

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

**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT**

YEARS ENDED SEPTEMBER 30, 2012 AND 2011

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

Table of Contents
Years Ended September 30, 2012 and 2011

	<u>Page No.</u>
I. FINANCIAL STATEMENTS	
Independent Auditors' Report	1
Management's Discussion and Analysis	3
Statements of Net Assets	9
Statements of Revenues, Expenses, and Changes in Net Assets	10
Statements of Cash Flows	11
Notes to Financial Statements	12
II. INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS	
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 <i>Government Auditing Standards</i>	19
Unresolved Prior Year Findings	21



Deloitte & Touche LLP
361 S. Marine Corps Drive
Tamuning, GU 96913-3911
USA

Tel: 1-671-646-3884
Fax: 1-671-649-4932
www.deloitte.com

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, 2012 and 2011, 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.

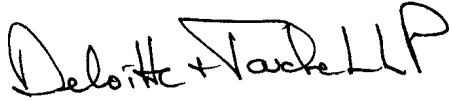
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and 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, 2012 and 2011, 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, 2013, 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.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. This supplementary information is the responsibility of the Administration's management. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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

June 13, 2013

CHUUK STATE HEALTH CARE PLAN

Management's Discussion and Analysis Years Ended September 30, 2012 and 2011

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, 2012. We encourage readers to consider this information in conjunction with the Plan's financial statements, which follow. Fiscal year 2011 and 2010 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, 2012, the Chuuk State Health Care Plan's net assets increased \$0.11 million (up 10%) from \$1.11 million in the prior year to \$1.213 million. The increase occurred because of increased other revenues and the implementation of the outpatient services to control medical costs, bills and stipend expenses. This is the third increase in net assets since fiscal 2006.
- During fiscal year 2012, the Plan had premium revenues of \$1.095 million compared to \$1.176 million in fiscal year 2011. The \$0.081 million decrease (or 6.9%) was the result of the revenue realized from a court order covers past due collection from 2009 to 2011, however, in fiscal year 2012, the adherence to the deadline of remittance, rigorous collection, and the new premiums from private sector enrollees the revenues became stabilized. Medical claim expenses of \$0.806 million in fiscal year 2012 increased \$0.067 million (or 9%) from \$0.740 million in the prior year. This increase in medical claims expense reflects the results from the greater plan utilization by enrollees and higher claims expense per patient.
- During fiscal year 2012, the Plan had net income of \$0.098 million compared with net income of \$0.232 million in fiscal year 2011. The Plan paid legal fees during the filing of legal cases 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, 2012 and 2011

SUMMARY NET ASSET STATEMENTS (In '000's)

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Assets:			
Current and other assets	\$ 1,235	\$ 1,194	\$ 872
Capital assets, net	<u>28</u>	<u>31</u>	<u>25</u>
Total assets	\$ <u>1,263</u>	\$ <u>1,225</u>	\$ <u>897</u>
Liabilities:			
Current liabilities	\$ 50	\$ 118	\$ 37
Non-current liabilities	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>50</u>	<u>118</u>	<u>37</u>
Net assets:			
Invested in capital assets	28	31	25
Restricted	<u>1,185</u>	<u>1,076</u>	<u>835</u>
Total net assets	<u>1,213</u>	<u>1,107</u>	<u>860</u>
Total liabilities and net assets	\$ <u>1,263</u>	\$ <u>1,225</u>	\$ <u>897</u>

The total assets at the end of fiscal year 2012 of \$1.263 million exceed the total liabilities of \$0.050 million, resulting in net assets of \$1.213 million. Of the total assets, \$1.002 million are held in cash, cash equivalents or short-term investments. Another \$0.183 million are in the form of accounts receivable. This contrasts to fiscal year 2011 when \$0.855 million of the total assets were held in cash, cash equivalents or short-term investments and accounts receivables were \$0.288 million. Liabilities of \$0.050 million in fiscal year 2012 compare favorably with the \$0.118 million in fiscal year 2011; down \$0.068 million (or 57%).

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, 2012 and 2011

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

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Revenues:			
Premiums	\$ 1,095	\$ 1,177	\$ 989
Other Revenues	7	5	4
Provisions for Premium losses	-	4	-
Claims expenses	<u>(806)</u>	<u>(740)</u>	<u>(642)</u>
Total net revenues	<u>296</u>	<u>446</u>	<u>351</u>
Expenses:			
Other operating expenses	<u>246</u>	<u>226</u>	<u>179</u>
Operating earnings	50	220	172
Non- operating revenues:			
Subsidy from FSM National Government	24	13	70
Investment income (loss)	<u>24</u>	<u>(1)</u>	<u>4</u>
Net income	98	232	246
Capital contribution from FSM National Government	<u>8</u>	<u>15</u>	<u>12</u>
Change in net assets	106	247	258
Net assets at beginning of year	<u>1,107</u>	<u>860</u>	<u>602</u>
Net assets at end of year	\$ <u>1,213</u>	\$ <u>1,107</u>	\$ <u>860</u>

In fiscal year 2012, the Plan showed positive improvements in virtually every aspect of its financial operations. The Statement of Revenues, Expenses, and Changes in Net Assets reflects \$1.213 million in net assets, with an overall \$0.11 million increase (or 10%) in net assets from the prior year.

