

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2012

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

YEAR ENDED SEPTEMBER 30, 2012

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**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**FINANCIAL STATEMENTS
YEAR ENDED SEPTEMBER 30, 2012**

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**FINANCIAL STATEMENTS
YEAR ENDED SEPTEMBER 30, 2012**

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**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2012

INDEPENDENT AUDITORS' REPORT

Honorable Johnson Elimo
Governor, State of Chuuk
Federated States of Micronesia:

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk (the State) as of and for the year ended September 30, 2012, which collectively comprise the State's basic financial statements as set forth in Section II of the foregoing table of contents. These financial statements are the responsibility of the management of the State. Our responsibility is to express opinions on these financial statements based on our audit.

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

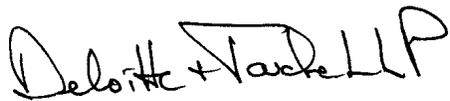
As discussed in Note 11 to the financial statements, the State has not recorded a liability for land leases and related claims payable in the governmental activities and the General Fund and, accordingly, has not recorded an expenditure/expense for the current period change in that liability. Accounting principles generally accepted in the United States of America require that liabilities incurred attributable to services already rendered and that are not contingent upon a specific event that is outside of the control of the State be accrued as liabilities and expenditures/expenses, which would increase the liabilities, decrease net assets, and change the expenses of the governmental activities and increase the liabilities, increase fund deficit, and change the expenditures of the General Fund. The amount by which this departure would affect the liabilities, net assets and expenses of the governmental activities and the liabilities, fund deficit, and expenditures of the General Fund is not reasonably determinable.

In our opinion, except for the effects of not recording a liability for land leases and related claims payable in the governmental activities and the General Fund, as discussed in the preceding paragraph, such financial statements, as set forth in Section II of the foregoing table of contents, present fairly, in all material respects, the respective financial position of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk as of September 30, 2012, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 24, 2013, on our consideration of the State's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 9, as well as the Schedule of Revenues, Expenditures, and Changes in Deficit - Budget and Actual - General Fund and notes thereto, as set forth in Section III of the foregoing table of contents, 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. 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State's financial statements. The combining and individual fund financial statements, as set forth in Section IV of the foregoing table of contents, are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining and individual fund financial statements, as set forth in Section IV of the foregoing table of contents, are fairly stated in all material respects in relation to the financial statements as a whole.

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

June 24, 2013

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2012

This analysis, prepared by the Department of Administrative Services, Division of Treasury, offers readers of the Chuuk State Government's (Chuuk State) financial statements a narrative overview of the activities of the government for the fiscal year ended September 30, 2012. We encourage readers to consider this information in conjunction with Chuuk State's financial statements, which follow. Fiscal year 2011 comparative information has been included, where appropriate. This analysis is required by the Governmental Accounting Standards Board, (GASB) which provides guidelines on what must be included and excluded from this analysis.

FINANCIAL HIGHLIGHTS

- For the fiscal year ended September 30, 2012, Chuuk State's total net assets increased by \$0.8 million (or 2.0%) from \$38.3 million in the prior year to \$39.1 million. This increase was primarily attributable to reduction of prior year liabilities and Chuuk State's revenues of \$36.44 million exceeding total expenses (\$35.65 million) by \$0.79 million.
- During fiscal year 2012, both revenues and expenses decreased from fiscal year 2011, by \$1.9 million (or 5.14%) and \$3.29 million (or 8.46%), respectively. Minor revenue decreases were attributable to the decline in Compact operating grants by \$2.5 million (8.8%) from fiscal year 2011. Expenses in fiscal year 2012 of \$35.65 million decreased by \$3.3 million (or 8.46%) from \$38.95 million in fiscal year 2011. Significant reductions were primarily in the education sector grant and municipal affairs.
- The General Fund deficit decreased by \$2.89 million in fiscal year 2012, decreasing from \$8.27 million in the prior year to \$5.38 million. The decrease is primarily the result of the State's robust general operating revenues and a transfer in of the prior assets held by the Compact Capital I fund reflected a small surplus even after repayment of ADB loan principal and interest (\$0.458 million).

OVERVIEW OF THE FINANCIAL STATEMENTS

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

Government-Wide Financial Statements

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

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis, Continued
September 30, 2012

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

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

Fund Financial Statements

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

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

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

FINANCIAL ANALYSIS OF CHUUK STATE AS A WHOLE

Net assets may serve over time as a useful indicator of a government's financial position. At the end of fiscal year 2012, Chuuk State's assets exceeded liabilities by \$39.1 million. However, all these net assets are restricted as to the purposes they can be used for or are invested in capital assets. Chuuk State uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although Chuuk State's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. The following summary of Chuuk State's net assets as of September 30, 2012, with comparable balances for fiscal year 2011, discloses this relationship.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis, Continued
September 30, 2012

	<u>2012</u>	<u>2011</u>	<u>Change</u>	<u>%</u>
Current and other non-capital assets	\$ 19,659,758	\$ 19,991,487	\$ (331,729)	(1.66)
Capital assets	<u>44,791,659</u>	<u>45,544,752</u>	<u>(753,093)</u>	(1.65)
Total Assets	<u>64,451,417</u>	<u>65,536,239</u>	<u>(1,084,822)</u>	(1.66)
Long-term liabilities	13,525,137	13,992,943	(467,806)	(3.34)
Other liabilities	<u>11,822,820</u>	<u>13,235,778</u>	<u>(1,412,958)</u>	(10.68)
Total Liabilities	<u>25,347,957</u>	<u>27,228,721</u>	<u>(1,880,764)</u>	(6.91)
Net Assets:				
Invested in capital assets	44,791,659	45,544,752	(753,093)	(1.65)
Restricted	19,328,760	20,367,882	(1,039,122)	(5.10)
Unrestricted	<u>(25,016,959)</u>	<u>(27,605,116)</u>	<u>2,588,157</u>	(9.38)
Total Net Assets	\$ <u>39,103,460</u>	\$ <u>38,307,518</u>	\$ <u>795,942</u>	2.08

At the end of fiscal year 2012, Chuuk State's unrestricted assets showed a deficit of \$25.02 million, a decrease of \$2.59 million from the prior year. This deficit is the result of having current and long-term commitments that are greater than currently available resources. Specifically, Chuuk State did not include in past annual budgets the full amounts needed to finance its current liabilities to municipalities, and others or its long-term liabilities arising from Asian Development Bank (ADB) loans and unused employee leave balances. Chuuk State will include these amounts in future years' budgets as funding permits.

Net assets increased \$0.80 million (or 2.08%) from the prior year. Key elements of the increase and the differences from the prior year are shown in the following schedule:

	<u>2012</u>	<u>2011</u>	<u>Change</u>	<u>%</u>
Revenues:				
Program Revenues:				
Charges for services	\$ 1,696,865	\$ 1,547,731	\$ 149,134	9.64
Operating grants and contributions	25,986,993	28,506,354	(2,519,361)	(8.84)
General Revenues:				
Taxes	5,882,505	5,809,622	72,883	1.25
Unrestricted investment earnings (losses)	740,417	(7,948)	748,365	9415.76
Other	<u>736,683</u>	<u>1,088,183</u>	<u>(351,500)</u>	(32.3)
Total revenues	<u>35,043,463</u>	<u>36,943,942</u>	<u>(1,900,479)</u>	(5.14)
Contributions to permanent fund	<u>1,405,096</u>	-	<u>1,405,096</u>	
Total revenues and contributions	<u>36,448,559</u>	<u>36,943,942</u>	<u>(495,383)</u>	(1.34)

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis, Continued
September 30, 2012

Expenses:				
General government	6,979,439	6,096,882	882,557	14.48
Health services	9,444,728	10,090,269	(645,541)	(6.40)
Education	11,170,011	14,324,701	(3,154,690)	(22.02)
Economic development	2,769,549	1,527,920	1,241,629	81.26
Public safety	1,007,517	849,268	158,249	18.63
Public works and transportation	2,543,562	2,360,942	182,620	7.74
Community affairs	35,587	33,430	2,157	6.45
Boards and commissions	413,917	538,849	(124,932)	(23.18)
Judiciary	451,622	402,335	49,287	12.25
Payments to component units	54,273	40,775	13,498	33.10
Municipal affairs	685,790	1,943,829	(1,258,039)	(64.72)
Other	86,843	507,936	(421,093)	(82.90)
Unallocated Interest	<u>9,779</u>	<u>228,678</u>	<u>(218,899)</u>	(95.72)
 Total expenses	 <u>35,652,617</u>	 <u>38,945,814</u>	 <u>(3,293,197)</u>	 (8.46)
 Change in net assets	 795,942	 (2,001,872)	 2,797,814	 (139.76)
 Net assets at the beginning of the year	 <u>38,307,518</u>	 <u>40,309,390</u>	 <u>(2,001,872)</u>	 (4.97)
 Net assets at the end of the year	 \$ <u>39,103,460</u>	 \$ <u>38,307,518</u>	 \$ <u>795,942</u>	 2.08

The detail indicates decreases in both revenue and expenses in fiscal year 2012, and the increase of net assets resulting in revenues exceeding expenses.

Revenues and contributions of \$36.44 million decreased by \$0.49 million (or 1.36%) from prior year \$36.94 million. The decrease was due to Compact revenues of \$25.97 million declining by \$2.52 million (or 8.8%) from \$28.51 million in fiscal year 2011. Despite the decrease, revenue sharing of \$3.23 million increased by \$0.13 million (or 3.93%) from fiscal 2011 of \$3.10 million. Combined local taxes, department charges, user fees and investment income of \$5.09 million in fiscal 2012, increased \$0.83 million (or 16.35%) from fiscal 2011's total of \$4.25 million. Both local revenue and revenue sharing proceeds benefited from the increased infrastructure construction projects.

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

SOURCE OF REVENUE	<u>2012</u>	<u>2011</u>
Compact funding	71.4%	77.1%
Investments	2.0%	(NM)
Revenue sharing	8.9%	8.4%
Federal and other grants	3.9%	0.0%
Taxes and fees	11.9%	11.5%
Other	<u>2.9%</u>	<u>1.0%</u>
 TOTAL	 <u>100.0%</u>	 <u>100.0%</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis, Continued
September 30, 2012

Notwithstanding the increases in both revenues shares passed through to the State and local tax and fee collections reduce the dependency on Compact funding, the predominance of sector funding as 71.4% of total revenue highlights the importance of optimizing sector grant utilization.

Expenses decreased by \$3.29 million (or 8.46%), from \$38.95 million in the prior fiscal year to \$35.65 million in fiscal year 2012. The most notable decreases in fiscal year 2012 was in the education sector where expenses of \$11.17 million decreased by 22% from \$14.32 million and municipal payments of \$0.65 million decreased by 64.7% from \$1.94 million in the prior year.

FINANCIAL ANALYSIS OF CHUUK STATE'S FUNDS

As noted earlier, Chuuk State uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. As of the end of fiscal year 2012, Chuuk State's governmental funds reported a combined fund balance of \$8.65 million, which represents a \$1.08 million increase (or 14.2%) from the \$7.57 million fund balance recorded at the end of fiscal 2011. Of this total combined fund balance, \$11.57 million is nonspendable because it is legally restricted to other purposes and \$9.25 million is restricted or committed to fund specific fund-related activities. These non-spendable and restricted fund balances are off-set by a combined unassigned fund deficit of \$12.18 million.

Footnote 10 of the financial statements gives further details of the fund balance components of Chuuk State's balance sheet.

GENERAL FUND BUDGETARY HIGHLIGHTS

In fiscal year 2012, actual revenues of \$8.95 million exceeded budgeted revenues of \$6.75 million by \$2.2 million. Actual expenditures of \$8.07 million were greater than budgetary appropriations of \$7.47 million by \$0.60 million, resulting in an overall excess of revenues over expenditures of \$1.6 million. When combined with the transfer out to the infrastructure maintenance fund (\$0.46 million), and a transfer in from the Compact Capital I fund, the net change in unreserved fund deficit on a budgetary basis was a positive \$3.86 million. In accord with the principles of budgetary accounting, the deficit includes encumbrances for which goods or services had not been received (\$0.62 million), the net change in unreserved fund deficit on a budgetary basis was a positive of \$4.48 million.

