

June 30, 2013

His Excellency Emmanuel Mori  
President  
Federated States of Micronesia:

Dear Mr. President:

We have performed an audit of the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Federated States of Micronesia (FSM) National Government as of and for the year ended September 30, 2012, in accordance with auditing standards generally accepted in the United States of America (“generally accepted auditing standards”) and have issued our report thereon dated June 30, 2013.

We have prepared the following comments to assist you in fulfilling your obligation to oversee the financial reporting and disclosure process for which management of the FSM National Government is responsible.

## **OUR RESPONSIBILITY UNDER GENERALLY ACCEPTED AUDITING STANDARDS AND GENERALLY ACCEPTED GOVERNMENT AUDITING STANDARDS**

Our responsibility under generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, have been described in our engagement letter dated November 26, 2012. As described in that letter, the objective of a financial statement audit conducted in accordance with the aforementioned standards is:

- To express an opinion on the fairness of each opinion unit in the FSM National Government’s basic financial statements and the accompanying supplementary information, and to disclaim an opinion on the required supplementary information for the year ended September 30, 2012 in conformity with accounting principles generally accepted in the United States of America (“generally accepted accounting principles”), in all material respects;
- To express an opinion on whether the supplementary information that accompanies the basic financial statements is presented fairly, in all material respects, in relation to the basic financial statements taken as a whole;
- To report on the FSM National Government’s internal control over financial reporting and on its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters for the year ended September 30, 2012 based on an audit of financial statements performed in accordance with the standards applicable to financial audits contained in *Government Auditing Standards*; and

- To report on the FSM National Government's compliance with requirements applicable to each major federal program and on internal control over compliance in accordance with the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* (OMB Circular A-133).

Our responsibilities under generally accepted auditing standards include forming and expressing an opinion about whether the financial statements that have been prepared with the oversight of management and the Office of the President are presented fairly, in all material respects, in conformity with generally accepted accounting principles. The audit of the financial statements does not relieve management or the Office of the President of their responsibilities.

We considered the FSM National Government's 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 FSM National Government's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the FSM National Government's internal control over financial reporting. Our consideration of internal control over financial reporting would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses.

We also considered the FSM National Government's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our 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. Our audit does not, however, provide a legal determination of the FSM National Government's compliance with those requirements.

## **ACCOUNTING ESTIMATES**

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's current judgments. Those judgments are ordinarily based on knowledge and experience about past and current events and on assumptions about future events. Significant accounting estimates reflected in the FSM National Government's 2012 financial statements include management's estimate of the allowance for uncollectible accounts, which is determined based upon past collection experience and aging of the accounts, and management's estimate of depreciation expense, which is based on estimated useful lives of the respective capital assets. During the year ended September 30, 2012, we are not aware of any significant changes in accounting estimates or in management's judgments relating to such estimates.

## **MATERIAL CORRECTED MISSTATEMENTS**

Material misstatements were brought to the attention of management as a result of our audit procedures and were corrected by management during the current period. We have attached to this letter, as Attachment I, a summary of misstatements corrected by management.

## **UNCORRECTED MISSTATEMENTS**

Our audit of the financial statements was designed to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud. We have attached to this letter, as Appendix A to Attachment II, a summary of uncorrected misstatements aggregated by us during the current engagement and pertaining to the latest period presented that were determined by management to be immaterial, both individually and in the aggregate, to the financial statements taken as a whole. We have also attached to this letter, as Appendix B to Attachment II, a summary of undisclosed financial statement disclosures aggregated by us that was determined by management to be immaterial to the financial statements.

## **SIGNIFICANT ACCOUNTING POLICIES**

The FSM National Government's significant accounting policies are set forth in Note 1 to the FSM National Government's 2012 financial statements. During the year ended September 30, 2012, there were no significant changes in previously adopted accounting policies or their application, except for the following pronouncements adopted by the FSM National Government:

- 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.
- 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 these pronouncements did not have a material effect on the financial statements of the FSM National Government.

## **DISAGREEMENTS WITH MANAGEMENT**

We have not had any disagreements with management related to matters that are material to the FSM National Government's 2012 financial statements.

## **CONSULTATION WITH OTHER ACCOUNTANTS**

We are not aware of any consultations that management may have had with other accountants about auditing and accounting matters during 2012.

## **MAJOR ISSUES DISCUSSED WITH MANAGEMENT PRIOR TO OUR RETENTION**

Throughout the year, routine discussions were held, or were the subject of correspondence, with management regarding the application of accounting principles or auditing standards in connection with transactions that have occurred, transactions that are contemplated, or reassessment of current circumstances. In our judgment, such discussions or correspondence were not held in connection with our retention as auditors.

