

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2013

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

YEAR ENDED SEPTEMBER 30, 2013

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FEDERATED STATES OF MICRONESIA**

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**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2013

INDEPENDENT AUDITORS' REPORT

Honorable John Ehsa
Governor, State of Pohnpei
Federated States of Micronesia:

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei (the State) as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the State's basic financial statements as set forth in Section III of the foregoing table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation, which represent 3%, 0.1%, and 3%, respectively, of the assets, net position, and revenues of the State's discretely presented component units. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation, is based solely on the reports of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei as of September 30, 2013, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 10 as well as the Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund and notes thereto, on pages 46 and 47, 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.

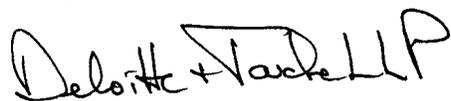
Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State's basic financial statements. The combining and individual fund financial statements, as set forth in Section V of the foregoing table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining and individual fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining and individual fund financial statements are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 29, 2014, on our consideration of the State's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the State's internal control over financial reporting and compliance.



June 29, 2014

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2013

This section of the Pohnpei State's financial report presents our Management's Discussion and Analysis (MD&A) for the fiscal year ended September 30, 2013. This MD&A is prepared in compliance with the GASB 34 requirement. Readers are requested to read this MD&A in conjunction with the State's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The Pohnpei State's primary government's total net position for this year are \$38,164,939.
- The net change in government fund balance is a decrease of \$154,192. Total revenues reported are \$32,314,839 against total expenditures of \$32,469,031.
- Actual revenues for the General Fund were \$280,971 higher than budgeted revenues. The total expenditures-budgetary basis showed an unfavorable variance of \$443,098. The General Fund reported an unassigned fund balance of \$1,585,025, which represents a decrease of \$404,866 from the prior year balance of \$1,989,891.

OVERVIEW OF THE FINANCIAL STATEMENTS

The annual report consists of four parts – management's discussion and analysis (this section), the basic financial statements, required supplemental information and the notes to the financial statements.

The basic financial statements include two kinds of statements that present different views of the State:

Government-Wide Financial Statements

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

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

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

The government-wide financial statements of the State consist of its government activities, which include public works, health, education and general administration. Sales taxes, revenue sharing, federal grants and Compact II/Sector grants are the major sources of these activities. Compact II/Sector grants replace the Compact I funding in the fiscal year 2004.

Fund Financial Statements

The fund financial statements provide more detailed information about the State's significant funds. The State uses fund accounting to comply with financial related legal requirements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2013

- Government funds. Most of the State's basic services are included in government funds, which focus on how cash and other financial assets that can readily be converted to cash flow in and out and the balances left at year-end that are available for spending. Unlike the government-wide financial statements, the government funds statements focus on the short-term financial requirements of the State. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide reconciliation at the bottom of the government funds statement, to explain the relationship between them. The State maintains individual government funds, which are categorized as major and non-major. The major fund includes the General Fund. The other major funds are consisting of the Grants Assistance Fund and the Compact Trust Fund.

FINANCIAL ANALYSIS OF THE STATE AS A WHOLE (GOVERNMENT-WIDE)

The following is a summary of the State's net position as of September 30:

	Governmental Activities			
	<u>2013</u>	<u>2012</u>	<u>Change</u>	<u>%</u>
Current and other assets	\$ 11,207,561	\$ 11,276,027	\$ (68,466)	(0.61)%
Capital assets	21,406,027	23,717,437	(2,311,410)	(9.75)%
Other noncurrent assets	<u>16,121,727</u>	<u>15,953,318</u>	<u>168,409</u>	1.06%
Total assets	<u>48,735,315</u>	<u>50,946,782</u>	<u>(2,211,467)</u>	(4.34)%
Current and other liabilities	5,079,349	4,834,681	244,668	5.06%
Long-term debt outstanding	<u>5,491,027</u>	<u>5,643,537</u>	<u>(152,510)</u>	(2.70)%
Total liabilities	<u>10,570,376</u>	<u>10,478,218</u>	<u>92,158</u>	0.88%
Net position:				
Net investment in capital assets	21,406,027	23,717,437	(2,311,410)	(9.75)%
Restricted	18,837,643	18,798,379	39,264	0.21%
Unrestricted	<u>(2,078,731)</u>	<u>(2,047,252)</u>	<u>(31,479)</u>	(1.54)%
Total net position	\$ <u>38,138,753</u>	\$ <u>40,468,564</u>	\$ <u>2,329,811</u>	(5.76)%

The following is a summary of the State's changes in net position for the fiscal year ended September 30:

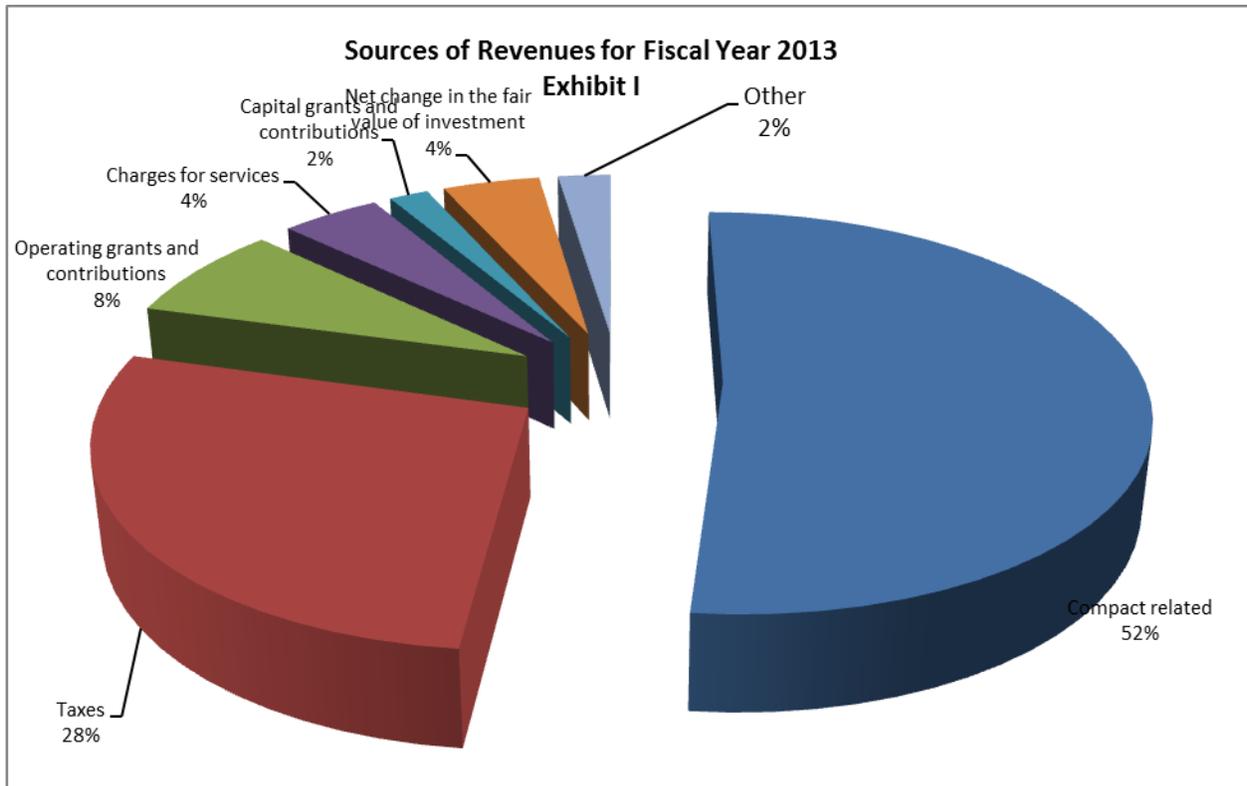
	Governmental Activities			
	<u>2013</u>	<u>2012</u>	<u>Change</u>	<u>%</u>
Revenues:				
Program revenues:				
Charges for services	\$ 1,442,121	\$ 1,089,477	\$ 352,644	32.37%
Operating grants and contributions	3,059,791	2,194,640	865,151	39.42%
Compact related	16,707,285	18,528,079	(1,820,794)	(9.83)%
Capital grants and contributions	-	688,059	(688,059)	(100.00)%
General revenues:				
Taxes	8,911,134	9,717,667	(806,533)	(8.30)%
Investment earnings	1,421,917	3,409,968	(1,988,051)	(58.30)%
Other	<u>772,591</u>	<u>161,562</u>	<u>611,029</u>	378.20%
Total revenues	<u>32,314,839</u>	<u>35,789,452</u>	<u>(3,474,613)</u>	(9.71)%

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2013

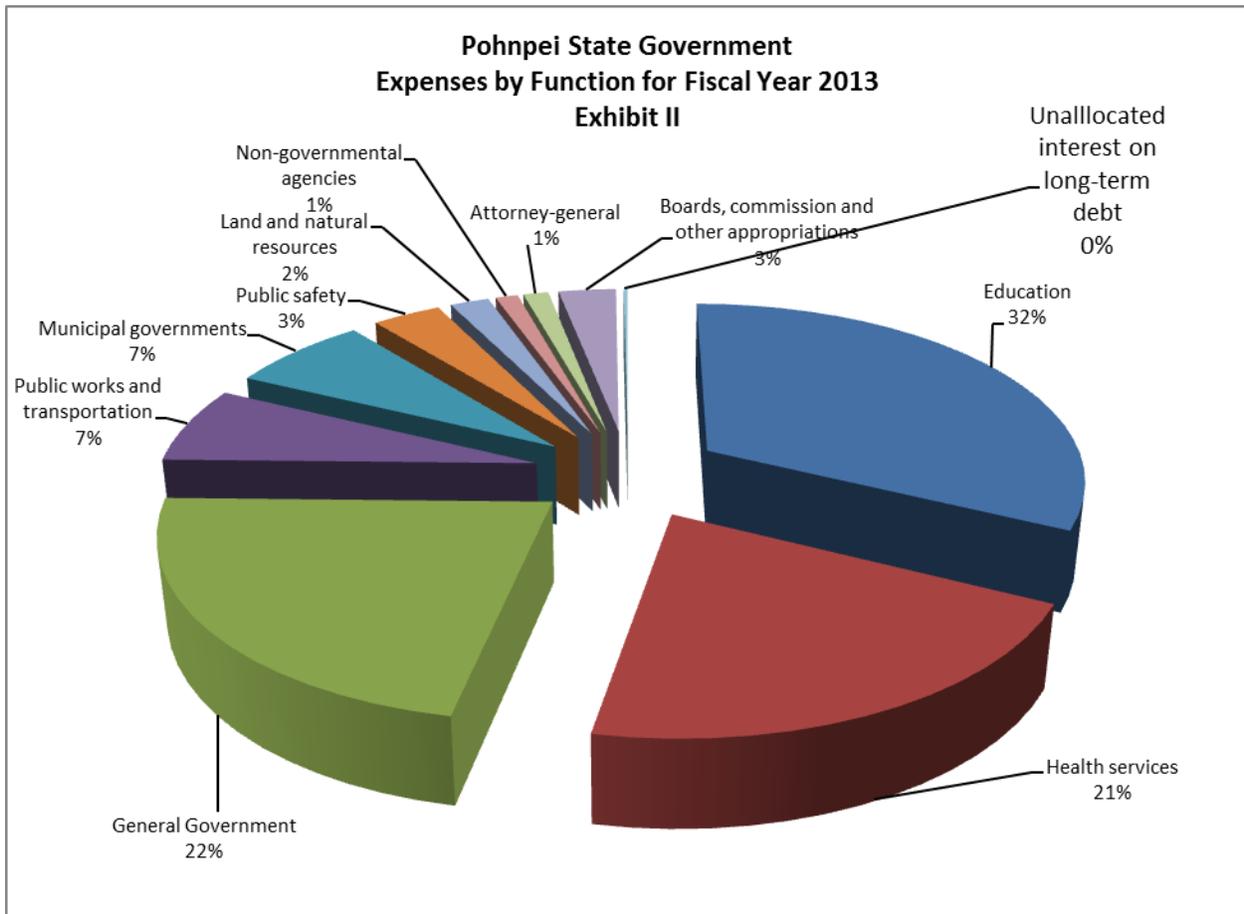
	Governmental Activities			
	<u>2013</u>	<u>2012</u>	<u>Change</u>	<u>%</u>
Expenses:				
General government	7,711,099	7,655,137	\$ 55,962	0.73%
Education	11,181,365	11,683,373	(502,008)	(4.30)%
Health services	7,187,579	8,053,522	(865,943)	(10.75)%
Land and natural resources	676,733	679,160	(2,427)	(0.36)%
Public works and transportation	2,367,442	173,954	2,193,488	1260.96%
Public safety	1,191,983	1,210,705	(18,722)	(1.55)%
Boards, commission and other appropriations	<u>4,302,264</u>	<u>5,847,590</u>	<u>(1,545,326)</u>	<u>(26.43)%</u>
Total expenses	<u>34,618,464</u>	<u>35,303,441</u>	<u>(684,977)</u>	<u>(1.94)%</u>
Increase (decrease) in net position	\$ <u>(2,303,625)</u>	\$ <u>486,011</u>	\$ <u>(2,789,636)</u>	<u>(573.99)%</u>

Exhibit I, below, showed that 52% of the State's revenues were derived from Compact II while 28% came from taxes and licenses. Exhibit II, next page, illustrated that Education represented 32% of the State's total expenses followed by General Government at 22%.



**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2013



FINANCIAL ANALYSIS OF THE STATE GOVERNMENTAL FUNDS

The State's governmental fund changes in fund balances for the years ended September 30, 2013 and 2012 are shown below.

	General Fund		Grants Assistance		Compact Trust		Other Funds	
	2013	2012	2013	2012	2013	2012	2013	2012
Revenues:								
Taxes	\$ 8,476,339	\$9,133,942	\$ -	\$ -	\$ -	\$ -	\$ 434,795	\$ 583,725
Compact	-	-	16,707,285	18,528,079	-	-	-	-
Other/transfers in	<u>2,652,494</u>	<u>3,886,842</u>	<u>3,131,754</u>	<u>2,559,686</u>	<u>102,432</u>	<u>1,717,306</u>	<u>1,097,185</u>	<u>1,657,632</u>
Total revenues	11,128,833	13,020,784	19,839,039	21,087,765	102,432	1,717,306	1,531,980	2,241,357
Expenditures/transfers out	<u>11,366,912</u>	<u>11,105,785</u>	<u>19,702,253</u>	<u>23,191,929</u>	-	-	<u>1,687,311</u>	<u>2,308,560</u>
Net change in fund balances	\$ <u>(238,079)</u>	\$ <u>1,914,999</u>	\$ <u>136,786</u>	\$ <u>(2,104,164)</u>	\$ <u>102,432</u>	\$ <u>1,717,306</u>	\$ <u>(155,331)</u>	\$ <u>(67,203)</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2013

General Fund

Revenues decreased by \$657,603 or 7% compared to fiscal year 2012. The decrease was primarily caused by a decrease in transfers in of \$1,954,828 offset by a positive adjustment to other revenue for \$500,000 while the tax revenue decreased compared in prior year. Expenditures and transfers out increased marginally by \$261,127 or 2% compared to fiscal year 2012.

Grants Assistance Fund

As mentioned in the preceding paragraph, Compact II/Sector Grants were the major sources of Pohnpei State's operating grants for fiscal year 2013. The total Compact II/Sector funding amounted to \$16,707,285 while total expenditures are in the amount of \$16,681,099, which is discussed below:

- The education sector grant that shall support and improve the educational system of the Federated States of Micronesia, including, without limitation, the systems for primary, secondary, and post-secondary education. The total revenues are \$7,355,017 against total expenditures of the same amount, which represents a decrease of \$161,207 or 2% compared to fiscal year 2012.
- The health sector grant that shall support and improve the delivery of preventive, curative and environmental care, and develop the human and material resources necessary for the Federated States of Micronesia to perform these services. The total revenues are \$5,449,176 against total expenditures of the same amount, which represents a decrease of \$1,348,299 or 20% compared to fiscal year 2012.
- The sector grant for private sector development shall support the efforts of the Federated States of Micronesia to attract new foreign investment and increase indigenous business activity. Priorities will be in advancing the private development of fisheries, tourism and agriculture; employing new telecommunications technologies; and analyzing and developing new systems, laws, and policies to foster private sector development, to facilitate investment by potential private investors, and develop business and entrepreneurial skills. The total revenues are \$3,013 against total expenditures of the same amount, which represents a decrease of \$83,464 or 97% compared to fiscal year 2012.
- The sector for capacity building shall support the efforts of the Federated States of Micronesia to build effective, accountable and transparent national and local government and other public sector institutions and systems. The total revenues are \$414,970 against expenditures of the same amount, which represents a decrease of \$18,079 or 4% compared to fiscal year 2012.
- The environment sector shall support the efforts of the Federated States of Micronesia to protect the Nation's land and marine environment and to conserve and achieve sustainable use of its natural resources. The total revenues are \$376,811, which exceeds expenditures of \$350,625 by \$26,186, and which represents a decrease of \$90,889 or 19% compared to fiscal year 2012.
- Public Infrastructure grant shall give priority to primary and secondary education capital projects and programs that directly affect health and safety including water and wastewater projects, solid waste disposal projects and health care facilities. The total revenues are \$96,188 against total expenditures of the same amount, which represents a decrease of \$202,450 or 68% compared in prior year.