Chuuk State retains a balanced operating budget but debt financing activities of the State that are not budgeted have negative impacts on overall State operations. In fiscal year 2012, principal and debt service charges on ADB loans of \$0.46 million contributed to the deficiency.

CAPITAL ASSET AND DEBT ADMINISTRATION

Chuuk State's investment in capital assets for the primary government as of September 30, 2012, amounted to \$118.6 million, net of accumulated depreciation of \$73.8 million, leaving a net book value of \$44.8 million. This represents a net decrease of \$0.75 million (or 1.7%) from fiscal year 2011. Chuuk State recorded major additions of \$2.5 million in 2012 related to buildings of \$1.8 million, vehicles and other equipment of \$0.5 million, and land of \$0.2 million, but current year depreciation charges of \$3.25 million resulted minor net increase. The table below summarizes Chuuk State's net capital assets:

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis, Continued
September 30, 2012

	<u>2012</u>	<u>2011</u>	<u>Change</u>	<u>%</u>
Land	\$ 17,948,262	\$ 17,721,622	\$ 226,640	1.28
Airport Facilities	10,674,578	11,627,263	(952,685)	(8.19)
Buildings	5,652,625	4,140,384	1,512,241	36.52
Seaport Facilities	6,629,303	7,292,233	(662,930)	(9.09)
Vehicles/ Equipment	2,897,870	2,785,208	112,662	4.05
Infrastructure	<u>989,021</u>	<u>1,978,042</u>	<u>(989,021)</u>	(50.00)
	<u>\$ 44,791,659</u>	<u>\$ 45,544,752</u>	<u>\$ (753,093)</u>	(1.65)

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

Long -Term Debt

The following schedule shows Chuuk State's summarized long-term debt for fiscal year 2012 and comparable amounts for fiscal year 2011.

	<u>2012</u>	<u>2011</u>	<u>Change</u>	<u>%</u>
ADB Water Supply Loan (1459)	\$ 4,052,173	\$ 4,144,208	\$ (92,035)	(2.22)
ADB Early Retirement Loan (1520)	5,512,255	5,624,605	(112,350)	(2.00)
ADB Private Sector Reform Program Loan (1873)	600,747	673,091	(72,344)	(10.75)
ADB Private Sector Reform Program Loan (1874)	1,190,915	1,249,258	(58,343)	(4.67)
ADB Basic Social Services Program Loan (1816)	<u>920,304</u>	<u>1,033,366</u>	<u>(113,062)</u>	(10.94)
	<u>\$ 12,276,394</u>	<u>\$ 12,724,528</u>	<u>\$ (448,134)</u>	(3.52)

Long-term debt decreased by \$0.448 million (or 3.52%) in fiscal year 2012 as the result of loan repayments resulting to gradual debts reductions.

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

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Chuuk economy in fiscal year 2013 continues to perform at levels seen in fiscal 2012 with revenue collections trending expected to remain same in prior year. As a result, State policymakers have cautiously kept general fund budgets capped within actual revenue collections, both in fiscal years 2013 and for the 2014 annual appropriation act. Revenue collections in excess of these fiscal ceilings will be used for debt relief payments of Chuuk's old liabilities.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis, Continued
September 30, 2012

CONTACTING CHUUK STATE'S FINANCIAL MANAGEMENT

The financial report is designed to provide our citizens, taxpayers, customers, and investments and creditors, a general overview of Chuuk State's finances to demonstrate its accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Director, Office of Administrative Services, P.O. Box 849, Weno, Chuuk FM 96942

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Net Assets
September 30, 2012

	Primary Government	Component Units
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ 1,083,616	\$ 676,916
Time certificates of deposit	-	200,000
Equity interest in internal investment pool	109,388	269,235
Receivables, net of allowance for uncollectibles	825,930	830,419
Inventories	-	316,094
Due from primary government	-	967
Prepayments	530,772	-
Restricted assets:		
Cash and cash equivalents	2,289,110	-
Total current assets	4,838,816	2,293,631
Noncurrent assets:		
Restricted assets:		
Investments	13,270,942	-
Investments	1,550,000	-
Deposits	-	536,262
Capital assets:		
Nondepreciable capital assets	17,948,262	1,813,695
Capital assets, net of accumulated depreciation	26,843,397	2,546,272
Total noncurrent assets	59,612,601	4,896,229
Total assets	\$ 64,451,417	\$ 7,189,860
<u>LIABILITIES</u>		
Current liabilities:		
Current portion of long-term debt	\$ 360,998	\$ 50,059
Note payable	561,987	732,898
Accrued interest payable	175,576	-
Accounts payable	1,633,381	491,666
Land acquisition payable	8,618,545	-
Compensated absences payable	450,000	-
Other liabilities and accruals	21,366	2,266,823
Due to component units	967	-
Deferred revenues	-	68,020
Total current liabilities	11,822,820	3,609,466
Noncurrent liabilities:		
Noncurrent portion of long-term obligations	11,915,396	2,185,077
Compensated absences payable, net of current portion	1,609,741	-
Total noncurrent liabilities	13,525,137	2,185,077
Total liabilities	25,347,957	5,794,543
<u>NET ASSETS</u>		
Invested in capital assets, net of related debt	44,791,659	1,307,186
Restricted for:		
Nonexpendable:		
Future operations	9,493,531	-
Expendable:		
Compact related	6,032,259	-
Debt service	3,777,411	-
Other purposes	25,559	582,401
Unrestricted	(25,016,959)	(494,270)
Total net assets	39,103,460	1,395,317
Total liabilities and net assets	\$ 64,451,417	\$ 7,189,860

See accompanying notes to financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Activities
Year Ended September 30, 2012

Functions/Programs	Program Revenues				Net (Expenses) Revenues and Changes in Net Assets	
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government	Component Units
Primary government:						
Governmental activities:						
General government	\$ 6,979,439	\$ 959,361	\$ 2,855,763	\$ -	\$ (3,164,315)	\$ -
Health services	9,444,728	102,683	9,075,000	-	(267,045)	-
Education	11,170,011	-	11,970,707	-	800,696	-
Economic development	2,769,549	-	1,437,000	-	(1,332,549)	-
Public safety	1,007,517	45,288	-	-	(962,229)	-
Public works and transportation	2,543,562	570,720	648,523	-	(1,324,319)	-
Community affairs	35,587	-	-	-	(35,587)	-
Boards and commissions	413,917	-	-	-	(413,917)	-
Judiciary	451,622	18,813	-	-	(432,809)	-
Payments to component units	54,273	-	-	-	(54,273)	-
Municipal affairs	685,790	-	-	-	(685,790)	-
Unallocated interest on long-term debt	9,779	-	-	-	(9,779)	-
Other	86,843	-	-	-	(86,843)	-
Total primary government	\$ 35,652,617	\$ 1,696,865	\$ 25,986,993	\$ -	(7,968,759)	-
Component units:						
Chuuk State Health Care Plan	\$ 1,052,470	\$ 1,101,760	\$ -	\$ 8,272	-	57,562
Chuuk Public Utility Corporation	5,676,006	5,357,313	-	661,509	-	342,816
Chuuk State Housing Authority	153,307	84,056	-	-	-	(69,251)
Total component units	\$ 6,881,783	\$ 6,543,129	\$ -	\$ 669,781	-	331,127
General revenues:						
Taxes:						
FSM revenue sharing:						
Gross revenue taxes					1,187,776	-
Import taxes					998,930	-
Income taxes					930,242	-
Other taxes					113,339	-
State taxes:						
Sales tax					2,604,533	-
Other excise taxes					47,685	-
Unrestricted investment income					740,417	-
Other					736,683	112,108
Total general revenues					7,359,605	112,108
Contributions to permanent fund					1,405,096	-
Change in net assets					795,942	443,235
Net assets at the beginning of the year					38,307,518	952,082
Net assets at the end of the year					\$ 39,103,460	\$ 1,395,317

See accompanying notes to financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Balance Sheet
Governmental Funds
September 30, 2012

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
<u>ASSETS</u>					
Cash and cash equivalents	\$ 1,083,616	\$ -	\$ -	\$ -	\$ 1,083,616
Equity interest in internal investment pool	109,388	-	-	-	109,388
Investments	1,550,000	-	-	-	1,550,000
Receivables, net	761,517	64,413	-	-	825,930
Prepayments	348,413	179,461	-	2,898	530,772
Due from other funds	961,611	6,097,134	-	22,950	7,081,695
Restricted assets:					
Cash and cash equivalents	2,289,110	-	-	-	2,289,110
Investments	3,777,411	-	9,493,531	-	13,270,942
Total assets	<u>\$ 10,881,066</u>	<u>\$ 6,341,008</u>	<u>\$ 9,493,531</u>	<u>\$ 25,848</u>	<u>\$ 26,741,453</u>
<u>LIABILITIES AND FUND BALANCES (DEFICIT)</u>					
Liabilities:					
Accounts payable	\$ 768,333	\$ 864,759	\$ -	\$ 289	\$ 1,633,381
Accrued liabilities	21,366	-	-	-	21,366
Land acquisition payable	8,618,545	-	-	-	8,618,545
Note payable	561,987	-	-	-	561,987
Accrued interest payable	175,576	-	-	-	175,576
Due to component units	967	-	-	-	967
Due to other funds	6,120,084	961,611	-	-	7,081,695
Total liabilities	<u>16,266,858</u>	<u>1,826,370</u>	<u>-</u>	<u>289</u>	<u>18,093,517</u>
Fund balances (deficit):					
Nonspendable	1,898,413	179,461	9,493,531	-	11,571,405
Restricted	3,777,411	5,449,932	-	-	9,227,343
Committed	-	-	-	25,559	25,559
Unassigned:					
General fund	(11,061,616)	-	-	-	(11,061,616)
Special revenue funds	-	(1,114,755)	-	-	(1,114,755)
Total fund balances (deficit)	<u>(5,385,792)</u>	<u>4,514,638</u>	<u>9,493,531</u>	<u>25,559</u>	<u>8,647,936</u>
Total liabilities and fund balances (deficit)	<u>\$ 10,881,066</u>	<u>\$ 6,341,008</u>	<u>\$ 9,493,531</u>	<u>\$ 25,848</u>	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are reported in the funds	44,791,659
Long-term liabilities, including loans payable, are not due and payable in the current period and, therefore, are not reported in the funds. The liabilities include:	
Long-term obligations	(12,276,394)
Compensated absences	(2,059,741)
	(14,336,135)
Net assets of governmental activities	\$ 39,103,460

See accompanying notes to financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures, and Changes in Fund Balances (Deficit)
Governmental Funds
Year Ended September 30, 2012