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

Premium revenues represent receipts from Plan enrollees. The following table indicates premium revenue activity for fiscal years 2012, 2011 and 2010 for both public and private sector enrollees:

	FY-	2012	FY-	2011	FY-	2010
	#	PREMIUMS	#	PREMIUMS	#	PREMIUMS
MEMBER	ENROLLED	PAID	ENROLLED	PAID	ENROLLED	PAID
COMPOSITION	@ 9-30-12	(000's)	@ 9-30-11	(000's)	@ 9-30-10	(000's)
Public Sector	10,359	\$ 847	10,250	\$ 779	10,739	\$ 905
Private Sector	3,709	248	2,437	398	2,009	84
TOTALS	14,068	\$ 1,095	12,687	\$ 1,177	12,748	\$ 989

CHUUK STATE HEALTH CARE PLAN

Management's Discussion and Analysis Years Ended September 30, 2012 and 2011

The chart reflects the increase in public sector enrollees in fiscal year 2012, increasing from 10,250 in fiscal year 2011 to 10,359 (or 1%) in fiscal year 2012. This is due to the increase in the number of enrollees and their dependents from the public sector. Furthermore, private sector enrollees increased in fiscal year 2012 from 2,437 in 2011 to 3,709 (or 52%) in fiscal year 2012. This is due to the increase in the number of dependents that has not made any effect as to the premium collection.

Management's control of claims expense continues the positive turnaround that commenced in fiscal year 2012. The recurring problem from prior years of medical claims expense 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>
2012	\$ 1,095,027	\$ 806,379	74%
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 2012, operating expenses of \$0.246 million increased from \$0.226 million incurred in the prior year. The Plan spent legal fees during the filing of the case against the Chuuk Public Utilities Corporation (CPUC) now pending for court judgment.. 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.

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.

CHUUK STATE HEALTH CARE PLAN

Management's Discussion and Analysis
Years Ended September 30, 2012 and 2011

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

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Cash provided by (used in):			
Operating activities	\$ 99	\$ 177	\$ 28
Capital and noncapital related financing activities	24	13	70
Investing activities	<u>(97)</u>	<u>(96)</u>	<u>4</u>
Net change in cash and cash equivalents	26	94	102
Cash and cash equivalents, beginning of year	<u>507</u>	<u>413</u>	<u>311</u>
Cash and cash equivalents, end of year	\$ <u>533</u>	\$ <u>507</u>	\$ <u>413</u>

The table indicates that cash and cash equivalents increased \$0.02 million in fiscal 2012, from \$0.51 million in fiscal 2011 to \$0.53 million in the current year. Notably, for the third time since fiscal 2006, operating activities provided positive cash flow (\$0.99 million) 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 2012, were a \$24 thousand subsidy from the FSM National Government.

Management's Discussion and Analysis for the year ended September 30, 2011 is set forth in the Plan's report on the audit of financial statements, which is dated June 4, 2012. That Discussion and Analysis explains the major factors impacting the 2011 financial statements and can be obtained via the Office of the Public Auditor's website at www.fsmopa.fm.

CAPITAL ASSET AND DEBT ADMINISTRATION

The Plan's net investment in capital assets of \$28 thousand at fiscal 2012 year end decreased from fiscal year 2011 of \$31 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.

ECONOMIC OUTLOOK

In fiscal year 2013, 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 2013 as the construction sector fuels a wave of private sector growth in Chuuk State. Finally, the Plan relocated its offices to Chuuk State Hospital in fiscal 2010; a move that allows closer scrutiny of medical referrals with State personnel and saves on rental expense.