## **OTHER SIGNIFICANT ISSUES DISCUSSED, OR SUBJECT OF CORRESPONDENCE, WITH MANAGEMENT**

Throughout the year, routine discussions were held, or were the subject of correspondence, with management. In our judgment, such discussions or correspondence did not involve significant issues requiring communication to the Office of the President.

## **SIGNIFICANT DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT**

In our judgment, we received the full cooperation of the FSM National Government's management and staff and had unrestricted access to the FSM National Government's senior management in the performance of our audit.

## MANAGEMENT'S REPRESENTATIONS

We have made specific inquiries of the FSM National Government's management about the representations embodied in the financial statements. Additionally, we have requested that management provide to us the written representations the FSM National Government is required to provide to its independent auditors under generally accepted auditing standards. We have attached to this letter, as Attachment II, a copy of the representation letter we obtained from management.

## CONTROL-RELATED MATTERS

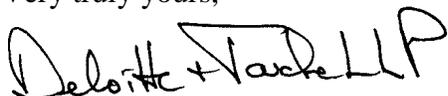
We have issued a separate report to you, also dated June 30, 2013, containing certain matters involving the FSM National Government's internal control over financial reporting that we consider to be material weaknesses or significant deficiencies under standards established by the American Institute of Certified Public Accountants, and on its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. We have also issued a separate report to you, also dated June 30, 2013, containing certain matters involving the FSM National Government's compliance with requirements applicable to each major program and on internal control over compliance in accordance with OMB Circular A-133. Although we have included management's written responses to our comments contained in those reports, such responses have not been subjected to the auditing procedures applied in our audit of the basic financial statements and, accordingly, we do not express an opinion or provide any form of assurance on the appropriateness of the responses or the effectiveness of any corrective actions described therein.

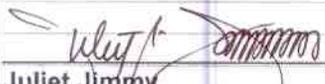
We also noted certain matters that we reported to management of the FSM National Government in a separate letter dated June 30, 2013.

\* \* \* \* \*

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

Very truly yours,

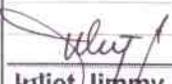
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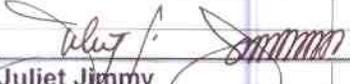
FSM National Government Appendix C - General Fund September 30, 2012			
#	Name	Debit	Credit
<b>5 AJE To record Grants Fund allowance</b>			
01-1811-AS	Allow for D/A General	193,123	0
01-1999-AS	Due to Treasury Fund	0	500,000
99-1999-AS-01	DUE TO	500,000	0
99-1999-AS-20	DUE TO	0	500,000
01-10-29-01095-8812-EX	Non-recurring Adj -Bad Debt Exp	306,877	0
		<b>1,000,000</b>	<b>1,000,000</b>
	To record allowance on Fund 20 - Grants Fund AR and transfer portion of GF allowance to Fund 20.		
<b>6 AJE To record transfer from Student Loan fund</b>			
01-1999-AS	Due to Treasury Fund	614,448	0
01-7910-RE	Operating Transfers In	0	614,448
99-1999-AS-01	DUE TO	0	614,448
99-1999-AS-38	DUE TO	614,448	0
		<b>1,228,896</b>	<b>1,228,896</b>
	To record transfer from student loan fund to GF. Student loan fund are for scholarship and scholarship appropriation and expenditure are recorded in GF.		
The above adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements. In connection with the Audit Adjustments listed above, we have reviewed and approve them on the basis of information we have provided you.			
	 <b>Juliet Jimmy</b> Assistant Secretary for National Treasury FSM National Government		

FSM National Government			
Appendix C - General Fund			
September 30, 2012			
#	Name	Debit	Credit
<b>1 RJE To reclass COM-FSM AP</b>			
01-3110-LI	Accounts Payable	25,443	0
25-3110-LI	Accounts Payable	10,500	0
25-3000 - DTT	AP - Component Unit	0	10,500
01-3000 - DTT	AP - Component Unit	0	25,443
53-3110	Payable	141,050	0
53-3000-LI-DTT	AP COMPONENT UNIT	0	141,050
		176,993	176,993
	To reclass COM-FSM AP for FS presentation		
<b>2 RJE To reclassify Chuuk Recovery interest</b>			
01-1710-AS	A/R Interest	0	175,576
01-1711-AS	Interest - Chuuk Recovery	175,576	0
		175,576	175,576
	To reclass interest on Chuuk Recovery Loan for FS presentation.		
<b>3 RJE To reclassify retainage</b>			
53-3110	Payable	218,701	0
53-3710-LI	Retention payable	0	218,701
		218,701	218,701
	To reclass retainaged of AIP for FS presentation purposes.		
<b>4 RJE To reclass bad debt recovery</b>			
01-10-29-7999-RE	GF Revenues -Other Miscellaneous	478,203	0
01-10-29-01095-881	Non-recurring Adj -Bad Debt Exp	0	478,203
		478,203	478,203
	To reclass collection from Continental (part of AR of prior year) to offset against the CY bad debt expense.		
<b>5 RJE To reclass Single Audit at Sector Holding</b>			
01-1999-AS	Due to Treasury Fund	0	689,497
99-1999-AS-01	DUE TO	689,497	0
99-1999-AS-20	DUE TO	0	689,497
01-3141-LI	Fed D/D Payable	689,497	0
		1,378,994	1,378,994
	To reverse the AR recorded at federal grants fund for Single Audit collection included at BOH Sector Holding account, deposited to GF Treasury in 2013.		
<b>6 RJE To offset cash at Sector holding against AR</b>			
01-1999-AS	Due to Treasury Fund	0	1,360,733
99-1999-AS-01	DUE TO	1,360,733	0
99-1999-AS-10	DUE TO	0	294,711
99-1999-AS-11	DUE TO	0	427,735
99-1999-AS-14	DUE TO	0	304,085
99-1999-AS-15	DUE TO	0	334,202
01-3141-LI	Fed D/D Payable	1,360,733	0
		2,721,466	2,721,466
	To offset cash at Sector Holding account against the AR at Sector grants fund.		

