

**YAP STATE PUBLIC SERVICE CORPORATION,  
A COMPONENT UNIT OF THE STATE OF YAP**

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**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT**

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**SEPTEMBER 30, 2013 AND 2012**

## **INDEPENDENT AUDITORS' REPORT**

The Board of Directors  
Yap State Public Service Corporation:

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Yap State Public Service Corporation (YSPSC), a component unit of the State of Yap, which comprise the statements of net position as of September 30, 2013 and 2012, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

### **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 an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and 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 opinion.

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Yap State Public Service Corporation as of September 30, 2013 and 2012, and the changes in its net position and its cash flows, for the years 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 to 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. 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 Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated June 18, 2014 on our consideration of the YSPSC'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 YSPSC's internal control over financial reporting and compliance.

*Deloitte & Touche LLP*

June 18, 2014

**YAP STATE PUBLIC SERVICE CORPORATION**  
**(A COMPONENT UNIT OF THE STATE OF YAP)**

Management's Discussion and Analysis  
Years Ended September 30, 2013 and 2012

The following Management's Discussion and Analysis is required by Statement No. 34 issued by the U.S. Governmental Accounting Standards Board (GASB). Its objective is to provide the reader with an introduction and overview of the financial statements of the Yap State Public Service Corporation (YSPSC) for the years ended September 30, 2013 and 2012. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes thereto which follow this section.

GASB Statement No. 34 requires that published financial statements must contain a management discussion and analysis. This section of the YSPSC's annual report presents our discussion of YSPSC's performance for the years ended September 30, 2013 and 2012.

The following table summarizes the financial condition and results of operations of YSPSC as of 2013, 2012 and 2011.

	<u>2013</u>	<u>2012</u>	<u>2011</u>
<b>ASSETS</b>			
Plant in Service, net	\$ 7,830,122	\$ 7,895,778	\$ 7,880,872
Work in progress	1,048,391	116,519	485,383
Current and other assets	3,456,011	3,751,940	3,174,010
Total assets	<u>\$ 12,334,524</u>	<u>\$ 11,764,237</u>	<u>\$ 11,540,265</u>
<b>NET POSITION AND LIABILITIES</b>			
Net position:			
Net investment in capital assets	\$ 6,277,955	\$ 5,013,820	\$ 5,638,236
Restricted	1,698,928	1,931,051	1,168,832
Unrestricted	608,062	(405,911)	(618,993)
Total net position	<u>8,584,945</u>	<u>6,538,960</u>	<u>6,188,075</u>
Liabilities:			
Notes payable, net of current portion	2,555,141	4,017,176	4,252,381
Current portion of notes payable	45,417	320,526	284,421
Other current liabilities	1,149,021	887,575	815,388
Total liabilities	<u>3,749,579</u>	<u>5,225,277</u>	<u>5,352,190</u>
Total net position and liabilities	<u>\$ 12,334,524</u>	<u>\$ 11,764,237</u>	<u>\$ 11,540,265</u>
<b>REVENUES, EXPENSES, AND CHANGES IN NET POSITION</b>			
Operating revenues	\$ 6,291,565	\$ 6,063,666	\$ 5,682,964
Operating expenses	6,539,253	6,789,033	6,172,497
Loss from operations	<u>(247,688)</u>	<u>(725,367)</u>	<u>(489,533)</u>

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	<u>2013</u>	<u>2012</u>	<u>2011</u>
Grants	2,113,081	725,775	709,686
Interest expense	(1,693)	(17,724)	(16,109)
Interest income	2,224	7,037	1,322
Training expense	(241,385)	(365,136)	(384,713)
Other grant expense	(164,831)	(165,269)	--
Gain (loss) on disposal of utility plant	(28,014)	--	--
Foreign exchange loss	(14,630)	(5,781)	(3,627)
Other income/(expenses)	10,490	14,129	(24,327)
Net income (loss)	<u>1,427,554</u>	<u>(532,336)</u>	<u>(207,301)</u>
Capital contributions	<u>618,431</u>	<u>883,221</u>	<u>1,168,832</u>
Change in net position	2,045,985	350,885	961,531
Net position, beginning	<u>6,538,960</u>	<u>6,188,075</u>	<u>5,226,544</u>
Net position, ending	<u>\$ 8,584,945</u>	<u>\$ 6,538,960</u>	<u>\$ 6,188,075</u>

## FINANCIAL OPERATIONS OVERVIEW

Fiscal year 2013 was another lackluster year for the Yap State Public Service Corporation in terms of financial results. Despite its efforts to contain costs and renewed efforts in 2013 to improve collections, the Corporation still ended the year with an operating loss of \$247,688. It had been the hope that with the more stable fuel prices in 2013, financial results for the Corporation would improve. But, the continued shrinkage of its electric customer base and the increased costs of supplies prevented the YSPSC from breaking even.

