

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2015

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

YEAR ENDED SEPTEMBER 30, 2015

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

YEAR ENDED SEPTEMBER 30, 2015

INDEPENDENT AUDITORS' REPORT

Honorable Lyndon Jackson
Governor, State of Kosrae
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 Kosrae (the State) as of and for the year ended September 30, 2015, 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 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, 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 Kosrae as of September 30, 2015, 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

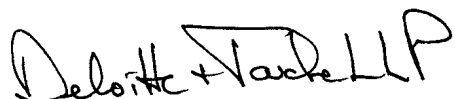
Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 10 as well as the Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund and notes thereto, on pages 42 and 43, 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 17, 2016, 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.

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

June 17, 2016

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2015

This analysis, prepared by the Department of Administration and Finance, offers readers of the Kosrae State Government's ("Kosrae State") financial statements a narrative overview of the activities of the government for the fiscal year ended September 30, 2015. We encourage readers to consider this information in conjunction with Kosrae State's financial statements, which follow. Fiscal year 2014 comparative information has been included, where appropriate. This analysis is required by the Governmental Accounting Standards Board (GASB) which provides guidelines on what must be included and excluded from this analysis.

FINANCIAL HIGHLIGHTS

- Kosrae State's total net position for the fiscal year ended September 30, 2015 decreased by \$0.94 million (or 3.4%) from \$27.51 million in the prior year to \$26.57 million in the current year. The decrease is due primarily to the \$1.34 million reduction in non-cash capital contributions because of depreciation.
- For the fiscal year ended September 30, 2015, the State's General Fund unassigned fund deficit has increased to \$0.75 million from \$0.58 million in the prior year or an increase of \$0.17 million. GASB defines unassigned fund balance as a residual fund balance that is not restricted, committed and assigned.
- For the year ended September 30, 2015, the General Fund total fund balance was reduced by \$0.35 million from \$1.38 million in fiscal year 2014 to \$1.03 million in fiscal year 2015. The decrease was due to a reduction of total revenues for the year of 2% and the absence of an operating transfer in for the year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to Kosrae State's basic financial statements. Kosrae State's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements.

This report also contains additional required supplementary information in the form of budgetary schedules, which are prepared on the budgetary basis of accounting, and other optional supplementary information, in addition to the basic financial statements themselves, which includes combining statements for governmental funds.

Government-Wide Financial Statements

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

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

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

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

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- Governmental activities- Most of Kosrae State's basic services are included here, such as education, health, special appropriations, finance, judiciary, and general administration. Compact sector and other federal grants finance most of these activities.
- Component Units-Kosrae State includes the operating results of the Kosrae Utilities Authority and Kosrae Port Authority in its report. Although separate, these "component units" are important because Kosrae State is financially accountable for them.

Fund Financial Statements

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

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

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

FINANCIAL ANALYSIS OF KOSRAE STATE AS A WHOLE

Kosrae State's assets at the end of fiscal year 2015 exceeded liabilities by \$26.57 million. The bulk of the amount is from net investment in capital assets, although \$7.97 million are restricted. Kosrae State uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although Kosrae State's net investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The following summary of Kosrae State's net position as of September 30, 2015, with comparable balances for the fiscal year 2014, discloses this relationship:

| | Governmental Activities | | | |
|-------------------------------|-------------------------|----------------------|-----------------------|----------|
| | <u>2015</u> | <u>2014</u> | <u>Change</u> | <u>%</u> |
| ASSETS | | | | |
| Current and other assets | \$ 9,483,338 | \$ 10,224,154 | \$ (740,816) | -7% |
| Capital assets | <u>22,731,481</u> | <u>23,226,910</u> | <u>(498,429)</u> | -2% |
| Total assets | \$ <u>32,214,819</u> | \$ <u>33,451,064</u> | \$ <u>(1,239,245)</u> | -4% |
| LIABILITIES | | | | |
| Long-term debt | \$ 3,944,367 | \$ 4,089,322 | \$ (144,955) | -4% |
| Current and other liabilities | <u>1,703,011</u> | <u>1,847,412</u> | <u>(144,401)</u> | -8% |
| Total liabilities | <u>5,647,378</u> | <u>5,936,734</u> | <u>(289,356)</u> | -5% |

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| | Governmental Activities | | | |
|----------------------------------|-------------------------|----------------------|---------------------|----------|
| | <u>2015</u> | <u>2014</u> | <u>Change</u> | <u>%</u> |
| NET POSITION | | | | |
| Net investment in capital assets | 22,039,039 | 23,226,910 | (1,187,871) | -5% |
| Restricted | 7,969,036 | 8,437,456 | (468,420) | -6% |
| Unrestricted | <u>(3,440,634)</u> | <u>(4,150,036)</u> | <u>709,402</u> | 17% |
| Total Net position | <u>\$ 26,567,441</u> | <u>\$ 27,514,330</u> | <u>\$ (946,889)</u> | -3% |

At the end of fiscal year 2015, Kosrae State's unrestricted net position showed a deficit of \$3.44 million, a decrease of \$0.71 million as compared with the prior year. The decrease in overall net position of \$0.94 million was due primarily to \$1.34 million of depreciation expense. The unrestricted deficit, however, is the result of having current and long-term commitments that are greater than currently available resources. Specifically, Kosrae State did not include in past annual budgets the full amounts needed to finance its current liabilities to vendors and others or its long-term liabilities arising from Asian Development Bank (ADB) loans and unused employee leave balances. Kosrae State will include these amounts in future year's budgets as funding permits.