CHUUK STATE HEALTH CARE PLAN

Management's Discussion and Analysis
Years Ended September 30, 2012 and 2011

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, 2012 and 2011

<u>ASSETS</u>	<u>2012</u>	<u>2011</u>
Current assets:		
Cash and cash equivalents	\$ 533,158	\$ 507,015
Time certificates of deposit	200,000	300,000
Investments	269,235	48,011
Premiums receivable, net of an allowance for doubtful premiums of \$42,872 in 2012 and 2011	168,264	280,252
Other receivables	14,431	8,473
Total current assets	1,185,088	1,143,751
Due from the State of Chuuk	50,000	50,000
Property and equipment, net	27,708	30,718
Total assets	<u>\$ 1,262,796</u>	<u>\$ 1,224,469</u>
 <u>LIABILITIES AND NET ASSETS</u> 		
Current liabilities:		
Medical claims and benefits payable	\$ 38,265	\$ 108,864
Accounts payable and accrued expenses	11,776	8,771
Total liabilities	50,041	117,635
Net assets:		
Invested in capital assets	27,708	30,718
Restricted	1,185,047	1,076,116
Total net assets	1,212,755	1,106,834
Total liabilities and net assets	<u>\$ 1,262,796</u>	<u>\$ 1,224,469</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, 2012 and 2011

	2012	2011
Revenues:		
Premiums	\$ 1,095,027	\$ 1,176,426
Others	6,733	5,148
	1,101,760	1,181,574
Benefits paid:		
Claims expenses	806,379	739,662
Net revenues	295,381	441,912
Recovery of premium losses	-	4,238
Net revenues after recovery of premium losses	295,381	446,150
Other operating expenses:		
Salaries, wages and other benefits	93,886	88,189
Travel	35,805	31,676
Coordinator's fee	33,500	27,600
Legal fees	25,295	25,000
Depreciation	11,282	8,592
Social security expense	8,938	7,827
Office/computer supplies	7,574	5,052
Board allowance	6,587	8,540
Rent	5,400	5,450
Telephone and telegraph	3,808	3,551
Repair and maintenance	3,259	2,364
Promotional	3,168	4,731
Gasoline and fuel	2,932	2,400
Utilities	2,847	196
Miscellaneous	1,810	4,734
Total other operating expenses	246,091	225,902
Earnings from operations	49,290	220,248
Non operating revenues:		
Subsidy from the FSM National Government	24,286	12,940
Net investment earnings (loss)	24,073	(1,008)
Net income	97,649	232,180
Capital contribution from the FSM National Government	8,272	14,553
Change in net assets	105,921	246,733
Net assets at beginning of year	1,106,834	860,101
Net assets at end of year	\$ 1,212,755	\$ 1,106,834

See accompanying notes to financial statements.

CHUUK STATE HEALTH CARE PLAN

Statements of Cash Flows Years Ended September 30, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Premiums received	\$ 1,213,748	\$ 1,054,187
Medical claims and benefits paid	(876,978)	(662,657)
Cash paid to employees and vendors	(237,762)	(213,898)
Net cash provided by operating activities	99,008	177,632
Cash flows from noncapital financing activities:		
Subsidy from the FSM National Government	24,286	12,940
Cash flows from capital and related financing activities:		
Capital contributions from the FSM National Government	8,272	14,553
Acquisition of property and equipment	(8,272)	(14,553)
Net cash used in capital and related financing activities	-	-
Cash flows from investing activities:		
Additions to investments	(200,000)	-
Liquidation (increase) of time certificates of deposit	100,000	(100,000)
Interest income received	2,849	3,658
Net cash used in investing activities	(97,151)	(96,342)
Net change in cash and cash equivalents	26,143	94,230
Cash and cash equivalents at beginning of year	507,015	412,785
Cash and cash equivalents at end of year	\$ 533,158	\$ 507,015
Reconciliation of earnings from operations to net cash provided by operating activities:		
Earnings from operations	\$ 49,290	\$ 220,248
Adjustments to reconcile earnings from operations to net cash provided by operating activities:		
Depreciation	11,282	8,592
Changes in assets and liabilities:		
Increase(decrease) in premiums receivable	111,988	(131,625)
Increase in other receivables	(5,958)	(1,211)
Decrease in other assets	-	743
Increase (decrease) in medical claims and benefits payable	(70,599)	77,005
Increase in accounts payable and accrued expenses	3,005	3,880
Net cash provided by operating activities	\$ 99,008	\$ 177,632

See accompanying notes to financial statements.

CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements
September 30, 2012 and 2011

(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, 2012 and 2011

(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, 2012 and 2011, 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, 2012 and 2011

(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.

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, 2012 and 2011, the carrying amount of the Plan's cash and cash equivalents and time certificates of deposit was \$733,158 and \$807,015, respectively, and the corresponding bank balances were \$725,346 and \$821,690, respectively. Of the bank balance amounts, \$724,173 and \$820,621, respectively, were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. The remaining amounts of \$1,173 and \$1,069 as of September 30, 2012 and 2011, respectively, represent deposits maintained in dollar denominated bank accounts maintained offshore. As of September 30, 2012 and 2011, bank deposits in the amount of \$536,930 and \$579,568, 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.