The YSPSC's financial difficulties were alleviated by the cash infusion from its renewable energy grants and were also mitigated by the Yap State Legislature's forgiveness of two loans owed by the YSPSC to the Yap State Government which combined principal totaled \$1,672,192. The capital contribution from the European Union renewable energy grants and the action of the Yap State Legislature to forgive YSPSC's loans resulted in a change in net position for the year of \$2 million, bringing the Corporation's net position to \$8.6 million at the end of fiscal year 2013.

### Results of Operations

*Operating Loss* – The operating loss for fiscal year 2013 of \$247,688 represents an improvement of 66% over fiscal year 2012. For fiscal year 2012, the disparity between utility revenue collected from customers and the actual paid by the YSPSC to its suppliers resulted in the operating loss of \$725,367, an increase of 48% over the operating loss for fiscal year 2011.

*Electric Revenue:* The fiscal year 2013 electricity revenue of \$5,796,010 represents a modest increase of 3% over fiscal year 2012. The slight increase is attributable to efforts to collect on past due accounts. However, much like 2012, actual electric revenue earned is approximately \$421,000 less than tariff projections due to lower consumption by customers.

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**Kilowatt Hours Billed:** Electricity consumption remained flat in 2013 compared with 2012. While the government class showed a slight increase in consumption of 10% in FY13, the commercial and residential consumption showed declines of 2% and 3%, respectively. The 9.8 million kilowatt hours billed in 2013 is only slightly higher than the 9.7 million kilowatt hours billed for 2012.

**Water Revenue:** Water revenue of \$495,555 is about the same as the \$496,224 for 2012, but gallons billed dropped to 86.1 million down from 90.5 million gallons in 2012. In the previous year, water consumption increased slightly to 90.5 million gallons from 89.2 million in 2011, but revenue decreased by 12%. The disparity between collections and gallons billed is attributable to timing differences.

**Production Fuel:** The YSPSC expended \$97,903 less for fuel in 2013 as compared to 2012 and \$372,071 more in 2012 than in 2011. The price per gallon of fuel reached \$5.036 in April 2012 but began to subside in the subsequent months. Consequently, the average monthly fuel price paid by the YSPSC in 2013 was \$4.73 compared to \$4.77 in 2012, and \$4.468 in 2011. Production fuel expense of \$4,542,079 and \$4,639,982 comprised 69% of total operating expenses of \$6,539,253 and \$6,789,033 for 2013 and 2012, respectively.

**Other Operating Expenses** – Other operating expenses declined 6% in 2013 as compared to 2012. In contrast, other operating expenses increased by \$150,000 in 2012 as compared to 2011. The 16% increase in salaries and wages in 2013 is due to a larger portion of Power Distribution crew salary which was transferred to operating funds after the completion of their DOI funded training programs. The 85% decrease in other production costs is due to the capitalization of much of the overhaul costs of the generator incurred during fiscal year 2013.

**Significant Changes to Net Position**

**Cash** – Ending cash at September 30, 2013 of \$1.2 million was 15% less than at fiscal year 2012 of \$1.4 million. Cash available at year-end consisted primarily of grant proceeds, specifically from the European Union for the EFII project. Even though a new electric tariff was adopted in February 2012, the budget restrictions imposed by JEMCO on the use of Compact Sector grant to cover utility payments prompted the State Government to restrict its use of electricity thereby reducing its consumption by 12% over 2011. Consequently, electric revenue for fiscal year 2012 fell \$421,000 short of projections.

**Receivables** – Efforts to step up collection of past due accounts resulted in a 6% decrease in customer receivables at September 30, 2013 as compared to 2012. In fiscal year 2012, customer receivables had increased 35% to \$1,196,563 as compared to fiscal year 2011. The increase was the result of revisions to YSPSC's disconnection policy after it was brought to management's attention that customers should be disconnected only after 90 days of delinquency, instead of the 60 days that had been the practice.

**Long-term Debt** – At September 30, 2012, YSPSC owed a combined total of \$4,337,702 for four loans of which \$320,526 was current. During 2013, the Yap State Legislature passed Bill No. 8-126 which became Law No. 8-47 on August 20, 2013 to forgive the two loans YSPSC owed to the Yap State Government with combined outstanding principals of \$1,672,192. The amount forgiven is recorded as a grant from the Yap State Government in the accompanying financial statements. The loan from the U.S. Rural Housing Authority matured in September 30, 2013. Consequently, at September 30, 2013, YSPSC's long term debt had dropped to \$2,600,558 of which \$45,417 was current. For additional information on YSPSC's financing activities, see note 5 to the financial statements.

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*Current Liabilities* – Total current liabilities decreased 1% in 2013 as compared to 2012. In particular, accounts payable in the amount of \$530,029 represents 44% of current liabilities at September 30, 2013, \$337,000 of which was for fuel. Accounts payable increased 28% in 2013 as compared to 2012. The increase from 2011 to 2012 was 78%. The lack of working capital in 2013 and 2012 necessitated that only the most pressing bills were paid each month.