The net position decrease of \$0.94 million (or 3%) compared with prior year and the key elements of the differences from the prior year are shown in the following schedule.

| | Governmental Activities | | | |
|---|-------------------------|----------------------|--------------------|----------------|
| | <u>2015</u> | <u>2014</u> | <u>Change</u> | <u>%</u> |
| Revenues: | | | | |
| Operating grants and contributions | \$ 8,888,152 | \$ 8,668,698 | \$ 219,454 | 2.5% |
| Capital grants and contributions | - | 7,142,051 | (7,142,051) | -100.0% |
| Charges for services | 454,830 | 432,373 | 22,457 | 5.2% |
| Revenue sharing | 1,009,802 | 1,005,708 | 4,094 | 0.4% |
| Unrestricted investment earnings | 148,443 | 328,241 | (179,798) | -54.8% |
| Taxes | 403,154 | 321,208 | 81,946 | 25.5% |
| Other | <u>55,606</u> | <u>8,654</u> | <u>46,952</u> | <u>542.6%</u> |
| Total revenues | <u>10,959,987</u> | <u>17,906,933</u> | <u>(6,946,946)</u> | <u>-38.8%</u> |
| Expenses: | | | | |
| General government | 1,798,590 | 1,786,858 | 11,732 | 0.7% |
| Education | 4,710,620 | 4,810,895 | (100,275) | -2.1% |
| Health services | 2,987,869 | 2,715,277 | 272,592 | 10.0% |
| Economic development | 833,952 | 610,104 | 223,848 | 36.7% |
| Boards, commissions and other | 1,280,344 | 1,489,657 | (209,313) | -14.1% |
| Environment protection and sanitation | 334,209 | 1,110,247 | (776,038) | -69.9% |
| Public order and safety | 357,777 | 352,781 | 4,996 | 1.4% |
| Unallocated interest | <u>41,962</u> | <u>59,779</u> | <u>(17,817)</u> | <u>-29.8%</u> |
| Total expenses | <u>12,345,323</u> | <u>12,935,598</u> | <u>(590,275)</u> | <u>-4.6%</u> |
| Special item - SDR Forex gain | 643,534 | - | 643,534 | |
| Contributions to permanent fund | <u>(205,087)</u> | <u>315,846</u> | <u>(520,933)</u> | <u>-164.9%</u> |
| Change in net position | (946,889) | 5,287,181 | (6,234,070) | -117.9% |
| Net position at the beginning of the year | <u>27,514,330</u> | <u>22,227,149</u> | <u>5,287,181</u> | <u>23.8%</u> |
| Net position at the end of the year | <u>\$ 26,567,441</u> | <u>\$ 27,514,330</u> | <u>(946,889)</u> | <u>-3.4%</u> |

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Figure 1 below showed that total revenues in fiscal year 2015 of \$10.96 million decreased by \$6.94 million (or 38.8%) from the prior year's \$17.90 million. The decrease was primarily due to the absence of capital grants and contributions this year of more than \$7 million. In fiscal year 2015, Grants Assistance Fund revenues comprised 84% of Kosrae State totaling funding sources whereas the General Fund revenues comprised only 16%.

Figure 2 presents that total expenses of \$12.35 million reflected a 5% decrease from the prior year expenses of \$12.93 million.

The following graphs show the major components of revenues and expenses for the year ended September 30, 2015.