**ATTACHMENT I, CONTINUED**

The above adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements. In connection with the Audit Adjustments listed above, we have reviewed and approve them on the basis of information we have provided you.

			
<b>Juliet Jimmy</b>			
Assistant Secretary for National Treasury			
<b>FSM National Government</b>			

FSM National Government			
Appendix C - U.S Federal & Comp 1 Grants			
September 30, 2012			
#	Name	Debit	Credit
<b>4 AJE To record allowance on AR.</b>			
20-1999-AS	Due to Treasury Fund	500,000	0
20-1811-AS	Allowance for bad debts	0	500,000
		500,000	500,000
	To record allowance on AR, expenditure absorbed by GF.		
<b>6 AJE To record related revenue for JVI0618</b>			
20-1410-AS	A/R Fed Grants FSM States	45,919	0
20-1410-AS	A/R Fed Grants FSM States	100,157	0
20-80-84-27412-7111-RE	PNI Airport Rehab Runway -Federal Grants-Accrued rev	0	146,076
		146,076	146,076
	To record related revenue		
<p>The above adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements. In connection with the Audit Adjustments listed above, we have reviewed and approve them on the basis of information we have provided you.</p>			
 Juliet Jimmy Assistant Secretary for National Treasury FSM National Government			

<b>FSM National Government</b>			
<b>Appendix C - U.S Federal &amp; Comp 1 Grants</b>			
<b>September 30, 2012</b>			
<b>#</b>	<b>Name</b>	<b>Debit</b>	<b>Credit</b>
	<b>1 RJE To reclass COM-FSM AP</b>		
20-3110-LI	Accounts Payable	6,000	0
20-3000-DTT	AP COMPONENT UNIT	0	6,000
		<b>6,000</b>	<b>6,000</b>
	To reclass COM-FSM AP for FS presentation.		
	<b>2 RJE To reclass retainage</b>		
20-3110-LI	Accounts Payable	4,155,318	0
20-3711-LI	Retainage Payable	0	4,155,318
		<b>4,155,318</b>	<b>4,155,318</b>
	To reclass retainage for AIP.		
	<b>3 RJE To reclass Single Audit collection</b>		
20-1310-AS	A/R Fed. Grants Natl	0	689,497
20-1999-AS	Due to Treasury Fund	689,497	0
		<b>689,497</b>	<b>689,497</b>
	To reclass Single audit collection/reimbursement from DOI included in the BOH Sector Holding account, transferred to GF Treasury checking account in 2013.		

The above adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements. In connection with the Audit Adjustments listed above, we have reviewed and approve them on the basis of information we have provided you.

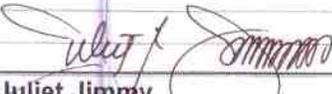
  
 \_\_\_\_\_  
**Juliet Jimmy**  
 Assistant Secretary for National Treasury  
 FSM National Government







FSM National Government			
Appendix C - Other Governmental (NM) Fund			
September 30, 2012			
#	Name	Debit	Credit
	<b>1 AJE To record transfer on Scholarship fund</b>		
38-1999-AS	Due to Treasury Fund	-	614,448
38-8910	Transfer out	614,448	-
		614,448	614,448
	To record transfer to GF from Loan fund.		
<p>This above adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements. In connection with the Audit Adjustments listed above, we have reviewed and approve them on the basis of information we have provided you.</p>			
 Juliet Jimmy Assistant Secretary for National Treasury FSM National Government			

