIABILITIES AND NET ASSETS</u>  		
Current liabilities:		
Medical claims and benefits payable	\$ 108,864	\$ 31,859
Accounts payable and accrued expenses	<u>8,771</u>	<u>4,891</u>
Total liabilities	<u>117,635</u>	<u>36,750</u>
Net assets:		
Invested in capital assets	30,718	24,757
Restricted	<u>1,076,116</u>	<u>835,344</u>
Total net assets	<u>1,106,834</u>	<u>860,101</u>
Total liabilities and net assets	<u><u>\$ 1,224,469</u></u>	<u><u>\$ 896,851</u></u>

See accompanying notes to financial statements.

## CHUUK STATE HEALTH CARE PLAN

### Statements of Revenues, Expenses and Changes in Net Assets Years Ended September 30, 2011 and 2010

	2011	2010
Revenues:		
Premiums	\$ 1,176,426	\$ 989,040
Others	5,148	4,007
	1,181,574	993,047
Benefits paid:		
Claims expenses	739,662	642,557
Net revenues	441,912	350,490
Recovery of premium losses	4,238	-
Net revenues after recovery of premium losses	446,150	350,490
Other operating expenses:		
Salaries, wages and other benefits	88,189	74,264
Travel	31,676	26,609
Coordinator's fee	27,600	16,400
Legal fee	25,000	560
Depreciation	8,592	12,736
Board allowance	8,540	4,010
Social security expense	7,827	5,980
Rent	5,450	16,800
Office/computer supplies	5,052	5,624
Promotional	4,731	1,600
Telephone and telegraph	3,551	1,923
Gasoline and fuel	2,400	2,200
Repair and maintenance	2,364	1,749
Utilities	196	5,697
Representation - board luncheon meeting	-	1,998
Miscellaneous	4,734	560
Total other operating expenses	225,902	178,711
Earnings from operations	220,248	171,779
Non operating revenues:		
Subsidy from the FSM National Government	12,940	70,000
Net investment earnings (loss)	(1,008)	3,938
Net income	232,180	245,717
Capital contribution from the FSM National Government	14,553	12,403
Change in net assets	246,733	258,120
Net assets at beginning of year	860,101	601,981
Net assets at end of year	\$ 1,106,834	\$ 860,101

See accompanying notes to financial statements.

## CHUUK STATE HEALTH CARE PLAN

### Statements of Cash Flows Years Ended September 30, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Premiums received	\$ 1,054,187	\$ 881,704
Medical claims and benefits paid	(662,657)	(678,216)
Cash paid to employees and vendors	(213,898)	(175,490)
Net cash provided by operating activities	177,632	27,998
Cash flows from noncapital financing activities:		
Subsidy from the FSM National Government	12,940	70,000
Cash flows from capital and related financing activities:		
Capital contributions from the FSM National Government	14,553	12,403
Acquisition of property and equipment	(14,553)	(12,403)
Net cash used in capital and related financing activities	-	-
Cash flows from investing activities:		
Additions to time certificates of deposit	(100,000)	-
Interest income received	3,658	3,938
Net cash provided by (used in) investing activities	(96,342)	3,938
Net change in cash and cash equivalents	94,230	101,936
Cash and cash equivalents at beginning of year	412,785	310,849
Cash and cash equivalents at end of year	\$ 507,015	\$ 412,785
Reconciliation of earnings from operations to net cash provided by operating activities:		
Earnings from operations	\$ 220,248	\$ 171,779
Adjustments to reconcile earnings from operations to net cash provided by operating activities:		
Depreciation	8,592	12,736
Changes in assets and liabilities:		
Increase in premiums receivable	(131,625)	(111,343)
Increase in other receivables	(1,211)	(7,262)
Decrease in other assets	743	99
Increase (decrease) in medical claims and benefits payable	77,005	(35,659)
Increase (decrease) in accounts payable and accrued expenses	3,880	(2,352)
Net cash provided by operating activities	\$ 177,632	\$ 27,998

See accompanying notes to financial statements.

# CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements  
September 30, 2011 and 2010

## (1) Nature of Operations

### Commencement of Operations

Chuuk State Health Care Plan (the “Plan” or “CSHCP”), a component unit of the State of Chuuk, was originally established under the Chuuk Health Care Plan Act of 1994 to provide eligible residents of Chuuk State with quality health care. The Plan commenced operations in September 2003 after final approval from the Board of Trustees, with Chuuk State Hospital (CSH) as the primary health care provider. The Board of Trustees comprises of five voting members appointed by the Governor of Chuuk, with the advice and consent of the Chuuk State Legislature, and the Executive Director as a non-voting member.