Figure 1: Kosrae State Sources of Revenue

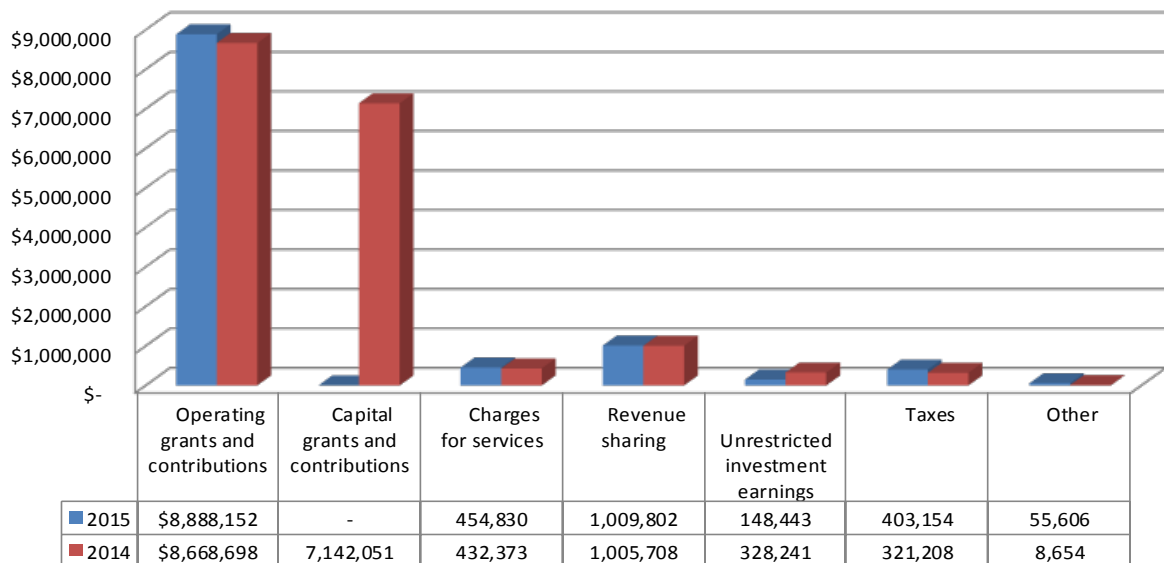
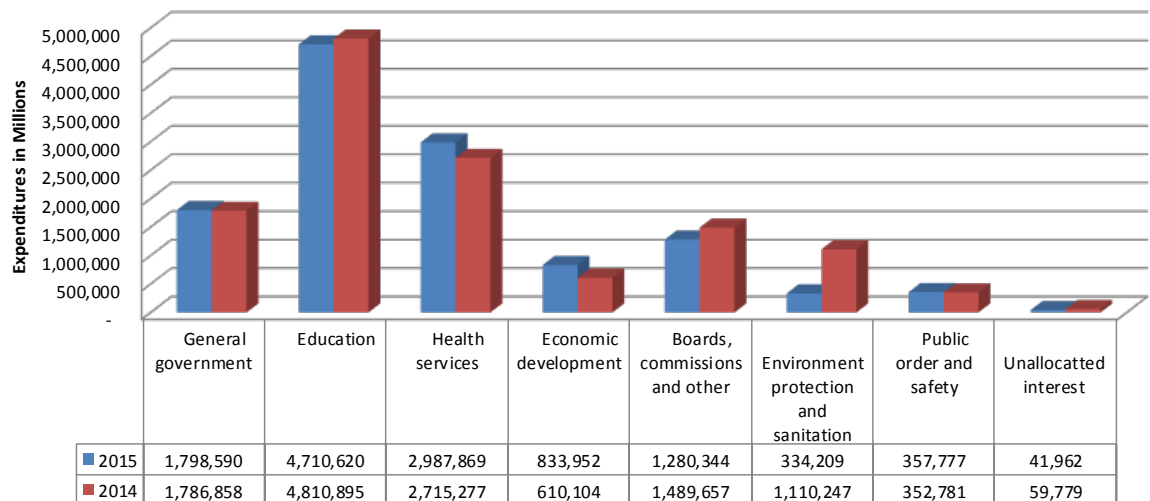


Figure 2: Kosrae State Expenses by Function



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FINANCIAL ANALYSIS OF KOSRAE STATE'S GOVERNMENTAL FUNDS

As noted earlier, Kosrae State uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. As of the end of fiscal year 2015, Kosrae State governmental funds reported a combined fund balance of \$7.90 million, which represents a \$0.64 million decrease (or 7.5%) from the \$8.54 million recorded at the end of fiscal 2014. The decrease was attributable mainly to the decrease in total revenues for the year of \$0.33 million, particularly the negative net change in the fair value of investment of the Compact Trust. Of the total combined fund balance of \$7.90 million, \$5.76 million is designated as non-spendable fund balance; \$2.49 million is restricted fund balance; \$0.48 million is for committed fund balance and (\$0.83 million) for unassigned fund deficit. Encumbrances identified in Note 10 are classified as restricted and committed fund balances depending on the revenue constraints of the particular programs.

The General Fund is the main operating fund of the State. At the end of the current fiscal year, the unassigned fund deficit was \$0.75 million, which increased by \$0.17 million from \$0.58 million from prior year. Consequently, the total fund balance for the General Fund decreased by \$0.35 million from \$1.38 million in fiscal year 2014 to \$1.03 million in the current year. The change in net position was negative \$0.35 million due to a decrease in revenues and the absence of operating transfers in for the current year.

The Grants Assistance Fund has a total fund balance of \$1.39 million. The net increase in fund balance during the current year was \$0.13 million or (10%), which primarily was the result of the increase in total revenues in fiscal year 2015 of \$0.32 million and the decrease in expenditures and operating uses of \$0.70 million.

The Compact Trust Fund has a total fund balance of \$3.95 million, all of which is restricted for funding future operations of the primary government commencing in fiscal year 2023. The decrease in fund balance during the current year was \$0.21 million (or 4.94%) which corresponds to the net decrease in the fair value of investments for the year.

GENERAL FUND BUDGETARY HIGHLIGHTS

During the course of the fiscal year, management and elected officials of Kosrae State Government made several revisions to the General Fund budget. For the year ended September 30, 2015, General Fund revenues of \$2.43 million, including other financing sources, were deficient against expenditures of \$2.77 million by \$0.34 million. The decrease in total revenue collections for the year of \$0.03 million (or 2%) and the absence of operating transfers-in of \$0.17 million as compared from prior year contributed to the decrease in total fund balance for the year of \$1.03 million compared with \$1.38 million in the prior year.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

Kosrae State's net investment in capital assets for the primary government as of September 30, 2015, amounted to \$67.24 million, net of accumulated depreciation of \$44.51 million, resulting in a net book value of \$22.73 million. The decrease in capital assets of \$0.5 million was due to a net amount of depreciation expense of \$1.34 million and capital outlays of \$0.84 million.

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The table below summarizes Kosrae State's capital assets:

| | Governmental Activities | | | |
|---------------------------------|-------------------------|----------------------|---------------------|----------|
| | <u>2015</u> | <u>2014</u> | <u>Change</u> | <u>%</u> |
| Buildings | \$ 12,606,217 | \$ 13,189,224 | \$ (583,007) | -4% |
| Infrastructure | 7,549,258 | 7,985,499 | (436,241) | -5% |
| Machinery, equipment and others | 1,883,564 | 2,052,187 | (168,623) | -8% |
| Construction work-in-progress | <u>692,442</u> | <u>-</u> | <u>692,442</u> | |
| | <u>\$ 22,731,481</u> | <u>\$ 23,226,910</u> | <u>\$ (495,429)</u> | -2% |

Significant capital additions during the year pertained to ADB-funded improvements to the Utwe Water Supply System. Additional information on Kosrae State's capital assets can be found in note 5 to the financial statements.