*Capital Projects* – Due to financial constraints, YSPSC did not undertake any capital projects in 2013 and 2012 other than the ongoing renewable energy project funded by the European Union and South Pacific Commission North Rep, the upgrade of the Utility Billing System. \$618,431 was recorded in 2013 as capital contributions from the European Union Energy Facility Grant for solar projects in the outer islands. See note 4 to the financial statements for additional information regarding movements in capital assets.

**U.S. Federal, Local and Other Grants**

*Pacific Linemen Training Program* – YSPSC took over administration of the training program from the American Samoa Power Authority (ASPA) with the revision of the program in 2007 to segregate training for Micronesian linemen from those of American Samoa. Funded by the U.S. Department of the Interior Office of Insular Affairs Operations and Maintenance Improvement Program (OMIP) funds, with matching share by participating utilities, the continuing program aims to train professional linemen for the Micronesian island utilities; specifically, Guam Power Authority, Palau Public Utility Corporation, Pohnpei Utilities Corporation, Commonwealth Utilities Corporation, and Yap Public Services Corporation. YSPSC received \$203,134 and \$331,438, respectively, in fiscal years 2013 and 2012 in cost reimbursements for the training program.

*CRISP Monitoring and Evaluation* – Due to its good track record in administering the various training programs funded by the U.S. Department of the Interior (DOI), DOI awarded YSPSC \$199,942 in 2011 to monitor and evaluate the Chuck Public Utilities Corporation's (CPUC) Capitalization, Recovery and Institutional Strengthening Project (CRISP). YSPSC received \$28,426 and \$83,737 in 2013 and 2012, respectively, for cost reimbursements for this program.

*Renewable Energy program (European Union EFII)* – As part of its ongoing renewable energy program, in 2011, YSPSC received \$33,562 from the French Embassy for solar systems training and \$1,168,832 from the European Union for the installation of solar systems in the neighboring islands. The European Union Energy Facility II grant project is worth approximately \$3.3 million and is designed to provide solar electricity to ten islands and atolls in the State of Yap, namely Ngulu, Falalus, Siliap, Tagailap and Wottegai in Woleai atoll, Eauripik, the two islands in the atoll of Faraulep (Falalop and Pigue) and finally Elato and Lamotrek. Yap State's required 25% matching share of \$843,750 was appropriated under YSL 8-3 and 8-9. The procurement process for the photovoltaic systems was begun in fiscal year 2012 with installations scheduled for fiscal year 2013. Expenditures for the EFII project of \$618,431 were recorded as capital contributions for the year ended September 30, 2013.

*Renewable Energy program (SPC North-Rep)* – In July 2012 YSPSC entered into a Memorandum of Agreement with the Secretariat of the Pacific Community (SPC) for joint activities aimed at the implementation of the North Pacific ACP Renewable Energy and Energy Efficiency Project (North Rep). The European Union is funding this program through the SPC North-Rep. Procurement and installation of the systems will be the responsibility of North-Rep with assistance provided by YSPSC as needed; however, upon commissioning, operation and maintenance of the systems will transfer to YSPSC.

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*ADB Loan for Small Generator and Yap Proper Renewable Energy Projects* – ADB has approved \$9 million in funding for Yap Proper Renewable Energy Development Project consisting of a wind farm which is expected to generate power equivalent to about 18% of the current delivered energy supply, grid-connected solar panels which will be installed on about 21 government buildings will produce energy equivalent to 4% and a new fuel-efficient diesel generator that will replace the existing equipment and is expected to reduce fuel consumption by 25%. A road to the wind mast site is in place and the wind mast has been installed. Technical engineers are expected to come in the early part of next year to advise on these projects.

*Woleai Cash Power* – Towards the end of fiscal year 2010, Yap State Public Services Corporation entered into a contract with the Yap State Government, to among other things, procure and install cash power meters in Falalop Woleai for \$79,012. In the middle of the fiscal year 2012, the Falalop Woleai Power System was converted or changed over to the Cash Power system. After the cash power meters arrived in Yap, transportation to the outer islands was arranged by the YSPSC main office for installation of the new cash-power meters and related training for YSPSC Woleai crew.

*Utility Billing System Upgrade* – In late fiscal year 2012, YSPSC purchased the upgraded version of its utility software to accommodate the integration of customers billing and payments with the general ledger in order to facilitate the maintenance, reporting and collection of customer accounts. The version of the Able Software previously in use did not allow integration with the general ledger, therefore, reconciliation with the general ledger was done manually. In August 2012, four employees traveled to San Diego, California to attend a training provided by Able Software for the new version of Utility STAR. The Billing Section became fully functional with the new utility billing system in December of 2012.

#### **HIGHLIGHTS FOR FISCAL YEAR 2014**

In the short-term the following projects will be the primary focus of activities for the Yap State Public Services Corporation:

*Billing Procedures* – With the continual decrease in electric consumption, there is a need to ensure that all customer billings are accurate and timely. Accordingly, management began in 2013 to review the application and billing process to ensure that accounts can be collected and to improve the accuracy of billings and detect and investigate anomalies in a timely manner.