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
Revenues:					
Compact funding	\$ -	\$ 25,887,730	\$ -	\$ -	\$ 25,887,730
Net change in the fair value of investments	740,417	-	1,405,096	-	2,145,513
Federal contributions and other grants	-	99,263	-	-	99,263
FSM revenue sharing	3,230,287	-	-	-	3,230,287
State taxes	2,652,218	-	-	-	2,652,218
Fees and charges	1,594,182	-	-	102,683	1,696,865
Other	736,683	-	-	-	736,683
Total revenues	<u>8,953,787</u>	<u>25,986,993</u>	<u>1,405,096</u>	<u>102,683</u>	<u>36,448,559</u>
Expenditures:					
Current:					
General government	3,761,913	2,357,216	-	-	6,119,129
Health services	-	9,400,764	-	118,524	9,519,288
Education	-	12,895,628	-	-	12,895,628
Economic development	86,162	2,683,387	-	-	2,769,549
Public safety	953,401	45,692	-	-	999,093
Public works and transportation	883,145	-	-	-	883,145
Community affairs	35,587	-	-	-	35,587
Boards and commissions	413,917	-	-	-	413,917
Judiciary	451,622	-	-	-	451,622
Payments to component units	54,273	-	-	-	54,273
Municipal affairs	685,790	-	-	-	685,790
Other	86,843	-	-	-	86,843
Debt service	457,913	-	-	-	457,913
Total expenditures	<u>7,870,566</u>	<u>27,382,687</u>	<u>-</u>	<u>118,524</u>	<u>35,371,777</u>
Excess (deficiency) of revenues over (under) expenditures	<u>1,083,221</u>	<u>(1,395,694)</u>	<u>1,405,096</u>	<u>(15,841)</u>	<u>1,076,782</u>
Other financing sources (uses):					
Operating transfers in	2,258,772	460,233	-	-	2,719,005
Operating transfers out	(460,233)	(2,258,772)	-	-	(2,719,005)
Total other financing sources (uses), net	<u>1,798,539</u>	<u>(1,798,539)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balances (deficit)	2,881,760	(3,194,233)	1,405,096	(15,841)	1,076,782
Fund balances (deficit) at the beginning of the year	<u>(8,267,552)</u>	<u>7,708,871</u>	<u>8,088,435</u>	<u>41,400</u>	<u>7,571,154</u>
Fund balances (deficit) at the end of the year	<u>\$ (5,385,792)</u>	<u>\$ 4,514,638</u>	<u>\$ 9,493,531</u>	<u>\$ 25,559</u>	<u>\$ 8,647,936</u>

See accompanying notes to financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Reconciliation of the Statement of Revenues, Expenditures,
and Changes in Fund Balances of Governmental Funds
to the Statement of Activities
Year Ended September 30, 2012

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

Net change in fund balances - total governmental funds	\$ 1,076,782
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Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

This is the amount by which depreciation exceeded capital outlays in the current period	(753,093)
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The incurrence of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction has any effect on net assets. For the current year, these amounts consist of:

Repayment of ADB Loans	448,134
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Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds. For the current year, these activities consist of:

Change in compensated absences	<u>24,119</u>
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Change in net assets of governmental activities	\$ <u>795,942</u>
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See accompanying notes to financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**DISCRETELY PRESENTED COMPONENT UNITS
Combining Statement of Net Assets (Deficiency)
September 30, 2012**

<u>ASSETS</u>	Chuuk State Health Care Plan	Chuuk Public Utility Corporation	Chuuk State Housing Authority	Total
Current assets:				
Cash and cash equivalents	\$ 533,158	\$ 47,626	\$ 96,132	\$ 676,916
Time certificates of deposit	200,000	-	-	200,000
Investments	269,235	-	-	269,235
Receivables, net	232,695	312,479	285,245	830,419
Inventories	-	316,094	-	316,094
Due from primary government	-	-	967	967
	<hr/>	<hr/>	<hr/>	<hr/>
Total current assets	1,235,088	676,199	382,344	2,293,631
Noncurrent assets:				
Deposits	-	536,262	-	536,262
Capital assets:				
Nondepreciable capital assets	-	1,813,695	-	1,813,695
Capital assets, net of accumulated depreciation	27,708	2,433,817	84,747	2,546,272
	<hr/>	<hr/>	<hr/>	<hr/>
Total assets	\$ 1,262,796	\$ 5,459,973	\$ 467,091	\$ 7,189,860
	<hr/>	<hr/>	<hr/>	<hr/>
<u>LIABILITIES AND NET ASSETS</u>				
Current liabilities:				
Notes payable	\$ -	\$ 732,898	\$ -	\$ 732,898
Current portion of long-term debt	-	50,059	-	50,059
Accounts payable	38,265	444,528	8,873	491,666
Accrued liabilities	11,776	2,255,047	-	2,266,823
Deferred income	-	68,020	-	68,020
	<hr/>	<hr/>	<hr/>	<hr/>
Total current liabilities	50,041	3,550,552	8,873	3,609,466
Noncurrent liabilities:				
Noncurrent portion of long-term debt	-	2,185,077	-	2,185,077
	<hr/>	<hr/>	<hr/>	<hr/>
Total liabilities	50,041	5,735,629	8,873	5,794,543
Net assets (deficiency):				
Invested in capital assets, net of related debt	27,708	1,279,478	-	1,307,186
Restricted	-	582,401	-	582,401
Unrestricted	1,185,047	(2,137,535)	458,218	(494,270)
	<hr/>	<hr/>	<hr/>	<hr/>
Total net assets (deficiency)	1,212,755	(275,656)	458,218	1,395,317
	<hr/>	<hr/>	<hr/>	<hr/>
Total liabilities and net assets (deficiency)	\$ 1,262,796	\$ 5,459,973	\$ 467,091	\$ 7,189,860
	<hr/>	<hr/>	<hr/>	<hr/>

See accompanying notes to financial statements.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

**DISCRETELY PRESENTED COMPONENT UNITS
Combining Statement of Revenues, Expenses, and Changes in Net Assets (Deficiency)
Year Ended September 30, 2012**

	Chuuk State Health Care Plan	Chuuk Public Utility Corporation	Chuuk State Housing Authority	Total
Operating revenues:				
Charges for services	\$ 1,095,027	\$ 5,246,951	\$ 84,056	\$ 6,426,034
Other	6,733	110,362	-	117,095
Total operating revenues	<u>1,101,760</u>	<u>5,357,313</u>	<u>84,056</u>	<u>6,543,129</u>
Operating expenses:				
Cost of services	806,379	4,180,611	-	4,986,990
Depreciation	11,282	376,801	-	388,083
Administration and general	234,809	1,118,594	153,307	1,506,710
Total operating expenses	<u>1,052,470</u>	<u>5,676,006</u>	<u>153,307</u>	<u>6,881,783</u>
Operating income (loss)	<u>49,290</u>	<u>(318,693)</u>	<u>(69,251)</u>	<u>(338,654)</u>
Nonoperating revenues (expenses):				
Other income (loss)	24,286	190,000	-	214,286
Interest expense	24,073	(126,251)	-	(102,178)
Total nonoperating revenues (expenses), net	<u>48,359</u>	<u>63,749</u>	<u>-</u>	<u>112,108</u>
Net income (loss) before capital contributions	97,649	(254,944)	(69,251)	(226,546)
Capital contributions	<u>8,272</u>	<u>661,509</u>	<u>-</u>	<u>669,781</u>
Change in net assets (deficiency)	105,921	406,565	(69,251)	443,235
Net assets (deficiency) at the beginning of the year	<u>1,106,834</u>	<u>(682,221)</u>	<u>527,469</u>	<u>952,082</u>
Net assets (deficiency) at the end of the year	<u>\$ 1,212,755</u>	<u>\$ (275,656)</u>	<u>\$ 458,218</u>	<u>\$ 1,395,317</u>

See accompanying notes to financial statements.

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies

The State of Chuuk (the State) was constituted on October 1, 1984, under the provisions of the Chuuk State Constitution (the Constitution) as approved by the people of Chuuk. The Constitution provides for the separation of powers of the executive, legislative, and judicial branches of the government.

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

A. Reporting Entity

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

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

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

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

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

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

i. Discretely Presented Component Units

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

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

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

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

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

ii. Omitted Governmental Funds

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

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

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

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

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

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

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

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

ii. Omitted Governmental Funds, Continued

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

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

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

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

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

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

iii. Omitted Component Units

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

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

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

B. Government-Wide Financial Statements

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements, Continued

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

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

The government-wide Statement of Net Assets reports \$19,328,760 of restricted net assets, of which \$25,559 is restricted by enabling legislation.

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

C. Fund Financial Statements

The fund financial statements present a balance sheet and a statement of revenues, expenditures, and changes in fund balances for its major and aggregated non-major funds. Major individual governmental funds are reported as separate columns in the fund financial statements pursuant to GASB reporting standards, with nonmajor governmental funds being combined into a single column.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

C. Fund Financial Statements, Continued

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

D. Measurement Focus and Basis of Accounting

Government-Wide Financial Statements:

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

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

Governmental Fund Financial Statements:

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

Component Unit Financial Statements:

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

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

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

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

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

E. Reporting Standards

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

F. Cash and Cash Equivalents and Time Certificates of Deposit

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

G. Investments

Investments and related investment earnings of the primary government and the discretely presented component units 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.

H. Receivables

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

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

I. Prepaid Items

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

J. Interfund Receivables/Payables

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

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

STATE OF CHUUK
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Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

K. Restricted Assets

Certain assets of the primary government are classified as restricted assets because their use is completely restricted through loan agreements or enabling legislation. Specifically, the State has collateralized Asian Development Bank loan proceeds and earnings for the Chuuk State Early Retirement Scheme with investments recorded in the General Fund of \$3,777,411. Furthermore, investments recorded in the Compact Trust Fund of \$9,493,531 are restricted in that they are not available to be used in current operations.

As of September 30, 2012, cash and cash equivalents of the primary government were restricted for the following uses:

Savings account established in accordance with Section 211(d)(2) of the Compact of Free Association, as amended, for the purpose of funding the State's infrastructure maintenance plan	\$ 1,537,869
Deposit accounts established for the purpose of receiving payments pursuant to the Compact of Free Association, as amended	<u>751,241</u>
	\$ <u>2,289,110</u>

L. Capital Assets

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

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

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

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

M. Interfund/Intrafund Transactions

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

N. Compensated Absences

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

O. Fund Balance

Fund balance classifications are based on the extent to which the State is bound to honor constraints on the specific purposes for which amounts in those funds can be spent and are reported under the following fund balance classifications:

- Non-spendable - includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.
- Restricted - includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.
- Committed - includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision making authority and does not lapse at year-end.
- Assigned - includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed.
- Unassigned includes negative fund balances in other governmental funds.

The State has a general policy to first use restricted resources for expenditures incurred for which both restricted and unrestricted (committed, assigned, and unassigned) resources are available. When expenditures are incurred for which only unrestricted resources are available, the general policy of the State is to use committed resources first, followed by assigned, and then unassigned. The use of restricted/committed resources may be deferred based on a review of the specific transaction.

A formal minimum fund balance policy has not been adopted.

**STATE OF CHUUK
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Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

P. Risk Financing

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

Q. Estimates

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

R. New Accounting Standards

During fiscal year 2012, the State 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 State.

**STATE OF CHUUK
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Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

R. New Accounting Standards, Continued

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 State.

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 State.

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 State.

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 State.

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 State.

**STATE OF CHUUK
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Notes to Financial Statements
September 30, 2012

(1) Summary of Significant Accounting Policies, Continued

R. New Accounting Standards, Continued

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 State.

S. Total Columns

Total columns are presented primarily to facilitate financial analysis. The Management's Discussion and Analysis includes certain prior year summarized comparative information in total. Such information does not include sufficient detail to constitute a full comparative presentation. Accordingly, such information should be read in conjunction with the State's financial statements for the year ended September 30, 2011 from which summarized information was derived.

(2) Deposits and Investments

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

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(2) Deposits and Investments, Continued

iii. Bonds - Confined to issues rated "A" or higher by a national rating service, except in the case of U.S. Treasury or government agency obligations which are not rated.

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

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

A. Deposits

Custodial credit risk is the risk that in the event of a bank failure, the State's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The State does not have a deposit policy for custodial credit risk or foreign currency risk.

As of September 30, 2012, the carrying amount of the primary government's total cash and cash equivalents were \$3,372,726 and the corresponding bank balances were \$5,174,218, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2012, bank deposits in the amount of \$4,616,415 were FDIC insured. The State does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

As of September 30, 2012, the carrying amount of the discretely presented component units' total cash and cash equivalents and time certificates of deposit was \$876,916 and the corresponding bank balances were \$999,143, which were maintained in financial institutions subject to FDIC insurance. As of September 30, 2012, bank deposits in the amount of \$876,916 were FDIC insured. The component units do not require collateralization of their cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Therefore, these deposits are exposed to custodial credit risk.

B. Investments

As of September 30, 2012, the State's investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	\$ 758,590
Other investments:	
Domestic equities	12,512,352
Cash management account	<u>109,388</u>
	\$ <u><u>13,380,330</u></u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(2) Deposits and Investments, Continued

B. Investments, Continued

As of September 30, 2012, the General Fund has an Automated Cash Management account with the Bank of Hawaii in the amount of \$109,388.