Long-Term Debt

The following schedule shows Kosrae State's long-term obligations for fiscal year 2015 with comparative balances from fiscal year 2014.

| | Governmental Activities | | | |
|-------------|-------------------------|---------------------|---------------------|----------|
| | <u>2015</u> | <u>2014</u> | <u>Change</u> | <u>%</u> |
| ABD Loans | \$ 3,829,641 | \$ 3,970,887 | \$ (141,246) | -4% |
| Malem Water | <u>114,726</u> | <u>118,435</u> | <u>(3,709)</u> | -3% |
| | <u>\$ 3,944,367</u> | <u>\$ 4,089,322</u> | <u>\$ (144,955)</u> | -4% |

The State's long-term debt decreased by \$0.14 million (or 4%) due primarily to principal repayments made during the year of \$0.19 million and an SDR adjustment of \$0.64 million offset by an additional loan of \$0.69 million. Additional information on Kosrae State's long-term debt obligations can be found in notes 7 and 8 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

General Fund

Revenues for the six months ending March 31, 2016 showed an increase of \$264,484 or 58% as compared to the same period in fiscal year 2015. If the trend remains through the remaining months of fiscal year 2016; the General Fund may partially recoup its fund deficit; however, if revenues decrease then the ensuing months for fiscal year 2016 are expected to be a challenge. This could result in a deficiency in revenues over expenditures.

The leaders of Kosrae State are aware of the current financial situation of the government and have taken steps with implementation of the Long-term Fiscal Framework (LTFF) through a task force created in the 2012 Kosrae Leadership Conference. The LTFF identified steps for reforms to remedy the financial burden of the State in the ensuing years. The LTFF has been implemented in FY 2014.

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Other measures are also being considered to increase general fund revenues.

Grant Assistance Funds

Grants Assistance Funds (specifically compact funding) will continue to be the major funding source for Kosrae State in fiscal year 2016 with total approved funding of \$6,606,643 as follows:

| | |
|--------------------------|-------------|
| Education Sector | \$2,383,075 |
| Health Sector | \$2,092,818 |
| Environment Sector | \$ 188,750 |
| Private Sector | \$ 303,684 |
| Capacity Building Sector | \$ 297,740 |
| SEG | \$1,146,609 |
| ERA | \$ 193,967 |

Grants from other countries were received at the beginning of fiscal year 2016 amounting to more than \$190,000.

In addition, FSM Congress appropriated grants of \$1.5 million for Kosrae State for various programs.

CONTACTING KOSRAE STATE'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors, a general overview of Kosrae State's finances to demonstrate its accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Director of Administration and Finance; P.O. Box 878, Kosrae, FM, 96944.

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FEDERATED STATES OF MICRONESIA**

Statement of Net Position
September 30, 2015

| | Primary Government | Component Units |
|---|-----------------------|----------------------|
| <u>ASSETS</u> | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 813,206 | \$ 372,220 |
| Investments | - | 298,588 |
| Receivables, net | 945,466 | 222,596 |
| Inventories | - | 217,061 |
| Prepayments | 156,229 | 1,981 |
| Advances | 81,578 | - |
| Restricted assets: | | |
| Time certificates of deposit | - | 166,121 |
| Total current assets | <u>1,996,479</u> | <u>1,278,567</u> |
| Noncurrent assets: | | |
| Capital assets: | | |
| Nondepreciable capital assets | 692,442 | 66,972 |
| Capital assets, net of accumulated depreciation | 22,039,039 | 20,054,257 |
| Investments | 1,320,000 | - |
| Other noncurrent assets | - | 252,800 |
| Restricted assets: | | |
| Cash and cash equivalents | 562,691 | - |
| Time certificates of deposit | 554,383 | - |
| Investments | 5,049,785 | - |
| Total noncurrent assets | <u>30,218,340</u> | <u>20,374,029</u> |
| Total assets | <u>\$ 32,214,819</u> | <u>\$ 21,652,596</u> |
| <u>LIABILITIES</u> | | |
| Current liabilities: | | |
| Current portion of long-term obligations | \$ 178,471 | \$ - |
| Accounts payable | 253,763 | 233,837 |
| Other liabilities and accruals | 351,416 | 129,117 |
| Unearned revenues | 977,832 | 12,111 |
| Total current liabilities | <u>1,761,482</u> | <u>375,065</u> |
| Noncurrent liabilities: | | |
| Noncurrent portion of long-term obligations | 3,765,896 | - |
| Other noncurrent liabilities | 120,000 | - |
| Total noncurrent liabilities | <u>3,885,896</u> | <u>-</u> |
| Total liabilities | <u>5,647,378</u> | <u>375,065</u> |
| Commitments and contingencies | | |
| <u>NET POSITION</u> | | |
| Net investment in capital assets | 22,039,039 | 20,121,229 |
| Restricted for: | | |
| Nonexpendable: | | |
| Future operations | 3,949,315 | - |
| Expendable: | | |
| Debt service | 1,100,470 | - |
| Compact related | 789,277 | - |
| Other purposes | 2,129,974 | 90,000 |
| Unrestricted | (3,440,634) | 1,066,302 |
| Total net position | <u>26,567,441</u> | <u>21,277,531</u> |
| Total liabilities and net position | <u>\$ 32,214,819</u> | <u>\$ 21,652,596</u> |