FSM National Government			
Appendix C - General Fixed Asset Accounts			
September 30, 2012			
#	Name	Debit	Credit
	<b>3 AJE To revert back to CIP Lelu &amp; Utwe Elem Bldg</b>		
95-2815	Fixed Assets Buildings & Impro	-	2,739,796
95-2818	Fixed Assets CIP	2,739,796	-
		2,739,796	2,739,796
	To revert back to CIP Lelu & Utwe Elem School Construction project as such are still in progress as of 9/30/12.		
<p>This above adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements. In connection with the Audit Adjustments listed above, we have reviewed and approve them on the basis of information we have provided you.</p>			
			
	<b>Juliet Jimmy</b>		
	Assistant Secretary for National Treasury		
	<b>FSM National Government</b>		



Secretary of Finance  
&  
Administration

**GOVERNMENT OF THE  
FEDERATED STATES OF MICRONESIA**  
Department of Finance and Administration

P.O. Box PS 158  
Palikir, Pohnpei FM 96941  
Tel: (691) 320-2640/5852 Fax: (691) 320-7728  
E-mail: fsmsofa@mail.fm

**ATTACHMENT II**

June 30, 2013

Deloitte & Touche LLP  
361 SOUTH MARINE CORPS DRIVE  
TAMUNING, GU 96913

We are providing this letter in connection with your audit of the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Federated States of Micronesia (FSM) National Government (the "Government"), as of and for the year ended September 30, 2012, which collectively comprise the Government's basic financial statements for the purpose of expressing an opinion as to whether the basic financial statements present fairly, in all material respects, the financial position, results of operations or changes in fund balances, and cash flows of the Government in conformity with accounting principles generally accepted in the United States of America.

We confirm that we are responsible for the following:

- a. The fair presentation in the basic financial statements of financial position of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information, in conformity with accounting principles generally accepted in the United States of America.
- b. The design, implementation, and maintenance of programs and controls to prevent and detect fraud, including fraud related to federal awards.
- c. Establishing and maintaining effective internal control over financial reporting.
- d. The review and approval of the financial statements and related notes and acknowledge your role in the preparation of this information. Specifically, we acknowledge that your role in the preparation of the financial statements was a matter of convenience rather than one of necessity. We have reviewed the financial statement preparation assistance provided by you and acknowledge that the financial statements are prepared in accordance with GAAP. Our review was based on the use of the financial statement disclosure checklist for a general-purpose government obtained from the Government Finance Officers Association.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

We confirm, to the best of our knowledge and belief, the following representations made to you during your audit.

1. The basic financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America. In addition:
  - a. The financial statements include all component units as well as joint ventures with an equity interest, and properly disclose all other joint ventures and other related organizations.
  - b. The financial statements properly classify all funds and activities, including special and extraordinary items.
  - c. All funds that meet the quantitative criteria in the GASB Codification of Government Accounting and Financial Reporting Standards section 2200.153 for presentation as major are identified and presented as such and all other funds that are presented as major are particularly important to financial statement users. Specifically, the FSM National Government has elected to add an additional major fund that is of specific public interest, namely the Compact Trust Fund.
  - d. Net asset components (invested in capital assets, net of related debt; restricted; and unrestricted) and fund balance reserves and designations are properly classified and, if applicable, approved.
  - e. Expenses have been appropriately classified in or allocated to functions and programs in the statement of activities, and allocations have been made on a reasonable basis.
  - f. Revenues are appropriately classified in the statement of activities within program revenues, general revenues, contributions to term or permanent endowments, or contributions to permanent fund principal.
  - g. Interfund, internal, and intra-government activity and balances have been appropriately classified and reported.
  - h. Deposits and investment securities are properly classified in the category of custodial credit risk.
  - i. Capital assets, including infrastructure assets, are properly capitalized, reported, and, if applicable, depreciated.
  - j. Required supplementary information is measured and presented within prescribed guidelines.
  - k. Applicable laws and regulations are followed in adopting, approving, and amending budgets.
  - l. Federal awards expenditures have been charged in accordance with applicable cost principles.
2. The Government has provided to you all relevant information and access as agreed in the terms of the audit engagement letter.