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Management's Discussion and Analysis
September 30, 2013

- The Supplemental Education Grant (SEG) is considered the seventh-sector grant. SEG has been offered in lieu of grants that were formerly available from various federal agencies. The federal programs that were incorporated into SEG are Territories and Freely Associated States Education Grant (T&FASEG), Adult Education and Family Literacy, Workforce Investment Act, Pacific Vocational Education Improvement Program and Early Childhood Program (formerly Head Start). The total revenues are \$2,719,379 against total expenditures of the same amount, which represents a decrease of \$210,301 or 7% compared to fiscal year 2012.
- The Enhanced Reporting and Accountability is a new grant that supports the finance functions of the Department of Treasury and Administration. For the year, total revenues and expenditures were \$292,731 compared to none in prior year.

Another major source of funding of the Grants Assistance Fund is the US Federal Grants, which supported \$2,360,889 of expenditures of the State, an increase of \$38,413 or 2% compared to fiscal year 2012.

General Fund Budgetary Highlights

During the year, the State revised its budget several times in the aggregate amount of \$75,335 to accommodate supplemental funding for departments and offices requiring increases in appropriations to avoid budget overruns. These matters are not believed to have a significant effect on future services. The State conforms to the most appropriate measures of utilizing its net position due to inflationary adjustments.

The net decrease in the State's General Fund unassigned fund balance of \$404,866 compared with net decrease of \$431,725 in fiscal year 2012.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

The State's capital assets at the end of fiscal year 2013 consist basically of equipment, buildings, roads and bridges. Increase in capital assets was due to purchases of machinery, equipment and others under the Infrastructure Account. The summary of capital assets at the end of September 30 is shown below:

	<u>Governmental Activities</u>			
	<u>2013</u>	<u>2012</u>	<u>Change</u>	<u>%</u>
Buildings	\$ 13,728,473	\$ 13,728,473	\$ -	0.00%
Infrastructure	52,881,727	52,786,727	95,000	0.18%
Machinery	<u>23,078,283</u>	<u>22,750,503</u>	<u>327,780</u>	1.44%
Total	\$ <u>89,688,483</u>	\$ <u>89,265,703</u>	\$ <u>422,780</u>	0.47%

Please refer to note 5 to the financial statements for additional information about the State's capital assets.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2013

Long-term Debt

At September 30 the State had long-term debt as shown below:

	<u>Governmental Activities</u>			
	<u>2013</u>	<u>2012</u>	<u>Change</u>	<u>%</u>
Asian Development Bank loans	\$ <u>5,491,027</u>	\$ <u>5,643,537</u>	\$ <u>(152,510)</u>	(2.70)%

Please refer to notes 6 and 8 to the financial statements for additional information about the State's long-term debt.

Economic Factors and Next Year's Budget

Funding for the operations of most of the government services in fiscal year 2014 will still come from the Compact II.

Fiscal year 2014 is the 11th year of the implementation of the economic assistance under the Compact II/Sector Grant. Sector funding replaces the funding sources from the old Compact I. Under the Compact II/Sector grant, the annual budget approved by JEMCO for fiscal year 2014 is as follows:

- For Education Sector Grant, which continues to be the funding priority, the annual budget is \$6,932,033.
- The Health Sector Grant's budget is \$5,408,076.
- The Private Sector Development Sector Grant's budget is nil.
- The Public Sector Capacity Building Sector Grant budget is \$407,653.
- The Environment Sector Grant is \$314,716.
- The Enhanced Reporting and Accounting Sector Grant budget is \$261,315.
- The cumulative grants for the Public Infrastructure from fiscal years 2005 through 2012 is more than \$40,000,000. Priority projects are education, health related and private sector development. It is required that 5% of the total grant be allocated to the Infrastructure Maintenance fund for the maintenance of the existing and new projects. Local matching of the same amount is required.
- In the case of the Supplemental Education Grant (SEG), the total funding for fiscal year 2014 is \$2,814,872. The programs covered in the funding are Early Childhood Education, Education Improvement Programs, Workforce Development/Skill Training, Vocational Education and Staff Development.

**STATE OF POHNPEI
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September 30, 2013

For fiscal year 2014, the locally generated revenues, investment income and the revenue shares from the FSM National Government are projected at about \$10,200,911. These projected revenues were \$927,922 less compared with fiscal year 2013 revenues. The net decrease is due mainly to projected decrease in investment income and the absence of one-time accounting adjustment made in FY2013. In its effort to close possible shortage, the Department of Treasury and Administration will continue to intensify its collection effort to raise more revenues in the ensuing year. Major changes shall be made at the Tax and Revenue Division to ensure higher tax collection. In addition, the revenue shall be monitored in order that the expenditures shall be adjusted accordingly. Finally, the final carry-over balances from the Compact II may be authorized to be used to fund other operations of the government.

FINANCIAL CONTACT

This financial report is designed to provide all interested users with a general overview of the State of Pohnpei's finances. If you have questions about this report or need additional financial information, please contact the Office of the Director of Treasury and Administration, P.O. Box 1567 Kolonia, Pohnpei FM 96941.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Net Position
September 30, 2013

	Primary Government	Component Units
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ -	\$ 3,207,432
Time certificate of deposit	-	43,251
Investments	6,306,556	1,758,905
Receivables, net	4,078,273	4,532,491
Advances	263,829	185,380
Inventories	29,947	1,456,984
Other current assets	-	46,614
Restricted assets:		
Cash and cash equivalents	528,956	822,877
Total current assets	11,207,561	12,053,934
Noncurrent assets:		
Capital assets:		
Nondepreciable capital assets	-	10,812,041
Capital assets, net of accumulated depreciation	21,406,027	27,656,563
Investments	1,500,000	-
Receivables	-	987,421
Other noncurrent assets	-	585,967
Restricted assets:		
Cash and cash equivalents	-	496,085
Investments	14,621,727	-
Total noncurrent assets	37,527,754	40,538,077
Total assets	\$ 48,735,315	\$ 52,592,011
<u>LIABILITIES</u>		
Current liabilities:		
Bank overdraft	\$ 126,410	\$ -
Short-term debt	-	190,000
Current portion of long-term obligations	170,629	376,519
Current portion of compensated absences payable	681,519	-
Accounts payable	1,769,303	1,709,946
Other liabilities and accruals	668,109	961,760
Due to primary government	-	1,795,261
Unearned revenues	1,623,040	181,551
Total current liabilities	5,039,010	5,215,037
Noncurrent liabilities:		
Long-term obligations, net of current portion	5,320,398	10,001,159
Claims and judgments payable	210,968	-
Total noncurrent liabilities	5,531,366	10,001,159
Total liabilities	10,570,376	15,216,196
Contingencies and commitments		
<u>NET POSITION</u>		
Net investment in capital assets	21,406,027	29,133,550
Restricted for:		
Nonexpendable:		
Future operations	10,940,700	-
Expendable:		
Compact related	119,862	-
Debt service	3,681,027	-
Other purposes	4,096,054	4,531,334
Unrestricted	(2,078,731)	3,710,931
Total net position	38,164,939	37,375,815
Total liabilities and net position	\$ 48,735,315	\$ 52,592,011

See accompanying notes to financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Activities
Year Ended September 30, 2013

Functions/Programs	Expenses	Program Revenues			Net (Expenses) Revenues and Changes in Net Position	
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government	Component Units
Primary government:						
Governmental activities:						
General government	\$ 7,711,099	661,463	\$ 1,882,615	\$ -	\$ (5,167,021)	\$ -
Land and natural resources	676,733	94,660	193,100	-	(388,973)	-
Education	11,181,365	-	11,117,278	-	(64,087)	-
Health services	7,187,579	586,789	6,574,083	-	(26,707)	-
Public safety	1,191,983	99,209	-	-	(1,092,774)	-
Attorney-general	435,423	-	-	-	(435,423)	-
Public works and transportation	2,367,442	-	-	-	(2,367,442)	-
Non-governmental agencies	388,806	-	-	-	(388,806)	-
Boards, commissions and others	1,000,235	-	-	-	(1,000,235)	-
Municipal governments	2,409,942	-	-	-	(2,409,942)	-
Unallocated interest on long-term debt	67,857	-	-	-	(67,857)	-
Total primary government	\$ 34,618,464	\$ 1,442,121	\$ 19,767,076	\$ -	(13,409,267)	-
Component units:						
Pohnpei Utilities Corporation	\$ 17,654,086	\$ 16,082,861	\$ -	\$ 6,578,629	-	5,007,404
Pohnpei Port Authority	2,641,960	3,699,007	-	53,181	-	1,110,228
Pohnpei Transportation Authority	744,061	802,332	-	-	-	58,271
Small Business Guarantee and Finance Corporation	226,995	62,842	-	-	-	(164,153)
Pohnpei State Housing Authority	122,039	204,575	-	-	-	82,536
Total component units	\$ 21,389,141	\$ 20,851,617	\$ -	\$ 6,631,810	-	6,094,286
General revenues:						
Taxes:						
FSM revenue sharing:						
Gross revenue taxes					2,265,569	-
Import taxes					1,668,273	-
Income taxes					2,069,793	-
Other taxes					288,571	-
State taxes					2,618,928	-
Unrestricted investment earnings					1,319,485	-
Other					772,591	627,232
Total general revenues					11,003,210	627,232
Contributions to permanent fund					102,432	-
Total general revenues and contributions					11,105,642	627,232
Change in net position					(2,303,625)	6,721,518
Net position at the beginning of the year					40,468,564	30,654,297
Net position at the end of the year					\$ 38,164,939	\$ 37,375,815

See accompanying notes to financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Balance Sheet
Governmental Funds
September 30, 2013

		Special Revenue	Permanent	Other Governmental Funds	Total
	General	Grants Assistance	Compact Trust		
ASSETS					
Investments	\$ 7,806,556	\$ -	\$ -	\$ -	\$ 7,806,556
Receivables, net:					
Taxes	1,938,587	-	-	-	1,938,587
Due from FSM National Government	-	1,415,123	-	-	1,415,123
Other	720,635	3,928	-	-	724,563
Due from other funds	818,222	1,827,664	-	4,522,840	7,168,726
Advances	131,239	126,969	-	5,621	263,829
Inventories	-	-	-	29,947	29,947
Restricted assets:					
Cash and cash equivalents	521,256	7,700	-	-	528,956
Investments	3,681,027	-	10,940,700	-	14,621,727
Total assets	<u>\$ 15,617,522</u>	<u>\$ 3,381,384</u>	<u>\$ 10,940,700</u>	<u>\$ 4,558,408</u>	<u>\$ 34,498,014</u>
LIABILITIES AND FUND BALANCES					
Liabilities:					
Bank overdraft	\$ 126,410	\$ -	\$ -	\$ -	\$ 126,410
Accounts payable	768,457	782,904	-	217,942	1,769,303
Other liabilities and accruals	386,341	278,886	-	2,882	668,109
Unearned revenues	-	1,381,510	-	241,530	1,623,040
Due to other funds	6,350,504	818,222	-	-	7,168,726
Total liabilities	<u>7,631,712</u>	<u>3,261,522</u>	<u>-</u>	<u>462,354</u>	<u>11,355,588</u>
Fund balances:					
Non-spendable	1,631,239	-	10,940,700	34,568	12,606,507
Restricted	3,897,842	119,862	-	-	4,017,704
Committed	414,074	-	-	3,072,198	3,486,272
Assigned	457,630	-	-	989,288	1,446,918
Unassigned	1,585,025	-	-	-	1,585,025
Total fund balances	<u>7,985,810</u>	<u>119,862</u>	<u>10,940,700</u>	<u>4,096,054</u>	<u>23,142,426</u>
Total liabilities and fund balances	<u>\$ 15,617,522</u>	<u>\$ 3,381,384</u>	<u>\$ 10,940,700</u>	<u>\$ 4,558,408</u>	

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

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds

21,406,027

Long-term liabilities, including loans payable, are not due and payable in the current period and, therefore, are not reported in the funds. The liabilities include:

Long-term debt payable	(5,491,027)
Compensated absences payable	(681,519)
Claims and judgments payable	(210,968)

(6,383,514)

Net position of governmental activities

\$ 38,164,939

See accompanying notes to financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures, and Changes in Fund Balances (Deficit)
Governmental Funds
Year Ended September 30, 2013

	General	Special Revenue	Permanent	Other	Total
		Grants Assistance	Compact Trust	Governmental Funds	
Revenues:					
Compact funding	\$ -	\$ 16,707,285	\$ -	\$ -	\$ 16,707,285
Net change in the fair value of investments	1,319,485	-	102,432	-	1,421,917
CFSM grants	137,222	436,145	-	-	573,367
Federal contributions and other grants	-	2,440,306	-	46,118	2,486,424
FSM revenue sharing	6,292,206	-	-	-	6,292,206
State taxes	2,184,133	-	-	434,795	2,618,928
Fees and charges	417,031	-	-	1,025,090	1,442,121
Other	778,756	(6,165)	-	-	772,591
Total revenues	11,128,833	19,577,571	102,432	1,506,003	32,314,839
Expenditures:					
Current:					
General government	4,178,017	1,817,792	-	1,247,753	7,243,562
Land and natural resources	477,167	193,100	-	-	670,267
Education	2,318	11,117,278	-	-	11,119,596
Health services	40,580	6,574,083	-	439,558	7,054,221
Public safety	1,178,065	-	-	-	1,178,065
Office of the Attorney-General	435,492	-	-	-	435,492
Public works	653,000	-	-	-	653,000
Payments to non-governmental agencies	388,806	-	-	-	388,806
Boards, commissions and other	1,095,713	-	-	-	1,095,713
Grants to local governments	2,409,942	-	-	-	2,409,942
Debt service	220,367	-	-	-	220,367
Total expenditures	11,079,467	19,702,253	-	1,687,311	32,469,031
Excess (deficiency) of revenues over (under) expenditures	49,366	(124,682)	102,432	(181,308)	(154,192)
Other financing sources (uses):					
Operating transfers in	-	261,468	-	25,977	287,445
Operating transfers out	(287,445)	-	-	-	(287,445)
Total other financing sources (uses), net	(287,445)	261,468	-	25,977	-
Net change in fund balances (deficit)	(238,079)	136,786	102,432	(155,331)	(154,192)
Fund balances (deficit) at the beginning of the year	8,223,889	(16,924)	10,838,268	4,251,385	23,296,618
Fund balances at the end of the year	\$ 7,985,810	\$ 119,862	\$ 10,940,700	\$ 4,096,054	\$ 23,142,426

See accompanying notes to financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Reconciliation of the Statement of Revenues, Expenditure, and Changes in Fund
Balances of Governmental Funds to the Statement of Activities
Year Ended September 30, 2013

Amounts reported for governmental activities in the statement of activities are different than the net change in fund balances because:

Net change in fund balances - total governmental funds \$ (154,192)

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlays in the current period (2,311,410)

The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction has any effect on net position. For the current year, these amounts consist of:

Repayment of ADB Loans 152,510

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

Change in compensated absences payable 9,467

Change in net position of governmental activities \$ (2,303,625)

See accompanying notes to financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Combining Statement of Net Position
Component Units
September 30, 2013

