THE DIVING SEAGULL, INC.
(A COMPONENT UNIT OF THE STATE OF YAP)

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2012 AND 2011

Deloitte.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
The Diving Seagull, Inc.:

We have audited the accompanying statement of net assets of The Diving Seagull, Inc. (the Company), a component unit of the State of Yap, as of September 30, 2012, and the related statement of revenues, expenses and changes in net assets and of cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. The financial statements of the Company as of and for the year ended September 30, 2011 were audited by other auditors whose report, dated March 15, 2012, expressed an unqualified opinion.

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

In our opinion, such financial statements, present fairly, in all material respects, the financial position of The Diving Seagull, Inc. as of September 30, 2012 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

We also examined the adjustments described in note 13 that were applied to restate the 2011 financial statements. In our opinion, such adjustments are appropriate and have been properly applied.

In accordance with *Government Auditing Standards*, we have also issued a report dated June 21, 2013 on our consideration of The Diving Seagull, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 4 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.

Deloitte + Touche LLP

June 21, 2013

THE DIVING SEAGULL, INC.

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

The Yap State Government was required to adopt the provisions of the Government Accounting Standards Board (GASB). The Diving Seagull, Inc. is accounted for and is reported as a component unit of the State of Yap.

In 2012, the Company's total assets increased 41% from $11,532,243 (as restated) to $16,311,013. The increase is due to higher fish prices. Fiscal year 2012 is the 2nd full year of operation for the F/V Yap Seagull which began fishing in fiscal year 2010. Accordingly, the new vessel's contribution to the 35% increase in operating revenue realized in 2012 led to an 116% increase in current assets comprising primarily cash and equivalents and broker receivables. The Company is making all efforts to improve its cash position in order to finance the anticipated dry dock of at least one of the fishing vessels in late summer 2013.

The scheduling of the dry dock for the vessels is intended to coincide with the FAD (floating aggregating device) closure season. In 2010, the Parties to the Nauru Agreement adopted a FAD fishing closure policy to extend from July to September of each year as a conservation measure for the tuna species and other species that have economic value. This policy has had a major impact on the Company's fishing operations in the Western Pacific region for the past two years and will continue to affect operations in the years to come.

Operating revenues generated from fish sales of $16,527,562 represents an increase of 35% over 2011. Cost of sales, however, only increased by $446,773 indicating that the same number of fishing trips occurred during fiscal year 2012 as in 2011. The increase in fish price and minimal rejection rates contributed to higher operating revenues in 2012.

Net income from operations in the fiscal year ended September 30, 2012 increased to $5,938,913 and in 2011 income from operations was $2,042,075. The increase in net income is attributable to an increase in fish prices and a decrease in cost of sales as a percentage of operating revenues.

The Company's operating cash flows totaled $5,119,847 in 2012 and $3,254,662 in 2011. During the year ended September 30, 2012, cash and equivalents increased from $1,749,088 to $5,255,523. The increase in cash and equivalents is due to increase in fish prices that increased to $2,100 per metric ton during fiscal year 2012.

The following table summarizes the financial condition and results of operations of the Company for 2012, 2011 and 2010.

	2012	2011 (as restated)	2010
Assets			
Property and equipment, net	$ 4,768,210	$ 5,146,481	$ 5,646,174
Current assets	9,312,612	4,309,353	2,499,401
Other assets	2,230,191	2,076,409	2,070,027
Total Assets	$ 16,311,013	$ 11,532,243	$ 10,215,602
Liabilities and Net Assets			
Liabilities:			
Long-term debt, net of current portion	$ 2,688,302	$ 3,368,421	$ 4,132,808
Current portion of long-term debt	655,562	884,141	1,248,023
Other current liabilities	2,134,620	2,238,287	1,660,690
Total Liabilities	5,478,484	6,490,849	7,041,521