*Pacific Linemen Training Program* – The highly successful training program to equip utility personnel with the basic skills necessary to ensure safety and successful operation and delivery of utility services will continue in 2014. Of the twelve YSPSC linemen, two are yet to be certified.

*European Union Energy Facility Grant* – \$1,168,832 was received from the European Commission for a budget of EUR2.5 million to fund solar photovoltaic systems for 10 targeted outer islands of Yap State. The grant required a match of 25% or approximately US\$843,750 which was appropriated by YSL 8-3 and 8-9. Purchase of the solar systems was completed in 2013 and installations began in the outer islands. It is estimated that by 2015, with the completion of EFII and similar projects, 100% of the Outer-islands' population of Yap State will be electrified with 100% renewable energy systems (14 islands with an approximate total population of 2,600 islanders.)

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Years Ended September 30, 2013 and 2012

*ADB Loan for Yap Energy Projects* – ADB has approved \$9 million in funding for Yap Proper Renewable Energy Development Project consisting of a wind farm which is expected to generate power equivalent to about 18% of the current delivered energy supply, grid-connected solar panels which will be installed on about 21 government buildings and is expected to produce energy equivalent to 4% and a new fuel-efficient diesel generator that will replace the existing equipment and should reduce production fuel consumption by 25%. A road to the wind mast site is in place and the wind mast has been installed. Technical engineers are supposed to come in the early part of 2014 to advise on these projects.

*Renewable Energy North Rep EDF10 Projects* – These are the solar systems for the islands of *Mogmog and Falalop Ulithi, Fais, Falalop Woleai and Satawal*. In Mogmog, a 47.88kwp solar system capacity was installed. The system will be enough for the entire island to be on solar power day and night without the generator. The system is in place with only minor wiring to be completed and it will be ready for commission very soon. This date has yet to be set as there are other issues related to structure designed in the proposal that need to be addressed before commissioning.

*PEC Fund* – PEC is a Japanese Grant to the FSM for solar systems. This grant is for 5 entities (the four states and the national government). Yap's share of the grant is approximately 200kwp capacities of solar PVs. The 200kwp panels will be installed on the YSPSC buildings. Assessment on the approximate area to be covered will be done toward the end of 2013 with installations to commence in the early part of 2014.

*World Bank* – World Bank has made available to the FSM a grant of U.S \$12 million to support the development of the energy sector in the FSM. At this time, the FSM national government is still in the discussion stages with the states and their priorities in their state energy plans. YSPSC at this time is in communication with the FSM national government on what projects are to be funded under the grant and addressing the technical issues with its consultants.

## **INFORMATION REQUESTS**

The management and staff of YSPSC will be pleased to answer any questions that may arise in relation to matters discussed in this report. Kindly refer your comments or questions to YSPSC at telephone no. (691) 350-4427, Colonia, Yap FM 96943.

The Management Discussion and Analysis for the years ended September 30, 2012 and 2011 is set forth in the report on the audit of YSPSC's financial statements which is dated June 29, 2013. That Discussion and Analysis explains in more detail major factors affecting the 2012 and 2011 financial statements.

**YAP STATE PUBLIC SERVICE CORPORATION**  
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Statements of Net Position  
September 30, 2013 and 2012

<u>ASSETS</u>	<u>2013</u>	<u>2012</u>
Non-current assets:		
Utility plant:		
Depreciable capital assets:		
Plant in service	\$ 21,420,636	\$ 20,850,094
Less accumulated depreciation	<u>(13,590,514)</u>	<u>(12,954,316)</u>
Depreciable utility plant, net	7,830,122	7,895,778
Non-depreciable capital assets:		
Work in progress	<u>1,048,391</u>	<u>116,519</u>
Utility plant, net	<u>8,878,513</u>	<u>8,012,297</u>
Current assets:		
Cash and cash equivalents	1,228,876	1,446,558
Accounts receivable and unbilled accrued revenue, net of an allowance for doubtful accounts	1,130,131	1,196,653
Other receivables	284,144	299,321
Inventory	791,085	777,846
Prepaid expenses	<u>21,775</u>	<u>31,562</u>
Total current assets	<u>3,456,011</u>	<u>3,751,940</u>
	<u>\$ 12,334,524</u>	<u>\$ 11,764,237</u>
 <u>NET POSITION AND LIABILITIES</u> 		
Net position (deficit):		
Net investment in capital assets	\$ 6,277,955	\$ 5,013,820
Restricted	1,698,928	1,931,051
Unrestricted	<u>608,062</u>	<u>(405,911)</u>
Total net assets	<u>8,584,945</u>	<u>6,538,960</u>
Contingencies		
Current liabilities:		
Current portion of notes payable	45,417	320,526
Accounts payable	530,029	414,486
Employees' annual leave and accrued payroll	82,864	83,969
Accrued taxes and other liabilities	1,260	5,260
Refunds payable to customers	181,368	181,368
Deferred revenue	180,431	55,340
Other payables and customer deposits	<u>173,069</u>	<u>147,152</u>
Total current liabilities	1,194,438	1,208,101
Notes payable, net of current portion	<u>2,555,141</u>	<u>4,017,176</u>
Total liabilities	<u>3,749,579</u>	<u>5,225,277</u>
	<u>\$ 12,334,524</u>	<u>\$ 11,764,237</u>

See accompanying notes to financial statements.