As of September 30, 2012, the General Fund holds 11% of the shares of the Bank of the Federated States of Micronesia in the amount of \$1,000,000, 3.8% of the shares of the Pacific Islands Development Bank in the amount of \$250,000, and 1% of the shares of the FSM Development Bank in the amount of \$300,000. As the fair market value of these investments is not readily available, such have been recorded at cost.

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

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the State will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The State's investments are held and administered by trustees. Based on negotiated trust and custody contracts, all of these investments were held in the State's name by the State's custodial financial institutions at September 30, 2012.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the State. As of September 30, 2012, the State did not hold an investment in any one issuer that represented more than 5% of the State's total investments.

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(2) Deposits and Investments, Continued

B. Investments, Continued

As of September 30, 2012, the State's fixed income securities, including their Moody's Investors Service credit ratings, had the following maturities:

Investment Type	Investment Maturities (In Years)					Credit Ratings
	Fair Value	Current	1-5	6-10	Over 10	
U.S. Treasury Notes and Bonds	\$ 42,210	\$ 23,479	\$ 4,550	\$ 14,181	\$ -	AAA
U.S. Government Agencies Obligations:						
Federal Home Loan Mortgage Corporation	130,883	-	1,073	31,082	98,728	AAA
Government National Mortgage	16,238	13,377	-	-	2,861	AAA
Federal National Mortgage Association	100,624	-	13,679	-	86,945	AAA
Tennessee Valley Authority	28,354	-	-	14,915	13,439	AAA
Housing Urban Development	21,024	-	21,024	-	-	No Rating
AID-TUNISIA	30,824	-	14,524	16,300	-	No Rating
Municipal Obligations	8,979	-	-	-	8,979	A2
Municipal Obligations	37,721	-	6,071	19,199	12,451	Aa1
Municipal Obligations	10,685	-	-	-	10,685	Aa2
Municipal Obligations	15,222	15,222	-	-	-	No rating
Municipal Obligations	7,307	7,307	-	-	-	WR
Corporate Bonds	18,461	-	-	-	18,461	A1
Corporate Bonds	26,859	-	26,859	-	-	A2
Corporate Bonds	47,618	11,326	36,292	-	-	A3
Corporate Bonds	22,540	18,373	-	4,167	-	Aa1
Corporate Bonds	47,271	-	24,145	7,499	15,627	Aa2
Corporate Bonds	65,317	6,640	22,495	13,921	22,261	Aaa
Corporate Bonds	32,799	13,899	18,900	-	-	Baa1
Corporate Bonds	15,516	-	7,625	-	7,891	Baa2
Corporate Bonds	<u>32,138</u>	<u>14,176</u>	<u>-</u>	<u>17,962</u>	<u>-</u>	No rating
	\$ <u>758,590</u>	\$ <u>123,799</u>	\$ <u>197,237</u>	\$ <u>139,226</u>	\$ <u>298,328</u>	

Discretely Presented Component Units

As of September 30, 2012, investments at fair value comprise the following:

Chuuk State Health Care Plan (CSHCP):

Fixed income securities:

Domestic fixed income \$ 60,150

Other investments:

Domestic equities 199,441

Money market funds 9,644

\$ 269,235

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(2) Deposits and Investments, Continued

B. Investments, Continued

Discretely Presented Component Units, Continued

Chuuk State Health Care Plan (CSHCP), Continued:

As of September 30, 2012, CSHCP's fixed income securities, including their Moody's Investors Service credit ratings, had the following maturities:

Investment Type	Investment Maturities (In Years)					Credit Ratings
	Fair Value	Current	1-5	6-10	Over 10	
U.S. Treasury Notes and Bonds	\$ 42,974	\$ -	\$ 28,128	\$ 14,846	\$ -	AAA
U.S. Government Agencies Obligations:						
Federal National Mortgage Association	17,176	17,176	-	-	-	AAA
	<u>\$ 60,150</u>	<u>\$ 17,176</u>	<u>\$ 28,128</u>	<u>\$ 14,846</u>	<u>\$ -</u>	

(3) Receivables

Primary Government

Receivables as of September 30, 2012, for the primary government's individual major funds and nonmajor funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	General	Grants Assistance	Total
Receivables:			
General receivables	\$ 375,216	\$ 64,413	\$ 439,629
FSM National Government	<u>626,045</u>	<u>-</u>	<u>626,045</u>
	1,001,261	64,413	1,065,674
Less: allowance for uncollectible accounts	<u>(239,744)</u>	<u>-</u>	<u>(239,744)</u>
Net receivables	<u>\$ 761,517</u>	<u>\$ 64,413</u>	<u>\$ 825,930</u>

Discretely Presented Component Units

Receivables as of September 30, 2012, for the discretely presented component units in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	Chuuk State Health Care Plan	Chuuk Public Utility Corporation	Chuuk State Housing Authority	Total
Receivables:				
General	\$ 211,136	\$ 500,441	\$ 2,182,301	\$ 2,893,878
Other	<u>64,431</u>	<u>69,945</u>	<u>-</u>	<u>134,376</u>
	275,567	570,386	2,182,301	3,028,254
Allowance for uncollectable accounts	<u>(42,872)</u>	<u>(257,907)</u>	<u>(1,897,056)</u>	<u>(2,197,835)</u>
	<u>\$ 232,695</u>	<u>\$ 312,479</u>	<u>\$ 285,245</u>	<u>\$ 830,419</u>

**STATE OF CHUUK
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Notes to Financial Statements
September 30, 2012

(4) Interfund Receivables and Payables

Receivables and payables between funds reflected as due to/from other funds in the combined balance sheet at September 30, 2012, are summarized as follows:

Receivable Fund	Payable Fund	Amount
Grants Assistance	General	\$ 6,097,134
General	Grants Assistance	961,611
Nonmajor governmental funds	General	<u>22,950</u>
		<u>\$ 7,081,695</u>

(5) Capital Assets

Capital asset activities for the year ended September 30, 2012, are as follows:

Primary Government

	Balance October <u>1, 2011</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2012</u>
Governmental activities:				
Depreciable assets:				
Airport facilities	\$ 38,107,415	\$ -	\$ -	\$ 38,107,415
Buildings	10,215,030	1,754,979	-	11,970,009
Seaport facilities	26,517,208	-	-	26,517,208
Vehicles and other equipment	8,699,391	517,154	-	9,216,545
Infrastructure	<u>14,835,315</u>	<u>-</u>	<u>-</u>	<u>14,835,315</u>
	<u>98,374,359</u>	<u>2,272,133</u>	<u>-</u>	<u>100,646,492</u>
Less accumulated depreciation for:				
Airport facilities	(26,480,152)	(952,685)	-	(27,432,837)
Buildings	(6,074,646)	(242,738)	-	(6,317,384)
Seaport facilities	(19,224,975)	(662,930)	-	(19,887,905)
Vehicles and other equipment	(5,914,183)	(404,492)	-	(6,318,675)
Infrastructure	<u>(12,857,273)</u>	<u>(989,021)</u>	<u>-</u>	<u>(13,846,294)</u>
	<u>(70,551,229)</u>	<u>(3,251,866)</u>	<u>-</u>	<u>(73,803,095)</u>
	<u>27,823,130</u>	<u>(979,733)</u>	<u>-</u>	<u>26,843,397</u>
Nondepreciable assets:				
Land	<u>17,721,622</u>	<u>226,640</u>	<u>-</u>	<u>17,948,262</u>
	<u>\$ 45,544,752</u>	<u>\$ (753,093)</u>	<u>\$ -</u>	<u>\$ 44,791,659</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(5) Capital Assets, Continued

Primary Government, Continued

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

General government	\$ 1,203,288
Health services	240,392
Education	139,345
Public safety	8,424
Public works and transportation	<u>1,660,417</u>
	<u>\$ 3,251,866</u>

Discretely Presented Component Units

	Balance October <u>1, 2011</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2012</u>
Depreciable assets:				
Buildings	\$ 415,089	\$ -	\$ -	\$ 415,089
Utility plant	25,228,964	2,189,108	(2,065,623)	25,352,449
Machinery, equipment, others	<u>245,962</u>	<u>8,272</u>	<u>-</u>	<u>254,234</u>
	25,890,015	2,197,380	(2,065,623)	26,021,772
Less accumulated depreciation	<u>(25,134,321)</u>	<u>(388,103)</u>	<u>2,046,924</u>	<u>(23,475,500)</u>
	755,694	1,809,277	(18,699)	2,546,272
Nondepreciable assets:				
Construction work-in-progress	<u>1,452,851</u>	<u>2,381,883</u>	<u>(1,978,591)</u>	<u>1,856,143</u>
	<u>\$ 2,208,545</u>	<u>\$ 4,191,160</u>	<u>\$ (1,977,290)</u>	<u>\$ 4,402,415</u>

(6) Short-Term Debt

Primary Government

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

No activity in short-term debt of the primary government occurred during the year ended September 30, 2012.

Discretely Presented Component Units

Chuuk Public Utility Corporation (CPUC):

Note payable to a commercial bank on an original line of credit of \$150,000 bearing interest of 7.25% per annum. The loan is collateralized by a security interest in fixed assets, accounts receivable and inventories and is past due, and is therefore presented as a current liability. \$ 81,921

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(6) Short-Term Debt, Continued

Discretely Presented Component Units, Continued

Chuuk Public Utility Corporation (CPUC), Continued:

Note payable to the Federated States of Micronesia Development Bank on an amount drawn with an available total of \$737,743 bearing interest of 9% per annum with principal installments of \$4,000 per month. Proceeds from the note were used for cash power meters and other equipment purchases and is collateralized by major machinery, equipment and assignment of income. The loan requires that CPUC maintain hazard insurance which has not been obtained. As a result, this note is presented as a current liability.

650,977

\$ 732,898

Changes in short-term debt of the discretely presented component units are as follows:

	Balance October 1, <u>2011</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2012</u>
Notes payable:				
CPUC	\$ <u>778,805</u>	\$ <u> -</u>	\$ <u>(45,907)</u>	\$ <u>732,898</u>

(7) Long-Term Obligations

Primary Government

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

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

Funds for the repayment of the ADB loan are expected to be derived from the annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The Financing Agreement requires the State to continue to appropriate salaries for the abolished positions and deposit the appropriated funds into the ERS Trust Account. These funds had not been deposited to the Trust Account as of September 30, 2012. As of September 30, 2012, the amount outstanding against this loan was \$5,512,255. Of the required \$5,300,000 identified for future debt service payments, \$3,777,411 is deposited in an investment account held jointly with the FSM National Government. That investment account is restricted for the repayment of this debt and other ADB related debt set forth below.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(7) Long-Term Obligations, Continued

Primary Government, Continued

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government Program Loan with ADB (Loan Number 1816 FSM (SF)) for the purpose of funding the Basic Social Services Project, with interest at 1% to 1.5% per annum. Principal payments shall be made semiannually commencing February 1, 2009, with a maturity date of August 1, 2032. As of September 30, 2012, the balance payable on this loan amounted to \$920,304.

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government Program Loans with ADB (Loan Number 1873 (SF) and Loan Number 1874 FSM (SF)) for the purpose of promoting private sector development in Chuuk, with interest at 1% to 1.5% per annum. Principal payments shall be made in 32 equal semi-annual payments with the first payment due on May 15, 2011 and the last payment on November 15, 2025. As of September 30, 2012, the balances payable on these loans amounted to \$600,747 and \$1,190,915, respectively.

On December 21, 2010, the Chuuk Public Utilities Corporation (CPUC) and the State agreed through memorandum of understanding to offset certain claims and transferred certain debt between CPUC and the State. The transferred debt was the FSM National Government Program Loan with ADB (Loan Number 1459 (SF)), totaling \$3,554,435, for water wells and electric construction purposes, with interest at 1% to 1.5% per annum. Principal payments shall be made semiannually commencing August 1, 2007, with a maturity date of August 1, 2036. As of September 30, 2012, the balance payable on this loan amounted to \$4,052,173.