### Entity’s Activities

As per Chuuk State Law No. 2-94-06 (Act No: 2-25), the Plan is dedicated to serve as a financial system to provide universal coverage of an essential level of health care for all eligible enrollees by collecting health care premiums under a plan and ensuring medical services to all members through its accredited health care providers.

Aside from CSH being its primary health provider, the Plan has also accredited two medical clinics in Chuuk – Family Clinic and Sefin Health Clinic, and six hospitals in the Philippines – Cardinal Santos Medical Center, Medical City, Capitol Medical Center, Kidney and Transplant Institute, Philippines Heart Center, and St. Luke’s Hospital to provide medical services to members of the Plan.

The Plan enables all eligible government employees to be members by contributing health premiums (50% employee share and 50% employer share) so as to claim medical benefits through the accredited health care providers. The Plan has also been extended to private sector employers and employees.

## (2) Summary of Significant Accounting Policies

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

The Plan has adopted GASB Statement No. 34, *Basic Financial Statements-and Management’s Discussion and Analysis-for State and Local Governments* (GASB 34), as amended by GASB Statement No. 37, *Basic Financial Statements – Management’s Discussion and Analysis-for State and Local Governments: Omnibus* and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. GASB Statement No. 34 establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into the following four net asset categories:

# CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements  
September 30, 2011 and 2010

## (2) Summary of Significant Accounting Policies, Continued

- Invested in capital assets, net of related debt:

Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted:

- Nonexpendable – Net assets subject to externally imposed stipulations that require the Plan to maintain them permanently. For the years ended September 30, 2011 and 2010, the Plan does not have nonexpendable net assets.
- Expendable – Net assets whose use by the Plan is subject to externally imposed stipulations that can be fulfilled by actions of the Plan pursuant to those stipulations or that expire by the passage of time.

- Unrestricted:

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

All of the Plan's net assets that are not otherwise invested in capital assets are restricted by law to be used for health care services.

### Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of the fund are included in the statements of net assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

### Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure 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 may differ from those estimates.

### Revenue and Expense Recognition

Health care premiums from enrolled members of the Plan are reported as revenue in the period such become due. The Plan considers health care premium revenues and costs that are directly related to the provision health care to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

### Medical Claims and Benefits Payable

Medical claims and benefits payable represent the actual liability on claims reported to the Plan. The liabilities for claims are determined based on actual billings received from accredited hospitals and clinics, representing medical procedures performed for members through the financial statement date.

## CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements  
September 30, 2011 and 2010

### (2) Summary of Significant Accounting Policies, Continued

#### Cash and Cash Equivalents and Time Certificates of Deposit

For purposes of the statements of net assets and cash flows, cash and cash equivalents is defined as amounts in demand deposits as well as short-term investments maturing within three months of the date acquired.

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 financial institution or its agent in the Plan'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 Plan'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 Plan's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Plan'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 Plan does not have a deposit policy for custodial credit risk.

Cash and cash equivalents include cash in various demand and savings bank accounts. Short-term investments in time certificates of deposit with original maturity dates greater than ninety days are separately classified. As of September 30, 2011 and 2010, the carrying amount of the Plan's cash and cash equivalents and time certificates of deposit was \$807,015 and \$612,785, respectively, and the corresponding bank balances were \$821,690 and \$623,503, respectively. Of the bank balance amounts, \$820,621 and \$622,497, respectively, were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC). The remaining amounts of \$1,069 and \$1,007 as of September 30, 2011 and 2010, respectively, represent deposits maintained in dollar denominated bank accounts maintained offshore. As of September 30, 2011 and 2010, bank deposits in the amount of \$579,568 and \$471,338, respectively, were FDIC insured. The Plan does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

#### Short-Term Investments

Interest-bearing deposits in banks mature within one or two years and are carried at cost. Investments in common stock are carried at fair value with unrealized gains and losses recognized in earnings.



## CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements  
September 30, 2011 and 2010

### (2) Summary of Significant Accounting Policies, Continued

#### Premiums Receivable

Premiums receivable are primarily due from the Chuuk State Government and the Chuuk Public Utilities Corporation as well as private sector employers operating in Chuuk. These receivable are interest free and uncollateralized. The allowance for uncollectible accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on the credit risk of specific customers, historical trends and other information. The allowance is established through a provision for bad debts charged to expense.

#### Property and Equipment

Property and equipment is stated at cost less accumulated depreciation. Depreciation is calculated using the straight-line method based on the estimated useful lives of the assets. All of the assets have an estimated useful life of five to eleven years. The Plan has adopted a capitalization policy of \$100,000 for buildings and \$50,000 for equipment. All vehicles and boats are capitalized regardless of the value of such items. Routine repairs and maintenance costs are expensed as incurred.

#### New Accounting Standards

During fiscal year 2011, the Plan implemented the following pronouncements:

- GASB 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.
- GASB Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting of certain financial instruments and external investment pools.