Net Assets:			
Invested in capital assets, net of related debt	$ 1,424,346	$ 976,771	$ 516,638
Restricted-expendable	2,230,191	2,076,289	2,070,027
Unrestricted	7,177,992	1,988,334	587,416
Total Net Assets	10,832,529	5,041,394	3,174,081
Total Liabilities and Net Assets	$ 16,311,013	$ 11,532,243	$ 10,215,602

Revenues, Expenses, and Changes in Net Assets

Operating revenues	$ 16,527,562	$ 12,266,007	$ 7,061,151
Cost of sales	(10,378,634)	(9,931,861)	(7,805,664)
Operating expenses	(210,015)	(292,071)	(388,467)
Net operating revenues	5,938,913	2,042,075	(1,132,980)
Nonoperating expenses	(147,778)	(281,172)	(179,711)
Change in net assets	$ 5,791,135	$ 1,760,903	$ (1,312,691)

Capital Assets and Debt

The Company did not acquire significant capital assets in the year ended September 30, 2012. For additional information concerning capital assets, please refer to note 6 to the financial statements.

Additionally, no additional debt was obtained in fiscal year 2012. For more information concerning debt, please refer to note 7 to the financial statements.

The Management Discussion and Analysis for the year ended September 30, 2011 is set forth in the Company's report on the audit of financial statements, which is dated March 15, 2012. That Discussion and Analysis explains the major factors impacting the 2011 financial statements and can be viewed at the FSM Office of the Public Auditor's website.

Plan of Action for 2013 – Economic Outlook

1. Challenges with FSM/PNA fishing regulations
2. Dry dock of the F/V Mathawmarfach
3. Improving profit margin of 2nd fishing vessel
4. Diversification
5. Replacement of fishing nets

THE DIVING SEAGULL, INC.

Statements of Net Assets
September 30, 2012 and 2011

	2012	2011 (As Restated) note 13
ASSETS		
Current assets:		
Cash and cash equivalents	$ 5,255,523	$ 1,749,088
Short-term investments	1,566,000	1,566,000
Investments	498,401	449,934
Net receivable from broker	1,496,575	-
Employee and director receivables	42,850	72,951
Other receivables, net	-	1,011
Prepaid expenses	103,263	95,369
Fuel inventory	350,000	375,000
Total current assets	9,312,612	4,309,353
Restricted cash and cash equivalents	2,230,191	2,076,289
Other assets	-	120
Property and equipment, net	4,768,210	5,146,481
	$ 16,311,013	$ 11,532,243
LIABILITIES AND NET ASSETS		
Current liabilities:		
Current portion of long-term debt	$ 655,562	$ 884,141
Accounts payable	1,601,296	1,524,296
Net payable to broker	-	2,851
Accrued expenses	533,324	711,140
Total current liabilities	2,790,182	3,122,428
Long-term debt, net of current portion	2,688,302	3,368,421
Total liabilities	5,478,484	6,490,849
Contingencies and commitments		
Net assets:		
Invested in capital assets, net of related debt	1,424,346	976,771
Restricted, expendable	2,230,191	2,076,289
Unrestricted	7,177,992	1,988,334
Total net assets	10,832,529	5,041,394
	$ 16,311,013	$ 11,532,243

See accompanying notes to financial statements.

THE DIVING SEAGULL, INC.

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2012 and 2011

	2012	2011 (As Restated) note 13
Operating revenues:		
Fish sales	$ 16,488,389	$ 12,019,924
Other revenues	73,198	246,083
Bad debts	(34,025)	-
Total operating revenues	16,527,562	12,266,007
Cost of sales	10,378,634	9,931,861
Gross margin	6,148,928	2,334,146
Operating expenses:		
Payroll, taxes and benefits	86,909	93,478
Travel	37,744	92,405
Professional fees	32,492	22,367
Rent	12,384	14,448
Communications and utilities	12,189	14,684
Board fees and expenses	10,227	19,550
Bank loan fees	8,886	7,036
Office expense	5,466	17,604
Insurance	546	-
Depreciation	528	6,800
Miscellaneous	2,644	3,699
Total operating expenses	210,015	292,071
Income from operations	5,938,913	2,042,075
Nonoperating revenues (expenses):		
Interest expense	(284,977)	(345,984)
Investment income	88,732	90,476
Gain (loss) on investments	48,467	(25,664)
Total nonoperating revenues (expenses), net	(147,778)	(281,172)
Change in net assets	5,791,135	1,760,903
Net assets at beginning of year	5,041,394	3,174,081
Prior period adjustment	-	106,410
Net assets at beginning of year, as stated	5,041,394	3,280,491
Net assets at end of year	$ 10,832,529	$ 5,041,394

See accompanying notes to financial statements.