	Pohnpei Utilities Corporation	Pohnpei Port Authority	Pohnpei Transportation Authority	Small Business Guarantee and Finance Corporation	Pohnpei State Housing Authority	Total
ASSETS						
Current assets:						
Cash and cash equivalents	\$ 411,374	\$ 2,271,585	\$ -	\$ 300	\$ 524,173	\$ 3,207,432
Time certificate of deposit	43,251	-	-	-	-	43,251
Investments	174,124	1,584,781	-	-	-	1,758,905
Receivables, net	1,528,419	787,917	2,924	50,517	2,162,714	4,532,491
Inventories	1,413,387	-	43,597	-	-	1,456,984
Advances	102,961	73,024	4,578	4,817	-	185,380
Other current assets	-	44,346	-	1,905	363	46,614
Restricted assets:						
Cash and cash equivalents	-	-	-	822,877	-	822,877
Total current assets	<u>3,673,516</u>	<u>4,761,653</u>	<u>51,099</u>	<u>880,416</u>	<u>2,687,250</u>	<u>12,053,934</u>
Noncurrent assets:						
Receivables, net	-	229,868	-	757,553	-	987,421
Capital assets:						
Nondepreciable capital assets	7,656,727	3,155,314	-	-	-	10,812,041
Capital assets, net of accumulated depreciation	24,229,134	3,273,583	-	62,193	91,653	27,656,563
Long-term deposits	576,213	-	-	-	-	576,213
Restricted:						
Cash and cash equivalents	496,085	-	-	-	-	496,085
Other noncurrent assets	-	9,754	-	-	-	9,754
Total noncurrent assets	<u>32,958,159</u>	<u>6,668,519</u>	<u>-</u>	<u>819,746</u>	<u>91,653</u>	<u>40,538,077</u>
Total assets	<u>\$ 36,631,675</u>	<u>\$ 11,430,172</u>	<u>\$ 51,099</u>	<u>\$ 1,700,162</u>	<u>\$ 2,778,903</u>	<u>\$ 52,592,011</u>
LIABILITIES						
Current liabilities:						
Short-term debt	\$ 190,000	\$ -	\$ -	\$ -	\$ -	\$ 190,000
Current portion of long-term debt	376,519	-	-	-	-	376,519
Accounts payable	1,567,973	38,634	85,406	-	17,933	1,709,946
Other liabilities and accruals	293,070	208,424	18,612	1,916	439,738	961,760
Due to primary government	200,000	-	1,595,261	-	-	1,795,261
Unearned revenue	181,551	-	-	-	-	181,551
Total current liabilities	<u>2,809,113</u>	<u>247,058</u>	<u>1,699,279</u>	<u>1,916</u>	<u>457,671</u>	<u>5,215,037</u>
Noncurrent liabilities:						
Noncurrent portion of long-term debt	10,001,159	-	-	-	-	10,001,159
Total liabilities	<u>12,810,272</u>	<u>247,058</u>	<u>1,699,279</u>	<u>1,916</u>	<u>457,671</u>	<u>15,216,196</u>
NET POSITION						
Net investment in capital assets	22,550,807	6,428,897	-	62,193	91,653	29,133,550
Restricted	721,325	-	-	1,580,430	2,229,579	4,531,334
Unrestricted	549,271	4,754,217	(1,648,180)	55,623	-	3,710,931
Total net position	<u>23,821,403</u>	<u>11,183,114</u>	<u>(1,648,180)</u>	<u>1,698,246</u>	<u>2,321,232</u>	<u>37,375,815</u>
	<u>\$ 36,631,675</u>	<u>\$ 11,430,172</u>	<u>\$ 51,099</u>	<u>\$ 1,700,162</u>	<u>\$ 2,778,903</u>	<u>\$ 52,592,011</u>

See accompanying notes to financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Combining Statement of Revenues, Expenses, and Changes in Net Position
Component Units
Year Ended September 30, 2013

	Pohnpei Utilities Corporation	Pohnpei Port Authority	Pohnpei Transportation Authority	Small Business Guarantee and Finance Corporation	Pohnpei State Housing Authority	Total
Operating revenues:						
Charges for services	\$ 16,082,861	\$ 3,699,007	\$ 801,542	\$ 62,842	\$ 204,575	\$ 20,850,827
Sales	-	-	790	-	-	790
Total operating revenues	<u>16,082,861</u>	<u>3,699,007</u>	<u>802,332</u>	<u>62,842</u>	<u>204,575</u>	<u>20,851,617</u>
Operating expenses:						
Cost of services	11,630,970	-	-	50,433	-	11,681,403
Administration costs	3,780,825	2,217,985	744,061	153,465	105,916	7,002,252
Depreciation and amortization	2,242,291	423,975	-	23,097	16,123	2,705,486
Total operating expenses	<u>17,654,086</u>	<u>2,641,960</u>	<u>744,061</u>	<u>226,995</u>	<u>122,039</u>	<u>21,389,141</u>
Operating income (loss)	<u>(1,571,225)</u>	<u>1,057,047</u>	<u>58,271</u>	<u>(164,153)</u>	<u>82,536</u>	<u>(537,524)</u>
Nonoperating revenues (expenses):						
Contributions from the primary government	-	119,000	-	90,000	87,398	296,398
Interest income (expense)	(170,941)	-	-	2,494	-	(168,447)
Other	393,462	104,665	-	1,154	-	499,281
Total nonoperating revenues (expenses), net	<u>222,521</u>	<u>223,665</u>	<u>-</u>	<u>93,648</u>	<u>87,398</u>	<u>627,232</u>
Net income (loss) before capital contributions	(1,348,704)	1,280,712	58,271	(70,505)	169,934	89,708
Capital contributions	<u>6,578,629</u>	<u>53,181</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,631,810</u>
Change in net position	5,229,925	1,333,893	58,271	(70,505)	169,934	6,721,518
Net position at the beginning of the year	<u>18,591,478</u>	<u>9,849,221</u>	<u>(1,706,451)</u>	<u>1,768,751</u>	<u>2,151,298</u>	<u>30,654,297</u>
Net position at the end of the year	<u>\$ 23,821,403</u>	<u>\$ 11,183,114</u>	<u>\$ (1,648,180)</u>	<u>\$ 1,698,246</u>	<u>\$ 2,321,232</u>	<u>\$ 37,375,815</u>

See accompanying notes to financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies

The State of Pohnpei (the State) was constituted on November 8, 1984, under the provisions of the Pohnpei State Constitution (the Constitution) as approved by the people of Pohnpei. The Constitution provides for the separation of powers of the executive, legislative, and judicial branches of the government.

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

A. Reporting Entity

The State is one of the four states that make up the Federated States of Micronesia (FSM), along with the states of Chuuk, Kosrae and Yap. The State is a constitutional government comprised of three branches: the Legislative Branch, consisting of 23 members elected for a term of four years by qualified voters of their respective election districts; the Executive Branch, headed by the Governor and Lt. Governor, who are primarily responsible for executing the laws and administering state government services; and the Judiciary Branch made up of the State Supreme Court, which consists of a Chief Justice and up to four Associate Justices, and other courts that may be created by law.

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

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

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

Discretely Presented Component Units:

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

Pohnpei Utilities Corporation (PUC): PUC was created by Pohnpei State Public Law (PSPL) No. 2L-179-91 and is responsible for providing electrical, water and sewer services to the people of Pohnpei through the operation of the electric power, water and sewer systems. PUC is governed by a seven-member Board of Directors appointed by the Governor with the advice and consent of the Legislature. The State provides financial support to PUC through legislative appropriations and has the ability to impose its will on PUC.

Pohnpei Port Authority (PPA): PPA was created by PSPL No. 2L-224-91 and is responsible for overseeing the use and maintenance of the State's sea and air ports. PPA is governed by a seven-member Board of Directors, consisting of representatives of the State appointed by the Governor with the advice and consent of the Legislature. The State has the ability to impose its will on PPA.

Pohnpei Transportation Authority (PTA): PTA was created by PSPL No. 169-69 and is responsible for promotion, development, and improving transportation facilities of the State. PTA is governed by a seven-member Board of Directors, consisting of representatives of the State appointed by the Governor with the advice and consent of the Legislature. The State has the ability to impose its will on PTA.

Small Business Guarantee and Finance Corporation (SBGFC): SBGFC was created by PSPL No. 3L-86-95 to provide, promote, develop and widen in both scope and services reach various alternative modes of financing for small enterprises, including, but not limited to, direct and indirect project lending, venture capital, financial leasing, secondary mortgage and rediscounting of loan papers to small businesses. SBGFC is governed by a seven-member Board of Directors, consisting of four representatives of the State and three representatives from the private sector appointed by the Governor with the advice and consent of the Legislature. The State provides financial support to SBGFC through legislative appropriations and has the ability to impose its will on SBGFC.

Pohnpei State Housing Authority (PSHA): PSHA was created by PSPL No. 2L-81-88 for the purpose of facilitating, through low-interest loans, the construction of safe and sanitary residential housing for low income families of the State, and for monitoring the Housing Preservation Grant (HPG) loan funds extended by United States Department of Agriculture Rural Development. PSHA is governed by a five-member Board of Directors appointed by the Governor with the advice and consent of the Legislature. The State provides financial support to PSHA through legislative appropriations and has the ability to impose its will on PSHA.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

Discretely Presented Component Units, Continued:

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

P.O. Box 370
Kolonias, Pohnpei, FSM 96941

B. Government-Wide Financial Statements

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

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

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

- Net investment in capital assets consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt that are attributed to the acquisition, construction or improvement of those assets.
- Restricted net position - nonexpendable consists of permanent funds in which donors or other outside sources have stipulated that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to the principal.
- Restricted net position - expendable consists of resources in which the State is legally or contractually obligated to spend resources in accordance with restrictions either externally imposed by creditors, grantors, contributors, and the like, or imposed by law.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements, Continued

- Unrestricted net position consists of net position, which does not meet the definition of the two preceding categories. Unrestricted net position often is designated, (for example, internally restricted), to indicate that management does not consider such to be available for general operations.

The government-wide Statement of Net Position reports \$18,837,643 of restricted net position, of which \$4,096,054 is restricted by enabling legislation.

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

C. Fund Financial Statements

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

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

D. Measurement Focus and Basis of Accounting

Government-Wide Financial Statements:

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

Governmental Fund Financial Statements:

Governmental fund financial statements account for the general governmental activities of the State and are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as they become susceptible to accrual; generally when they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

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

Component Unit Financial Statements:

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

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

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

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

E. Cash and Cash Equivalents and Time Certificates of Deposit

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

F. Investments

Investments and related investment earnings of the primary government and the discretely presented component units are recorded at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Investments in the equity of companies are carried at cost if less than twenty percent of the companies' total equity, on the equity method if greater than twenty percent and less than fifty percent and on a consolidated basis if greater than fifty percent.

G. Receivables

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

H. Prepaid Items

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

I. Interfund Receivables/Payables

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

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

J. Inventories

Inventories of materials and supplies are determined by physical count and are valued at the lower of cost (principally average cost) or market.

Inventories of the discretely presented component units are comprised of materials and diesel fuel and are valued at the lower of cost (FIFO) or market.

K. Restricted Assets

Certain assets of the primary government are classified as restricted assets because their use is completely restricted through enabling legislation and loan agreements. Specifically, the State has collateralized investments in the amount of \$3,681,027 for the Pohnpei State Early Retirement Scheme. Furthermore, investments recorded in the Compact Trust Fund of \$10,940,700 are restricted in that they are not available to be used in current operations.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

K. Restricted Assets, Continued

As of September 30, 2013, cash and cash equivalents were restricted for the following uses:

Primary Government:

Deposits with a local bank restricted for the purchase of medical supplies for the State hospital.	\$ 3,386
State Hospital's Honolulu imprest fund.	7,700
Savings accounts established in accordance with Section 211(d)(2) of the Compact of Free Association, as amended, for the purpose of funding the State's infrastructure maintenance plan	257,880
Deposit accounts established for the purpose of receiving payments pursuant to the Compact of Free Association, as amended	6,762
Small Business Development Center deposit account	14,589
Aluminum Recycling Project	21,824
Loan Guarantee Escrow Account established for the sole purpose of loan collateralization made through the USDA Rural Development. The escrow account may be drawn down in the event of a borrower's default on the obligation under the terms of the promissory note and the deed of trust security instrument supporting such note and for which such note is guaranteed by the Pohnpei State Housing Authority, the trustee of the Loan Guarantee Escrow Account.	<u>216,815</u>
	<u>\$ 528,956</u>

Discretely Presented Component Units:

Pohnpei Utilities Corporation:

Deposit accounts collateralizing loans payable to the FSM Development Bank and the Bank of the FSM	\$ 496,085
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Small Business Guarantee and Finance Corporation:

Deposit accounts restricted for various operations of the Small Business Guarantee and Finance Corporation	<u>822,877</u>
	<u>\$ 1,318,962</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

L. Capital Assets

Capital assets, which include property, plant, equipment and infrastructure assets (e.g. roads, bridges, ramps and other similar items), are reported in the governmental activity column of the government-wide financial statements. Such assets, whether purchased or constructed, are recorded at historical cost or estimated historical cost. Donated capital assets are recorded at fair market value at the date of donation.

The State currently holds no title to land. Machinery and equipment, other than vehicles and boats, are capitalized when the cost of individual items exceed \$50,000. Vehicles and boats, along with significant repair and maintenance qualifying as a betterment of such, are capitalized regardless of cost and depreciated. Building and infrastructure projects, along with significant improvements or reconstruction qualifying as a betterment of such, are capitalized when the cost of individual items or projects exceed \$100,000. The costs of normal maintenance and repairs that do not add to the value of the capital asset or materially extend capital asset lives are not capitalized. Additionally, as of fiscal year 2004, the State chose to capitalize assets acquired with U.S. federal funds that have an acquisition cost of \$5,000 or more.

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

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

M. Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (deduction of net position) until then. The State has no items that qualify for reporting in this category.

N. Compensated Absences

It is the government's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. There is no liability for unpaid accumulated sick leave since the government does not have a policy to pay any amounts when employees separate from service with the government. All vacation pay is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements. Annual leave accumulates at 240 hours per calendar year. All unused annual leave is cancelled at the end of each calendar year.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

O. Deferred Inflows of Resources

In addition to liabilities, the statements of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (additions to net position) until then. The State has no items that qualify for reporting in this category.

P. Unearned Revenue

In the government-wide financial statements, unearned revenue is recognized when cash, receivables or other assets are recorded prior to their being earned. In the governmental fund financial statements, unearned revenue represents monies received or revenues accrued which have not been earned or do not meet the “available” criterion for revenue recognition under the modified accrual basis of accounting. The unearned revenue in the governmental fund financial statements has primarily resulted as federal funds are received in advance of eligible expenditures.

Q. Fund Balance

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

Q. Fund Balance, Continued

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

A formal minimum fund balance policy has not been adopted.

R. Interfund/Intrafund Transactions

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

S. Risk Financing

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

T. New Accounting Standards

During fiscal year 2013, the State implemented the following pronouncements:

- GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addressed 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.
- GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*, which improved 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.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

T. New Accounting Standards, Continued

- GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which enhanced 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 issued on or before November 30, 1989, which does not conflict or contradict GASB pronouncements. GASB Statement No. 62 superseded GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*.
- GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which established guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position, and GASB 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. These Statements amend the net asset reporting requirements in Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. With the implementation of GASB Statement No. 63 and Statement No. 65, the Statement of Net Assets was renamed the Statement of Net Position. In addition, the Statement of Net Position includes two new classifications separate from assets and liabilities. Amounts reported as deferred outflows of resources are reported in a separate section following assets. Likewise, amounts reported as deferred inflows of resources are reported in a separate section following liabilities.

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

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(1) Summary of Significant Accounting Policies, Continued

T. New Accounting Standards, Continued

In January 2013, GASB issued Statement No. 69, *Government Combinations and Disposals of Government Operations*, which improves accounting and financial reporting for state and local governments' combinations and disposals of government operations. Government combinations include mergers, acquisitions, and transfers of operations. A disposal of government operations can occur through a transfer to another government or a sale. The provisions in Statement 69 are effective for fiscal years beginning after December 15, 2013. Management has not yet determined the effect of implementation of these statements on the financial statements of the State.

In April 2013, GASB issued Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, which requires a state or local government guarantor that offers a nonexchange financial guarantee to another organization or government to recognize a liability on its financial statements when it is more likely than not that the guarantor will be required to make a payment to the obligation holders under the agreement. The provisions in Statement 70 are effective for fiscal years beginning after June 15, 2013. Management has not yet determined the effect of implementation of these statements on the financial statements of the State.

U. Estimates

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

V. Total Columns

Total columns are presented primarily to facilitate financial analysis. The Management's Discussion and Analysis includes certain prior year summarized comparative information in total. Such information does not include sufficient detail to constitute a full comparative presentation. Accordingly, such information should be read in conjunction with the State's financial statements for the year ended September 30, 2012 from which summarized information was derived.

(2) Deposits and Investments

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(2) Deposits and Investments, Continued

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

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

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

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

A. Deposits

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

As of September 30, 2013, the carrying amount of the primary government's total cash and cash equivalents were \$402,546 and the corresponding bank balances were \$697,654, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2013, bank deposits were fully FDIC insured.