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

<u>Year Ending</u> <u>September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 360,998	\$ 136,576	\$ 497,574
2014	360,998	132,233	493,231
2015	360,998	127,890	488,888
2016	360,998	123,547	484,545
2017	453,088	119,204	572,292
2018-2022	2,877,788	502,367	3,380,155
2023-2027	2,812,107	342,933	3,155,040
2028-2032	2,658,847	191,886	2,850,733
2033-2037	<u>2,030,573</u>	<u>56,824</u>	<u>2,087,397</u>
	<u>\$ 12,276,394</u>	<u>\$ 1,733,459</u>	<u>\$ 14,009,853</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(7) Long-Term Obligations, Continued

Discretely Presented Component Units

Chuuk Public Utility Corporation:

Loan payable to the State, facilitated by an ADB loan (Loan Number 2099-FSM) to the FSM National Government, original amount of \$1,800,000 due in semi-annual installments of \$85,883 from January 15, 2013 to July 15, 2036. Interest is payable at 1% per annum during the grace period and at 1.5% per annum thereafter. Proceeds were used for infrastructure projects: power distribution upgrades, decommissioning and environmental remediation of the existing power station, and institutional strengthening. \$ 314,439

Loan payable to the State, facilitated by an ADB loan (Loan Number 2100-FSM) to the FSM National Government, original amount of \$2,800,000, due in semi-annual installments of varying amounts through January 15, 2019. Interest is payable at LIBOR plus 0.6% per annum (2.1% at September 30, 2012). Proceeds were used for the purchase of two generator sets and related costs. 1,920,607

\$ 2,235,136

Principal payments for subsequent years ending September 30 and applicable interest due are as follows:

<u>Year Ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 50,059	\$ 49,266	\$ 99,325
2014	54,798	44,052	98,850
2015	60,353	42,857	103,210
2016	66,112	41,642	107,754
2017	72,483	40,098	112,581
2018-2022	484,061	173,388	657,449
2023-2027	766,796	108,455	885,251
2028-2032	445,170	34,506	479,676
2033-2036	<u>225,304</u>	<u>15,450</u>	<u>240,754</u>
	<u>\$ 2,235,136</u>	<u>\$ 549,714</u>	<u>\$ 2,784,850</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(8) Changes in Long-Term Obligations

Primary Government

Long-term liabilities will be liquidated in the future from governmental funds. During the year ended September 30, 2012, the following changes occurred in liabilities reported as part of the primary government's long-term liabilities in the statement of net assets:

	Balance October 1, <u>30, 2011</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2012</u>	Due Within <u>One Year</u>
Loans payable:					
ADB loans:					
Loan 1459	\$ 4,144,208	\$ -	\$ (92,035)	\$ 4,052,173	\$ 91,947
Loan 1520	5,624,605	-	(112,350)	5,512,255	122,469
Loan 1816	1,033,366	-	(113,062)	920,304	45,918
Loan 1873	673,091	-	(72,344)	600,747	43,787
Loan 1874	<u>1,249,258</u>	<u>-</u>	<u>(58,343)</u>	<u>1,190,915</u>	<u>56,877</u>
	12,724,528	-	(448,134)	12,276,394	360,998
Other:					
Compensated absences	<u>2,083,860</u>	<u>450,000</u>	<u>(474,119)</u>	<u>2,059,741</u>	<u>450,000</u>
	<u>\$14,808,388</u>	<u>\$ 450,000</u>	<u>\$ (472,253)</u>	<u>\$14,336,135</u>	<u>\$ 810,998</u>

Discretely Presented Component Units

During the year ended September 30, 2012, the following changes occurred in long-term obligations of the discretely presented component units:

	Balance October 1, <u>2011</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2012</u>	Due Within <u>One Year</u>
Loans payable:					
CPUC	<u>\$458,877</u>	<u>\$1,811,059</u>	<u>\$(34,800)</u>	<u>\$2,235,136</u>	<u>\$50,059</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(9) Interfund/Intrafund Transactions

Operating transfers in/out for each major governmental fund and nonmajor governmental funds in the aggregate, for the year ended September 30, 2012, are as follows:

	<u>Transfers Out</u>	<u>Transfers In</u>
General Fund:		
Grants Assistance Fund	\$ <u>460,233</u>	\$ <u>2,258,772</u>
Grants Assistance Fund:		
General Fund	<u>2,258,772</u>	<u>460,233</u>
	<u>\$ 2,719,005</u>	<u>\$ 2,719,005</u>

Transfers are used to 1) move revenues from the fund that enabling legislation or budget requires to collect them to the fund that enabling legislation or budget requires to expend them, 2) use unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations, and 3) record reductions in interfund loans for amounts that are not expected to be repaid. Specifically, the State transferred \$460,233 from the General Fund to the Grants Assistance Fund to primarily finance infrastructure maintenance programs; and \$2,258,772 from the Grants Assistance Fund to the General Fund representing reduction in interfund balances.

(10) Fund Balance

Classifications of fund balances comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds. The following table enumerates the fund balance classifications:

	General <u>Fund</u>	Grants Assistance <u>Fund</u>	Compact Trust <u>Fund</u>	Nonmajor Funds	Total Governmental <u>Funds</u>
Non-spendable:					
General government	\$ 348,413	\$ 179,461	\$ -	\$ -	\$ 527,874
FSM Development Bank	300,000	-	-	-	300,000
Pacific Islands Development Bank	250,000	-	-	-	250,000
Bank of the FSM	1,000,000	-	-	-	1,000,000
Permanent fund principal	-	-	9,493,531	-	9,493,531
Restricted for:					
Debt service	3,777,411	-	-	-	3,777,411
Capital projects	-	1,709,221	-	-	1,709,221
General government	-	1,046,856	-	-	1,046,856
Economic development	-	141,411	-	-	141,411
Education	-	1,042,989	-	-	1,042,989
Health services	-	1,301,122	-	-	1,301,122
Environment	-	68,132	-	-	68,132
Other foreign assistance	-	140,201	-	-	140,201
Committed:					
Health services	-	-	-	25,559	25,559
Unassigned	<u>(11,061,616)</u>	<u>(1,114,755)</u>	<u>-</u>	<u>-</u>	<u>(12,176,371)</u>
	<u>\$ (5,385,792)</u>	<u>\$ 4,514,638</u>	<u>\$ 9,493,531</u>	<u>\$ 25,559</u>	<u>\$ 8,647,936</u>

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2012

(11) Contingencies

Sick Leave

It is the policy of the State to record expenditures for sick leave when leave is actually taken. Sick leave is compensated time for absence during working hours arising from employee illness or injury. The estimated accumulated amount of unused sick leave as of September 30, 2012 is \$4,968,208.

Insurance Coverage

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

Encumbrances

The State utilizes encumbrance accounting to identify fund obligations. Encumbrances represent commitments related to unperformed contracts for goods. At September 30, 2012, the State has significant encumbrances summarized as follows:

<u>General</u>	<u>Grants Assistance</u>	<u>Compact Trust</u>	<u>Other Governmental Funds</u>	<u>Total</u>
\$ <u>200,277</u>	\$ <u>4,329,935</u>	\$ <u>-</u>	\$ <u>7,103</u>	\$ <u>4,537,315</u>

Federal Grants

The State participates in a number of federally assisted grant programs. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. The ultimate disposition of questioned costs can be determined only by final action of the respective grantor agencies. No provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

Litigation

The State is a party to various legal proceedings in which the State's Attorney General indicates that pending land lease cases and other related claims against the State exist at September 30, 2012 in an amount that is material to the financial statements. Due to an inability to predict the ultimate outcome of these matters, no provision for these liabilities has been made in the accompanying financial statements.

Delinquent Taxes

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

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2012

(11) Contingencies, Continued

General Fund Financial Position

The State's General Fund has sustained recurring operating deficits and has an unassigned fund deficit of \$11,061,616 at September 30, 2012. In addition, at September 30, 2012, the primary government's current liabilities exceed current assets by \$6,984,004.

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

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2012

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Revenues, Expenditures and Changes in Deficit
Budget and Actual - General Fund
Year Ended September 30, 2012

	Budgeted Amounts		Actual - Budgetary Basis (see Note 1)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues:				
Local revenues	\$ 6,652,494	\$ 6,747,878	\$ 8,213,370	\$ 1,465,492
Net change in fair value of investments	-	-	740,417	740,417
Total revenues	6,652,494	6,747,878	8,953,787	2,205,909
Expenditures:				
Current:				
General government	3,669,018	3,669,018	3,869,388	(200,370)
Education	997	997	-	997
Economic development	86,736	86,736	86,164	572
Public safety	1,009,140	1,009,140	959,834	49,306
Public works and transportation	974,826	974,826	910,907	63,919
Community affairs	37,698	37,698	35,587	2,111
Boards and commissions	383,626	383,626	416,507	(32,881)
Judiciary	484,784	484,784	452,103	32,681
Payments to component units	55,512	55,512	54,709	803
Municipal affairs	651,746	651,746	708,380	(56,634)
Other	113,004	113,004	119,352	(6,348)
Debt service	-	-	457,913	(457,913)
Total expenditures	7,467,087	7,467,087	8,070,844	(603,757)
Excess (deficiency) of revenues over (under) expenditures	(814,593)	(719,209)	882,943	1,602,152
Other financing sources (uses):				
Operating transfers in	-	-	2,258,772	2,258,772
Operating transfers out	(460,223)	(460,223)	(460,233)	(10)
Total other financing sources (uses), net	(460,223)	(460,223)	1,798,539	2,258,762
Net change in deficit	(1,274,816)	(1,179,432)	2,681,482	3,860,914
Other changes in fund deficit:				
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes	-	-	615,488	615,488
Fund deficit at the beginning of the year	(8,682,762)	(8,682,762)	(8,682,762)	-
Fund deficit at the end of the year	\$ (9,957,578)	\$ (9,862,194)	\$ (5,385,792)	\$ 4,476,402

See accompanying notes to required supplementary information - budgetary reporting.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting
September 30, 2012

(1) Budgetary Information

The Governor shall submit an annual budget to the Legislature at a time prescribed by statute. The budget shall contain a complete plan of proposed expenditures, anticipated revenues, and other monies available to the State for the next fiscal year, and any additional information which the Legislature may require. The Legislature may alter all or any portion of the proposed budget.