THE DIVING SEAGULL, INC.

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

	2012	2011 (As Restated) note 13
Cash flows from operating activities:		
Cash received from customers	$ 15,062,161	$ 12,188,241
Cash payments to suppliers for goods and services	(8,082,732)	(7,438,236)
Cash payments to boat crew and employees for services	(1,859,582)	(1,495,343)
Net cash provided by operating activities	5,119,847	3,254,662
Cash flows from investing activities:		
Increase in short-term investments and time certificate of deposit	(65,170)	-
Interest received from short-term investments	-	64,812
Net cash used in (provided by) investing activities	(65,170)	64,812
Cash flows from capital and related financing activities:		
Acquisition of property and equipment	(354,567)	(203,735)
Principal repayments of long-term debt	(908,698)	(1,328,269)
Payments received on loan	-	38,500
Interest paid on long-term debt	(284,977)	(359,231)
Net cash used in capital and related financing activities	(1,548,242)	(1,852,735)
Net change in cash	3,506,435	1,466,739
Cash and cash equivalents at beginning of year	1,749,088	282,349
Cash and cash equivalents at end of year	$ 5,255,523	$ 1,749,088
Reconciliation of income from operations to net cash provided by operating activities:		
Operating income	$ 5,938,913	$ 2,042,075
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	732,838	703,428
Bad debt expense	34,025	-
Prior period adjustment	-	106,410
Changes in assets and liabilities:		
Net receivable from broker	(1,496,575)	-
Employee and director receivables	(2,913)	61,207
Other receivables	-	1
Prepaid expenses	(7,894)	(55,085)
Fuel inventory	25,000	(375,000)
Other assets	120	-
Accounts payable	77,000	697405
Net payable to broker	(2,851)	(138,974)
Accrued expenses	(177,816)	213,195
Net cash provided by operating activities	$ 5,119,847	$ 3,254,662

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

Reporting Entity

The Diving Seagull, Inc. (the "Company"), a component unit of the State of Yap, was incorporated in Yap in the Federated States of Micronesia on March 17, 1997. The Company is organized primarily to pursue fishing and other fishing related activities by operating fishing vessels, marketing and selling fish, and developing cold storage and/or transshipment facilities. A seven member Board of Directors is responsible for managing the business affairs and directing the daily operations of the corporation.

The Articles of Incorporation authorized the issuance of 6,500,000 shares of common stock at $1 par value per share. All such shares were issued to the Yap Investment Trust fund, a fund of the State of Yap, under the terms of a twenty-five year lease agreement for use of the fishing vessel, Mathawmarfach, and a purse seine fishing net. This Bareboat Charter Agreement expires in March 2022. The Company also purchased another fishing vessel, the Yap Seagull, in February 2010.

Basis of Accounting

The financial statements of the Company have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. Governmental Accounting Standards Board (GASB) Statement No. 20, "*Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*," requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principle Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Company has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

The Company adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34 (Basic Financial Statements – Management's Discussion and Analysis for State and Local Governments). GASB Statement No. 34 establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into four net asset categories:

(a) *Invested in capital assets, net of related debt* – Capital assets, net of accumulated depreciation, and outstanding principle balances of debt attributable to the acquisition, construction, or improvement of those assets.

(b) *Restricted Nonexpendable* – Net assets subject to externally imposed stipulations that require the Company to maintain them permanently.