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

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 Plan.

## CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements  
September 30, 2011 and 2010

### (2) Summary of Significant Accounting Policies, Continued

#### New Accounting Standards, Continued

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*, which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity*, and No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Plan.

In July 2011, GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions* (an amendment of GASB Statement No. 53), which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The provisions of this statement are effective 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 Plan.

#### Risk Management

The Plan carries workmen's compensation liability insurance for all employees of the Plan; however, the Plan is substantially self-insured for all other risks. Management is of the opinion that no material losses have been sustained as a result of this practice during the past three years.

# CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements  
September 30, 2011 and 2010

## (3) Short-Term Investments

The Plan has time certificates of deposit with federally insured banks of \$300,000 in 2011 and \$200,000 in 2010. These deposits have initial maturity dates of one year and have interest rates ranging from 0.75% to 4.9% per annum.

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 Plan or its agent in the Plan'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 Plan'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 Plan'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.

In addition, short-term investments also comprise the following:

	<u>2011</u>	<u>2010</u>
Common stock	\$ 44,903	\$ 49,794
Money market funds	<u>3,108</u>	<u>2,883</u>
	\$ <u>48,011</u>	\$ <u>52,677</u>

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Plan will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The Plan's investments are held and administered by trustees. Accordingly, these investments are exposed to custodial credit risk. Based on negotiated trust and custody contracts, all of these investments were held in the Plan's name by the Plan's custodial financial institutions at September 30, 2011 and 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 Plan. As of September 30, 2011 and 2010, there was no concentration of credit risk for the Plan's investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The Plan 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.

## CHUUK STATE HEALTH CARE PLAN

### Notes to Financial Statements September 30, 2011 and 2010

#### (4) Property and Equipment

A summary of the Plan's property and equipment at September 30, 2011 and 2010, is as follows:

	Estimated Useful Lives	Balance at October 1, 2010	Transfers and Additions	Transfers and Deletions	Balance at September 30, 2011
Office furniture and equipment	5 - 10 years	\$ 33,854	\$ 7,553	\$ -	\$ 41,407
Vehicles	5 years	<u>49,660</u>	<u>7,000</u>	<u>-</u>	<u>56,660</u>
		83,514	14,553	-	98,067
Less accumulated depreciation		<u>(58,757)</u>	<u>(8,592)</u>	<u>-</u>	<u>(67,349)</u>
Property and equipment, net		\$ <u>24,757</u>	\$ <u>5,961</u>	\$ <u>-</u>	\$ <u>30,718</u>
	Estimated Useful Lives	Balance at October 1, 2009	Transfers and Additions	Transfers and Deletions	Balance at September 30, 2010
Office furniture and equipment	5 - 10 years	\$ 21,787	\$ 12,403	\$ (336)	\$ 33,854
Vehicles	5 years	<u>49,660</u>	<u>-</u>	<u>-</u>	<u>49,660</u>
		71,447	12,403	(336)	83,514
Less accumulated depreciation		<u>(46,357)</u>	<u>(12,736)</u>	<u>336</u>	<u>(58,757)</u>
Property and equipment, net		\$ <u>25,090</u>	\$ <u>(333)</u>	\$ <u>-</u>	\$ <u>24,757</u>

#### (5) Related Parties

As of September 30, 2011 and 2010, premium receivables from Chuuk State Government amounted to \$33,015 and \$138,788, respectively, and related premium revenue earned for the years then ended amounted to \$778,750 and \$903,233, respectively. As of September 30, 2011 and 2010, the Plan has an outstanding receivable of \$50,000 from the Chuuk State Government, representing advances made to a component unit of the State. Management cannot assess when the State will be able to repay this advance and has accordingly, in 2011 and 2010 respectively, reflected the balance as noncurrent. At September 30, 2011, the Plan has an outstanding receivable from Chuuk Public Utility Corporation of \$113,714. Additionally, during the year ended September 30, 2011, the Plan paid attorney fees to a member of its board of directors who is representing the Plan in various collection cases.

**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**

The Board of Trustees  
Chuuk State Health Care Plan:

We have audited the financial statements of the Chuuk State Health Care Plan (the Plan) as of and for the year ended September 30, 2011, and have issued our report thereon dated June 13, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

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

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 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.

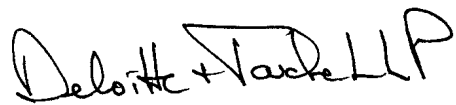
Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Plan'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 and other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Plan in a separate letter dated June 13, 2012.

This report is intended solely for the information and use of management, the Board of Trustees, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

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

June 13, 2012

**CHUUK STATE HEALTH CARE PLAN**

Summary Schedule of Prior Year Findings  
Year Ended September 30, 2011

There are no prior year findings unresolved as of September 30, 2011.