**YAP STATE PUBLIC SERVICE CORPORATION**  
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Statements of Revenues, Expenses and Changes in Net Position  
Years Ended September 30, 2013 and 2012

	2013	2012
Operating revenues:		
Electricity sales	\$ 5,796,010	\$ 5,651,175
Water sales and wastewater services	495,555	496,224
Total operating revenues	6,291,565	6,147,399
Less provision for uncollectible receivables	-	(83,733)
Net operating revenues	6,291,565	6,063,666
Operating expenses:		
Production fuel	4,542,079	4,639,982
Depreciation	851,561	747,591
Salaries and wages and related expenses	875,331	751,418
Administrative and general	240,744	292,709
Other production costs	29,538	357,333
Total operating expenses	6,539,253	6,789,033
Operating loss	(247,688)	(725,367)
Nonoperating income (loss):		
Interest income	2,224	7,037
Foreign exchange loss	(14,630)	(5,781)
Operating grants and subsidies	2,113,081	725,775
Interest expense	(1,693)	(17,724)
Training expense	(241,385)	(365,136)
Grant expenses	(164,831)	(165,269)
Other expenses	10,490	14,129
Loss on disposal of utility plant	(28,014)	-
Total nonoperating income, net	1,675,242	193,031
Net income (loss) before capital contributions	1,427,554	(532,336)
Capital contributions	618,431	883,221
Change in net position	2,045,985	350,885
Net position at beginning of year	6,538,960	6,188,075
Net position at end of year	\$ 8,584,945	\$ 6,538,960

See accompanying notes to financial statements.

**YAP STATE PUBLIC SERVICE CORPORATION**  
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Statements of Cash Flows  
Years Ended September 30, 2013 and 2012

	2013	2012
Cash flows from operating activities:		
Cash received from customers	\$ 6,399,181	\$ 5,808,838
Cash refunds paid to customers	-	(21,741)
Cash paid to suppliers	(4,704,270)	(4,995,495)
Cash paid to employees	(876,436)	(748,524)
Net cash provided by operating activities	818,475	43,078
Cash flows from investing activities:		
Interest and other income (loss)	(12,406)	1,256
Cash flows from noncapital financing activities:		
Proceeds from operating grants and subsidies	565,980	357,070
Other income	10,490	14,129
Expenses paid from operating grant proceeds	(406,216)	(530,405)
Net cash provided by (used in) noncapital financing activities	170,254	(159,206)
Cash flows from capital and related financing activities:		
Capital contributions	618,431	883,221
Acquisition of utility plant	(1,745,791)	(393,633)
Interest paid	(1,693)	(17,724)
Repayment of notes payable	(64,952)	(199,100)
Net cash (used in) provided by capital and related financing activities	(1,194,005)	272,764
Net change in cash and cash equivalents	(217,682)	157,892
Cash and cash equivalents at beginning of year	1,446,558	1,288,666
Cash and cash equivalents at end of year	\$ 1,228,876	\$ 1,446,558
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (247,688)	\$ (725,367)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	851,561	747,591
Provision for uncollectible receivables	-	83,733
Decrease (increase) in assets:		
Receivables	66,522	(330,837)
Inventory	(13,239)	93,358
Prepaid expenses	9,787	19,442
Other receivables	15,177	(11,189)
Increase (decrease) in liabilities:		
Accounts payable	115,543	181,729
Employees' annual leave and accrued payroll	(1,105)	(2,366)
Accrued taxes and other withholdings	(4,000)	5,260
Other payables and customer deposits	25,917	(18,276)
Net cash provided by operating activities	\$ 818,475	\$ 43,078

Non-cash financing activity:

In 2013, notes payable to Yap State of \$332,375 and \$1,339,225 were forgiven and recorded as operating grants and subsidies.

See accompanying notes to financial statements.

**YAP STATE PUBLIC SERVICE CORPORATION**  
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Notes to Financial Statements  
September 30, 2013 and 2012

(1) Organization and Summary of Significant Accounting Policies

Organization

Yap State Public Service Corporation (YSPSC) is a legally separate component unit of the Government of Yap State. YSPSC provides electrical, water and sewer services in the State of Yap. YSPSC commenced operations on April 1, 1996, with the assets and liabilities of the Division of Public Utilities of the Yap State Department of Public Utilities and Contracts transferred as of that date. YSPSC is governed by a seven member Board of Directors who are nominated by the Governor of Yap with the advice and consent of the Yap State Legislature.