See accompanying notes to financial statements.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Statement of Activities
Year Ended September 30, 2015

| 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 | \$ 1,798,590 | \$ 454,830 | \$ 1,037,373 | \$ - | \$ (306,387) | \$ - |
| Economic development | 833,952 | - | 626,270 | - | (207,682) | - |
| Education | 4,710,620 | - | 4,369,059 | - | (341,561) | - |
| Health services | 2,987,869 | - | 2,578,554 | - | (409,315) | - |
| Public order and safety | 357,777 | - | - | - | (357,777) | - |
| Environment protection and sanitation | 334,209 | - | 276,896 | - | (57,313) | - |
| Boards, commissions and other | 1,280,344 | - | - | - | (1,280,344) | - |
| Unallocated interest on long-term debt | 41,962 | - | - | - | (41,962) | - |
| Total primary government | <u>\$ 12,345,323</u> | <u>\$ 454,830</u> | <u>\$ 8,888,152</u> | <u>\$ -</u> | <u>(3,002,341)</u> | <u>-</u> |
| Component units: | | | | | | |
| Kosrae Port Authority | \$ 1,116,070 | \$ 337,609 | \$ - | \$ - | - | (778,461) |
| Kosrae Utilities Authority | 2,603,237 | 2,485,483 | - | 175,000 | - | 57,246 |
| Total component units | <u>\$ 3,719,307</u> | <u>\$ 2,823,092</u> | <u>\$ -</u> | <u>\$ 175,000</u> | <u>-</u> | <u>(721,215)</u> |
| General revenues: | | | | | | |
| Taxes: | | | | | | |
| FSM revenue sharing: | | | | | | |
| Gross revenue taxes | | | | | 309,398 | - |
| Import taxes | | | | | 301,970 | - |
| Income taxes | | | | | 325,815 | - |
| Other taxes | | | | | 72,619 | - |
| State taxes | | | | | 403,154 | - |
| Unrestricted investment earnings | | | | | 148,443 | (9,447) |
| Other | | | | | 55,606 | (150,211) |
| Total general revenues | | | | | 1,617,005 | (159,658) |
| Special item - gain on SDR foreign exchange | | | | | 643,534 | - |
| Contributions to permanent fund | | | | | (205,087) | - |
| Total general revenues, special item and contributions | | | | | <u>2,055,452</u> | <u>(159,658)</u> |
| Change in net position | | | | | (946,889) | (880,873) |
| Net position at the beginning of the year | | | | | <u>27,514,330</u> | <u>22,158,404</u> |
| Net position at the end of the year | | | | | <u>\$ 26,567,441</u> | <u>\$ 21,277,531</u> |

See accompanying notes to financial statements.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Balance Sheet

**Governmental Funds
September 30, 2015**

| | | Special Revenue | Permanent | Other Governmental Funds | Total |
|--------------------------------------|---------------------|----------------------|---------------------|--------------------------------|----------------------|
| | General | Grants Assistance | Compact Trust | | |
| ASSETS | | | | | |
| Cash and cash equivalents | \$ 813,206 | \$ - | \$ - | \$ - | \$ 813,206 |
| Investments | 327,000 | 900,000 | - | 93,000 | 1,320,000 |
| Receivables, net: | | | | | |
| General | 214,590 | - | - | 12,812 | 227,402 |
| Loans | 30,000 | - | - | 424,857 | 454,857 |
| Federal agencies | - | 263,207 | - | - | 263,207 |
| Due from other funds | 80,635 | 1,504,152 | - | 666,067 | 2,250,854 |
| Prepaid items | - | 147,346 | - | 8,883 | 156,229 |
| Advances | 33,230 | 48,348 | - | - | 81,578 |
| Restricted assets: | | | | | |
| Cash and cash equivalents | 525,393 | - | - | 37,298 | 562,691 |
| Time certificates of deposit | 200,000 | - | - | 354,383 | 554,383 |
| Investments | 1,100,470 | - | 3,949,315 | - | 5,049,785 |
| Total assets | <u>\$ 3,324,524</u> | <u>\$ 2,863,053</u> | <u>\$ 3,949,315</u> | <u>\$ 1,597,300</u> | <u>\$ 11,734,192</u> |
| LIABILITIES AND FUND BALANCES | | | | | |
| Liabilities: | | | | | |
| Accounts payable | \$ 62,418 | \$ 155,495 | \$ - | \$ 35,850 | \$ 253,763 |
| Other liabilities and accruals | 35,126 | 307,135 | - | 9,155 | 351,416 |
| Due to other funds | 2,170,219 | 59,702 | - | 20,933 | 2,250,854 |
| Unearned revenues | 25,000 | 952,799 | - | 33 | 977,832 |
| Total liabilities | <u>2,292,763</u> | <u>1,475,131</u> | <u>-</u> | <u>65,971</u> | <u>3,833,865</u> |
| Fund balances: | | | | | |
| Non-spendable | 390,230 | 903,431 | 3,949,315 | 517,857 | 5,760,833 |
| Restricted | 1,384,612 | 544,193 | - | 561,756 | 2,490,561 |
| Committed | 3,889 | - | - | 474,455 | 478,344 |
| Unassigned: | | | | | |
| General fund | (746,970) | - | - | - | (746,970) |
| Special revenue funds | - | (59,702) | - | (22,739) | (82,441) |
| Total fund balances | <u>1,031,761</u> | <u>1,387,922</u> | <u>3,949,315</u> | <u>1,531,329</u> | <u>7,900,327</u> |
| Total liabilities and fund balances | <u>\$ 3,324,524</u> | <u>\$ 2,863,053</u> | <u>\$ 3,949,315</u> | <u>\$ 1,597,300</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