(c) *Restricted Expendable* – Net assets whose use by the Company is subject to externally imposed stipulations that can be fulfilled by actions of the Company pursuant to those stipulations or that expire by the passage of time.

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

(1) Summary of Significant Accounting Policies, Continued

Basis of Accounting, Continued

The Company's 6,500,000 shares of authorized, issued and outstanding common stock with par value of $1 per share represent capital net assets. However, since all shares are held by the State and since the Company is a component unit of the State, these shares are not presented in the accompanying statement of net assets.

Operating and Non-Operating Revenues and Expenses

Operating revenues and expenses generally result directly from the operation and maintenance of the Company. Non-operating revenues and expenses result from capital and financing activities, costs and related recoveries from natural disasters, and certain other non-recurring income and costs.

New Accounting Standards

During the year ended September 30, 2012, the Company 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 Company.

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 Company.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards

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

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

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 Company.

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 Company.

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 Company.

Cash and Cash Equivalents

Cash and cash equivalents includes cash on hand as well as cash in various bank accounts and time certificates of deposit with initial maturity dates of three months or less but excludes restricted cash and cash equivalents. Deposits maintained in time certificates of deposit with original maturity dates greater than three months are separately classified as short-term investments.

(1) Summary of Significant Accounting Policies, Continued

Investments

Investments and related investment earnings and losses 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.

Fuel Inventory

Fuel inventory consists of fuel on two fishing vessels and is stated at purchased cost.

Property and Equipment

Property and equipment is stated at cost less accumulated depreciation. Routine maintenance and repairs are expensed as incurred. Depreciation is recorded in the financial statements under the straight-line method based on the estimated useful lives of the assets as follows:

Mathawmarfach vessel	20 years
Yap Seagull vessel	25 years
Fishing net and other vessel parts	5 years
Leasehold improvements	3-10 years
Vessel improvements	3-5 years
Office furniture and equipment	3-5 years
Vehicles	5 years

Leased assets and leasehold improvements are capitalized over the lesser of the useful life or the lease term. Capitalization thresholds are $1,000 for leasehold improvements and $500 for all other assets.

Revenue Recognition

The Company's primary source of revenue is derived from the sale of fish. Sales of fish are only considered earned upon offloading the catch to a designated third party. The sales are estimated, less a provision for rejected fish, based on broker commitments per ton and are adjusted upon receipt of a final settlement from the broker.

Other revenue is recorded when earned and measurable.

Translation of Foreign Currencies

Gains and losses that arise from exchange rate changes on transactions denominated in a currency other than U.S. dollars are included in the statement of revenues, expenses and changes in net assets.

(1) Summary of Significant Accounting Policies, Continued

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Allowance for Doubtful Accounts

The Company establishes an allowance for doubtful accounts receivable based on the credit risk of specific customers, historical trends, and other information. Bad debts are written off against the allowance based on the direct identification method.

(2) Deposits

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

The deposit and investment policies of the Company are governed by its enabling legislation. The Board of Directors is required to engage one or more fund custodians to assume responsibility for the physical possession of the Company's investments.

GASB Statement No. 40 requires disclosures for deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Company'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 Company does not have a deposit policy for custodial credit risk.

As of September 30, 2012 and 2011, the carrying amount of the Company's total cash and cash equivalents and time certificates of deposit was $9,051,714 and $5,391,377, respectively, and the corresponding bank balances were $9,055,585 and $5,800,143, respectively. Of the bank balances, $7,232,217 and $4,083,215, respectively, is maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2012 and 2011, bank deposits in the amount of $5,458,316 and $2,312,748, respectively, were FDIC insured. The Company 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. The Company has not experienced any losses on such accounts and management believes it is not exposed to any significant credit risk on its deposits.