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

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

OTHER SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2012

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account
Governmental Funds
Year Ended September 30, 2012

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
Expenditures:					
Salaries and wages					
Regular	\$ 3,873,941	\$ 10,091,364	\$ -	\$ 10,790	\$ 13,976,095
Overtime	39,650	656,956	-	-	696,606
Fringe benefits	458,050	1,335,408	-	-	1,793,458
Travel and transportation	428,813	599,293	-	14,225	1,042,331
Books and library materials	-	9,339	-	-	9,339
Communications	42,468	125,989	-	559	169,016
Dues, membership, and subscriptions	11,500	1,360	-	320	13,180
Food stuffs	43,141	459,767	-	7,423	510,331
Port charges	2,182	19,594	-	3,141	24,917
Office supplies and materials	64,533	1,604,691	-	6,198	1,675,422
POL	201,244	882,707	-	260	1,084,211
Printing and reproduction	(2,708)	17,193	-	420	14,905
Rental services	6,691	101,120	-	3,756	111,567
Repairs and maintenance	15,132	284,086	-	1,726	300,944
Constructional materials	2,177	101,524	-	-	103,701
Utilities	153,338	913,311	-	-	1,066,649
Goods and services	208,779	20,981	-	13,842	243,602
Subsidies and contributions	11,300	204,786	-	-	216,086
Medical referrals	-	287,244	-	5,447	292,691
Medical supplies	-	1,514,584	-	18,641	1,533,225
Contractual services	240,955	5,520,703	-	-	5,761,658
Professional services	-	322,536	-	-	322,536
Housing allowance	24,847	69,555	-	-	94,402
Compensation non-payroll	-	13,750	-	-	13,750
Scholarships and allowances	3,439	670,129	-	-	673,568
Training	300	185,189	-	-	185,489
Official allowance	606,052	-	-	-	606,052
Meeting fees and allowance	-	725	-	2,950	3,675
Representation allowance	4,250	-	-	-	4,250
Insurance	-	9,129	-	-	9,129
Leased housing, buildings and land	38,781	301,586	-	14,000	354,367
Equipment	60,861	579,117	-	7,840	647,818
Furniture and fixtures	4,181	90,076	-	-	94,257
Vehicles	88,849	374,578	-	6,986	470,413
Land	216,640	-	-	-	216,640
Principal repayment	448,134	-	-	-	448,134
Interest payments	9,779	-	-	-	9,779
Payout to municipalities	205,362	-	-	-	205,362
Bank charges	4,824	62	-	-	4,886
Bad debt	205,348	-	-	-	205,348
Miscellaneous	147,733	14,255	-	-	161,988
	<u>\$ 7,870,566</u>	<u>\$ 27,382,687</u>	<u>\$ -</u>	<u>\$ 118,524</u>	<u>\$ 35,371,777</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GENERAL FUND

September 30, 2012

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

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function, and Changes in Deficit
General Fund
Year Ended September 30, 2012
(with comparative totals for the year ended September 30, 2011)

	2012	2011
Revenues:		
FSM revenue sharing:		
Gross revenue taxes	\$ 1,187,776	\$ 1,061,967
Import taxes	998,930	921,830
Income taxes	930,242	959,833
Other taxes	113,339	159,579
FSM revenue sharing	3,230,287	3,103,209
State taxes:		
Sales tax	2,604,533	2,115,045
Other excise taxes	47,685	591,368
	2,652,218	2,706,413
Fees and charges:		
Licenses and permits	854,573	710,925
Leases and other rentals	168,889	130,994
	1,023,462	841,919
Departmental charges:		
Transportation collections	570,720	624,273
Net change in the fair value of investments	740,417	(7,948)
Other revenues	736,683	1,088,183
Total revenues	8,953,787	8,356,049
Expenditures:		
Current:		
General government:		
Office of the Governor	502,271	384,825
State Legislature	2,365,561	2,242,369
Department of Planning and Statistics	74,697	59,620
Department of Administrative Services	819,384	512,782
	3,761,913	3,199,596
Education:		
Department of Education	-	2,850
Economic development:		
Department of Agriculture	-	39,363
Department of Marine Resources	43,876	35,019
Historic Preservation Office	13,719	12,154
Department of Commerce & Industries	28,567	19,068
	86,162	105,604
Public safety:		
Office of the Attorney General	228,332	216,207
Department of Public Safety	725,069	566,739
	953,401	782,946
Public works and transportation:		
Department of Transportation	883,145	694,766
Community affairs:		
Broadcast	35,587	33,430

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function, and Changes in Deficit, Continued
General Fund
Year Ended September 30, 2012
(with comparative totals for the year ended September 30, 2011)

	2012	2011
Expenditures, continued:		
Current, continued:		
Boards and commissions:		
Land Commission	156,175	92,313
Public Service Commission	103,688	87,969
Election Commission	154,054	358,567
	413,917	538,849
Judiciary:		
State Court	451,622	402,335
Payments to component units:		
Chuuk State Housing Authority	54,273	40,775
Municipal affairs:		
Payments to municipalities	685,790	1,943,829
Other:		
Farmers Home Administration	24,851	22,675
Peace Corps	15,063	9,994
Micro Games	14,765	14,418
Goodwill games	2,500	-
Guandong Province	-	4,000
2011 Economic Summit	(500)	59,096
Insurance broker	-	15,750
ESG	-	88,812
Disaster Coordinating Office	-	19,460
Labor and Manpower	13,276	8,709
Chuuk Women Council	9,998	-
Other	6,890	51,762
	86,843	294,676
Debt service:		
Principal repayment	448,134	401,774
Interest payment	9,779	237,824
	457,913	639,598
Total expenditures	7,870,566	8,679,254
Excess (deficiency) of revenues over (under) expenditures	1,083,221	(323,205)
Other financing sources (uses):		
Operating transfers in	2,258,772	-
Operating transfers out	(460,233)	(393,065)
Total other financing sources (uses), net	1,798,539	(393,065)
Net change in deficit	2,881,760	(716,270)
Deficit at the beginning of the year	(8,267,552)	(7,551,282)
Deficit at the end of the year	\$ (5,385,792)	\$ (8,267,552)

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures and Changes in Deficit
Budget and Actual - General Fund
Year Ended September 30, 2012

	Budgeted Amounts		Actual	Variance with
	Original	Final	Budgetary Basis (see Note 1)	Final Budget Positive/(Negative)
Revenues:				
Local revenues	\$ 6,652,494	\$ 6,747,878	\$ 8,213,370	\$ 1,465,492
Net change in fair value of investments	-	-	740,417	740,417
Total revenues	6,652,494	6,747,878	8,953,787	2,205,909
Expenditures:				
Current:				
General government:				
Office of the Governor	599,064	599,064	513,886	85,178
State Legislature	2,485,646	2,485,646	2,440,933	44,713
Department of Planning and Statistics	75,630	75,630	76,936	(1,306)
Department of Administrative Services	508,678	508,678	837,633	(328,955)
	<u>3,669,018</u>	<u>3,669,018</u>	<u>3,869,388</u>	<u>(200,370)</u>
Education:				
Department of Education	997	997	-	997
Economic development:				
Department of Marine Resources	45,210	45,210	43,876	1,334
Historic Preservation Office	11,415	11,415	13,719	(2,304)
Department of Commerce & Industry	30,111	30,111	28,569	1,542
	<u>86,736</u>	<u>86,736</u>	<u>86,164</u>	<u>572</u>
Public safety:				
Office of the Attorney General	238,980	238,980	232,936	6,044
Department of Public Safety	770,160	770,160	726,898	43,262
	<u>1,009,140</u>	<u>1,009,140</u>	<u>959,834</u>	<u>49,306</u>
Public works and transportation:				
Department of Transportation	974,826	974,826	910,907	63,919
Community affairs:				
Department of Public Affairs	37,698	37,698	35,587	2,111
Boards and commissions:				
Land Commission	116,392	116,392	156,835	(40,443)
Election Commission	166,102	166,102	154,054	12,048
Public Service Commission	101,132	101,132	105,618	(4,486)
	<u>383,626</u>	<u>383,626</u>	<u>416,507</u>	<u>(32,881)</u>
Judiciary:				
State Court	484,784	484,784	452,103	32,681
Payments to component units:				
Chuuk State Housing Authority	55,512	55,512	54,709	803
Municipal affairs:				
Payments to municipalities	651,746	651,746	708,380	(56,634)
Other:				
Farmers Home Administration	21,924	21,924	24,851	(2,927)
Peace Corps	15,150	15,150	15,063	87
Micro Games	18,063	18,063	14,765	3,298
Goodwill Games	-	-	2,500	(2,500)
Guandong Province	2,000	2,000	2,000	-
2011 Economic Summit	-	-	(500)	500
ESG	7,339	7,339	-	7,339
Chuuk Women Council	10,000	10,000	-	10,000
Labor and Manpower	13,410	13,410	13,276	134
Other	23,978	23,978	40,507	(16,529)
China Travel	1,140	1,140	6,890	(5,750)
	<u>113,004</u>	<u>113,004</u>	<u>119,352</u>	<u>(6,348)</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures and Changes in Deficit
Budget and Actual - General Fund, Continued
Year Ended September 30, 2012

	Budgeted Amounts		Actual Budgetary Basis (see Note 1)	Variance with Final Budget Positive/(Negative)
	Original	Final		
Debt service:				
Principal repayment	-	-	448,134	(448,134)
Interest payments	-	-	9,779	(9,779)
	-	-	457,913	(457,913)
Total expenditures	7,467,087	7,467,087	8,070,844	(603,757)
Deficiency of revenues under expenditures	(814,593)	(719,209)	882,943	1,602,152
Other financing sources (uses):				
Operating transfers in	-	-	2,258,772	2,258,772
Operating transfers out	(460,223)	(460,223)	(460,233)	(10)
Total other financing sources (uses), net	(460,223)	(460,223)	1,798,539	2,258,762
Net change in deficit	(1,274,816)	(1,179,432)	2,681,482	3,860,914
Other changes in fund deficit:				
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes	-	-	615,488	615,488
Fund deficit at the beginning of the year	(8,682,762)	(8,682,762)	(8,682,762)	-
Fund deficit at the end of the year	\$ (9,957,578)	\$ (9,862,194)	\$ (5,385,792)	\$ 4,476,402

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS - SPECIAL REVENUE FUNDS

September 30, 2012

Special revenue funds are used to account for specific revenues that are legally restricted for particular purposes. A brief discussion of the State's Nonmajor Governmental Funds - Special Revenue Funds as of September 30, 2012, follows:

Hospital Revolving Fund

This fund accounts for the operations of the hospital and the purchase of pharmaceutical and medical supplies.

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Balance Sheet
September 30, 2012

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	ERA	IMF	Infrastructure	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
ASSETS														
Advances	\$ 9,189	\$ 15,793	\$ 1,359	\$ 4,890	\$ 10,645	\$ 16,622	\$ 5,915	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 64,413
Prepayments	-	97,404	11,192	17,784	25,525	24,458	3,098	-	-	-	-	-	-	179,461
Due from other funds	-	1,886,533	82,447	145,565	1,036,453	1,095,351	-	1,710,584	-	12,519	127,682	-	-	6,097,134
	<u>\$ 9,189</u>	<u>\$ 1,999,730</u>	<u>\$ 94,998</u>	<u>\$ 168,239</u>	<u>\$ 1,072,623</u>	<u>\$ 1,136,431</u>	<u>\$ 9,013</u>	<u>\$ 1,710,584</u>	<u>\$ -</u>	<u>\$ 12,519</u>	<u>\$ 127,682</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 6,341,008</u>
LIABILITIES AND FUND BALANCES (DEFICITS)														
Liabilities:														
Accounts payable	\$ 154,261	\$ 601,204	\$ 15,674	\$ 9,044	\$ 242	\$ 68,984	\$ 2,596	\$ 1,363	\$ -	\$ -	\$ -	\$ 11,391	\$ -	\$ 864,759
Due to other funds	806,744	-	-	-	-	-	19,981	-	-	-	-	134,886	-	961,611
Total liabilities	<u>961,005</u>	<u>601,204</u>	<u>15,674</u>	<u>9,044</u>	<u>242</u>	<u>68,984</u>	<u>22,577</u>	<u>1,363</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>146,277</u>	<u>-</u>	<u>1,826,370</u>
Fund balances:														
Non-spendable	-	97,404	11,192	17,784	25,525	24,458	3,098	-	-	-	-	-	-	179,461
Restricted	-	1,301,122	68,132	141,411	1,046,856	1,042,989	-	1,709,221	-	12,519	127,682	-	-	5,449,932
Unassigned	(951,816)	-	-	-	-	-	(16,662)	-	-	-	-	(146,277)	-	(1,114,755)
Total fund balances (deficits)	<u>(951,816)</u>	<u>1,398,526</u>	<u>79,324</u>	<u>159,195</u>	<u>1,072,381</u>	<u>1,067,447</u>	<u>(13,564)</u>	<u>1,709,221</u>	<u>-</u>	<u>12,519</u>	<u>127,682</u>	<u>(146,277)</u>	<u>-</u>	<u>4,514,638</u>
Total liabilities and fund balances (deficits)	<u>\$ 9,189</u>	<u>\$ 1,999,730</u>	<u>\$ 94,998</u>	<u>\$ 168,239</u>	<u>\$ 1,072,623</u>	<u>\$ 1,136,431</u>	<u>\$ 9,013</u>	<u>\$ 1,710,584</u>	<u>\$ -</u>	<u>\$ 12,519</u>	<u>\$ 127,682</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 6,341,008</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances (Deficits)
Year Ended September 30, 2012