22,731,481

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 (3,944,367)
Claims payable (120,000)

(4,064,367)

Net position of governmental activities

\$ 26,567,441

See accompanying notes to financial statements.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
Year Ended September 30, 2015

| | General | Special Revenue Grants Assistance | Permanent Compact Trust | Other Governmental Funds | Total |
|--|--------------|--|-------------------------------|--------------------------------|--------------|
| Revenues: | | | | | |
| Compact funding | \$ - | \$ 7,369,472 | \$ - | \$ - | \$ 7,369,472 |
| Net change in the fair value of investments | 29,495 | - | (205,087) | - | (175,592) |
| Federal contributions | - | 1,128,679 | - | - | 1,128,679 |
| FSM revenue sharing | 1,009,802 | - | - | - | 1,009,802 |
| State taxes | 403,154 | - | - | - | 403,154 |
| CFSM grants | - | - | - | 141,848 | 141,848 |
| Fees and charges | 199,464 | - | - | 255,366 | 454,830 |
| Other grants | - | 248,153 | - | - | 248,153 |
| Interest income | 35,439 | - | - | 83,509 | 118,948 |
| Other | 55,606 | - | - | - | 55,606 |
| Total revenues | 1,732,960 | 8,746,304 | (205,087) | 480,723 | 10,754,900 |
| Expenditures: | | | | | |
| Current: | | | | | |
| General government | 1,023,991 | 769,324 | - | - | 1,793,315 |
| Economic development | 25,231 | 626,270 | - | 172,164 | 823,665 |
| Education | 25,662 | 4,369,059 | - | - | 4,394,721 |
| Health services | - | 2,578,554 | - | 308,886 | 2,887,440 |
| Public order and safety | 320,828 | - | - | 26,250 | 347,078 |
| Environment protection and sanitation | - | 276,896 | - | 57,313 | 334,209 |
| Boards, commissions and other | 1,140,901 | - | - | 133,403 | 1,274,304 |
| Debt service | 235,825 | - | - | - | 235,825 |
| Total expenditures | 2,772,438 | 8,620,103 | - | 698,016 | 12,090,557 |
| Excess (deficiency) of revenues over (under) expenditures | (1,039,478) | 126,201 | (205,087) | (217,293) | (1,335,657) |
| Other financing sources: | | | | | |
| Proceeds from issuance of long-term debt | 692,442 | - | - | - | 692,442 |
| Net change in fund balances | (347,036) | 126,201 | (205,087) | (217,293) | (643,215) |
| Fund balances at the beginning of the year | 1,378,797 | 1,261,721 | 4,154,402 | 1,748,622 | 8,543,542 |
| Fund balances at the end of the year | \$ 1,031,761 | \$ 1,387,922 | \$ 3,949,315 | \$ 1,531,329 | \$ 7,900,327 |

See accompanying notes to financial statements.

**STATE OF KOSRAE
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, 2015

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

| | |
|--|--------------|
| Net change in fund balances - total governmental funds | \$ (643,215) |
|--|--------------|

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 | (495,429) |
|---|-----------|

| | |
|--|---------|
| Special item associated with gain on SDR foreign exchange adjustment | 643,534 |
|--|---------|

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

| | |
|------------------------------|------------------|
| Debt proceeds from ADB loans | \$ (692,442) |
| Repayment of ADB loans | 190,154 |
| Repayment of RUS loan | 3,709 |
| Payment of claims | <u>46,800</u> |
| | <u>(451,779)</u> |

| | |
|---|---------------------|
| Change in net position of governmental activities | \$ <u>(946,889)</u> |
|---|---------------------|

See accompanying notes to financial statements.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Combining Statement of Net Position

Component Units
September 30, 2015

| <u>ASSETS</u> | Kosrae Port Authority | Kosrae Utilities Authority | Total |
|---|-----------------------------|----------------------------------|---------------|
| Current assets: | | | |
| Cash and cash equivalents | \$ 50,124 | \$ 322,096 | \$ 372,220 |
| Investments | - | 298,588 | 298,588 |
| Time certificate of deposit - restricted | - | 166,121 | 166,121 |
| Receivables: | | | |
| General | 130,603 | 321,742 | 452,345 |
| Allowance for doubtful debts | (74,286) | (155,463) | (229,749) |
| Net receivables | 56,317 | 166,279 | 222,596 |
| Inventories | - | 217,061 | 217,061 |
| Prepayments | - | 1,981 | 1,981 |
| Total current assets | 106,441 | 1,172,126 | 1,278,567 |
| Noncurrent assets: | | | |
| Deposit for fuel purchase contract | - | 252,800 | 252,800 |
| Capital assets: | | | |
| Nondepreciable capital assets | - | 66,972 | 66,972 |
| Capital assets, net of accumulated depreciation | 17,458,399 | 2,595,858 | 20,054,257 |
| Total assets | \$ 17,564,840 | \$ 4,087,756 | \$ 21,652,596 |
| <u>LIABILITIES AND NET POSITION</u> | | | |
| Current liabilities: | | | |
| Accounts payable | \$ 24,417 | \$ 209,420 | \$ 233,837 |
| Accrued liabilities | 97,509 | 31,608 | 129,117 |
| Unearned revenues | - | 12,111 | 12,111 |
| Total liabilities | 121,926 | 253,139 | 375,065 |
| Net position: | | | |
| Net investment in capital assets | 17,458,399 | 2,662,830 | 20,121,229 |
| Restricted | - | 90,000 | 90,000 |
| Unrestricted | (15,485) | 1,081,787 | 1,066,302 |
| Total net position | 17,442,914 | 3,834,617 | 21,277,531 |
| Total liabilities and net position | \$ 17,564,840 | \$ 4,087,756 | \$ 21,652,596 |