(3) Investments

GASB Statement No. 40 requires disclosures addressing common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Company will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Company's investments are held and administered by trustees. Based on negotiated trust and custody contracts, all of these investments were held in the Company's name by the Company's custodial financial institutions. Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

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

As of September 30, 2012 and 2011, investments at fair value comprise the following:

	2012	2011
Fixed income securities:		
U.S. Treasury obligations	$ 79,176	$ 76,577
U.S. Government agencies	34,479	29,358
Corporate notes	78,874	82,763
	192,529	188,698
Other Investments:		
Common equities	288,133	243,262
Money market funds	17,739	17,974
	305,872	261,236
	$ 498,401	$ 449,934

As of September 30, 2012, the Company's fixed income securities had the following maturities:

2012					
		Fair Value	Less than 1 Year	1 to 5 Years	6 to 10 Years
U.S. Treasury obligations	AAA	$ 78,904	$ 29,438	$ 35,685	$ 13,781
U.S. Government agencies obligations	AAA	34,751	20,645	14,106	-
Corporate Notes	A1	28,436	-	15,977	12,459
Corporate Notes	A2	16,744	-	-	16,744
Corporate Notes	A3	33,694	-	23,181	10,513
		$ 192,529	$ 50,083	$ 88,949	$ 53,497

THE DIVING SEAGULL, INC.

Notes to Financial Statements
September 30, 2012 and 2011

(3) Investments, Continued

As of September 30, 2011, the Company's fixed income securities had the following maturities:

2011					
	Fair Value	% of Investments	Interest Rate	Investment maturities in years > 1	Investment maturities in years 1-5
Total Government and Government Sponsored Entity Bonds:					
Federal National Mortgage Assn	$ 7,827	1.74%	4.625%	$ -	$ 7,827
U.S. Treasury Notes	4,635	1.03%	4.50%	-	4,635
U.S. Treasury Notes	4,070	0.90%	4.875%	4,070	-
Federal National Mortgage Assn	10,796	2.40%	4.375%	-	10,796
Federal National Mortgage Assn	10,735	2.39%	4.500%	-	10,735
U.S. Treasury Notes	10,423	2.32%	4.00%	-	10,423
U.S. Treasury Notes	19,338	4.30%	1.375%	-	19,338
U.S. Treasury Notes	10,720	2.38%	3.125%	-	10,720
U.S. Treasury Notes	20,975	4.66%	2.250%	-	20,975
Total Government and Government	6,416	1.43%	2.625%	-	6,416
Sponsored Entity Bonds	$ 105,935	23.54%			
Other Investments:					
Equity mutual funds	$ 16,476	3.66%			
Equity securities – domestic	201,500	44.78%			
Equity securities – international	41,762	9.28%			
Domestic corporate bonds	82,763	18.39%			
Total Other Investments	342,501	76.12%			
Cash balance	1,498	0.33%			
Total Investments	$ 449,934	100%			

Investment Type	Fair Value	Moody's	S & P	% of Total Investments
U.S. Treasury Securities	$ 76,577	AAA	AAA	17%
U.S. Government Backed Mortgage Securities	29,538		AAA	7%
Equity Mutual Funds	16,476		unrated	4%
Equity securities - domestic	201,500		unrated	45%
Equity securities - international	41,762		unrated	9%
Cash balance	1,498		unrated	-%
Domestic corporate bonds	11,835	A2	A	3%
Domestic corporate bonds	10,514	A2	A+	2%
Domestic corporate bonds	10,502	AA2	AA+	2%
Domestic corporate bonds	22,578	A3	A-	5%
Domestic corporate bonds	10,324	A1	A	2%
Domestic corporate bonds	5,127	A1	A+	1%
Domestic corporate bonds	11,883	A1	AA	3%
Total	$ 449,934			100%

(4) Net Receivable from/Payable to Broker

Approximately 92% of fish sales in the years ended September 30, 2012 and 2011 were conducted with a single broker based in Taiwan. Upon offloading the fish catch from the vessel to a designated third party, the broker pays 95% of the estimated settlement. When the final settlement is determined, the Company may either be entitled to an additional amount due from the broker or be liable for an amount due to the broker. The net broker account is a receivable of $1,496,575 at September 30, 2012 and a payable of $2,851 at September 30, 2011.