Basis of Accounting

The accounting policies of YSPSC conform to accounting principles generally accepted in the United States of America as applicable to governmental entities, specifically proprietary funds. All proprietary funds are accounted for on a flow of economic resources measurement focus. The accrual basis of accounting is utilized by proprietary funds. Under this method of accounting, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Government Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Net Position

Net position represents the residual interest in YSPSC's assets and deferred outflows of resources after liabilities and deferred inflows of resources are deducted and consist of the following net position categories:

- Net investment in capital assets:
  - Net investment in capital assets includes restricted and unrestricted capital assets, net of accumulated depreciation and reduced by outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.
- Restricted:
  - Nonexpendable – Net position subject to externally imposed stipulations that require YSPSC to maintain them permanently.
  - Expendable – Net position whose use by YSPSC is subject to externally imposed stipulations that can be fulfilled by actions of YSPSC pursuant to those stipulations or that expire with the passage of time.

- Unrestricted:

Net position that is not subject to externally imposed stipulations. Unrestricted net position may be designated for specific purposes by action by management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

YSPSC has no nonexpendable restricted net position at September 30, 2013 and 2012.

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Notes to Financial Statements  
September 30, 2013 and 2012

(1) Organization and Summary of Significant Accounting Policies, Continued

Utility Plant

Utility plant assets were transferred from Division of Public Utilities to YSPSC as of April 1, 1996 at the estimated net book value in the absence of documents to support cost. The net book value of the utility plant assets transferred was \$6,805,075 as of April 1, 1996. Depreciation is computed using the straight-line method over the estimated useful lives of the assets (3-40 years for plant assets).

Cash and Cash Equivalents

For purposes of the statements of net position and the statements of cash flows, cash and cash equivalents are defined as cash on hand, cash in bank and time certificates of deposit with original maturities of three months or less. Time certificates of deposit with original maturities in excess of three months are classified separately.

Receivables

All receivables are due from government agencies, businesses and individuals located within the State of Yap and are interest free and uncollateralized. The allowance for uncollectible accounts is estimated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. The allowance is established through a provision for bad debts charged to expense. Bad debts are written off against the allowance or the specific identifiable method.

Inventory

Supply inventories are carried at specific identification cost or at estimated values when contributed by the State of Yap. Fuel inventories are carried at cost and are determined using the first in-first out method.

Annual and Sick Leave

Earned but unused annual leave is paid to employees upon termination of their employment. Accordingly, YSPSC accrues these benefits in the period earned.

Revenues

Sales of electricity and water are recorded as billed to customers on a monthly billing basis. At September 30, 2013 and 2012, unbilled revenues of \$227,018 and \$243,235, respectively, are estimated and accrued based on the most recent billing cycles.

Operating and Non-operating Revenues and Expenses

YSPSC considers revenues and expenses directly related to utility operations to be operating revenues and expenses. Revenues and expenses related to investing, financing and capital activities and revenues and expenses related to natural disasters are reflected as non-operating.

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Notes to Financial Statements  
September 30, 2013 and 2012

(1) Organization and Summary of Significant Accounting Policies, Continued

Risk Management

YSPSC is exposed to various risks of loss from torts, theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; and natural disasters. Commercial insurance coverage has been obtained for claims arising from most of these matters. YSPSC is self-insured for typhoon risks. Management is of the opinion that no material losses have been sustained as a result of this practice during the past three years.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America require 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 expenses during the reporting period. The most significant estimates are depreciation and allowance for doubtful accounts. Actual results could differ from those estimates.

New Accounting Standards

During the year ended September 30, 2013, YSPSC 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. The implementation of this statement did not have a material effect on the accompanying financial statements.
- 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. The implementation of this statement did not have a material effect on the accompanying financial statements.
- 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*. The implementation of this statement did not have a material effect on the accompanying financial statements.

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Notes to Financial Statements  
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(1) Organization and Summary of Significant Accounting Policies, Continued

New Accounting Standards

- 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.

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 YSPSC.

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 YSPSC.

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 this statement on the financial statements of YSPSC.

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(1) Organization and Summary of Significant Accounting Policies, Continued

New Accounting Standards

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 this statement on the financial statements of YSPSC.

(2) Cash and Cash Equivalents

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

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

As of September 30, 2013 and 2012, the carrying amount of the YSPSC's total cash and cash equivalents was \$1,228,876 and \$1,446,558, respectively, and the corresponding bank balances were \$1,248,030 and \$1,365,566, respectively, which are maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. At September 30, 2013 and 2012, bank deposits in the amount of \$307,889 and \$946,173, respectively, were FDIC insured. Collateralization of deposits is not required; therefore deposits in excess of the FDIC insured amounts are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

(3) Accounts Receivable and Accrued Unbilled Revenue

YSPSC's accounts receivable, less allowance for doubtful accounts, and accrued unbilled revenue at September 30, 2013 and 2012 were as follows:

	<u>2013</u>	<u>2012</u>
Gross accounts receivable	\$ 1,130,516	\$ 1,180,821
Less allowance for doubtful accounts	<u>(227,403)</u>	<u>(227,403)</u>
Net accounts receivable	903,113	953,418
Accrued unbilled revenue	<u>227,018</u>	<u>243,235</u>
Net accounts receivable and accrued unbilled revenue	\$ <u>1,130,131</u>	\$ <u>1,196,653</u>

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Notes to Financial Statements  
September 30, 2013 and 2012

(4) Utility Plant

A summary of changes in capital assets for the years ended September 30, 2013 and 2012 is as follows:

	<u>Beginning Balance</u> <u>October 1, 2012</u>	<u>Transfers and</u> <u>Additions</u>	<u>Transfers and</u> <u>Deletions</u>	<u>Ending Balance</u> <u>September 30, 2013</u>
Depreciable plant:				
Production plant	\$ 10,487,037	\$ 649,545	\$ (85,889)	\$ 11,050,693
Distribution plant	8,818,561	24,520	(157,487)	8,685,594
General plant	<u>1,544,495</u>	<u>151,508</u>	<u>(11,654)</u>	<u>1,684,349</u>
	20,850,093	825,573	(255,030)	21,420,636
Less accumulated depreciation	<u>(12,954,315)</u>	<u>(851,561)</u>	<u>215,362</u>	<u>(13,590,514)</u>
Net depreciable plant	7,895,778	(25,988)	(39,668)	7,830,122
Non-depreciable plant:				
Work in progress	<u>116,519</u>	<u>1,048,057</u>	<u>(116,185)</u>	<u>1,048,391</u>
	<u>\$ 8,012,297</u>	<u>\$ 1,022,069</u>	<u>\$ (155,853)</u>	<u>\$ 8,878,513</u>
	<u>Beginning Balance</u> <u>October 1, 2011</u>	<u>Transfers and</u> <u>Additions</u>	<u>Transfers and</u> <u>Deletions</u>	<u>Ending Balance</u> <u>September 30, 2012</u>
Depreciable plant:				
Production plant	\$ 9,792,283	\$ 694,754	\$ -	\$ 10,487,037
Distribution plant	8,794,455	24,106	-	8,818,561
General plant	<u>1,500,858</u>	<u>43,637</u>	<u>-</u>	<u>1,544,495</u>
	20,087,596	762,497	-	20,850,093
Less accumulated depreciation	<u>(12,206,724)</u>	<u>(747,591)</u>	<u>-</u>	<u>(12,954,315)</u>
Net depreciable plant	7,880,872	14,906	-	7,895,778
Non-depreciable plant:				
Work in progress	<u>485,383</u>	<u>117,735</u>	<u>(486,599)</u>	<u>116,519</u>
	<u>\$ 8,366,255</u>	<u>\$ 132,641</u>	<u>\$ (486,599)</u>	<u>\$ 8,012,297</u>

(5) Notes Payable

Notes payable at September 30, 2013 and 2012 are as follows:

	<u>2013</u>	<u>2012</u>
Uncollateralized loan of original principal of \$2,270,837 payable to the Asia Development Bank (ADB) borrowed through the Federated States of Micronesia (FSM) and Yap State for construction of certain water projects. YSPSC was to be liable to Yap State for interest at 6.82% on the outstanding balance; however, Yap State has waived the interest payment requirement. The loan is repayable semiannually in Special Drawing Rights (SDR) commencing August 2007. An SDR adjustment and additional consulting fees increased the loan balance by \$639,957 in fiscal year 2009.	\$ 2,600,558	\$ 2,660,995

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Notes to Financial Statements  
September 30, 2013 and 2012

(5) Notes Payable, Continued

Uncollateralized note of original principal of \$824,420 payable to Yap State in quarterly interest only payments through March 2003; monthly principal and interest payment of \$5,651 starting June 1, 2003; interest at 2%, maturing in May 2017. The proceeds of the note were used for the construction of the warehouse facility and main office.	-	332,375
Uncollateralized note of original principal of \$1,600,000 payable to Yap State in monthly principal and interest payments of \$10,202 starting November 1, 2009; interest at 1 %, maturing in October 2023. The proceeds of the note were used for the repayment to prior non-government utility customers pursuant to Yap State Law (YSL) Bill # 7-38 & 7-79.	-	1,339,225
Note of original principal of \$103,000 payable to United States of America, acting through the Rural Housing Service, for the construction of the warehouse facility and main office. The note is payable in monthly installments of \$1,075 including interest at 4.625% starting March 26, 2003 and maturing in September 2013. The note is collateralized by equipment, furniture, and fixtures located at YSPSC's office.	-	<u>5,107</u>
Total notes payable	2,600,558	4,337,702
Less current portion	<u>45,417</u>	<u>320,526</u>
	\$ <u>2,555,141</u>	\$ <u>4,017,176</u>

The scheduled debt service of the note payable is as follows:

<u>Year ending</u> <u>September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$ 45,417	\$ -	\$ 45,417
2015	45,417	-	45,417
2016	45,417	-	45,417
2017	83,272	-	83,272
2018	121,126	-	121,126
2019 through 2023	605,632	-	605,632
2024 through 2028	605,632	-	605,632
2029 through 2033	605,405	-	605,405
2034 through 2036	<u>443,240</u>	-	<u>443,240</u>
	\$ <u>2,600,558</u>	\$ -	\$ <u>2,600,558</u>

During 2013, notes payable to Yap State of \$332,372 and \$1,339,225 were forgiven through YSL 8-47 and were recorded as operating grants and subsidies.