As of September 30, 2013, the carrying amount of the discretely presented component units' total cash and cash equivalents and time certificates of deposit was \$4,569,645 and the corresponding bank balances were \$4,843,186, which were maintained in financial institutions subject to FDIC insurance. As of September 30, 2013, bank deposits in the amount of \$1,617,721 were FDIC insured. The component units do not require collateralization of their cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Therefore, these deposits are exposed to custodial credit risk.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(2) Deposits and Investments, Continued

B. Investments

Primary Government:

As of September 30, 2013, the State's investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	\$ 2,632,845
Other investments:	
Domestic equities	18,048,660
Cash management account	<u>246,778</u>
	\$ <u>20,928,283</u>

As of September 30, 2013, the State's fixed income securities, including their Moody's Investors Service credit ratings, had the following maturities:

Investment Type	Investment Maturities (In Years)					Credit Ratings
	Fair Value	Current	1-5	6-10	Over 10	
U.S. Treasury Notes and Bonds	\$ 520,885	\$ 84,699	\$ 225,995	\$ 183,708	\$ 26,483	AAA
U.S. Government Agencies Obligations:						
Federal Home Loan Mortgage Corporation	122,546	54,303	9,153	1,756	57,334	AAA
Government National Mortgage Association	190,462	-	-	-	190,462	AAA
Federal National Mortgage Association	417,044	-	136,884	-	280,160	AAA
Small Business Administration	13,219	-	-	-	13,219	AAA
National Credit Union	46,329	-	6,492	-	39,837	AAA
Housing Urban Development	9,580	9,580	-	-	-	No rating
FISCO Debentures	12,285	-	12,285	-	-	No rating
AID-Tunisia	40,246	-	40,246	-	-	AAA/No rating
Financing Corporation	19,295	-	19,295	-	-	No rating
Municipal Obligations	46,335	-	-	-	46,335	A1
Municipal Obligations	35,556	-	7,945	8,467	20,144	A2
Municipal Obligations	84,035	29,707	-	24,442	29,886	Aa1
Municipal Obligations	9,871	-	-	-	9,871	Aa2
Municipal Obligations	3,141	3,141	-	-	-	Aa3
Municipal Obligations	47,060	29,382	-	17,678	-	No rating
Municipal Obligations	7,102	-	7,102	-	-	WR
Corporate Bonds	133,033	33,530	59,409	-	40,094	A1
Corporate Bonds	134,713	-	115,887	18,826	-	A2
Corporate Bonds	153,920	9,345	75,433	49,394	19,748	A3
Corporate Bonds	35,794	-	29,584	6,210	-	Aa1
Corporate Bonds	25,858	-	11,691	9,140	5,027	Aa2
Corporate Bonds	87,073	-	64,752	22,321	-	Aa3
Corporate Bonds	22,705	-	-	16,466	6,239	Aaa
Corporate Bonds	5,304	-	5,304	-	-	Ba1
Corporate Bonds	9,059	-	-	9,059	-	Ba2/Ba3
Corporate Bonds	112,758	-	56,085	46,924	9,749	Baa1
Corporate Bonds	163,778	8,364	79,351	15,782	60,281	Baa2
Corporate Bonds	68,359	-	24,854	22,013	21,492	Baa3
Corporate Bonds	54,500	-	12,455	22,739	19,306	No rating
	\$ <u>2,632,845</u>	\$ <u>262,051</u>	\$ <u>1,000,202</u>	\$ <u>474,925</u>	\$ <u>895,667</u>	

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(2) Deposits and Investments, Continued

B. Investments, Continued

Primary Government, Continued:

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

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the State will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The State's investments are held and administered by trustees. Based on negotiated trust and custody contracts, all of these investments were held in the State's name by the State's custodial financial institutions at September 30, 2013.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the State. As of September 30, 2013, the State did not hold an investment in any one issuer that represented more than 5% of the State's total investments.

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

As of September 30, 2013, the General Fund holds 5.4% of the outstanding shares of the Bank of the Federated States of Micronesia in the amount of \$500,000 and 13% of the outstanding shares of the Pacific Islands Development Bank in the amount of \$1,000,000. As the fair market value of these investments is not readily available, such have been recorded at cost. Additionally, the State acquired an interest in an airline during fiscal year 2004 and recorded an impairment of such investment in the same period. Financial statements from the investee are not currently available.

Discretely Presented Component Units:

Investments of the discretely presented component units at fair value are as follows:

Pohnpei Utilities Corporation:	
Mutual funds	\$ 174,124
Pohnpei Port Authority:	
Mutual funds	<u>1,584,781</u>
	\$ <u>1,758,905</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(3) Receivables

Primary Government:

Receivables as of September 30, 2013, for the primary government's individual major governmental funds, and nonmajor governmental funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	<u>General</u>	<u>Grants Assistance</u>	<u>Compact Trust</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Receivables:					
Taxes	\$ 1,977,739	\$ -	\$ -	\$ -	\$ 1,977,739
Due from FSM National Government	-	1,868,721	-	-	1,868,721
Other	<u>2,947,040</u>	<u>3,928</u>	<u>-</u>	<u>-</u>	<u>2,950,968</u>
	4,924,779	1,872,649	-	-	6,797,428
Allowance for uncollectible accounts	<u>(2,265,557)</u>	<u>(453,598)</u>	<u>-</u>	<u>-</u>	<u>(2,719,155)</u>
	<u>\$ 2,659,222</u>	<u>\$ 1,419,051</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 4,078,273</u>

Discretely Presented Component Units:

Receivables as of September 30, 2013, for the discretely presented component units, including applicable allowances for uncollectible accounts, are as follows:

	<u>Pohnpei Utilities Corporation</u>	<u>Pohnpei Port Authority</u>	<u>Pohnpei Transportation Authority</u>	<u>Small Business Guarantee and Finance Corporation</u>	<u>Pohnpei State Housing Authority</u>	<u>Total</u>
Loans	\$ -	\$ -	\$ -	\$ 870,452	\$ 7,685,418	\$ 8,555,870
General	5,750,606	2,323,097	853,313	-	-	8,927,016
Other	<u>-</u>	<u>229,868</u>	<u>-</u>	<u>50,517</u>	<u>49,189</u>	<u>329,574</u>
	5,750,606	2,552,965	853,313	920,969	7,734,607	17,812,460
Less: allowance for uncollectibles	<u>(4,222,187)</u>	<u>(1,535,180)</u>	<u>(850,389)</u>	<u>(112,899)</u>	<u>(5,571,893)</u>	<u>(12,292,548)</u>
	<u>\$ 1,528,419</u>	<u>\$ 1,017,785</u>	<u>\$ 2,924</u>	<u>\$ 808,070</u>	<u>\$ 2,162,714</u>	<u>\$ 5,519,912</u>

Loans receivable consist of the following:

Small Business Guarantee and Finance Corporation

Loans to qualified businesses under Micro Loan and Loan Guarantee Programs with interest at 9% per annum. \$ 870,452

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(3) Receivables, Continued

Discretely Presented Component Units, Continued:

Pohnpei State Housing Authority (PSHA)

PSHA's loan portfolio is derived from three sources: (1) capital contributions of Compact of Free Association Capital Account Funds - Capital Projects by Pohnpei State to fund the Housing Development Loan Fund; (2) Housing Preservation Grant (HPG) loans from a grant extended by the United States Department of Agriculture (USDA) Rural Development through the Housing and Community Facilities Program; and (3) Rural Development loans under the USDA funded Direct Single Family Housing Program. Loans are stated at face value, net of an allowance for loan losses. The allowance represents an amount which, in management's judgment, will be adequate to absorb possible losses on existing loans that may become uncollectible. Management's judgment in determining the adequacy of the allowance is based on evaluations of the collectability of loans. The allowance for loan losses are reported based on certain assumptions pertaining to PSHA's periodic review and evaluation of the loan portfolio, which is subject to change. A summary of loans receivable as of September 30, 2013 are presented below:

Pohnpei State Housing Authority loans	\$ 6,475,248
HPG loans	261,434
USDA Rural Development loans	<u>948,827</u>
	7,685,418
Less allowance for loan losses	<u>(5,571,893)</u>
Loans receivable, net	\$ <u>2,113,616</u>

All loans, other than USDA Rural Development loans, are at fixed rates (substantially 4.5%) and the loan terms range from 3 to 25 years. The USDA Rural Development loans are non-interest bearing.

(4) Interfund Receivables and Payables

Receivables and payables between funds reflected as due to/from other funds in the combined balance sheet at September 30, 2013, are summarized as follows:

Receivable Fund	Payable Fund	Amount
Grants Assistance	General	\$ 1,827,664
Nonmajor governmental funds	General	4,522,840
General	Grants Assistance	<u>818,222</u>
		\$ <u>7,168,726</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(4) Interfund Receivables and Payables, Continued

The amount recorded as due from component units of the primary government does not equal the corresponding due to primary government of the discretely presented component units of \$1,795,261 due to an allowance for doubtful accounts recorded by the General Fund of \$1,795,261.

(5) Capital Assets

Capital asset activities for the year ended September 30, 2013, are as follows:

Primary Government:

	Balance October <u>1, 2012</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2013</u>
Governmental activities:				
Capital assets, being depreciated:				
Buildings	\$ 13,728,473	\$ -	\$ -	\$ 13,728,473
Machinery, equipment and others	22,750,503	327,780	-	23,078,283
Infrastructure	<u>52,786,727</u>	<u>95,000</u>	<u>-</u>	<u>52,881,727</u>
Total capital assets, being depreciated	<u>89,265,703</u>	<u>422,780</u>	<u>-</u>	<u>89,688,483</u>
Less accumulated depreciation for:				
Buildings	(4,999,435)	(453,286)	-	(5,452,721)
Machinery, equipment and others	(21,171,080)	(642,015)	-	(21,813,095)
Infrastructure	<u>(39,377,751)</u>	<u>(1,638,889)</u>	<u>-</u>	<u>(41,016,640)</u>
	<u>(65,548,266)</u>	<u>(2,734,190)</u>	<u>-</u>	<u>(68,282,456)</u>
Governmental activities capital assets, net	\$ <u>23,717,437</u>	\$ <u>(2,311,410)</u>	\$ <u>-</u>	\$ <u>21,406,027</u>

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

General government	\$ 550,696
Land and natural resources	19,056
Education	258,631
Health services	166,624
Public safety	24,568
Public works and transportation	<u>1,714,615</u>
	<u>\$ 2,734,190</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(5) Capital Assets, Continued

Discretely Presented Component Units:

	Balance October <u>1, 2012</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2013</u>
Depreciable assets:				
Buildings	\$ 15,045,131	\$ 250,363	\$ -	\$ 15,295,494
Utility plant	56,572,456	6,271,951	(2,183,477)	60,660,930
Machinery, equipment and others	<u>7,024,508</u>	<u>235,624</u>	<u>(2,427)</u>	<u>7,257,705</u>
Total capital assets, being depreciated	78,642,095	6,757,938	(2,185,904)	83,214,129
Less accumulated depreciation	<u>(55,038,996)</u>	<u>(2,702,047)</u>	<u>2,183,477</u>	<u>(55,557,566)</u>
	<u>23,603,099</u>	<u>4,055,891</u>	<u>(2,427)</u>	<u>27,656,563</u>
Nondepreciable assets:				
Land	2,776,034	-	-	2,776,034
Construction work-in-progress	<u>5,547,942</u>	<u>2,490,438</u>	<u>(2,373)</u>	<u>8,036,007</u>
	<u>8,323,976</u>	<u>2,490,438</u>	<u>(2,373)</u>	<u>10,812,041</u>
	<u>\$ 31,927,075</u>	<u>\$ 6,546,329</u>	<u>\$ (4,800)</u>	<u>\$ 38,468,604</u>

(6) Long-Term Obligations

Primary Government:

The State implemented an Early Retirement Scheme (ERS) in which employees holding certain nonessential positions as identified by the State were retired early with a payout of the equivalent of two-years wages. This ERS program is funded by a \$4,200,000 loan from the ADB (Loan Number 1520 (SF)) through the FSM National Government, non-interest bearing with a service charge of 1% per annum on the amount of the loan withdrawn from the Loan Account. The activities of the ERS Program are recorded in the General Fund.

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

Funds for the repayment of the ADB loan are expected to be derived from the annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The Financing Agreement requires the State to continue to appropriate salaries for the abolished positions and deposit the appropriate funds into the ERS Trust Account. These funds had not been deposited to the Trust Account as of September 30, 2002. Of the required \$4,200,000 identified for future debt service payments, \$3,618,027 is deposited in an investment account held jointly with the FSM National Government. That investment account is restricted for the repayment of this debt. As of September 30, 2013, the balance payable on this loan amounted to \$4,277,765.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(6) Long-Term Obligations, Continued

Primary Government, Continued:

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government Program Loans with ADB (Loan Number 1873 (SF) and Loan Number 1874 FSM (SF)) for the purpose of promoting private sector development in Pohnpei, with interest at 1% to 1.5% per annum. Principal payments shall be made in 32 equal semi-annual payments with the first payment due on May 15, 2010 and the last payment on November 15, 2025. As of September 30, 2013, the balances payable on these loans amounted to \$455,407 and \$757,855, respectively.

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

<u>Year Ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$ 170,629	\$ 60,977	\$ 231,606
2015	170,629	58,903	229,532
2016	170,629	56,830	227,459
2017	170,629	54,757	225,386
2018	267,857	50,739	318,596
2019-2021	1,339,286	217,733	1,557,019
2022-2026	1,248,204	142,687	1,390,891
2027-2033	1,157,123	77,750	1,234,873
2034-2037	<u>796,040</u>	<u>19,712</u>	<u>815,752</u>
	\$ <u>5,491,027</u>	\$ <u>740,088</u>	\$ <u>6,231,115</u>

Discretely Presented Component Units:

Pohnpei Utilities Corporation (PUC)

Loan payable to the State, facilitated by an Asian Development Bank (ADB) loan (Loan Number 1459-FSM (SF)) to the FSM National Government, in the original amount of \$2,118,767 due in semi-annual installments of \$33,500 from February 2007 to August 2044. The State has not imposed collateralization on PUC and has waived its rights to receive 6.82% in interest. The loan includes a 1% per annum service charge to be added to the principal until installment payments commence. This service charge was paid by the State during the year ended September 30, 2013. During 2012, an additional \$294,720 was allocated to PUC which extended the maturity date to February 2052.

\$ 2,431,000

Loan payable to United States Department of Agriculture, Rural Utilities Service (RUS), in the original amount of \$578,000, interest at 4.5% per annum, with principal and interest payable commencing October 2006 of \$2,654 through July 2044. The loan is collateralized by a revenue pledge.

529,361

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(6) Long-Term Obligations, Continued

Discretely Presented Component Units, Continued:

Pohnpei Utilities Corporation (PUC), Continued

Loan payable to bank in the original amount of \$773,122, interest at 9% per annum, with principal and interest payable commencing September 2008 of \$9,794 through August 2013, collateralized by a diesel power comprehensive generator plant, two Daihatsu model 12D532 engines, building and materials, and existing and future receivables. 470,065

Loan payable to FSM Development Bank (FSMDB) in the original amount of \$481,701, interest at 9% per annum, with principal and interest payable commencing December 31, 2011 in monthly installments of \$9,807, collateralized by a \$150,000 time certificate of deposit, receivables, inventory and property, plant and equipment. 327,820

Loan payable to the State, facilitated by an ADB loan (Loan Number 2099-FSM) to the FSM National Government, in the original amount of \$3,752,000 due in semi-annual installments of \$85,883 from January 15, 2013 to July 15, 2036. Interest is payable at 1% per annum during the grace period and at 1.5% per annum thereafter. Proceeds were used to fund the overhaul of sewage pumps, extension of sewage lines, and treatment plants. 5,246,749

Loan payable to the State, facilitated by an ADB loan (Loan Number 2100-FSM) to the FSM National Government, in the original amount of \$2,000,000, due in semi-annual installments of varying amounts through January 15, 2019. Interest is payable at LIBOR plus 0.6% per annum (2.1% at September 30, 2013). Proceeds were used to fund the overhaul of sewage pumps, extension of sewage lines, and treatment plants. 1,277,944

Loan payable to bank in the original amount of \$140,000, interest at 2% per annum, with principal and interest payable commencing May 30, 2012 in monthly installments of \$3,039 through April 30, 2016, collateralized by a savings account of \$140,000. 94,739

\$ 10,377,678

**STATE OF POHNPEI
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Notes to Financial Statements
September 30, 2013

(6) Long-Term Obligations, Continued

Discretely Presented Component Units, Continued:

Pohnpei Utilities Corporation (PUC), Continued

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

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$ 376,519	\$ 206,829	\$ 583,348
2015	405,313	197,565	602,878
2016	417,246	176,550	593,796
2017	313,083	157,726	470,809
2018	314,647	144,772	459,419
2019-2023	1,173,173	633,105	1,806,278
2024-2028	1,435,260	527,451	1,962,711
2029-2033	1,092,333	412,478	1,504,811
2034-2038	1,023,665	328,802	1,352,467
2039-2043	2,856,755	237,347	3,094,102
2044-2048	318,382	41,823	360,205
2049-2053	308,679	26,321	335,000
2054-2058	324,421	10,579	335,000
2059-2063	<u>18,202</u>	<u>162</u>	<u>18,364</u>
	\$ <u>10,377,678</u>	\$ <u>3,101,510</u>	\$ <u>13,479,188</u>

(7) Short-term Debt

Discretely Presented Component Units:

Pohnpei Utilities Corporation (PUC)

Line of credit with a bank in the original amount of \$190,000, interest at 5% over the TCD rate (5.5% per annum at September 30, 2013), collateralized by a time certificate of deposit (TCD) with the bank, and expires on November 22, 2013.