3. The Government has provided you:
  - a. Public Laws as enacted by the FSM Congress.
  - b. Financial records and related data for all financial transactions of the Government and for all funds administered by the Government except as described in your Independent Auditors' Reports on Internal Control and on Compliance. The records, books, and accounts, as provided to you, record the financial and fiscal operations of all funds administered by the Government and provide the audit trail to be used in a review of accountability. Information presented in financial reports is supported by the books and records from which the financial statements have been prepared.
  - c. Contracts and grant agreements (including amendments, if any) and any other correspondence that has taken place with federal agencies.
4. There has been no:
  - a. Action taken by Government management that contravenes the provisions of federal laws and FSM laws and regulations, or of contracts and grants applicable to the Government.
  - b. Communication from other regulatory agencies concerning noncompliance with or deficiencies in financial reporting practices or other matters that could have a material effect on the financial statements.
5. We believe the effects of any uncorrected financial statement misstatements aggregated by you during the current audit engagement and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. A summary of such uncorrected misstatements has been attached as Appendix A.
6. We have completed our procedures to evaluate the accuracy and completeness of the disclosures in our financial statements. As a result of the evaluation process, we identified certain disclosures that, although required by generally accepted accounting principles, have been omitted from our financial statements. Those omitted disclosures that are regarded as more than clearly trivial are attached as Appendix B. We believe the effects of the omitted disclosures are quantitatively and qualitatively immaterial, both individually and in the aggregate, to the financial statements as a whole.
7. The Government has not performed a risk assessment, including the assessment of the risk that the financial statements may be materially misstated as a result of fraud. However, management has made available to you their understanding about the risks of fraud in the Government and do not believe that the financial statements are materially misstated as a result of fraud.
8. We have no knowledge of any fraud or suspected fraud affecting the Government involving:
  - a. Management.
  - b. Employees who have significant roles in internal control over financial reporting.
  - c. Others if the fraud could have a material effect on the financial statements.

9. We have no knowledge of any allegations of fraud or suspected fraud affecting the Government received in communications from employees, former employees, analysts, regulators, or others.
10. There are no unasserted claims or assessments that legal counsel has advised us are probable of assertion and must be disclosed in accordance Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 450, *Contingencies*, except as disclosed in note 10 to the financial statements.
11. Significant assumptions used by us in making accounting estimates are reasonable.
12. The Schedule of Expenditures of Federal Awards was prepared in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. We have identified in that schedule all awards provided by federal agencies in the form of grants, contracts, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, or direct appropriations. We have also properly identified subrecipient expenditures. In addition, we have accurately completed the appropriate sections of the data collection form.
13. We are responsible for compliance with local, state, and federal laws, rules, and regulations, including compliance with the requirements of OMB Circular A-133, and provisions of grants and contracts relating to the Government's operations. We are responsible for establishing and maintaining the components of internal control relating to our activities in order to achieve the objectives of providing reliable financial reports, effective and efficient operations, and compliance with laws and regulations. The Government is responsible for maintaining accounting and administrative control over revenues, obligations, expenditures, assets, and liabilities.
14. We are responsible for establishing and maintaining, and have established and maintained, effective internal control over compliance for federal programs that provides reasonable assurance that we are managing federal awards in compliance with laws, regulations, and provisions of contracts or grant agreements that could have a material effect on its federal programs.
15. We have disclosed to you all deficiencies in the design or operation of internal control over financial reporting identified as part of our evaluation, including separately disclosing to you all such deficiencies that are significant deficiencies or material weaknesses in internal control over financial reporting.
16. We have:
  - a. Identified the requirements of laws, regulations, and the provisions of contracts and grant agreements that are considered to have a direct and material effect on each federal program as identified in Part 3 of the Compliance Supplement dated August 2012.
  - b. Complied, in all material respects, with the requirements identified above in connection with federal awards.
  - c. Identified and disclosed interpretations of any compliance requirements that have varying interpretations.

- d. Made available all information related to federal financial reports and claims for advances and reimbursements. Federal financial reports and claims for advances and reimbursements are supported by the books and records from which the financial statements have been prepared and are prepared on a basis consistent with that presented in the Schedule of Expenditures of Federal Awards. The copies of federal program financial reports provided are true copies of the reports submitted, or electronically transmitted, to the federal agency or pass-through entity, as applicable.
  - e. Monitored subrecipients to determine that they have expended pass-through assistance in accordance with applicable laws and regulations and have met the requirements of Circular A-133.
  - f. Taken appropriate corrective action on a timely basis after receipt of a subrecipient's auditor's report that identifies noncompliance with laws, regulations, or the provisions of contracts or grant agreements.
  - g. Considered the results of the subrecipient's audits and made any necessary adjustments to the auditee's own books and records.
  - h. Identified and disclosed all amounts questioned and any known noncompliance with the requirements of federal awards, including the results of other audits or program reviews related to the objectives of the audit.
  - i. Identified previous financial audits, attestation engagements, performance audits, or other studies related to the objectives of the audit and the corrective actions taken to address significant findings and recommendations, including the status of follow-up on prior audit findings (and information about all management decisions) by federal awarding agencies and pass-through entities.
  - j. Provided to you our views on the reported findings, conclusions, and recommendations for your report.
17. We are responsible for follow-up on all prior-year(s) findings. We have prepared a summary schedule of prior-year findings reporting the status of our efforts in implementation of the prior-year's corrective action plan.
  18. We have included in the corrective action plan for current-year findings, the name of the person in our organization responsible for implementation of the actions, the best actions to be taken, and the estimate of a completion date. We have taken timely and appropriate steps to remedy fraud, illegal acts, violation of provisions of contracts or grant agreements, or abuse that you report.
  19. Management has identified and disclosed to you all laws and regulations that have a direct and material effect on the determination of financial statement amounts.
  20. We have adopted the provisions of GASB Codification of Government Accounting and Financial Reporting Standards Section 2100, *Defining the Financial Reporting Entity*. We believe that we have properly identified and reported as a component unit of the Government each organization that meets the criteria established in GASB Codification of Government Accounting and Financial Reporting Standards Section 2100, *Defining the Financial Reporting Entity*.