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.

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.

CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements
September 30, 2012 and 2011

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During fiscal year 2012, the Plan implemented the following pronouncements:

- GASB 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 the frequency and timing of measurements for actuarial valuations first used to report funded status information in OPEB plan financial statements. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.
- GASB 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 implementation of this pronouncement did not have a material effect on the accompanying financial statements.

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 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 has not yet determined the effect of implementation of this statement on the financial statements of the Plan.

CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements
September 30, 2012 and 2011

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In April 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of the Plan.

In April 2012, GASB issued Statement No. 66, *Technical Corrections - 2012*, which enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of the Plan.

In June 2012, GASB issued Statement No. 67, *Financial Reporting for Pension Plans*, which revises existing guidance for the financial reports of most pension plans, and Statement No. 68, *Accounting and Financial Reporting for Pensions*, which revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The provisions in Statement 67 are effective for financial statements for periods beginning after June 15, 2013. The provisions in Statement 68 are effective for fiscal years beginning after June 15, 2014. Management has not yet determined the effect of implementation of these statements 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.

(3) Investments

Investments recorded at fair value are comprised of the following:

	<u>2012</u>	<u>2010</u>
Common stock	\$ 199,441	\$ 44,903
Money market funds	9,644	3,108
Fixed income securities	60,031	-
Other	<u>119</u>	<u>-</u>
	\$ <u>269,235</u>	\$ <u>48,011</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, 2012 and 2011.

CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements
September 30, 2012 and 2011

(3) Investments, Continued

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, 2012 and 2011, 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.

As of September 30, 2012, the Plan's investments in debt securities were as follows:

	Moody's Credit Rating	Investment Maturities (In Years)				Fair Value
		Less Than 1	1 to 5	6 to 10	Greater Than 10	
U.S. Treasury obligations	Aaa	\$ -	\$ 28,070	\$ 14,809	\$ -	\$ 42,879
U.S. Government Agencies: Federal National Mortgage Association	Aaa	<u>17,152</u>	-	-	-	<u>17,152</u>
		<u>\$ 17,152</u>	<u>\$ 28,070</u>	<u>\$ 14,809</u>	<u>\$ -</u>	<u>\$ 60,031</u>

(4) Property and Equipment

A summary of the Plan's property and equipment at September 30, 2012 and 2011, is as follows:

	Estimated Useful Lives	Balance at October 1, 2011	Transfers and Additions	Transfers and Deletions	Balance at September 30, 2012
Office furniture and equipment	5 - 10 years	\$ 41,407	\$ 8,272	\$ -	\$ 49,679
Vehicles	5 years	<u>56,660</u>	-	-	<u>56,660</u>
		98,067	8,272	-	106,339
Less accumulated depreciation		<u>(67,349)</u>	<u>(11,282)</u>	-	<u>(78,631)</u>
Property and equipment, net		<u>\$ 30,718</u>	<u>\$ (3,010)</u>	<u>\$ -</u>	<u>\$ 27,708</u>
		<u>\$ 33,854</u>	<u>\$ 7,553</u>	<u>\$ -</u>	<u>\$ 41,407</u>
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>56,660</u>
		83,514	14,553	-	98,067
Less accumulated depreciation		<u>(58,757)</u>	<u>(8,592)</u>	-	<u>(67,349)</u>
Property and equipment, net		<u>\$ 24,757</u>	<u>\$ 5,961</u>	<u>\$ -</u>	<u>\$ 30,718</u>

CHUUK STATE HEALTH CARE PLAN

Notes to Financial Statements
September 30, 2012 and 2011

(5) Related Parties

As of September 30, 2012 and 2011, premium receivables from Chuuk State Government amounted to \$23,913 and \$33,015, respectively, and related premium revenue earned for the years then ended amounted to \$779,491 and \$778,750, respectively. As of September 30, 2012 and 2011, 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 2012 and 2011, respectively, reflected the balance as noncurrent. At September 30, 2012 and 2011, the Plan has an outstanding receivable from Chuuk Public Utility Corporation of \$109,289 and \$113,714, respectively.

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, 2012, and have issued our report thereon dated June 13, 2013. Our report includes an explanatory paragraph concerning the receivable from the State of Chuuk. 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.

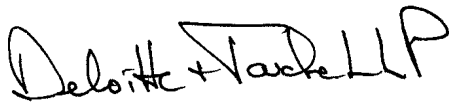
Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. 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, 2013.

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 + Tatchell LLP". The signature is written in a cursive, stylized font.

June 13, 2013

CHUUK STATE HEALTH CARE PLAN

Summary Schedule of Prior Year Findings
Year Ended September 30, 2012

There are no prior year findings unresolved as of September 30, 2012.