Short-term activity for the year ended September 30, 2013, was as follows:

	Balance October 1, <u>2012</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2013</u>
Note payable:				
PUC	\$ <u>190,000</u>	\$ _____	\$ _____	\$ <u>190,000</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(8) Change in Long-Term Obligations

Primary Government:

Long-term liabilities will be liquidated in the future from governmental funds. During the year ended September 30, 2013, the following changes occurred in liabilities reported as part of the primary government's long-term liabilities in the statement of net position:

	Balance October 1, 2012	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2013	Due Within <u>One Year</u>
Loans payable:					
ADB loans:					
Loan 1520	\$ 4,368,107	\$ -	\$ (90,342)	\$ 4,277,765	\$ 97,228
Loan 1873	493,061	-	(37,654)	455,407	36,432
Loan 1874	<u>782,369</u>	<u>-</u>	<u>(24,514)</u>	<u>757,855</u>	<u>36,969</u>
	5,643,537	-	(152,510)	5,491,027	170,629
Other:					
Compensated absences	690,986	820,504	(829,971)	681,519	681,519
Claims	<u>210,968</u>	<u>-</u>	<u>-</u>	<u>210,968</u>	<u>-</u>
	<u>\$ 6,545,491</u>	<u>\$ 820,504</u>	<u>\$ (982,481)</u>	<u>\$ 6,383,514</u>	<u>\$ 852,148</u>

Discretely Presented Component Units:

During the year ended September 30, 2013, the following changes occurred in long-term obligations of the discretely presented component units:

	Balance October 1, 2012	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2013	Due Within <u>One Year</u>
Loans payable:					
Pohnpei Utilities Corporation	\$ <u>9,452,323</u>	\$ <u>1,598,648</u>	\$ <u>(673,293)</u>	\$ <u>10,377,678</u>	\$ <u>376,519</u>

(9) Contingencies and Commitments

Sick Leave

It is the policy of the State to record expenditures for sick leave when leave is actually taken. Sick leave is compensated time for absence during working hours arising from employee illness or injury.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(9) Contingencies and Commitments, Continued

Encumbrances

The State utilizes encumbrance accounting to identify fund obligations. Encumbrances represent commitments related to unperformed contracts for goods. At September 30, 2013, the State has significant encumbrances summarized as follows:

	<u>General</u>	<u>Grants Assistance</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Encumbrances	\$ <u>457,630</u>	\$ <u>1,606,588</u>	\$ <u>991,103</u>	\$ <u>3,055,321</u>

Federal Grants

The State participates in a number of federally assisted grant programs. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed.

Pursuant to Title I, Section 105 of United States Public Law 99-239, the Government of the Federated States of Micronesia (FSM) (which includes the State) is no longer liable for debts to U.S. federal agencies arising prior to the date of the implementation of the Compact of Free Association. This matter has not yet been officially resolved with the U.S. Government.

Loan Guarantees

As discussed in Note 1K, if after exhaustive efforts between Pohnpei State Housing Authority (the Authority) and Rural Development (parties to the MOU) have failed to collect from the defaulted borrowers, the State may be ultimately responsible for various USDA Rural Development loans. On March 28, 2007, the State was notified that various loans in the program may be in default. No provision for any liability that may result from this matter has been provided for within the accompanying financial statements.

The Authority's management is of the opinion that the primary government will become ultimately liable for such defaulted liabilities to USDA Rural Development. Therefore, such loans and related liability are not recorded by the Authority in the accompanying financial statements. The State is of the opinion that these loans have not been communicated timely in accordance with the underlying agreement and therefore, does not believe that it is liable for the balance.

Litigation

The State is party to several legal proceedings arising from governmental operations. Claims are filed with the State's Attorney General. Approved claims are usually paid under general appropriations to the affected government agency. The State Attorney General is of the opinion that the probable outcome of suits existing at September 30, 2013, is not predictable but could have a material impact on the accompanying financial statements. Such impact has currently been estimated to approximate \$210,968.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(9) Contingencies and Commitments, Continued

Insurance Coverage

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

Other

The State Legislature has authorized various Compact Infrastructure and Infrastructure Maintenance projects. However, the State Legislature has required that additional approvals be provided by that body prior to these projects being expended. As a result, no continuing appropriation has been recorded or will be recorded for these authorizations until such time as the additional requirements have been satisfied. State law mandates that 30% of fishing fines be shared with applicable municipalities. Given the lack of certain legal clarifications, no specific dollar amount can be determined to be recorded as either a continuing appropriation or as a liability due to the municipalities.

(10) Self-Insurance Fund - Component Units

In accordance with section 2(5) of State Law 3L-41-93, an amendment was made to the original enabling legislation for Pohnpei Utilities Corporation (PUC) establishing a self-insurance fund to defray costs of any unforeseen accidents or disasters. The funds are accumulated in a restricted self-insurance fund, held by a trustee, in the name of PUC. No other insurance is maintained by PUC.

Pohnpei Port Authority (PPA) purchase insurance to cover workmen's compensation and life insurance risks but is substantially self-insured for all other risks. Management of PPA is of the opinion that no material losses have been sustained as a result of this practice.

Pohnpei Transportation Authority (PTA) does not purchase commercial insurance covering potential risks. Management of PTA represents that no material losses have been sustained as a result of this practice during the last three years.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2013

(11) Fund Balance

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

	General <u>Fund</u>	Grants Assistance <u>Fund</u>	Compact Trust <u>Fund</u>	Nonmajor <u>Funds</u>	Total Governmental <u>Funds</u>
Non-spendable:					
General government	\$ 131,239	\$ -	\$ -	\$ -	\$ 131,239
Economic development	-	-	-	34,568	34,568
Pacific Islands Development Bank	1,000,000	-	-	-	1,000,000
Bank of the FSM	500,000	-	-	-	500,000
Permanent fund principal	-	-	10,940,700	-	10,940,700
Restricted for:					
General government	-	35,588	-	-	35,588
Debt service	3,681,027	-	-	-	3,681,027
USDA development loans	216,815	-	-	-	216,815
Education	-	58,797	-	-	58,797
Health services	-	4,787	-	-	47,787
Infrastructure maintenance	-	20,690	-	-	20,690
Committed:					
General government	148,716	-	-	959,421	1,108,137
Economic development	-	-	-	186,576	186,576
Health services	-	-	-	1,926,201	1,926,201
ADB private sector development	265,358	-	-	-	265,358
Assigned	457,630	-	-	989,288	1,446,918
Unassigned	<u>1,585,025</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,585,025</u>
	<u>\$ 7,985,810</u>	<u>\$ 119,862</u>	<u>\$ 10,940,700</u>	<u>\$ 4,096,054</u>	<u>\$ 23,142,426</u>

(12) Budgetary Compliance

For the year ended September 30, 2013, significant over-expenditures exceeded appropriations within the General Fund for the following:

Department of Treasury and Administration	\$ 529,473
Department of Public Works	\$ 71,827
Non-U.S. Grants Assistance Fund	\$ 261,468

These over-expenditures of the General Fund have not been funded by legislative authorization.

(13) FSM Development Bank Loan Funds

Compact Capital Account funds in an aggregate amount of \$1.7 million were transferred to the control of the FSM Development Bank (FSMDB) (a component unit of the FSM National Government) to be loaned out to borrowers from the State mainly for economic development projects. The loan fund is administered by FSMDB in a Trust capacity. All loan decisions are made by management of the State. These loans are not controlled by the State and are not currently recorded in the accompanying financial statements. As of December 31, 2013 (FSMDB fiscal year end), the outstanding fund balance aggregated \$898,481.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

**REQUIRED SUPPLEMENTARY INFORMATION-
OTHER THAN MANAGEMENT'S DISCUSSION AND ANALYSIS**

YEAR ENDED SEPTEMBER 30, 2013

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual
General Fund
Year Ended September 30, 2013

	Budgeted Amounts		Actual - Budgetary	Variance with <u>Final Budget -</u>
	Original	Final	Basis (see Note 1)	
Revenues:				
Grants	\$ -	\$ -	\$ 137,222	\$ 137,222
FSM revenue sharing	7,121,844	7,197,179	6,292,206	(904,973)
State taxes	2,698,334	2,698,334	2,184,133	(514,201)
Fees and charges	194,000	194,000	417,031	223,031
Net change in the fair value of investments	570,367	570,367	1,319,485	749,118
Other	187,982	187,982	778,756	590,774
Total revenues	<u>10,772,527</u>	<u>10,847,862</u>	<u>11,128,833</u>	<u>280,971</u>
Expenditures:				
Current:				
General government	3,949,522	3,797,522	4,324,123	(526,601)
Department of Land and Natural Resources	514,622	509,822	484,965	24,857
Department of Education	8,281	8,281	3,281	5,000
Department of Health Services	44,153	44,153	40,580	3,573
Department of Public Safety	1,233,091	1,233,091	1,220,720	12,371
Office of the Attorney-General	432,181	522,848	455,534	67,314
Department of Public Works	656,652	656,652	728,479	(71,827)
Boards, Commissions and Other	1,119,108	1,141,508	1,123,302	18,206
Payments to Non-governmental Agencies	313,834	432,902	421,252	11,650
Grants to local governments	2,422,301	2,422,301	2,409,942	12,359
Debt service	220,367	220,367	220,367	-
Total expenditures	<u>10,914,112</u>	<u>10,989,447</u>	<u>11,432,545</u>	<u>(443,098)</u>
Deficiency of revenues over expenditures	(141,585)	(141,585)	(303,712)	(162,127)
Other financing uses:				
Operating transfers out	-	-	(287,445)	(287,445)
Net change in fund balance	(141,585)	(141,585)	(591,157)	(449,572)
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes	291,174	291,174	353,078	61,904
	149,589	149,589	(238,079)	(387,668)
Fund balance at the beginning of the year	8,223,889	8,223,889	8,223,889	-
Fund balance at the end of the year	<u>\$ 8,373,478</u>	<u>\$ 8,373,478</u>	<u>\$ 7,985,810</u>	<u>\$ (387,668)</u>

See accompanying notes to required supplementary information - budgetary reporting.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting
September 30, 2013

(1) Budgetary Information

The Governor presents to the Pohnpei State Legislature, prior to September 30, proposed budget estimates for the fiscal year commencing October 1. The budget estimates include the overall and total proposed expenditures of the State and the means of financing those expenditures. The Pohnpei State Legislature reviews and approves these estimates making changes, as it deems appropriate. The Appropriation Committee of the Pohnpei State Legislature, during the regular session of the Pohnpei State Legislature, holds public hearings at which time Departments and Offices are required to justify their budget estimates. During the regular session of the Pohnpei State Legislature, an appropriation bill, as required by the Constitution, is introduced and budget estimates are then legally enacted by the Pohnpei State Legislature.

Formal budget integration is employed as a management control device during the year for all funds. The Pohnpei State Legislature has the authority to reprogram budgeted estimates in accordance with the Constitution. All annual appropriations lapse at the end of the fiscal year unless otherwise specified by law. Supplemental appropriations may occur throughout the year. Unexpended encumbrances at each fiscal year end are carried forward until they are expended or canceled without further legislative action. The State does not establish budgets for the operations of its other governmental funds.

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

OTHER SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2013

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account
Governmental Funds
Year Ended September 30, 2013

	General	Special Revenue	Permanent	Other Governmental Funds	Total
		Grants Assistance	Compact Trust		
Expenditures:					
Salaries and wages					
Regular	\$ 4,545,501	\$ 9,898,227	\$ -	\$ 143,467	\$ 14,587,195
Overtime	73,866	139,435	-	21,316	234,617
Fringe benefits	931,318	2,230,190	-	6,981	3,168,489
Travel and transportation					
Travel and transportation	182,873	456,192	-	7,414	646,479
Books and instructional materials	-	523,409	-	-	523,409
Communications	134,072	118,075	-	8,192	260,339
Customs and taxes	104	-	-	(28)	76
Dues, membership, and subscriptions	12,725	9,856	-	-	22,581
Food stuffs	82,015	571,800	-	5,723	659,538
Freight and port charges	52	10,670	-	1,005	11,727
Non-capitalized equipment	15,217	59,768	-	1,768	76,753
Capital outlays	63,041	309,848	-	120,794	493,683
Office supplies and materials	263,184	547,347	-	202,704	1,013,235
POL	214,627	194,870	-	19,756	429,253
Printing and reproduction	34,386	22,836	-	3,762	60,984
Rental services	15,812	34,664	-	413	50,889
Repairs and maintenance	23,803	82,359	-	2,439	108,601
Utilities	380,650	1,078,508	-	40,419	1,499,577
Miscellaneous goods and services	9,672	238,102	-	521	248,295
Subsidies and contributions	260,560	68,850	-	28,000	357,410
Medical referrals	-	249,275	-	-	249,275
Medical supplies	-	1,159,947	-	427,685	1,587,632
Contractual services	328,651	960,801	-	445,690	1,735,142
Housing allowance	37,900	131,247	-	-	169,147
Non-payroll compensation	4,907	241,372	-	-	246,279
Court settlements	132,941	-	-	-	132,941
Scholarships and allowances	-	348,598	-	193,155	541,753
Insurance	36,393	-	-	-	36,393
Official allowance	115,060	-	-	-	115,060
Meeting allowance	7,170	11,675	-	5,620	24,465
Leased housing, buildings and land	2,618	-	-	-	2,618
Principal repayment	152,510	-	-	-	152,510
Interest payments	67,857	-	-	-	67,857
Payments to municipalities	2,409,942	-	-	-	2,409,942
Bank charges	43	4,332	-	-	4,375
Miscellaneous	539,997	-	-	515	540,512
	<u>\$ 11,079,467</u>	<u>\$ 19,702,253</u>	<u>\$ -</u>	<u>\$ 1,687,311</u>	<u>\$ 32,469,031</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function,
and Changes in Fund Balance
General Fund
Year Ended September 30, 2013
(with comparative totals for the year ended September 30, 2012)

	2013	2012
Revenues:		
CFSM grants	\$ 137,222	\$ -
FSM revenue sharing:		
Gross revenue taxes	2,265,569	2,209,724
Import taxes	1,668,273	2,370,570
Income taxes	2,069,793	1,925,080
Other taxes	288,571	353,795
	6,292,206	6,859,169
State taxes:		
Sales tax	2,093,832	2,197,348
Hotel tax	90,301	77,425
	2,184,133	2,274,773
Fees and charges:		
Licenses and fees:	417,031	144,198
Net change in the fair value of investments	1,319,485	1,692,662
Other revenues	778,756	95,154
Total revenues	11,128,833	11,065,956
Expenditures:		
Current:		
General government:		
Governor and Staff	487,954	603,178
Department of Treasury and Administration	1,161,833	1,123,364
Office of Pohnpei Public Auditor	1,699	3,298
Judiciary Branch	728,008	737,484
Legislative Branch	1,798,523	1,747,620
	4,178,017	4,214,944
Department of Land and Natural Resources:		
Office of the Director	85,153	88,174
Division of Public Land	14,638	21,812
Land Use Planning and Zoning Commission	920	-
Division of Surveying and Mapping	184,270	168,264
Division of Forestry and Marine Conservation	73,827	87,972
Division of Historic Preservation	50,880	119,603
Division of Parks and Recreation	67,479	-
	477,167	485,825
Department of Education:		
Division of Primary Education	2,318	2,318
Department of Health:		
Medical services	40,580	-
Department of Public Safety:		
Office of the Director	81,274	72,347
Search and Rescue	1,383	2,488
Fish & Wildlife	105,039	151
Police Commission	25,720	26,811
Division of Police and Security	744,547	837,703
Division of Correction and Rehabilitation	220,102	248,070
	1,178,065	1,187,570
Office of the Attorney-General	435,492	310,577
Public Works	653,000	513,954

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function,
and Changes in Fund Balance, Continued
General Fund
Year Ended September 30, 2013
(with comparative totals for the year ended September 30, 2012)

	2013	2012
Expenditures, continued:		
Current:		
Boards, Commissions and Other:		
Office of Economic Affairs	309,326	337,126
Office of Social Affairs	99,739	99,847
Election Commissioner's Office	51,671	198,442
Pohnpei Public Broadcasting Corporation	123,747	116,450
Foreign Investment Board	41,780	55,330
Pohnpei Housing Authority	117,105	128,766
Sports and Recreation	139,881	129,275
Office of Fisheries and Aquaculture	206,304	3,788
Environmental Protection Agency	6,160	-
	1,095,713	1,069,024
Payments to Non-governmental Agencies:		
Small Business Guarantee and Finance Corporation	90,000	110,000
Pohnpei Public Library	58,000	58,000
Micronesian Legal Services Corporation	57,920	38,280
U.S.D.A. Rural Development	92,341	92,559
Pohnpei Visitors' Bureau	65,082	1,445
Pahap Power Extension	-	10,500
Small Business Development	25,000	52,000
Island Food Community	-	20,000
Other	463	565
	388,806	383,349
Grants to local governments	2,409,942	2,394,925
Debt Service:		
Principal payments	152,510	171,476
Interest charges	67,857	48,891
	220,367	220,367
Total expenditures	11,079,467	10,782,853
Excess of revenues over expenditures	49,366	283,103
Other financing sources (uses):		
Operating transfers in	-	1,954,828
Operating transfers out	(287,445)	(322,932)
Total other financing sources (uses), net	(287,445)	1,631,896
Net change in fund balance	(238,079)	1,914,999
Fund balance at the beginning of the year	8,223,889	6,308,890
Fund balance at the end of the year	\$ 7,985,810	\$ 8,223,889

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function and Changes in Fund Balance
Budget and Actual - General Fund
Year Ended September 30, 2013