(5) Notes and Other Receivables

Outstanding balances from notes and other receivables due the Company from various parties are detailed below.

	2012	2011
Palau Micronesia Air (PMAir)	$ 550,000	$ 550,000
Others	31,140	31,140
	581,140	581,140
Less: allowance for doubtful accounts	(581,140)	(580,129)
	$ -	$ 1,011

(6) Property and Equipment

Property and equipment consist of the following at September 30, 2012 and 2011:

	Beginning Balance Oct. 1, 2011	Transfers and Additions	Transfers and Disposals	Ending Balance Sept.30, 2012
Leased fishing vessel and purse seine net	$ 6,821,012	$ -	$ -	$ 6,821,012
Purchased fishing vessel and purse seine net	5,717,316	-	-	5,717,316
Leasehold improvements	3,871,346	277,203	-	4,148,549
Vessel improvements	183,872	77,364	-	261,236
Office furniture and equipment	33,785	-	-	33,785
Vehicle	26,568	-	-	26,568
Total cost	16,653,899	354,567	-	17,008,466
Less accumulated depreciation	(11,507,418)	(732,838)	-	(12,240,256)
	$ 5,146,481	$ (378,271)	$ -	$ 4,768,210

(6) Property and Equipment, Continued

	Beginning Balance Oct. 1, 2010	Transfers and Additions	Transfers and Disposals	Ending Balance Sept.30, 2011
Leased fishing vessel and purse seine net	$ 6,821,012	$ -	$ -	$ 6,821,012
Purchased fishing vessel and purse seine net	5,552,316	165,000	-	5,717,316
Leasehold improvements	3,849,555	21,791	-	3,871,346
Vessel improvements	167,598	16,274	-	183,872
Office furniture and equipment	33,115	670	-	33,785
Vehicle	26,568	-	-	26,568
Total cost	16,450,164	203,735	-	16,653,899
Less accumulated depreciation	(10,803,990)	(703,428)	-	(11,507,418)
	$ 5,646,174	$ (499,693)	$ -	$ 5,146,481

(7) Long-Term Debt

On July 28, 2006, the Company signed a five-year loan agreement with the Federated States of Micronesia Development Bank (FSMDB) authorizing a maximum loan of $1,300,000 to cover the dry-dock costs of the fishing vessel. The agreement stipulates a 1.5% loan fee and interest rate of 9%. Interest is due monthly during the six-month grace period. Interest and principal are payable in monthly installments of $26,986 beginning January 30, 2007. Part of the loan agreement requires the Company to establish a joint account with FSMDB and to make deposits therein as required by that agreement. This loan was fully paid in the year ended September 30, 2012.

On February 16, 2007, a loan of $1,370,000 was granted by FSMDB to cover additional dry dock costs of the fishing vessel. Interest of 9% and principal are payable in monthly installments of $28,606 beginning June 15, 2007. This loan was fully paid in the year ended September 30, 2012.

On October 27, 2009, a loan of $3,000,000 was granted by FSMDB to purchase a fishing vessel. Interest of 9% and principal are payable in monthly installments of $38,003, which began on April 25, 2010. The balance on the loan was $2,509,851 and $2,722,415 as at September 30, 2012 and 2011, respectively.

On June 16, 2010, a line of credit was issued for working capital from FSMDB in the amount of $500,000, with an interest rate of 9%. The balance on the line of credit was $0 as at September 30, 2012 and 2011.

On September 29, 2010, a loan of $2,000,000 was granted by the Bank of Guam, with interest of 2.12%, to assist in the purchase of a new vessel. Interest and principal are payable in monthly installments of $35,778, which began on October 29, 2010. Part of the agreement requires the Company to have on deposit with the Bank of Guam a $2,000,000 certificate of deposit. The balance of this restricted certificate of deposit at September 30, 2012 and 2011 was $2,023,901 and $2,020,466, respectively. The balance on the loan was $834,013 and $1,268,265 as at September 30, 2012 and 2011, respectively.