See accompanying notes to financial statements.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Combining Statement of Revenues, Expenses, and Changes in Net Position

Component Units
Year Ended September 30, 2015

| | Kosrae Port Authority | Kosrae Utilities Authority | Total |
|---|-----------------------------|----------------------------------|---------------|
| Operating revenues: | | | |
| Charge for services | \$ 337,609 | \$ 2,485,483 | \$ 2,823,092 |
| Operating expenses: | | | |
| Cost of services | - | 1,487,923 | 1,487,923 |
| Depreciation and amortization | 799,598 | 368,256 | 1,167,854 |
| Administration and general | 316,472 | 740,031 | 1,056,503 |
| Total operating expenses | 1,116,070 | 2,596,210 | 3,712,280 |
| Operating loss | (778,461) | (110,727) | (889,188) |
| Nonoperating revenues (expenses): | | | |
| Interest income | - | 807 | 807 |
| Net change in fair value of investments | - | (10,254) | (10,254) |
| Interest expense | - | (7,027) | (7,027) |
| Other | 32,786 | (182,997) | (150,211) |
| Total nonoperating revenues (expenses), net | 32,786 | (199,471) | (166,685) |
| Net loss before capital contributions | (745,675) | (310,198) | (1,055,873) |
| Capital contributions | - | 175,000 | 175,000 |
| Change in net position | (745,675) | (135,198) | (880,873) |
| Net position at beginning of year | 18,188,589 | 3,969,815 | 22,158,404 |
| Net position at end of year | \$ 17,442,914 | \$ 3,834,617 | \$ 21,277,531 |

See accompanying notes to financial statements.

STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies

The State of Kosrae (the State) was constituted on January 11, 1984, under the provisions of the Kosrae State Constitution (the Constitution) as approved by the people of Kosrae. 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, Pohnpei and Yap. The State is a constitutional government comprised of three branches: the Legislative Branch, consisting of 14 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 KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(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:

Kosrae Port Authority (KPA): KPA was created by Kosrae State Law (KSL) No. 7-91 to operate, manage, equip, and maintain all ports of entry and to expand and improve upon services offered at the ports of entry. KPA is governed by a five-member Board of Directors, of which four members are appointed by the Governor subject to the advice and consent of the Legislature, and, ex-officio, the Director of the Department of Transportation and Infrastructure. The State has the ability to impose its will on KPA.

Kosrae Utilities Authority (KUA): KUA was created by KSL No. 5-38 and is responsible for operating and maintaining, on a commercially accepted basis, the State's electric power. KUA is governed by a five-member Board of Directors, of which four members are appointed by the Governor subject to the advice and consent of the Legislature and, ex-officio, the Director of the Department of Transportation and Infrastructure. The State has the ability to impose its will on KUA.

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 727
Tofol, Kosrae, FSM 96944

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.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements, Continued

The Statement of Net Position presents all of the reporting entity's non-fiduciary assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as net position. Net position is reported in the following 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.
- Unrestricted net position consists of net position, which does not meet the definition of the three 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 \$7,969,036 of restricted net position, of which \$2,129,974 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.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting

Government-wide Financial Statements:

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

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

Governmental Fund Financial Statements:

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

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

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

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

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

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

E. 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 a maturity date within three months of the date acquired by the State. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified on the statement of net 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.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

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.

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

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 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 loan agreements or enabling legislation. Specifically, the State has collateralized investments in the amount of \$1,100,470 for the Early Retirement Scheme. Furthermore, investments recorded in the Compact Trust Fund of \$3,949,315 are restricted in that they are not available to be used in current operations.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

K. Restricted Assets, Continued

As of September 30, 2015, cash and cash equivalents and time certificates of deposit were restricted for the following uses:

Primary Government:

| | |
|---|---------------------|
| Deposit account established for the purpose of receiving payments pursuant to the Compact of Free Association, as amended. | \$ 441,251 |
| Deposit account established for the Housing Renovation program. | 84,142 |
| Deposit account established for the Gifford scholarship fund. | 37,298 |
| Time certificate of deposit with a local bank restricted for scholarships for post-secondary students. | 354,383 |
| Time certificate of deposit for the 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 State, the trustee of the Loan Guarantee Escrow Account. | <u>200,000</u> |
| | <u>\$ 1,117,074</u> |

Discretely Presented Component Units:

| | |
|--|-------------------|
| Time certificate of deposit with a local bank pledged supporting Kosrae Utility Authority short-term debt. | \$ <u>166,121</u> |
|--|-------------------|

L. Capital Assets

Capital assets, including property, plant, equipment and infrastructure (e.g. roads, bridges, ramps and other similar items), are reported in the governmental activity column of the government-wide financial statements. Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at fair market value at the date of donation. Singular pieces of machinery and equipment, other than vehicles, that equal or exceed \$50,000 are capitalized. Buildings and infrastructure projects with a cost that equals or exceeds \$100,000 are capitalized. The costs of normal maintenance and repairs that do not add to the value of assets or materially extend asset lives are not capitalized.