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	ERA	IMF	Infrastructure	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
Revenues:														
Compact funding	\$ 7,740,000	\$ 9,075,000	\$ 642,000	\$ 795,000	\$ 1,860,500	\$ 4,230,707	\$ 541,000	\$ 355,000	\$ 648,523	\$ -	\$ -	\$ -	\$ -	\$ 25,887,730
Federal and other grants	-	-	-	-	-	-	-	-	-	-	99,263	-	-	99,263
Total revenues	<u>7,740,000</u>	<u>9,075,000</u>	<u>642,000</u>	<u>795,000</u>	<u>1,860,500</u>	<u>4,230,707</u>	<u>541,000</u>	<u>355,000</u>	<u>648,523</u>	<u>-</u>	<u>99,263</u>	<u>-</u>	<u>-</u>	<u>25,986,993</u>
Expenditures by function:														
Current:														
General government	-	-	-	-	1,685,775	-	-	-	570,927	-	100,514	-	-	2,357,216
Health services	-	9,400,764	-	-	-	-	-	-	-	-	-	-	-	9,400,764
Education	7,640,065	-	-	-	-	4,700,999	554,564	-	-	-	-	-	-	12,895,628
Economic development	-	-	650,865	884,545	-	-	-	1,147,977	-	-	-	-	-	2,683,387
Public safety	-	-	-	-	-	-	-	-	-	-	-	45,692	-	45,692
Total expenditures	<u>7,640,065</u>	<u>9,400,764</u>	<u>650,865</u>	<u>884,545</u>	<u>1,685,775</u>	<u>4,700,999</u>	<u>554,564</u>	<u>1,147,977</u>	<u>570,927</u>	<u>-</u>	<u>100,514</u>	<u>45,692</u>	<u>-</u>	<u>27,382,687</u>
Excess (deficiency) of revenues over (under) expenditures	<u>99,935</u>	<u>(325,764)</u>	<u>(8,865)</u>	<u>(89,545)</u>	<u>174,725</u>	<u>(470,292)</u>	<u>(13,564)</u>	<u>(792,977)</u>	<u>77,596</u>	<u>-</u>	<u>(1,251)</u>	<u>(45,692)</u>	<u>-</u>	<u>(1,395,694)</u>
Other financing sources (uses):														
Operating transfers out	-	-	-	-	-	-	-	-	-	-	-	-	(2,258,772)	(2,258,772)
Operating transfers in	-	-	-	-	-	-	-	460,233	-	-	-	-	-	460,233
Total other financing sources (uses), net	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>460,233</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(2,258,772)</u>	<u>(1,798,539)</u>
Net change in fund balances (deficits)	<u>99,935</u>	<u>(325,764)</u>	<u>(8,865)</u>	<u>(89,545)</u>	<u>174,725</u>	<u>(470,292)</u>	<u>(13,564)</u>	<u>(332,744)</u>	<u>77,596</u>	<u>-</u>	<u>(1,251)</u>	<u>(45,692)</u>	<u>(2,258,772)</u>	<u>(3,194,233)</u>
Fund balances (deficits) at the beginning of the year	<u>(1,051,751)</u>	<u>1,724,290</u>	<u>88,189</u>	<u>248,740</u>	<u>897,656</u>	<u>1,537,739</u>	<u>-</u>	<u>2,041,965</u>	<u>(77,596)</u>	<u>12,519</u>	<u>128,933</u>	<u>(100,585)</u>	<u>2,258,772</u>	<u>7,708,871</u>
Fund balances (deficits) at the end of the year	<u>\$ (951,816)</u>	<u>\$ 1,398,526</u>	<u>\$ 79,324</u>	<u>\$ 159,195</u>	<u>\$ 1,072,381</u>	<u>\$ 1,067,447</u>	<u>\$ (13,564)</u>	<u>\$ 1,709,221</u>	<u>\$ -</u>	<u>\$ 12,519</u>	<u>\$ 127,682</u>	<u>\$ (146,277)</u>	<u>\$ -</u>	<u>\$ 4,514,638</u>

See Accompanying Independent Auditors' Report.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances (Deficits)
Year Ended September 30, 2012

	Education Sector	Health Sector	Environment Sector	Private Sector Development	Capacity Building Sector	Supplemental Education	ERA	IMF	Infrastructure	U.S. Federal Grants	Foreign Assistance	CFSM Grants	Compact I Capital Projects	Total
Revenues:														
Compact funding	\$ 7,740,000	\$ 9,075,000	\$ 642,000	\$ 795,000	\$ 1,860,500	\$ 4,230,707	\$ 541,000	\$ 355,000	\$ 648,523	\$ -	\$ -	\$ -	\$ -	\$ 25,887,730
Federal and other grants	-	-	-	-	-	-	-	-	-	-	99,263	-	-	99,263
Total revenues	<u>7,740,000</u>	<u>9,075,000</u>	<u>642,000</u>	<u>795,000</u>	<u>1,860,500</u>	<u>4,230,707</u>	<u>541,000</u>	<u>355,000</u>	<u>648,523</u>	<u>-</u>	<u>99,263</u>	<u>-</u>	<u>-</u>	<u>25,986,993</u>
Expenditures by account:														
Salaries and wages:														
Regular	5,506,812	2,807,809	280,875	332,284	-	748,374	415,210	-	-	-	-	-	-	10,091,364
Overtime	13,344	625,498	2,312	11,699	-	1,311	2,792	-	-	-	-	-	-	656,956
Fringe benefits	679,771	410,466	34,403	45,188	15,005	99,724	50,851	-	-	-	-	-	-	1,335,408
Travel and transportation	26,579	166,578	26,503	80,219	83,841	174,092	26,783	-	-	-	-	14,698	-	599,293
Books and library materials	-	-	-	-	467	8,872	-	-	-	-	-	-	-	9,339
Communications	632	19,707	11,897	16,910	12,930	56,260	7,074	-	-	-	-	579	-	125,989
Dues, memberships, and subscriptions	-	1,000	-	300	-	60	-	-	-	-	-	-	-	1,360
Food stuffs	2,238	262,527	-	-	620	193,261	-	-	-	-	-	1,121	-	459,767
Freight and port charges	3,600	6,142	306	1,521	2,172	5,853	-	-	-	-	-	-	-	19,594
Office supplies and materials	168,042	189,272	62,239	71,137	47,942	1,048,521	12,219	-	339	-	1,251	3,729	-	1,604,691
POL	4,410	544,226	59,912	41,053	23,961	193,111	8,353	-	4,681	-	-	3,000	-	882,707
Printing and reproduction	-	10,964	-	359	3,155	2,715	-	-	-	-	-	-	-	17,193
Rental services	41,237	12,974	9,163	4,444	5,185	26,953	-	-	1,164	-	-	-	-	101,120
Repairs and maintenance	958	178,683	19,494	17,184	525	63,245	53	-	1,096	-	-	2,848	-	284,086
Construction materials	-	50,762	2,282	35,307	-	13,173	-	-	-	-	-	-	-	101,524
Utilities	103,100	627,549	17,500	12,608	13,464	112,374	26,716	-	-	-	-	-	-	913,311
Goods and services	1,520	10,032	120	1,010	2,955	5,344	-	-	-	-	-	-	-	20,981
Subsidies and contributions	194,786	-	10,000	-	-	-	-	-	-	-	-	-	-	204,786
Medical referrals	-	287,244	-	-	-	-	-	-	-	-	-	-	-	287,244
Medical supplies	-	1,514,584	-	-	-	-	-	-	-	-	-	-	-	1,514,584
Contractual services	112,618	1,053,774	28,509	131,989	1,125,682	1,354,807	1,334	1,147,977	563,647	-	-	366	-	5,520,703
Professional services	3,425	-	-	101	260,141	58,869	-	-	-	-	-	-	-	322,536
Housing allowance	7,125	62,430	-	-	-	-	-	-	-	-	-	-	-	69,555
Scholarships and allowances	670,129	-	-	-	-	-	-	-	-	-	-	-	-	670,129
Fees and meeting allowances	725	-	-	-	-	-	-	-	-	-	-	-	-	725
Training	46,280	19,987	-	-	17,612	101,310	-	-	-	-	-	-	-	185,189
Insurance	-	7,169	-	1,960	-	-	-	-	-	-	-	-	-	9,129
Leased housing, buildings and land	-	185,995	-	788	50,213	64,590	-	-	-	-	-	-	-	301,586
Compensation non-payroll	-	13,750	-	-	-	-	-	-	-	-	-	-	-	13,750
Equipment	7,813	196,197	21,970	58,244	9,570	274,831	3,179	-	-	-	-	7,313	-	579,117
Furniture and fixtures	211	11,703	1,224	-	3,445	73,493	-	-	-	-	-	-	-	90,076
Vehicles	43,421	123,680	62,156	20,240	6,890	6,890	-	-	-	-	99,263	12,038	-	374,578
Bank charges	-	62	-	-	-	-	-	-	-	-	-	-	-	62
Miscellaneous	1,289	-	-	-	-	12,966	-	-	-	-	-	-	-	14,255
Total expenditures	<u>7,640,065</u>	<u>9,400,764</u>	<u>650,865</u>	<u>884,545</u>	<u>1,685,775</u>	<u>4,700,999</u>	<u>554,564</u>	<u>1,147,977</u>	<u>570,927</u>	<u>-</u>	<u>100,514</u>	<u>45,692</u>	<u>-</u>	<u>27,382,687</u>
Excess (deficiency) of revenues over (under) expenditures	99,935	(325,764)	(8,865)	(89,545)	174,725	(470,292)	(13,564)	(792,977)	77,596	-	(1,251)	(45,692)	-	(1,395,694)
Other financing sources (uses):														
Operating transfers out	-	-	-	-	-	-	-	-	-	-	-	-	(2,258,772)	(2,258,772)
Operating transfers in	-	-	-	-	-	-	-	460,233	-	-	-	-	-	460,233
Total other financing sources (uses), net	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>460,233</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(2,258,772)</u>	<u>(1,798,539)</u>
Net change in fund balances (deficits)	99,935	(325,764)	(8,865)	(89,545)	174,725	(470,292)	(13,564)	(332,744)	77,596	-	(1,251)	(45,692)	(2,258,772)	(3,194,233)
Fund balances (deficits) at the beginning of the year	<u>(1,051,751)</u>	<u>1,724,290</u>	<u>88,189</u>	<u>248,740</u>	<u>897,656</u>	<u>1,537,739</u>	<u>-</u>	<u>2,041,965</u>	<u>(77,596)</u>	<u>12,519</u>	<u>128,933</u>	<u>(100,585)</u>	<u>2,258,772</u>	<u>7,708,871</u>
Fund balances (deficits) at the end of the year	<u>\$ (951,816)</u>	<u>\$ 1,398,526</u>	<u>\$ 79,324</u>	<u>\$ 159,195</u>	<u>\$ 1,072,381</u>	<u>\$ 1,067,447</u>	<u>\$ (13,564)</u>	<u>\$ 1,709,221</u>	<u>\$ -</u>	<u>\$ 12,519</u>	<u>\$ 127,682</u>	<u>\$ (146,277)</u>	<u>\$ -</u>	<u>\$ 4,514,638</u>

See Accompanying Independent Auditors' Report.

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

Honorable Johnson Elimo
Governor, State of Chuuk
Federated States of Micronesia:

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk as of and for the year ended September 30, 2012, which collectively comprise the State of Chuuk's basic financial statements and have issued our report thereon dated June 24, 2013, which report was qualified with respect to a liability for land leases and related claims payable in the governmental activities and the General Fund. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

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

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs (pages 67 through 72), we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

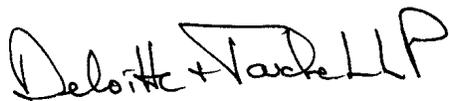
A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 2012-3 through 2012-5 to be a material weaknesses. A *significant deficiency* is a deficiency, or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 2012-1 and 2012-2 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Chuuk's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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

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



June 24, 2013

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB
CIRCULAR A-133 AND ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

Honorable Johnson Elimo
Governor, State of Chuuk
Federated States of Micronesia:

Compliance

We have audited the State of Chuuk's compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on the State of Chuuk's major federal programs for the year ended September 30, 2012. The State of Chuuk's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (pages 67 through 72). Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the State of Chuuk's management. Our responsibility is to express an opinion on the State of Chuuk's compliance based on our audit.