(7) Long-Term Debt, Continued

Future debt service on the above debt is as follows:

Year ending September 30,	Principal	Interest	Total
2013	$ 655,562	$ 229,810	$ 885,372
2014	680,722	198,408	879,130
2015	287,001	169,035	456,036
2016	313,924	142,112	456,036
2017	343,372	112,664	456,036
2018-2020	1,063,283	134,629	1,197,912
	$ 3,343,864	$ 986,658	$ 4,330,522

Changes in debt during the years ended September 30, 2012 and 2011 follows:

2012				
Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
$ 4,252,562	$ -	$ (908,698)	$ 3,343,864	$ 655,562

2011				
Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
$ 5,542,331	$ 38,500	$ (1,328,269)	$ 4,252,562	$ 884,141

(8) Lease Commitments

The Company leases the fishing vessel and purse seine fishing net from Yap Investment Trust, a fund of the Yap State Government (the "State"), with a lease term through July 2022. Common stock was issued by the Company as total consideration for the agreement.

(9) Cost of Sales

Details of cost of sales for the years ended September 30, 2012 and 2011 are as follows:

	2012	2011
Fuel	$ 4,751,869	$ 4,698,252
Crew salaries and wages	1,518,928	1,449,499
License, agent and port fees	991,891	749,906
Repair and maintenance	757,292	737,365
Depreciation	732,310	696,628
Insurance	449,577	463,469
Salt and provisioning	407,152	404,875
Management fee	256,892	311,439
Supplies and freight	157,239	33,264
Crew travel	150,214	139,415
Communications	107,334	103,208
Stevedoring	78,515	93,780
Other vessel expenses	19,421	50,761
	$ 10,378,634	$ 9,931,861

(10) Risk Management

The Company 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. The Company has elected to purchase commercial insurance for the risks of loss to which it is exposed. The Company claims expenses and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. No losses as a result of these risks have occurred in any of the past three years.

(11) Related Parties

The Company has entered into significant transactions with the State, as discussed in Note 8. Several board members and officers of the Company hold management positions and other positions of influence with the State. Furthermore, included in employee and director receivables is $26,700 and $65,328 as at September 30, 2012 and 2011, respectively, representing amounts owed by previous board members and current management to the Company for reimbursement of travel expenses, net of allowance for doubtful accounts.

(12) Subsequent Events

On October 1, 2012, a settlement agreement was entered into between the National Government of the Federated States of Micronesia and the Company. The agreement stipulated that $50,000 USD be paid in penalty for fishing in the closed high seas pocket, which is in violation of the Tuna Convention conservation measure and section 906(1) of the FSM Marine Resources Act 2002. $50,000 was fully paid by the Company on October 8, 2012. As of September 30, 2012, $50,000 was accrued in accounts payable and included in cost of sales license, agent and port fees.

(13) Prior Period Adjustments and Restated Financial Statements

A prior period adjustment of $106,410 was recorded in the year ended September 30, 2011 as reflected in the Statement of Changes in Net Assets. Please refer to the audit report ending September 30, 2011 dated March 15, 2012 for details of this prior period adjustment.

Additionally, the 2011 financial statements were restated to correct errors in the following accounts.

Accounts Affected	Original Balance	Restated Balance	Difference
Fuel inventory	$ -	$ 375,000	$ 375,000
Accounts payable	(1,260,355)	(1,524,296)	(263,941)
Accrued expense	(640,572)	(711,140)	(70,568)
Unrestricted net assets	(1,947,843)	(1,988,334)	(40,491)
Cost of sales	9,972,352	9,931,861	(40,491)

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

To the Board of Directors of
The Diving Seagull, Inc.:

We have audited the financial statements of The Diving Seagull, Inc. (the Company), as of and for the year ended September 30, 2012, and have issued our report thereon dated June 21, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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

Compliance and Other Matters

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

We noted other matters that we reported to management of the Company in a separate letter dated June 21, 2013.

This report is intended for the information of the Board of Directors and management of The Diving Seagull, Inc, and others within the entity, and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte + Touche LLP

June 21, 2013