	Budgeted Amounts		Actual - Budgetary Basis	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues:				
CFSM grants	\$ -	\$ -	\$ 137,222	\$ 137,222
FSM revenue sharing	7,121,844	7,197,179	6,292,206	(904,973)
State taxes:				
Sales tax	2,610,185	2,610,185	2,093,832	(516,353)
Hotel tax	88,149	88,149	90,301	2,152
	<u>2,698,334</u>	<u>2,698,334</u>	<u>2,184,133</u>	<u>(514,201)</u>
Fees and charges:				
Licenses and fees	194,000	194,000	417,031	223,031
Net change in the fair value of investments	570,367	570,367	1,319,485	749,118
Other	187,982	187,982	778,756	590,774
Total revenues	<u>10,772,527</u>	<u>10,847,862</u>	<u>11,128,833</u>	<u>280,971</u>
Expenditures:				
Current:				
General government:				
Governor and Staff	515,729	515,729	545,478	(29,749)
Department of Treasury and Administration	800,070	648,070	1,177,543	(529,473)
Office of the Pohnpei Public Auditor	2,000	2,000	1,999	1
Judiciary Branch	747,387	747,387	746,742	645
Legislative Branch	1,884,336	1,884,336	1,852,361	31,975
	<u>3,949,522</u>	<u>3,797,522</u>	<u>4,324,123</u>	<u>(526,601)</u>
Department of Land and Natural Resources:				
Office of the Director	90,458	90,458	86,394	4,064
Division of Public Land	23,452	23,452	14,638	8,814
Land Use Planning and Zoning Commission	-	-	920	(920)
Division of Surveying and Mapping	198,116	198,116	184,711	13,405
Division of Forestry and Marine Conservation	79,327	76,927	77,032	(105)
Division of Historic Preservation	53,269	50,869	51,824	(955)
Division of Parks and Recreation	70,000	70,000	69,446	554
	<u>514,622</u>	<u>509,822</u>	<u>484,965</u>	<u>24,857</u>
Department of Education:				
Division of Primary Education	8,281	8,281	3,281	5,000
Department of Health Services:				
Division of Medical Services	44,153	44,153	40,580	3,573
Department of Public Safety:				
Office of the Director	156,184	156,184	93,351	62,833
Search and Rescue	5,000	5,000	1,383	3,617
Police Commission	26,095	26,095	25,919	176
Division of Police and Security	688,452	688,452	753,851	(65,399)
Division of Correction and Rehabilitation	239,431	239,431	222,950	16,481
Fish and Wildlife	117,339	117,339	122,676	(5,337)
Hazard Mitigation Project	590	590	590	-
	<u>1,233,091</u>	<u>1,233,091</u>	<u>1,220,720</u>	<u>12,371</u>
Office of the Attorney-General	432,181	522,848	455,534	67,314
Department of Public Works:				
Office of Transportation and Infrastructure	656,652	656,652	728,479	(71,827)

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function and Changes in Fund Balance, Continued
Budget and Actual - General Fund
Year Ended September 30, 2013

	Budgeted Amounts		Actual - Budgetary Basis	Variance with Final Budget - Positive (Negative)
	Original	Final Budget		
Expenditures, continued:				
Boards, Commissions and Other:				
Office of Economic Affairs	321,372	321,372	311,961	9,411
Office of Social Affairs	106,217	106,217	100,159	6,058
Election Commissioner's Office	52,144	52,144	52,186	(42)
Pohnpei Public Broadcasting Corporation	133,610	133,610	123,853	9,757
Foreign Investment Board	55,703	55,703	48,661	7,042
Pohnpei Housing Authority	123,366	120,766	118,236	2,530
Sports & Recreation	146,889	171,889	154,430	17,459
Office of Fisheries and Aquaculture	179,807	179,807	207,656	(27,849)
Environmental Protection Agency	-	-	6,160	(6,160)
	<u>1,119,108</u>	<u>1,141,508</u>	<u>1,123,302</u>	<u>18,206</u>
Payments to Non-Governmental Agencies:				
Small Business Guarantee and Finance Corporation				
	100,000	100,000	90,000	10,000
Pohnpei Public Library	58,000	58,000	58,000	-
Micronesia Legal Services Corporation	57,920	57,920	57,920	-
U.S.D.A. Rural Development	96,683	96,683	96,396	287
Pohnpei Visitors Bureau	860	54,360	68,351	(13,991)
Small Business Development Center	-	25,000	25,000	-
Traditional Leaders Conference	-	40,568	24,500	16,068
Other	371	371	1,085	(714)
	<u>313,834</u>	<u>432,902</u>	<u>421,252</u>	<u>11,650</u>
Grants to local governments	<u>2,422,301</u>	<u>2,422,301</u>	<u>2,409,942</u>	<u>12,359</u>
Debt service:				
Principal and interest repayment				
	<u>220,367</u>	<u>220,367</u>	<u>220,367</u>	<u>-</u>
	<u>220,367</u>	<u>220,367</u>	<u>220,367</u>	<u>-</u>
Total expenditures	<u>10,914,112</u>	<u>10,989,447</u>	<u>11,432,545</u>	<u>(443,098)</u>
Deficiency of revenues under expenditures	(141,585)	(141,585)	(303,712)	(162,127)
Other financing sources:				
Operating transfers out				
	-	-	(287,445)	(287,445)
Net change in fund balance	(141,585)	(141,585)	(591,157)	(449,572)
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes				
	291,174	291,174	353,078	61,904
	149,589	149,589	(238,079)	(387,668)
Fund balance at the beginning of the year	<u>8,223,889</u>	<u>8,223,889</u>	<u>8,223,889</u>	<u>-</u>
Fund balance at the end of the year	<u>\$ 8,373,478</u>	<u>\$ 8,373,478</u>	<u>\$ 7,985,810</u>	<u>\$ (387,668)</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Balance Sheet
September 30, 2013

	26	27	29	32	33	34	35	36	37	38	18	87	Total
	Alien Registration Revolving	Pohnpei State Farmers' Revolving	Fisheries Enforcement and Development	Recycling Revolving	Paved Road Maintenance	Medical Supplies Revolving	Public Broadcasting Corporation	Health Care Premium	Department of Public Safety Fees	Environmental Quality	Infrastructure Maintenance	Public Lands Trust	
ASSETS													
Due from other funds	\$ 107,621	\$ 7,551	\$ 201,542	\$ -	\$ 1,668,413	\$ 257,459	\$ 7,882	\$ 1,909,495	\$ 2,862	\$ -	\$ 240,530	\$ 119,485	\$ 4,522,840
Advances	-	-	4,621	-	-	-	-	-	-	-	1,000	-	5,621
Inventories	-	29,947	-	-	-	-	-	-	-	-	-	-	29,947
Total assets	<u>\$ 107,621</u>	<u>\$ 37,498</u>	<u>\$ 206,163</u>	<u>\$ -</u>	<u>\$ 1,668,413</u>	<u>\$ 257,459</u>	<u>\$ 7,882</u>	<u>\$ 1,909,495</u>	<u>\$ 2,862</u>	<u>\$ -</u>	<u>\$ 241,530</u>	<u>\$ 119,485</u>	<u>\$ 4,558,408</u>
LIABILITIES AND FUND BALANCES													
Liabilities:													
Accounts payable	\$ 70,336	\$ 682	\$ 3,836	\$ -	\$ 12,663	\$ 125,388	\$ 2,199	\$ -	\$ -	\$ -	\$ -	\$ 2,838	\$ 217,942
Other liabilities and accruals	-	-	-	-	-	-	-	-	2,862	-	-	20	2,882
Deferred revenue	-	-	-	-	-	-	-	-	-	-	241,530	-	241,530
Total liabilities	<u>70,336</u>	<u>682</u>	<u>3,836</u>	<u>-</u>	<u>12,663</u>	<u>125,388</u>	<u>2,199</u>	<u>-</u>	<u>2,862</u>	<u>-</u>	<u>241,530</u>	<u>2,858</u>	<u>462,354</u>
Fund balances:													
Non-spendable	-	29,947	4,621	-	-	-	-	-	-	-	-	-	34,568
Committed	37,285	156	186,523	-	802,416	16,706	4,609	1,909,495	-	-	-	115,008	3,072,198
Assigned	-	6,713	11,183	-	853,334	115,365	1,074	-	-	-	-	1,619	989,288
Total fund balances	<u>37,285</u>	<u>36,816</u>	<u>202,327</u>	<u>-</u>	<u>1,655,750</u>	<u>132,071</u>	<u>5,683</u>	<u>1,909,495</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>116,627</u>	<u>4,096,054</u>
Total liabilities and fund balances	<u>\$ 107,621</u>	<u>\$ 37,498</u>	<u>\$ 206,163</u>	<u>\$ -</u>	<u>\$ 1,668,413</u>	<u>\$ 257,459</u>	<u>\$ 7,882</u>	<u>\$ 1,909,495</u>	<u>\$ 2,862</u>	<u>\$ -</u>	<u>\$ 241,530</u>	<u>\$ 119,485</u>	<u>\$ 4,558,408</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Statement of Revenues, Expenditures By Function,
and Changes in Fund Balances
Year Ended September 30, 2013

	26	27	29	32	33	34	35	36	37	38	18	87	Total
	Alien Registration Revolving	Pohnpei State Farmers' Revolving	Fisheries Enforcement and Development	Recycling Revolving	Paved Road Maintenance	Medical Supplies Revolving	Public Broadcasting Corporation	Health Care Premium	Department of Public Safety Fees	Environmental Quality	Infrastructure Maintenance	Public Lands Trust	Total
Revenues:													
Federal grants	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 46,118	\$ -	\$ 46,118
Excise tax	-	-	-	-	434,795	-	-	-	-	-	-	-	434,795
Fees and charges	55,440	94,660	-	97,266	-	524,904	18,622	61,885	99,209	-	-	73,104	1,025,090
Total revenues	<u>55,440</u>	<u>94,660</u>	<u>-</u>	<u>97,266</u>	<u>434,795</u>	<u>524,904</u>	<u>18,622</u>	<u>61,885</u>	<u>99,209</u>	<u>-</u>	<u>46,118</u>	<u>73,104</u>	<u>1,506,003</u>
Expenditures by function:													
Current:													
General government	221,155	71,247	52,188	127,030	497,462	-	22,879	-	149,541	4,512	46,118	55,621	1,247,753
Health services	-	-	-	-	-	439,558	-	-	-	-	-	-	439,558
Total expenditures	<u>221,155</u>	<u>71,247</u>	<u>52,188</u>	<u>127,030</u>	<u>497,462</u>	<u>439,558</u>	<u>22,879</u>	<u>-</u>	<u>149,541</u>	<u>4,512</u>	<u>46,118</u>	<u>55,621</u>	<u>1,687,311</u>
Excess (deficiency) of revenues over (under) expenditures	(165,715)	23,413	(52,188)	(29,764)	(62,667)	85,346	(4,257)	61,885	(50,332)	(4,512)	-	17,483	(181,308)
Other financing sources:													
Operating transfers in	-	-	-	12,700	-	-	-	-	10,930	2,347	-	-	25,977
Net change in fund balances	<u>(165,715)</u>	<u>23,413</u>	<u>(52,188)</u>	<u>(17,064)</u>	<u>(62,667)</u>	<u>85,346</u>	<u>(4,257)</u>	<u>61,885</u>	<u>(39,402)</u>	<u>(2,165)</u>	<u>-</u>	<u>17,483</u>	<u>(155,331)</u>
Fund balances at the beginning of the year	<u>203,000</u>	<u>13,403</u>	<u>254,515</u>	<u>17,064</u>	<u>1,718,417</u>	<u>46,725</u>	<u>9,940</u>	<u>1,847,610</u>	<u>39,402</u>	<u>2,165</u>	<u>-</u>	<u>99,144</u>	<u>4,251,385</u>
Fund balances at the end of the year	<u>\$ 37,285</u>	<u>\$ 36,816</u>	<u>\$ 202,327</u>	<u>\$ -</u>	<u>\$ 1,655,750</u>	<u>\$ 132,071</u>	<u>\$ 5,683</u>	<u>\$ 1,909,495</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 116,627</u>	<u>\$ 4,096,054</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Statement of Revenues, Expenditures By Account,
and Changes in Fund Balances
Year Ended September 30, 2013

	26	27	29	32	33	34	35	36	37	38	18	87	Total
	Alien Registration Revolving	Pohnpei State Farmers' Revolving	Fisheries Enforcement and Development	Recycling Revolving	Paved Road Maintenance	Medical Supplies Revolving	Public Broadcasting Corporation	Health Care Premium	Department of Public Safety Fees	Environmental Quality	Infrastructure Maintenance	Public Lands Trust	
Revenues:													
Federal grants	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 46,118	\$ -	\$ 46,118
Excise tax	-	-	-	-	434,795	-	-	-	-	-	-	-	434,795
Fees and charges	55,440	94,660	-	97,266	-	524,904	18,622	61,885	99,209	-	-	73,104	1,025,090
Total revenues	55,440	94,660	-	97,266	434,795	524,904	18,622	61,885	99,209	-	46,118	73,104	1,506,003
Expenditures by account:													
Salaries and wages:													
Regular	-	-	-	-	-	-	-	-	98,934	3,659	-	40,874	143,467
Overtime	-	-	-	-	-	-	-	-	21,316	-	-	-	21,316
Fringe benefits	-	-	-	-	-	-	-	-	1,492	-	-	5,489	6,981
Travel	-	650	6,336	-	-	-	332	-	96	-	-	-	7,414
Communications	-	2,189	2,947	-	-	-	-	-	3,056	-	-	-	8,192
Custom and tax	-	(28)	-	-	-	-	-	-	-	-	-	-	(28)
Food stuff	-	-	1,097	-	-	-	-	-	4,626	-	-	-	5,723
Freight and port charges	-	899	106	-	-	-	-	-	-	-	-	-	1,005
Non-capitalized equipment	-	1,228	-	-	-	-	-	-	-	-	-	540	1,768
Capital outlay	-	1,805	-	-	103,363	-	5,371	-	10,255	-	-	-	120,794
Office supplies and materials	-	49,529	5,316	126,515	-	11,873	-	-	5,026	-	-	4,445	202,704
POL	-	11,546	5,366	-	-	-	-	-	2,832	-	-	-	19,756
Printing and reproduction	-	134	3,337	-	-	-	-	-	83	-	-	208	3,762
Rental	-	20	13	-	-	-	-	-	380	-	-	-	413
Repairs and maintenance	-	485	1,270	-	-	-	-	-	411	-	-	273	2,439
Utilities	-	2,791	25,900	-	-	-	11,216	-	512	-	-	-	40,419
Subsidies and contributions	28,000	-	-	-	-	-	-	-	-	-	-	-	28,000
Miscellaneous goods and services	-	(1)	-	-	-	-	-	-	522	-	-	-	521
Medical supplies	-	-	-	-	-	427,685	-	-	-	-	-	-	427,685
Contractual services	-	-	-	-	394,099	-	4,620	-	-	853	46,118	-	445,690
Scholarships and allowances	193,155	-	-	-	-	-	-	-	-	-	-	-	193,155
Bank charges	-	-	-	515	-	-	-	-	-	-	-	-	515
Meeting allowance	-	-	500	-	-	-	1,340	-	-	-	-	3,780	5,620
Total expenditures	221,155	71,247	52,188	127,030	497,462	439,558	22,879	-	149,541	4,512	46,118	55,621	1,687,311
Excess (deficiency) of revenues over (under) expenditures	(165,715)	23,413	(52,188)	(29,764)	(62,667)	85,346	(4,257)	61,885	(50,332)	(4,512)	-	17,483	(181,308)
Other financing sources:													
Operating transfers in	-	-	-	12,700	-	-	-	-	10,930	2,347	-	-	25,977
Net change in fund balances	(165,715)	23,413	(52,188)	(17,064)	(62,667)	85,346	(4,257)	61,885	(39,402)	(2,165)	-	17,483	(155,331)
Fund balances at the beginning of the year	203,000	13,403	254,515	17,064	1,718,417	46,725	9,940	1,847,610	39,402	2,165	-	99,144	4,251,385
Fund balances at the end of the year	\$ 37,285	\$ 36,816	\$ 202,327	\$ -	\$ 1,655,750	\$ 132,071	\$ 5,683	\$ 1,909,495	\$ -	\$ -	\$ -	\$ 116,627	\$ 4,096,054