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Notes to Financial Statements  
September 30, 2013 and 2012

(5) Notes Payable, Continued

Two new loan agreements with ADB were executed on June 24, 2013 for \$4,680,000 and ADB SDR 2,896,000. As of September 30, 2013, there were no drawdowns made on the notes.

Changes in long-term liabilities for the years ended September 30, 2013 and 2012 are as follows:

	Outstanding September 30, 2012	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, 2013	<u>Current</u>
ADB loan	\$ 2,660,995	\$ -	\$ 60,437	\$ 2,600,558	\$ 45,417
Yap State loan	332,375	-	332,375	-	-
YSL 7-38 loan	1,339,225	-	1,339,225	-	-
USA loan	<u>5,107</u>	<u>-</u>	<u>5,107</u>	<u>-</u>	<u>-</u>
	<u>\$ 4,337,702</u>	<u>\$ -</u>	<u>\$ 1,737,144</u>	<u>\$ 2,600,558</u>	<u>\$ 45,417</u>
	Outstanding September 30, 2011	<u>Increases</u>	<u>Decreases</u>	Outstanding September 30, 2012	<u>Current</u>
ADB loan	\$ 2,706,412	\$ -	\$ 45,417	\$ 2,660,995	\$ 45,417
Yap State loan	383,006	-	50,631	332,375	95,887
YSL 7-38 loan	1,429,915	-	90,690	1,339,225	174,115
USA loan	<u>17,469</u>	<u>-</u>	<u>12,362</u>	<u>5,107</u>	<u>5,107</u>
	<u>\$ 4,536,802</u>	<u>\$ -</u>	<u>\$ 199,100</u>	<u>\$ 4,337,702</u>	<u>\$ 320,526</u>

(6) Contingencies

YSPSC does not currently hold title to real property underlying its operating sites. Such property substantially is held in the name of the State of Yap. YSPSC is not charged for use of this property.

Payable to Federated States of Micronesia

In February 2008, the Yap State Legislature enacted YSL No. 7-25 to amend No. 4-4, YSPSC's enabling legislation, mandating that YSPSC credit back certain charges to prior customers. YSL No. 7-25 directed YSPSC to repeal all fuel surcharges and fees in excess of \$0.035 per kWh and to refund to customers all fuel surcharges and fees collected in excess of \$0.035 per kWh from March 2006 to February 2008. At September 30, 2011, the total variable fuel charge refund has been repaid to residential and commercial customers. The repayment of those costs over the legislated \$0.035 was facilitated by a loan from the State of Yap for \$1,600,000 authorized by YSL No. 7-38.

YSL No. 39 then authorized the Governor to forgive any refund that may be owed by YSPSC to Yap State Government agencies for these declared excessive surcharges. The refund owed FSM National Government as a prior customer remains outstanding at \$181,368, and is included as a current liability in the Statement of Net Assets. Although FSM National Government has not asserted a claim to this liability, it has not forgiven this debt.

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Notes to Financial Statements  
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(7) Grants

YSPSC received the following grants and capital contributions during the years ended September 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
U.S. Department of the Interior grants	\$ 231,610	\$ 415,220
Yap State matching and operating grants	1,672,192	883,221
Japan fuel grant	-	274,545
French Embassy grant	-	36,010
European Union (EU) capital grant	732,297	-
SPC-North REP	82,239	-
Other	<u>13,174</u>	<u>-</u>
	<u>\$ 2,731,512</u>	<u>\$ 1,608,996</u>

(8) Restricted Net Assets

Restricted net assets consist of the following at September 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Unexpended portion of EU capital grant	\$ 1,059,037	\$ 1,107,684
Unexpended portion of Yap State matching grant	563,052	823,367
Unexpended portion of SPC-North REP	<u>76,839</u>	<u>-</u>
	<u>\$ 1,698,928</u>	<u>\$ 1,931,051</u>

(9) Related Party Transactions

In the ordinary course of business, YSPSC enters into transactions with the State of Yap and private businesses in which certain YSPSC's board members hold positions of influence. Several board members hold management positions with the State of Yap, of which YSPSC is a component unit. Several board members hold management positions with private companies with which YSPSC, from time to time, engages in business transactions. YSPSC management is of the opinion that its transactions with related parties are executed under the same laws and conditions as are entered into with unrelated entities.