Except where otherwise stated below, matters less than \$240,000 collectively are not considered to be exceptions that require disclosure for the purpose of the following representations. This amount is not necessarily indicative of amounts that would require adjustment to, or disclosure in, the basic financial statements.

21. Except as listed in Appendix A, there are no transactions that have not been properly recorded in the accounting records underlying the financial statements.
22. The Government has no plans or intentions that may affect the carrying value or classification of assets and liabilities.
23. The following, to the extent applicable, have been appropriately identified, properly recorded, and disclosed in the financial statements:
  - a. Related-party transactions and associated amounts receivable or payable, including sales, purchases, loans, transfers, leasing arrangements, and guarantees (written or oral).
  - b. Guarantees, whether written or oral, under which the Government is contingently liable.
24. In preparing the financial statements in conformity with accounting principles generally accepted in the United States of America, management uses estimates. All estimates have been disclosed in the financial statements for which known information available prior to the issuance of the financial statements indicates that both of the following criteria are met:
  - a. It is at least reasonably possible that the estimate of the effect on the financial statements of a condition, situation, or set of circumstances that existed at the date of the financial statements will change in the near term due to one or more future confirming events.
  - b. The effect of the change would be material to the financial statements.
25. Risks associated with concentrations, based on information known to management, that meet all of the following criteria have been disclosed in the financial statements:
  - a. The concentration exists at the date of the financial statements.
  - b. The concentration makes the enterprise vulnerable to the risk of a near-term severe impact.
  - c. It is at least reasonably possible that the events that could cause the severe impact will occur in the near term.
26. There are no:
  - a. Violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency.

- b. Other liabilities or gain or loss contingencies that are required to be accrued or disclosed by FASB ASC 450, *Contingencies*, except as disclosed in note 10 to the financial statements.
27. The Government has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor has any asset been pledged as collateral except as disclosed in note 1L to the financial statements.
28. The Government has complied with all aspects of contractual agreements that may have an effect on the financial statements in the event of noncompliance.
29. No department or agency of the Government has reported a material instance of noncompliance to us.
30. The Government has identified all derivative instruments as defined by GASB Codification of Government Accounting and Financial Reporting Standards Section D40, *Derivative Instruments*, and appropriately recorded and disclosed such derivatives in accordance with GASB Codification of Government Accounting and Financial Reporting Standards Section D40.
31. No events have occurred after September 30, 2012, but before the date of this letter, the date the financial statements were available to be issued that require consideration as adjustments to or disclosures in the financial statements.
32. Regarding required supplementary information:
  - a. We confirm that we are responsible for the required supplementary information.
  - b. The required supplementary information is measured and presented in accordance with GASB Codification of Government Accounting and Financial Reporting Standards Section 2200, *Comprehensive Annual Financial Report*.
  - c. The methods of measurement and presentation of the supplementary information have not changed from those used in the prior period.
33. Regarding supplementary information:
  - a. We are responsible for the fair presentation of the supplementary information in accordance with GASB Codification of Government Accounting and Financial Reporting Standards Section 2200, *Comprehensive Annual Financial Report*.
  - b. We believe the supplementary information, including its form and content, is fairly presented in accordance with GASB Codification of Government Accounting and Financial Reporting Standards Section 2200, *Comprehensive Annual Financial Report*.
  - c. The methods of measurement and presentation of the supplementary information have not changed from those used in the prior period.

34. During fiscal year 2012, the Government implemented the following pronouncements, implementation of which did not have a material effect on the financial statements:
- 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.
  - 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.
35. 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. 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 Government.
36. 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 Government.
37. 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 Government.
38. 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 Government.

39. 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 Government.
40. 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 Government.
41. 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 Government.
42. Management of the Government believes that it is in compliance with all significant limitations and restrictions of the Asian Development Bank loan covenants as of September 30, 2012.
43. Arrangements with financial institutions involving compensating balances or other arrangements involving restrictions on cash balances, line of credit, or similar arrangements have been properly disclosed in the financial statements.
44. The Government 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 Government management believes it is more economical to manage its risks internally. In the event of claim settlements and judgments, the Government 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.
45. We have appropriately identified and properly recorded and disclosed in the financial statements, where applicable, all interfund transactions, including repayment terms.
46. Receivables recorded in the financial statements represent valid claims against debtors for sales or other charges arising on or before the balance-sheet date and have been appropriately reduced to their estimated net realizable value.
47. No evidence of fraud, possible irregularities, or dishonesty in fiscal operations of federal programs administered by the Government has been discovered.