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUNDS

**Combining Balance Sheet
September 30, 2013**

	10	11	12	13	14	15	16	19	6	7	20	23	25	
	Section 211(a)(1) Education Sector	Section 211(a)(2) Health Sector	Section 211(a)(5) Environment	Section 211(a)(3) Private Sector Development	Section 211(a)(4) Capacity Building	Section 211(a)(1) Supplemental Education	Enhanced Reporting Accountability	Infrastructure Maintenance	Section 221(b) Special Block Grant	Compact I Other Grants	U.S. Federal Grants	Non-U.S. Grants	CFSM Grants	Total
ASSETS														
Receivables:														
Due from FSM National Government	\$ -	\$ -	\$ 87,770	\$ -	\$ -	\$ 223,964	\$ 4,085	\$ 306,577	\$ -	\$ -	\$ 273,232	\$ 8,750	510,745	\$ 1,415,123
Other	-	-	-	-	-	-	-	-	-	-	-	-	3,928	3,928
Due from other funds	842,689	698,689	-	87,897	61,041	-	8,706	-	44,188	35,588	-	48,866	-	1,827,664
Advances	10,030	6,362	288	1,759	58,738	19,058	-	-	-	-	20,006	3,958	6,770	126,969
Restricted cash	-	7,700	-	-	-	-	-	-	-	-	-	-	-	7,700
	<u>\$ 852,719</u>	<u>\$ 712,751</u>	<u>\$ 88,058</u>	<u>\$ 89,656</u>	<u>\$ 119,779</u>	<u>\$ 243,022</u>	<u>\$ 12,791</u>	<u>\$ 306,577</u>	<u>\$ 44,188</u>	<u>\$ 35,588</u>	<u>\$ 293,238</u>	<u>\$ 61,574</u>	<u>\$ 521,443</u>	<u>\$ 3,381,384</u>
LIABILITIES AND FUND BALANCES														
Liabilities:														
Accounts payable	\$ 114,130	\$ 119,670	\$ 6,220	\$ -	\$ 4,170	\$ 121,635	\$ 7,327	\$ -	\$ -	\$ -	\$ 53,267	\$ 1,916	\$ 354,569	\$ 782,904
Other liabilities and accruals	139,168	57,035	4,177	-	5,256	29,060	5,464	-	-	-	38,715	-	11	278,886
Deferred revenue	592,305	531,259	-	89,119	109,169	-	-	-	-	-	-	59,658	-	1,381,510
Due to other funds	-	-	77,661	-	-	84,834	-	287,608	-	-	201,256	-	166,863	818,222
Total liabilities	<u>845,603</u>	<u>707,964</u>	<u>88,058</u>	<u>89,119</u>	<u>118,595</u>	<u>235,529</u>	<u>12,791</u>	<u>287,608</u>	<u>-</u>	<u>-</u>	<u>293,238</u>	<u>61,574</u>	<u>521,443</u>	<u>3,261,522</u>
Fund balances:														
Restricted	7,116	4,787	-	537	1,184	7,493	-	18,969	44,188	35,588	-	-	-	119,862
Total fund balances	<u>7,116</u>	<u>4,787</u>	<u>-</u>	<u>537</u>	<u>1,184</u>	<u>7,493</u>	<u>-</u>	<u>18,969</u>	<u>44,188</u>	<u>35,588</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>119,862</u>
Total liabilities and fund balances	<u>\$ 852,719</u>	<u>\$ 712,751</u>	<u>\$ 88,058</u>	<u>\$ 89,656</u>	<u>\$ 119,779</u>	<u>\$ 243,022</u>	<u>\$ 12,791</u>	<u>\$ 306,577</u>	<u>\$ 44,188</u>	<u>\$ 35,588</u>	<u>\$ 293,238</u>	<u>\$ 61,574</u>	<u>\$ 521,443</u>	<u>\$ 3,381,384</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUNDS

**Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2013**

	10	11	12	13	14	15	16	19	6	7	20	23	25	
	Section	Section	Section	Section	Section	Section	Enhanced	Infrastructure	Section	Compact I	U.S.	Non-U.S.	CFSM	
	211(a)(1)	211(a)(2)	211(a)(5)	211(a)(3)	211(a)(4)	211(a)(1)	Reporting	Maintenance	221(b)	Other	Federal	Grants	Grants	Total
	Education	Health	Environment	Private Sector	Capacity	Supplemental	Accountability		Special Block	Grants	Grants	Grants	Grants	
	Sector	Sector		Development	Building	Education			Grant					
Revenues:														
Compact funding	\$ 7,355,017	\$ 5,449,176	\$ 376,811	\$ 3,013	\$ 414,970	\$ 2,719,379	\$ 292,731	\$ 96,188	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 16,707,285
CFSM grants	-	-	-	-	-	-	-	-	-	-	-	-	436,145	436,145
Federal contributions and other grants	-	-	-	-	-	-	-	-	-	-	2,360,889	79,417	-	2,440,306
Other	-	-	-	-	-	-	-	-	-	-	-	(6,165)	-	(6,165)
	<u>7,355,017</u>	<u>5,449,176</u>	<u>376,811</u>	<u>3,013</u>	<u>414,970</u>	<u>2,719,379</u>	<u>292,731</u>	<u>96,188</u>	<u>-</u>	<u>-</u>	<u>2,360,889</u>	<u>73,252</u>	<u>436,145</u>	<u>19,577,571</u>
Expenditures by function:														
Current:														
General government	-	-	350,625	3,013	414,970	-	292,731	96,188	-	-	-	224,120	436,145	1,817,792
Land and natural resources	-	-	-	-	-	-	-	-	-	-	193,100	-	-	193,100
Education	7,355,017	-	-	-	-	2,719,379	-	-	-	-	1,042,882	-	-	11,117,278
Health services	-	5,449,176	-	-	-	-	-	-	-	-	1,124,907	-	-	6,574,083
Total expenditures	<u>7,355,017</u>	<u>5,449,176</u>	<u>350,625</u>	<u>3,013</u>	<u>414,970</u>	<u>2,719,379</u>	<u>292,731</u>	<u>96,188</u>	<u>-</u>	<u>-</u>	<u>2,360,889</u>	<u>224,120</u>	<u>436,145</u>	<u>19,702,253</u>
Excess (deficiency) of revenues over (under) expenditures	-	-	26,186	-	-	-	-	-	-	-	-	(150,868)	-	(124,682)
Other financing sources:														
Operating transfers in	-	-	-	-	-	-	-	-	-	-	-	261,468	-	261,468
Net change in fund balances (deficit)	-	-	26,186	-	-	-	-	-	-	-	-	110,600	-	136,786
Fund balances (deficit) at the beginning of the year	<u>7,116</u>	<u>4,787</u>	<u>(26,186)</u>	<u>537</u>	<u>1,184</u>	<u>7,493</u>	<u>-</u>	<u>18,969</u>	<u>44,188</u>	<u>35,588</u>	<u>-</u>	<u>(110,600)</u>	<u>-</u>	<u>(16,924)</u>
Fund balances at the end of the year	<u>\$ 7,116</u>	<u>\$ 4,787</u>	<u>\$ -</u>	<u>\$ 537</u>	<u>\$ 1,184</u>	<u>\$ 7,493</u>	<u>\$ -</u>	<u>\$ 18,969</u>	<u>\$ 44,188</u>	<u>\$ 35,588</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 119,862</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUNDS

**Combining Statement of Revenues, Expenditures by Account,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2013**

	10	11	12	13	14	15	16	19	6	7	20	23	25	
	Section 211(a)(1) Education Sector	Section 211(a)(2) Health Sector	Section 211(a)(5) Environment	Section 211(a)(3) Private Sector Development	Section 211(a)(4) Capacity Building	Section 211(a)(1) Supplemental Education	Enhanced Reporting Accountability	Infrastructure	Section 221(b) Special Block Grant	Compact I Other Grants	U.S. Federal Grants	Non-U.S. Grants	CFSM Grants	Total
Revenues:														
Compact funding	\$ 7,355,017	\$ 5,449,176	\$ 376,811	\$ 3,013	\$ 414,970	\$ 2,719,379	\$ 292,731	\$ 96,188	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 16,707,285
CFSM grants	-	-	-	-	-	-	-	-	-	-	-	-	436,145	436,145
Federal contributions and other grants	-	-	-	-	-	-	-	-	-	-	2,360,889	79,417	-	2,440,306
Other	-	-	-	-	-	-	-	-	-	-	-	(6,165)	-	(6,165)
	<u>7,355,017</u>	<u>5,449,176</u>	<u>376,811</u>	<u>3,013</u>	<u>414,970</u>	<u>2,719,379</u>	<u>292,731</u>	<u>96,188</u>	<u>-</u>	<u>-</u>	<u>2,360,889</u>	<u>73,252</u>	<u>436,145</u>	<u>19,577,571</u>
Expenditures by account:														
Salaries and wages:														
Regular	4,898,014	2,062,462	157,564	387	193,796	986,449	201,025	-	-	-	1,381,484	-	17,046	9,898,227
Overtime	57	64,739	5,980	-	3,085	-	-	-	-	-	56,500	-	9,074	139,435
Fringe benefits	1,130,264	399,076	41,068	188	29,362	254,940	43,695	-	-	-	325,973	-	5,624	2,230,190
Travel and transportation	24,959	89,833	-	-	68,923	82,507	-	-	-	-	142,779	21,678	25,513	456,192
Communications	5,302	21,215	4,234	-	2,880	67,597	1,436	-	-	-	12,486	1,823	1,102	118,075
Dues, membership, and subscriptions	100	4,356	-	-	5,400	-	-	-	-	-	-	-	-	9,856
Food stuffs	256,772	92,696	-	-	15,116	181,230	-	-	-	-	3,549	12,670	9,767	571,800
Freight and port charges	2,520	7,109	-	-	184	728	129	-	-	-	-	-	-	10,670
Non-capitalized equipment and furnitures	(605)	31,410	-	-	5,234	10,685	990	-	-	-	11,414	-	640	59,768
Capital outlays	75,400	22,275	-	1,005	-	103,641	-	-	-	-	34,601	65,771	7,155	309,848
Office supplies and materials	67,561	131,783	3,494	633	21,106	101,228	24,488	-	-	-	174,354	18,482	4,218	547,347
Books and instructional supplies	273,579	-	-	-	-	245,422	-	-	-	-	4,408	-	-	523,409
POL	64,353	18,050	1,073	800	2,590	57,431	2,516	-	-	-	43,778	3,131	1,148	194,870
Printing and reproduction	550	13,456	157	-	1,290	796	-	-	-	-	4,612	1,975	-	22,836
Rental services	-	6,045	-	-	34	4,570	-	-	-	-	16,200	7,815	-	34,664
Repairs and maintenance	26,735	1,416	417	-	386	38,695	4,324	-	-	-	9,068	-	1,318	82,359
Utilities	166,563	823,450	5,811	-	12,500	34,317	3,000	-	-	-	25,694	2,750	4,423	1,078,508
Subsidies and contributions	68,250	-	-	-	-	600	-	-	-	-	-	-	-	68,850
Medical referrals	-	249,275	-	-	-	-	-	-	-	-	-	-	-	249,275
Medical supplies	-	1,145,818	-	-	-	-	-	-	-	-	14,129	-	-	1,159,947
Contractual services	42,000	169,872	130,267	-	52,974	211,203	-	96,188	-	-	64,070	64,227	130,000	960,801
Scholarships and allowances	252,303	-	-	-	-	96,295	-	-	-	-	-	-	-	348,598
Housing allowance	-	87,100	-	-	-	23,237	6,000	-	-	-	15,000	-	-	131,247
Meeting allowance	340	260	560	-	-	-	-	-	-	-	10,000	515	-	11,675
Non-payroll compensation	-	7,570	-	-	-	218,604	-	-	-	-	5,900	9,298	-	241,372
Miscellaneous goods and services	-	-	-	-	110	-	-	-	-	-	4,890	13,985	219,117	238,102
Bank charges	-	-	-	-	-	-	4,332	-	-	-	-	-	-	4,332
Total expenditures	<u>7,355,017</u>	<u>5,449,176</u>	<u>350,625</u>	<u>3,013</u>	<u>414,970</u>	<u>2,719,379</u>	<u>292,731</u>	<u>96,188</u>	<u>-</u>	<u>-</u>	<u>2,360,889</u>	<u>224,120</u>	<u>436,145</u>	<u>19,702,253</u>
Excess (deficiency) of revenues over (under) expenditures	-	-	26,186	-	-	-	-	-	-	-	-	(150,868)	-	(124,682)
Other financing sources:														
Operating transfers in	-	-	-	-	-	-	-	-	-	-	-	261,468	-	261,468
Net change in fund balances (deficit)	<u>-</u>	<u>-</u>	<u>26,186</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>110,600</u>	<u>-</u>	<u>136,786</u>
Fund balances (deficit) at the beginning of the year	<u>7,116</u>	<u>4,787</u>	<u>(26,186)</u>	<u>537</u>	<u>1,184</u>	<u>7,493</u>	<u>-</u>	<u>18,969</u>	<u>44,188</u>	<u>35,588</u>	<u>-</u>	<u>(110,600)</u>	<u>-</u>	<u>(16,924)</u>
Fund balances at the end of the year	<u>\$ 7,116</u>	<u>\$ 4,787</u>	<u>\$ -</u>	<u>\$ 537</u>	<u>\$ 1,184</u>	<u>\$ 7,493</u>	<u>\$ -</u>	<u>\$ 18,969</u>	<u>\$ 44,188</u>	<u>\$ 35,588</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 119,862</u>

See Accompanying Independent Auditors' Report.

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

Honorable John Ehsa
Governor, the State of Pohnpei
Federated States of Micronesia:

We have audited, in accordance with the 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, the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the State of Pohnpei's basic financial statements, and have issued our report thereon dated June 29, 2014. Our report includes a reference to other auditors. Other auditors audited the financial statements of the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation, as described in our report on the State of Pohnpei's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those other auditors.

For purposes of this report, our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants, and other matters did not include the Pohnpei Utilities Corporation, the Pohnpei Port Authority, and the Pohnpei State Housing Authority, which were all audited by us. We have issued separate reports on our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters for these entities. Other auditors issued separate reports on their consideration of internal control over financial reporting and their tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters for the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation. The findings, if any, included in those reports are not included herein.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the State of Pohnpei's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State of Pohnpei's internal control. Accordingly, we do not express an opinion on the effectiveness of the State of Pohnpei's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Questioned Costs as items 2013-001, 2013-002 and 2013-005, which we consider to be significant deficiencies.

Compliance and Other Matters

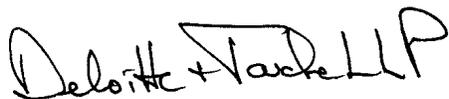
As part of obtaining reasonable assurance about whether the State of Pohnpei's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and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

The State of Pohnpei's Response to Findings

The State of Pohnpei's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. The State of Pohnpei's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



June 29, 2014

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM; REPORT ON INTERNAL CONTROL OVER COMPLIANCE; AND REPORT ON SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS REQUIRED BY OMB CIRCULAR A-133

Honorable John Ehsa
Governor, the State of Pohnpei
Federated States of Micronesia:

Report on Compliance for Each Major Federal Program

We have audited the State of Pohnpei's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the State of Pohnpei's major federal programs for the year ended September 30, 2013. The State of Pohnpei's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs.

As discussed in Note 2B to the Schedule of Expenditures of Federal Awards, the State of Pohnpei's basic financial statements include the operations of certain entities whose federal awards are not included in the Schedule of Expenditures of Federal Awards for the year ended September 30, 2013. Our audit, described below, did not include the operations of the entities identified in Note 2B as these entities conducted separate audits in accordance with OMB Circular A-133, if required.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the State of Pohnpei's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of Pohnpei's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the State of Pohnpei's compliance.

Basis for Qualified Opinion on CFDA 15.875 Compact Sector Grants

As described in the accompanying Schedule of Findings and Questioned Costs, the State of Pohnpei did not comply with requirements regarding CFDA 15.875 Economic, Social and Political Development of the Territories – Compact Sector Grants as described in item 2013-003 for Procurement and Suspension and Debarment. Compliance with such requirements is necessary, in our opinion, for the State of Pohnpei to comply with the requirements applicable to that program.

Qualified Opinion on CFDA 15.875 Compact Sector Grants

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the State of Pohnpei complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on CFDA 15.875 Economic, Social and Political Development of the Territories – Compact Sector Grants for the year ended September 30, 2013.

Unmodified Opinion on Each of the Other Major Federal Programs

In our opinion, the State of Pohnpei complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its other major federal programs identified in the summary of auditors’ results section of the accompanying Schedule of Findings and Questioned Costs for the year ended September 30, 2013.

Other Matters

The results of our auditing procedures disclosed other instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items 2013-001, 2013-002 and 2013-004 regarding the following:

<u>Finding #</u>	<u>CFDA #</u>	<u>Compliance Requirement</u>
2013-001	15.875	Equipment and Real Property Management
2013-002	15.875	Allowable Costs/Cost Principles
2013-004	15.875	Period of Availability of Federal Funds

Our opinion on each major federal program is not modified with respect to these matters.

The State of Pohnpei’s responses to the noncompliance findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. The State of Pohnpei’s responses were not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the responses.

Report on Internal Control Over Compliance

Management of the State of Pohnpei is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the State of Pohnpei’s internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the State of Pohnpei’s internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item 2013-003 to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned costs as items 2013-001, 2013-002 and 2013-004 to be significant deficiencies.