As discussed in Note 2B to the Schedule of Expenditures of Federal Awards, the State of Chuuk's basic financial statements include the operations of certain entities whose federal awards are not included in the Schedule of Expenditures of Federal Awards for the year ended September 30, 2012. Our audit, described below, did not include the operations of the entities identified in Note 2B as these entities conducted separate audits in accordance with OMB Circular A-133, if required.

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

In our opinion, the State of Chuuk complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2012. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as item 2012-1.

Internal Control Over Compliance

Management of the State of Chuuk is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the State of Chuuk's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the State of Chuuk's internal control over compliance.

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

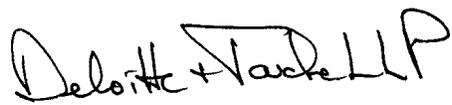
Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying Schedule of Findings and Questioned Costs as item 2012-1. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Chuuk as of and for the year ended September 30, 2012, and have issued our report thereon dated June 24, 2013, which contained a qualified opinion on those financial statements. Our audit was conducted for the purpose of forming our opinions on the financial statements that collectively comprise the State of Chuuk's financial statements. The accompanying Schedule of Expenditures of Federal Awards (pages 63 and 64) is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated in all material respects in relation to the financial statements as a whole.

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

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

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

June 24, 2013

STATE OF CHUUK
FEDERATED STATES OF MICRONESIA

Summary Schedule of Expenditures of Federal Awards, by Grantor
Year Ended September 30, 2012

<u>Agency/Program</u>	<u>Expenditures</u>
U.S. Department of the Interior	\$ <u>27,236,481</u>
GRAND TOTAL	\$ <u><u>27,236,481</u></u>
Reconciliation to the basic financial statements:	
Grants Assistance Fund	\$ 27,382,687
Less: CFSM Grants	(45,692)
Non-US Grants	<u>(100,514)</u>
	\$ <u><u>27,236,481</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2012

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF THE INTERIOR		
Economic, Social and Political Development of the Territories:		
Compact Sector Grants - Capacity Building Sector		\$ 1,685,775
Compact Sector Grants - Education Sector		7,640,065
Supplemental Education Grant		4,700,999
Compact Sector Grants - ERA		554,564
Compact Sector Grants - Environment Sector		650,865
Compact Sector Grants - Health Sector		9,400,764
Compact Sector Grants - Private Sector Development		884,545
Compact Sector Grants - Infrastructure Maintenance		1,147,977
Compact Sector Grants - Infrastructure		<u>570,927</u>
Total Compact Sector Grants Fund	15.875	<u>27,236,481</u>
U.S. DEPARTMENT OF THE INTERIOR TOTAL		<u><u>\$ 27,236,481</u></u>

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

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2012

1. Scope of Audit

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

- Programs Subject to Single Audit

The Schedule of Expenditures of Federal Awards presents each federal program related to the following agency:

- U.S. Department of the Interior

2. Summary of Significant Accounting Policies

A. Basis of Accounting

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

B. Reporting Entity

For purposes of complying with The Single Audit Act of 1984, as amended in 1996, the State's reporting entity is defined in Note 1A to its September 30, 2012 basic financial statements; and all of the discretely presented component units are excluded. Accordingly, the accompanying Schedule of Expenditures of Federal Awards presents the federal award programs administered by the State, as defined above, for the year ended September 30, 2012.

C. Subgrantees

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

D. Indirect Cost Allocation

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2012

2. Summary of Significant Accounting Policies, Continued

E. CFDA #15.875

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

3. Component Units

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

Chuuk Public Utility Corporation

The Chuuk Public Utility Corporation, (CPUC), a discretely presented component unit, is the recipient of various pass-through funds from Chuuk State and direct grants from the U.S. Department of the Interior. The CPUC is to separately satisfy its 2012 reporting responsibilities under the Single Audit Act.

Chuuk State Housing Authority

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

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs
Year Ended September 30, 2012

Part I - Summary of Auditors' Results

Financial Statements

- | | |
|--|-----------|
| 1. Type of auditors' report issued: | Qualified |
| Internal control over financial reporting: | |
| 2. Material weakness(es) identified? | Yes |
| 3. Significant deficiency(ies) identified? | Yes |
| 4. Noncompliance material to financial statements noted? | No |

Federal Awards

- | | |
|---|-------------|
| Internal control over major programs: | |
| 5. Material weakness(es) identified? | No |
| 6. Significant deficiency(ies) identified? | Yes |
| 7. Type of auditors' report issued on compliance for major programs: | Unqualified |
| 8. Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? | Yes |
| 9. Identification of major programs: | |

<u>CFDA Number</u>	<u>Federal Program</u>	
15.875	Economic, Social and Political Development of the Territories – Compact of Free Association Sector Grants	

- | | |
|--|-----------|
| 10. Dollar threshold used to distinguish between Type A and Type B Programs: | \$817,094 |
| 11. Auditee qualified as a low-risk auditee? | No |

Part II - Financial Statement Findings Section

<u>Reference #</u>	<u>Findings</u>
2012-1	Equipment and Real Property Management
2012-2	Payments to Municipalities
2012-3	Leases payable
2012-4	Housing Loans/Fixed Assets
2012-5	Timely and Accurate Reconciliations

Part III - Federal Award Findings and Questioned Cost Section

<u>Reference #</u>	<u>CFDA #</u>	<u>Findings</u>	<u>Questioned Costs</u>
2012-1	15.875	Equipment and Real Property Management	\$ -

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2012

Finding No.: 2012-1
Federal Agency: U.S. Department of the Interior
CFDA Program: 15.875 Economic, Social and Political Development of the Territories
Grant Number: Compact of Free Association Compact Sector Grants
Requirement: Equipment and Real Property Management
Questioned Cost: \$0

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

Condition: No documented procedures are currently in place requiring that fixed assets undergo required maintenance.

Cause: This appears to be a potential weakness in internal control requiring that fixed assets be periodically maintained.

Effect: The expected life of fixed assets may be lessened. However, no questioned costs result from this finding as no specific instances came to our attention in fiscal year 2012 of unnecessary expenditures that occurred due to this condition.

Prior Year Status: Noncompliance with maintenance of fixed assets was reported as a finding in prior single audits as items 2006-26, 2007-08, 2008-4, 2009-02, 2010-1, and 2011-1.

Recommendation: We recommend that the State strengthen internal control requiring that periodic reviews be performed and that asset maintenance activities be documented and monitored.

Auditee Response and Corrective Action Plan: We agree with the finding and recommendation. Chuuk State DAS, Supply and Procurement staff in collaboration with the corresponding staff of departments, agencies and offices are working together and taking all necessary steps to ensure compliance with federal equipment requirements and resolve this audit finding this fiscal year.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2012

Finding No.: 2012-2
Area: Payments to Municipalities

Criteria: Disbursements of funds to the municipalities should be subject to standard State accounting controls.

Condition: We were not provided documentary evidence indicating the adequacy of payments of \$216,539 to municipalities during fiscal year 2012. The source of funds used for this payment came from Chuuk State investments administered by the FSM National Government. We were unable to determine if the respective municipalities possess effective accounting systems that can adequately account for and document the use of these funds. We also were not provided with memorandums of agreement executed with the municipalities that set forth terms and conditions underlying the use of these funds.

Cause: The cause of this finding is our inability to access agreements underlying the payments and to establish whether municipal accounting systems are sufficient to protect the State's interests.

Effect: The effect of the condition is potential noncompliance with local laws.

Recommendation: We recommend that disbursements of funds follow local laws and regulations and that these funds be subject to audit.

Prior Year Status: This condition was cited in the 2011 Single Audit as item 2011-4.

Auditee Response and Corrective Action Plan: We agree with the finding and recommendation. Payouts to municipalities were made by the National Government in accordance with the Presidential Order dated January 14, 2010 and opinion from FSM AG's office. There was no requirement to convey intended uses of each fund by the municipalities prior to payouts and the same Governor's approval was not required for these disbursements. Consequently, Chuuk State finance had no means to verify or substantiate the manner in which funds were disbursed thereby. However, DAS will look into the matter to obtain information from the relevant municipalities to clear out this audit finding.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2012

Finding No.: 2012-3
Area: Leases Payable

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

Condition: The State lost many of its lease agreements in a fire some years ago and has been working to compile all of its land and building leases and to determine if liabilities should be recorded for delinquent lease payments. Due to the state of this project, we were not able to obtain documentation and to determine if an associated liability should be recorded in the financial statements and if all requisite lease disclosures have been included in notes thereto.

Cause: The cause of this condition is that management is still researching and reconstructing the underlying lease data.

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

Recommendation: The State should set a timetable and obtain technical assistance to assist in resolution of this matter.

Prior Year Status: This condition was cited in the 2011 Single Audit as item 2011-5.

Auditee Response and Correction Action Plan: We agree with the audit finding and recommendation. DAS legal advisor and staff had started working to deal with this audit finding and with almost 50% into completion at fiscal year end. Despite the transfer of the DAS legal advisor to other office, DAS will continue gather records to reconstruct or compile all lost lease agreements until finally completed and ascertained liabilities. The recommendation to seek technical or legal assistance will also be considered for the resolution of this matter.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2012

Finding No.: 2012-4
Area: Housing Loans/Fixed Assets

Criteria: A functioning system of internal control requires that subsidiary ledgers be maintained and be supported by underlying supporting documentation, such as housing loan ledgers, fixed asset register, etc.

Condition: We were not able to obtain housing loan ledgers and fixed asset register of Chuuk State Housing Authority (CSHA) and to determine if the associated accounts should be recorded in the financial statements and if all disclosures have been included in notes thereto.

Cause: Reconciliations of CSHA's accounts were not accurately performed, and the supporting documents were not timely filed.

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

Recommendation: The State should set a timetable and obtain technical assistance to assist in resolution of this matter.

Auditee Response and Correction Action Plan: We agree with the audit finding and recommendation on fixed asset register of Chuuk State Housing Authority (CSHA), but however disagree with regards to housing loan ledgers audit finding. The housing ledgers were available for inspection and provided during fieldwork. CSHA will be advised for the resolution of the stated finding.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2012

Finding No.: 2012-5
Area: Timely and Accurate Reconciliations

Criteria: Reconciliations of accounts should be performed timely and accurately.

Condition: Audit adjustments were proposed to correct and reconcile various cash accounts:

CIB-C/A Sector Payroll BFSM	\$ 409
CIB BOG IMF Matching	(149,714)
CIB-C/A Local Payroll BFSM	(640)
CIB-Savings State CIP BOG	427
CIB-Savings Depository BFSM	(532)
CIB-C/A Gnrl NS BFSM - New	(50)
CIB-C/A Hospital BFSM	(648)
CIB- Chuuk Gnrl Sector BOG	<u>(23,796)</u>
Total corrected	\$ <u>(149,714)</u>
Total uncorrected	\$ <u>(24,830)</u>

CIB - Chuuk General Sector – Bank statements were not available for inspection.

Cause: Reconciliations of the above accounts were not timely or accurately performed.

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

Recommendation: The State should require that the subsidiary ledgers be maintained to support general ledger balances.

Auditee Response and Correction Action Plan: We agree with the audit finding and recommendation. DAS has standard procedure for the timely preparation of bank reconciliations. However, the preparation of adjusting entries for the reconciling items such as for bank interest, bank charges and debit/credit memos was overlooked. Accordingly, the necessary adjustments to correct and reconcile the various accounts will be made immediately to clear out this audit finding and ensure nonoccurrence.

**STATE OF CHUUK
FEDERATED STATES OF MICRONESIA**

Schedule of Prior Audit Findings
Year Ended September 30, 2012

The status of unresolved prior audit findings is disclosed within the Schedule of Findings and Questioned Costs section of this report (pages 67 through 72).