48. The Government is pursuing long outstanding receivables from federal grant agencies. Uncollectible accounts, if any, that result from this exercise will be accounted for prospectively.



Kensley Ikosia  
Secretary, Department of Finance & Administration

FSM National Government  
Appendix A – Gov wide Level  
September 30, 2012

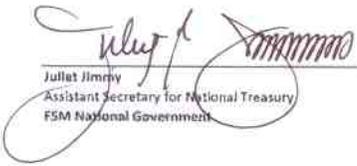
Entry Description	Type of Entry	Assets	Liabilities	Other Equity A/Cs	Fund Balance Beg of Year	Income Statements
		Dr (Cr)	Dr (Cr)	Dr (Cr)	Dr (Cr)	Dr (Cr)
PAJE <1>.GR & GF Bad debt expense Allowance for bad debts To record additional allowance for fund 20	Judgmental Judgmental	(232,745)				232,745
PRJE<2>.GR Other Revenue Beginning Net asset To recals presentation of transfer.	Known Known				(200,000)	200,000
PAJE <3>.GR Accounts Receivable Beginning Net asset Revenue To correct erroneous recording of retainage matching.	Known Known Known	128,116			(154,431)	28,315
PRJE<4>.GR Accounts Payable Fund 20- 3110 Accounts Receivable Fund 20 -1310 To offset federal collection not yet deposited to the General Fund Treasury.	Known Known	(108,650)		106,550		
PAJE<5>.GW Dr. Beginning Fund Balance Dr. Accumulated Depreciation Cr. Fixed Assets - Computer Equipment Cr. Depreciation Expense To correct fixed assets account balance.	Known Known Known Known	20,000 (100,000)			100,000	(20,000)
PAJE<6>.GW Dr. Dr Investment in Fixed Assets 4020 - Fund 95 Cr Fixed Assets CIP 2818 Fund 95 \$209,515 To correct CIP due to erroneous retainaged recorded.	Known Known	(286,025)		286,025		
PAJE<7>.GF Advance to Chuuk Advance to Pohnpei Expenditure Accounts payable To correct recording of the 25% FSMNG CVF share allocated to States and record as receivable the excess payment over 2012 collection.	Known Known Known Known	11,067 13,303		(96,105)		71,735
PAJE<8>.GF & NM Beginning Fund Balance Beginning Fund Balance Expenditures Expenditures To reverse FY11 expenditures recorded in FY12.	Known Extrapolated Known Extrapolated				25,158 49,209	(25,158) (49,209)
PRJE<9>.GF Accounts Payable Accounts Payable Component Unit To reclass payable to COM-FSM.	Known Known		55,919 (55,919)			
PRJE<10>.NM Advances Expense	Known Known	24,750				(24,750)
		(528,084)	0	296,470	(180,064)	411,678

This above uncorrected adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements.

  
Juliet Jimmy  
Assistant Secretary for National Treasury  
FSM National Government

	Type of Entry			Fund Balance Reg		
		Asset	Liabilities		Other Equity	Income Statement
PAJE <1>.GF						
Advance to Chuuk	Known	11,067				
Advance to Pohnpei	Known	13,103				
Expenditure	Known					71,735
Accounts payable	Known		(96,105)			
To correct recording of the 25% FSMNG CVF share allocated to States and record as receivable the excess payment over 2012 collection.						
PAJE <2>.GF						
Dr. Encumbrances	Known				19,510	
Dr. Encumbrances	Extrapolated				82,834	
Cr. Unreserved Fund Balance	Known				(19,510)	
Cr. Unreserved Fund Balance	Extrapolated				(82,834)	
To reverse invalid encumbrances						
PAJE <3>.GF-ADB						
Dr. Encumbrances	Known				27,896	
Dr. Encumbrances	Extrapolated				4,677	
Cr. Unreserved Fund Balance	Known				(27,896)	
Cr. Unreserved Fund Balance	Extrapolated				(4,677)	
To reverse invalid encumbrances						
PAJE <4>.GF						
Dr. Beginning Fund Balance (Factual)	Known				7,510	
Dr. Beginning Fund Balance (Extrapolated)	Extrapolated				33,550	
Cr. Expenditures (Factual)	Known				(7,510)	
Cr. Expenditures (Extrapolated)	Extrapolated				(33,550)	
To reverse FY11 expenditures recorded in FY12						
PAJE <5>.GF						
Bad debt expense						232,745
Allowance for bad debts	Likely	(232,745)				
To record additional allowance for federal grants fund.						
PRJE <1>.GF						
Dr. Accounts Payable 3110	Known		55,919			
Cr. Accounts Payable Component Unit	Known		(55,919)			
To reclass COM-FSM balance						
		(208,375)	(96,106)	0	0	304,480