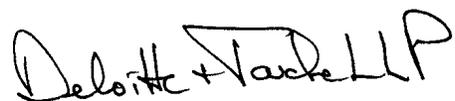
The State of Pohnpei's responses to the internal control over compliance findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. The State of Pohnpei's responses were not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the responses.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by OMB A-133

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the State of Pohnpei's basic financial statements. We issued our report thereon dated June 29, 2014, which contained unmodified opinions on those financial statements and which report included a reference to other auditors. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. We did not audit the financial statements of the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation which represent 3%, 0.1% and 3%, respectively, of the assets, net position, and revenues of the State of Pohnpei's discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation, is based solely on the reports of the other auditors. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements.

The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

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

June 29, 2014

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Expenditures of Federal Awards, by Grantor
Year Ended September 30, 2013

Agency/Program	Expenditures
U.S. Department of Agriculture	\$ 27,698
U.S. Department of the Interior	16,868,705
U.S. Department of Education	1,043,327
U.S. Department of Homeland Security	-
U.S. Department of Health and Human Services	1,125,317
GRAND TOTAL	\$ 19,065,047

Note: All awards are received in a subgrantee capacity through the FSM National Government, except for the following, which are received directly from the grantor agency:

Direct from the U.S. Department of Health and Human Services:

Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, Public Housing Primary Care and School Based Health Centers)

93.224 \$ 309,642

Reconciliation to the basic financial statements:

Other Nonmajor Funds	\$ 1,687,311
Grants Assistance Fund	19,702,253
Less:	
Non-U.S. Grants	(224,120)
CFSM Grants	(436,145)
Non-federal	(1,664,252)
	\$ 19,065,047

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2013

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF AGRICULTURE		
Cooperative Forestry Assistance	10.664	\$ 27,698
Community Facilities Loans and Grants	10.766	<u>-</u>
U.S. DEPARTMENT OF AGRICULTURE TOTAL		<u>\$ 27,698</u>
U.S. DEPARTMENT OF THE INTERIOR		
Economic, Social and Political Development of the Territories:	15.875	
Compact of Free Association Sector Grants:		
Compact II Education Sector		\$ 7,355,017
Compact II Health Sector		5,449,176
Compact II Capacity Building Sector		414,970
Compact II Environment Sector		350,625
Compact II Private Sector		3,013
Compact II Supplemental Education		2,719,379
Compact II ERA		292,731
Compact II Infrastructure Fund		96,188
Compact II Infrastructure Maintenance		23,059
Section 221b Special Block Grant		-
Technical Assistance:		
Survey and Mapping		-
Historic Preservation Fund Grants-In-Aid	15.904	<u>164,547</u>
U.S. DEPARTMENT OF THE INTERIOR TOTAL		<u>\$ 16,868,705</u>
U.S. DEPARTMENT OF EDUCATION		
Special Education - Grants to States	84.027	<u>\$ 1,043,327</u>
U.S. DEPARTMENT OF EDUCATION TOTAL		<u>\$ 1,043,327</u>
U.S. DEPARTMENT OF HOMELAND SECURITY		
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	<u>\$ -</u>
U.S. DEPARTMENT OF HOMELAND SECURITY		<u>\$ -</u>

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2013

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES		
Affordable Care Act (ACA) Personal Responsibility Education Program	93.092	\$ 29,445
Project Grants and Cooperative Agreements for Tuberculosis		
Control Programs	93.116	49,523
Technical and Non-Financial Assistance to Health Centers	93.129	8,634
Family Planning - Services	93.217	64,190
Consolidated Health Centers	93.224	309,642
Affordable Care Act (ACA) Abstinence Education Program	93.235	32,000
Substance Abuse and Mental Health Services - Projects of Regional and National Significance	93.243	97,738
Universal Newborn Hearing Screening	93.251	-
Immunization Cooperative Agreements	93.268	130,229
CDC & Prevention-Investigations and Technical Assistance	93.283	79,078
ACA Coordinated Chronic Disease prevention and Health Promotion Program	93.544	9,685
ARRA Grants to Health Center Programs	93.703	20
HIV Care Formula Grants	93.917	2,392
HIV Prevention Activities-Health Department Based	93.940	89,999
HIV/AIDS Surveillance	93.944	-
Block Grants for Prevention and Treatment of Substance Abuse	93.959	94,866
Preventive Health Services - Sexually Transmitted Diseases Control Grants	93.977	9,355
Cooperative Agreements for State-Based Diabetes Control Programs and Evaluation of Surveillance Systems	93.988	12,087
Preventive Health and Health Services Block Grant	93.991	1,134
Maternal and Child Health Services Block Grant to the States	93.994	81,763
CCPI Cancer Program	93.UNKNOWN	17,917
Center for Excellence	93.UNKNOWN	5,620
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES TOTAL		\$ <u>1,125,317</u>
TOTAL FEDERAL AWARDS		\$ <u>19,065,047</u>

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2013

1. Scope

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

• Programs Subject to Single Audit

The Schedule of Expenditures of Federal Awards presents federal programs related to the following agencies:

- U.S. Department of Agriculture
- U.S. Department of Education
- U.S. Department of Health and Human Services
- U.S. Department of Homeland Security
- U.S. Department of the Interior

2. Summary of Significant Accounting Policies

A. Basis of Accounting

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

B. Reporting Entity

For purposes of complying with The Single Audit Act of 1984, as amended in 1996, the State of Pohnpei's reporting entity is defined in Note 1A to its September 30, 2013 basic financial statements; and all of the discretely presented component units are excluded. Accordingly, the accompanying Schedule of Expenditures of Federal Awards presents the federal award programs administered by the State of Pohnpei, as defined above, for the year ended September 30, 2013.

C. Subgrantees

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

D. Indirect Cost Allocation

The State of Pohnpei did not receive any indirect cost allocation and did not charge indirect costs against federal programs.

E. CFDA #15.875

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs
Year Ended September 30, 2013

Section I - Summary of Auditors' Results

Financial Statements

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

Federal Awards

Internal control over major programs:

- | | |
|---|------------|
| 5. Material weakness(es) identified? | Yes |
| 6. Significant deficiency(ies) identified? | Yes |
| 7. Type of auditors' report issued on compliance for major programs: | |
| CFDA Program 15.875 | Qualified |
| CFDA Program 84.027 | Unmodified |
| 8. Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? | Yes |

9. Identification of major programs:

<u>CFDA Numbers</u>	<u>Name of Federal Program or Cluster</u>
15.875	Economic, Social and Political Development of the Territories – Compact of Free Association Compact Sector Grants
84.027	Special Education – Grants to States

- | | |
|--|-----------|
| 10. Dollar threshold used to distinguish between Type A and Type B Programs: | \$571,951 |
| 11. Auditee qualified as low-risk auditee? | Yes |

Section II – Financial Statements Findings

<u>Finding #</u>	<u>Finding</u>
2013-001	Equipment and Real Property Management
2013-002	Allowable Costs/Cost Principles
2013-005	Cash and Equivalent

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2013

Section III - Federal Award Findings and Questioned Costs

<u>Finding #</u>	<u>CFDA #</u>	<u>Finding</u>	<u>Questioned Costs</u>
2013-001	15.875	Equipment and Real Property Management	\$ -
2013-002	15.875	Allowable Costs/Cost Principles	54,887
2013-003	15.875	Procurement and Suspension and Debarment	25,701
2013-004	15.875	Period of Availability of Federal Funds	<u>41,094</u>
			\$ <u>121,682</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2013

Finding No.: 2013-001
Federal Agency: U.S. Department of the Interior
CFDA Program: 15.875 Economic, Social and Political Development of the Territories
Grant Number: Compact Sector Grants
Requirement: Equipment and Real Property Management
Questioned Cost: \$0

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

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

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

Effect: The expected life of fixed assets may be lessened. However, no questioned costs result from this finding as no specific instances came to our attention in fiscal year 2013 of unnecessary expenditures that occurred due to this condition.

Prior Year Status: Noncompliance with maintenance of fixed assets was reported in prior Single Audits as items 2007-4, 2008-2, 2009-1, 2010-1, 2011-1, and 2012-1.

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

Auditee Response and Corrective Action Plan: We concur with the finding. We have implemented in FY2013 a maintenance plan schedule for each vehicle in all departments who are primary recipients of the Sector funds. In addition, the Department of Health and Services has their own maintenance plan for their medical equipment available for inspection. Similar with previous years, the Department of Treasury and Administration (DOTA) has an existing documentation of a maintenance plan for the procurement of a new fixed asset and the said plan is attached to every purchase requisition. We shall ensure that a quarterly maintenance schedule from each department is submitted to DOTA.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2013

Finding No.: 2013-002
 Federal Agency: U.S. Department of the Interior
 CFDA Program: 15.875 Compact of Free Association, Compact Sector Grants
 Requirement: Allowable Costs/Cost Principles
 Questioned Costs: \$ 54,887

Criteria: In accordance with applicable allowable costs/cost principles, expenditures should be necessary and reasonable for program needs and should be in accordance with program requirements. Furthermore, financial and programmatic records should be maintained on file for at least three years.

In accordance with applicable procurement requirements, procurements shall provide full and open competition among vendors, and allowable exceptions should be approved and documented in procurement files.

Condition: For 11 (or 29%) of 38 transactions tested, there was either partial or no financial and/or programmatic records (i.e., contracts, receiving reports, invoices, boarding passes, trip reports, etc.) on file to substantiate certain transactions as follows:

<u>Sel no.</u>	<u>Fund</u>	<u>Prog</u>	<u>YR</u>	<u>REF1</u>	<u>TRN_NO</u>	<u>AMT</u>	<u>Amount</u>
2	10	10100	13	121507	157175	1,103	\$ 1,103
7	10	10300	13	112141	143027	5,990	5,990
10	11	11100	13	V130020	139720	7,417	7,417
11	11	11110	13	108968	138206	3,000	3,000
17	11	11515	12	97575	137252	17,680	17,680
18	11	11515	13	111442		5,275	5,275
24	13	13960	12	108244		801	801
27	14	14141	13	120149	155098	4,000	4,000
35							1,275
36	16	16100	13	V130173	153777	1,713	1,713
38	19	19500	11	109302	138644	6,633	<u>6,633</u>
Questioned costs presented							<u>\$54,887</u>

Cause: The cause of the condition appears to be due to the process of maintaining documentation in disparate locales and a lack of documentation on file.

Effect: The effect of this condition is questioned costs and potential noncompliance with the criteria.

Recommendation: We recommend that necessary communications and documentation in support of the above be retained in file.

Auditee Response and Corrective Action Plan: We concur with the entire finding. We will ensure that the above questioned costs are resolved in fiscal year 2014.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2013

Finding No.: 2013-003
 Federal Agency: U.S. Department of the Interior
 CFDA Program: 15.875 Compact of Free Association, Compact Sector Grants
 Requirement: Procurement and Suspension and Debarment
 Questioned Costs: \$ 25,701

Criteria: In accordance with applicable allowable costs/cost principles, expenditures should be necessary and reasonable for program needs and should be in accordance with program requirements. Furthermore, financial and programmatic records should be maintained on file for at least three years.

In accordance with applicable procurement requirements, procurements shall provide full and open competition among vendors, and allowable exceptions should be approved and documented in procurement files.

Condition: For 10 (or 26%) of 38 transactions tested for the Compact Sector Programs, there was either insufficient documentation or none was provided to support competitive procurement requirements.

<u>Sel no.</u>	<u>Fund</u>	<u>Prog</u>	<u>YR</u>	<u>REF1</u>	<u>TRN_NO</u>	<u>AMT</u>	<u>Amount</u>
7	10	10300	13	112141	143027	5,990	\$ 5,990
12	11	11250	13	116855	150827	8,580	8,580
14	11	11350	13	108507	137561	15,546	15,546
17	11	11515	12	97575	137252	17,680	17,680
18	11	11515	13	111442		5,275	5,275
23	12	12910	13	115800		1,575	1,575
24	13	13960	12	108244		801	801
27	14	14141	13	120149	155098	4,000	4,000
35							1,275
36	16	16100	13	V130173	153777	1,713	<u>1,713</u>
							62,435
							Less costs already questioned under 2013-002
							(36,734)
							Questioned costs presented
							<u>\$25,701</u>

Cause: The cause of the condition appears to be due to the process of maintaining documentation in disparate locales and a lack of documentation on file.

Effect: The effect of this condition is questioned costs and potential noncompliance with the criteria.

Recommendation: We recommend that necessary communications and documentation in support of the above be retained in file.

Auditee Response and Corrective Action Plan: We concur with the entire finding. We will ensure that the above questioned costs are resolved in fiscal year 2014.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2013

Finding No: 2013-004
Federal Agency: U.S. Department of the Interior
CFDA Program: 15.875 Economic, Social and Political Development of the Territories
Requirement: Period of Availability of Federal Funds
Questioned Costs: \$41,094

Criteria: The Government of the States of Pohnpei shall liquidate all obligations incurred under a grant not later than ninety days after the end of the funding period or as otherwise mutually agreed.

Condition: Expenditures were recorded in FY2013 for the funding period 2007, 2008, 2009, 2010, 2011, and 2012 Compact Sector Grants and were liquidated after the period of availability specified in the related grant award, as follows:

<u>Program Account</u>	<u>Amount outside POA</u>
Various Compact Sector Funds	\$41,094

Cause: There appears to be a lack of monitoring over compliance with period of availability requirements.

Effect: Questioned costs result from this noncompliance.

Recommendation: The Pohnpei State Government should timely monitor compliance with period of availability requirements.

Auditee Response and Corrective Action Plan: We concur with the finding. The Department is cognizant of the period of availability of federal funds. From the given list above, obviously, we need to strictly monitor the recording of transactions to appropriate fund year.

We believe we need to explain what happened to the \$54,888 above. Per our record, it was \$54,988.

The \$54,988 was an adjustment made in August 1, 2013 instead of recording as of 2/28/2013, closing date for liquidating FY12 Sector. This negative balance was a result from a prior wrong accounting adjustment posted.

To correct the negative balance, we proposed an accounting adjustment to transfer the negative salary expense account from FY12 to FY13 (these are year classification only posted within the current year under audit). After this adjustment, the salary expense for this fund (FY12) dropped to zero while the FY13 salary expense account went up by \$54,988 which corrected the FY13 salary expense account. In other words, this accounting adjustment was prepared in order to correct the year classification of the salary. Overall, whether the \$54,988 was adjustment or not, there is no effect on the bottom line of the salary expenditure for the year FY2013.

For its corrective action plan, we shall work with the Sector agency to resolve the issue and present the outcome to Deloitte in July 2014. In addition, the Division of Finance shall strictly monitor the period of availability requirements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2013

Finding No: 2013-005
Area: Cash and Equivalents

Criteria: Reconciling all bank accounts to the general ledger on a regular basis is fundamental and critical for maintaining accurate financial records and helping to avoid misappropriation of funds or fraudulent activities.

Condition: Bank accounts contained material variances that are not consistently reconciled on a timely basis.

1. Pohnpei State has not reconciled certain general ledger cash accounts to the adjusted bank balances as of September 30, 2013. This condition results in a misstatement of the financial statements.

<u>Bank Account:</u>	<u>Amount</u>
Small Business Dev Center	\$14,589
CIB Payroll	1,661
CIB General Fund	912
CIB Sector Grants	<u>200</u>
	<u>\$17,362</u>

2. We found no evidence of review of the outstanding check list for stale dated checks for all checking accounts maintained by Pohnpei State Division of Finance.
3. During tests of cash, State Finance was not able to provide bank reconciliations for the Honolulu Medical Imprest Account.

Cause: The cause of this condition is internal control weaknesses over the cash bank reconciliation cycle.

Effect: The effect of these conditions is potential misstatements of the financial statements. In addition, failure to clear items on a timely basis results in misstatements of cash in the financial statements and creates an opportunity to manipulate cash.

Recommendation: We recommend that the Division of Finance ensure that bank reconciliations are performed timely and all misstatements corrected.

Auditee Response and Corrective Action Plan: We believe that if there was a misstatement of the financial statements, it would just be \$2,773 (Payroll, General and Sector). The Small Business Dev Center Account of \$14,589 balance has been in our general ledger cash accounts since FY2010 and was never brought to our attention.

Bank reconciliation is performed monthly as soon as bank statements are received. However, due to late bank statements and staff transition in the Department, the general ledger cash balance used for the bank reconciliation together with the outstanding checks was not updated promptly when checks are cancelled. For instance, checks cancelled or voided to date (if the check was dated FY2013) would change the general ledger cash as of 9/30/13. As a result, if the bank reconciliation is not promptly adjusted in September 2013, this will result to the difference as shown above. Thus, we believe this would not result to misstatement of the financial statements because adjustment of the bank reconciliation in 9/30/13 would be: the amount of the outstanding checks.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2013

Finding No: 2013-005, Continued
Area: Cash and Equivalents

Auditee Response and Corrective Action Plan, Continued:

For our corrective action plan, the Finance Division shall ensure the prior bank reconciliation is promptly updated to reflect changes e.g. cancellation or voiding of checks performed in the current period.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Prior Audit Findings and Questioned Costs
Year Ended September 30, 2013

The status of unresolved prior year audit findings is disclosed within the Schedule of Findings and Questioned Cost section of this report (pages 70 through 77).

Questioned Costs FY 2013 \$ 121,682