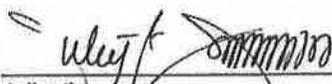
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 Juliet Jiminy  
 Assistant Secretary for National Treasury  
 FSM National Government

FSM National Government  
 Appendix A – Grants fund  
 September 30, 2012

Entry Description	Type of Entry	Assets	Liabilities	Retained Earnings Beg of Year	Income Statements
		Dr (Cr)	Dr (Cr)	Dr (Cr)	Dr (Cr)
PAJE <1>.GR Allowance for bad debts Interfund To record additional allowance for fund 20	Judgmental Judgmental	(232,745)	232,745		
PRJE<2>.GR Other Revenue Transfer in To recalss	Known Known				200,000 (200,000)
PAJE <3>.GR Accounts Receivable 10 - 1310 Fund balance - beg fund 10 Revenue fund 10	Known Known Known	101,029		(93,060)	(7,969)
Accounts Receivable 11 - 1310 Revenue Fund 11 Fund balance - beg fund 11	Known Known Known	300		(61,371)	61,071
Accounts Receivable 14 - 1310 Revenue Fund 14 To correct erroneous recording & application of sector revenue.	Known Known	26,787			(26,787)
To correct erroneous recording of retainage matching.					
PRJE<4>.GR Accounts Payable Fund 20- 3110 Accounts Receivable Fund 20 -1310	Known Known	(108,550)	108,550		
		<u>(211,179)</u>	<u>339,295</u>	<u>(154,431)</u>	<u>26,315</u>

This above uncorrected adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements.

  
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 Juliet Jimmy  
 Assistant Secretary for National Treasury  
 FSM National Government

FSM National Government  
 Appendix A – Non-Major  
 September 30, 2012

Entry Description	Type of Entry	Assets	Other Equity A/Cs	Retained Earnings Beg of Year	Income Statement
		Dr (Cr)	Dr (Cr)	Dr (Cr)	Dr (Cr)
<b>PAJE&lt;1&gt;.NM</b>	Known				
Dr. Encumbrances	Extrapolated			1,766	
Dr. Encumbrances	Known			19,199	
Cr. Unreserved Fund Balance	Extrapolated			(1,766)	
Cr. Unreserved Fund Balance				(19,199)	
To adjust invalid encumbrances					
<b>PAJE&lt;2&gt;.NM</b>	Known				
Dr. Advance to Contractors	Known	24,750			
Dr. Expense - General Contractual Services					(24,750)
To record advance recorded as expense in FY12					
<b>PAJE&lt;3&gt;.NM</b>	Known				
Dr. Beginning Fund Balance (Factual)	Extrapolated		17,648		
Dr. Beginning Fund Balance (Extrapolated)	Known		15,659		
Cr. Expenditures (Factual)	Extrapolated				(17,648)
Cr. Expenditures (Extrapolated)					(15,659)
To reverse FY11 expenditures recorded in FY12					
		24,750	33,307	0	(58,057)

The above uncorrected adjusting and reclassifying entries are not due to fraud or illegal acts. Rather, we believe that the above constitute misstatements.

  
 Juliet Jimmy  
 Assistant Secretary for National Treasury  
 FSM National Government

FSM – National Government  
Disclosure Items Passed  
September 30, 2012

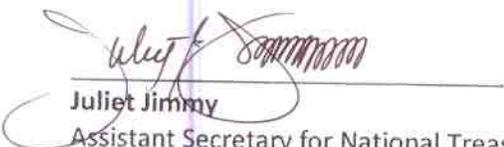
Government Fund Level

Footnote Number	FS Section	Description of Omitted or Unclear Disclosure	Dollar Amount of Omitted or Unclear Disclosure (if applicable)
10	Encumbrance	Overstatement of amount	\$ 134,917
N/A	Accounts Payable Component Units	Overstatement of amount	\$ 55,919
N/A	Budgetary Section	Non-disclosure of overexpenditure	\$ 86,133

Government Wide Level

Footnote Number	Footnote Title	Description of Omitted or Unclear Disclosure	Dollar Amount of Omitted or Unclear Disclosure (if applicable)
5	Property Plant and Equipment	Obsolete and non-working assets still forms part of the account	\$ (1,672,268)
5	Accumulated Depreciation	As above	\$ 1,672,268

We have reviewed the disclosure items passed above as of September 30, 2012. The above disclosures are not material to the current fiscal year financial statements. The above are not the results of fraud or illegal acts.



Juliet Jimmy

Assistant Secretary for National Treasury