All vehicles have been grouped together regardless of cost and depreciated on a composite basis.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

L. Capital Assets, Continued

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 | 10 - 40 years |
| Infrastructure - roads and bridges | 5 - 50 years |
| Machinery, equipment and others | 5 - 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 200 hours per year. All unused annual leave is cancelled at the end of each fiscal year. Accordingly, no liability is recorded for compensated absences in the accompanying financial statements.

O. Unearned Revenues

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.

P. 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.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

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.

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 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.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

S. New Accounting Standards

During fiscal year 2015, the State implemented the following pronouncements:

- GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date - an amendment of GASB Statement No. 68*, which revise and establish new financial reporting requirements for most governments that provide their employees with pension benefits. The implementation of these statements did not have a material effect on the accompanying financial statements.
- GASB 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 implementation of this statement did not have a material effect on the accompanying financial statements.

In February 2015, GASB issued Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and financial reporting issues related to fair value measurements and requires entities to expand their fair value disclosures by determining major categories of debt and equity securities within the fair value hierarchy on the basis of the nature and risk of the investment. The provisions in Statement 72 are effective for fiscal years beginning after June 15, 2015. Management believes that the implementation of this statement only requires additional disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques and will not have a material effect on the financial statements of the State.

In June 2015, GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements 67 and 68 with the reporting requirements in Statement 68. The provisions in Statement No. 73 are effective for fiscal years beginning after June 15, 2015, with the exception of the provisions that address employers and governmental nonemployer contributing entities for pensions that are not within the scope of Statement 68, which are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

S. New Accounting Standards, Continued

In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and addresses financial reporting requirements for governments whose employees are provided with postemployment benefits other than pensions (other postemployment benefits or OPEB). The provisions in Statement No. 74 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In June 2015, GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which eliminates two of the four categories of authoritative GAAP that exist under the existing hierarchy prescribed by Statement 55. The two categories that will remain under the new standard are (1) GASB Statements and (2) GASB technical bulletins and implementation guides in addition to AICPA guidance that the GASB clears. The provisions in Statement No. 76 are effective for fiscal years beginning after June 15, 2015. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In August 2015, GASB issued Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements. The provisions in Statement No. 77 are effective for fiscal years beginning after December 15, 2015. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(1) Summary of Significant Accounting Policies, Continued

T. 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. However, no material losses have been sustained from this practice in the last three years.

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, deferred outflows of resources, liabilities, and deferred inflows of resources and disclosure 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, 2014 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 KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(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.

The Secretary of Administration and Finance shall be responsible for investment of all public funds collected or appropriated for use by the State. Funds under this arrangement shall include all appropriations from the State, whether funds are appropriated from the State Treasury or funds from other sources. Any funds in excess of the amount necessary for the operation of the State shall be deposited or invested to earn the safest optimum interest. The Secretary shall determine the amount to be invested with the consideration that such amount should not cause disruption of any government service due to low or lack of funds in the operational budget. The Secretary shall cause all investments to be made into financially secure institutions in Kosrae or abroad as determined by the financial institution paying the highest rate of interest on savings when the investment is made.

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.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(2) Deposits and Investments, Continued

A. Deposits, Continued

As of September 30, 2015, the carrying amount of the primary government's total cash and cash equivalents and time certificates of deposit was \$1,930,280 and the corresponding bank balance was \$2,317,324, which is maintained in financial institutions subject to FDIC insurance. As of September 30, 2015, bank deposits in the amount of \$497,738 were FDIC insured. The State does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Therefore, these deposits are exposed to custodial credit risk.

As of September 30, 2015, the carrying amount of the discretely presented component units' total cash and cash equivalents and time certificates of deposit was \$538,341 and the corresponding bank balance was \$541,396, which were maintained in financial institutions subject to FDIC insurance. As of September 30, 2015, bank deposits in the amount of \$363,502 were FDIC insured. The component units do not require collateralization of their cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Therefore, these deposits are exposed to custodial credit risk.

B. Investments

Primary Government

As of September 30, 2015, the State's investments at fair value are as follows:

| | |
|--------------------------|----------------------------|
| Fixed income securities: | |
| Domestic fixed income | \$ 417,243 |
| Other investments: | |
| Common equities | 662,882 |
| Money market funds | 3,949,315 |
| Cash management account | <u>20,345</u> |
| | <u>\$ 5,049,785</u> |

As of September 30, 2015, the State's fixed income securities, including their Moody's investors service credit ratings, had the following maturities:

| Investment Type | Fair Value | Investment Maturities (In Years) | | | | Credit Ratings |
|---------------------------------------|------------------|----------------------------------|------------------|------------------|-----------------|----------------|
| | | Current | 1-5 | 6-10 | Over 10 | |
| U.S. Treasury Notes and Bonds | \$ 89,521 | \$ - | \$ 42,847 | \$ 32,687 | \$13,987 | AAA |
| U.S. Government Agencies Obligations: | | | | | | |
| Federal Home Loan Mortgage Corp. | 37,181 | - | 16,518 | 14,007 | 6,656 | AAA |
| Government National Mortgage Assoc. | 311 | - | - | - | 311 | AAA |
| Federal National Mortgage Association | 92,954 | 24,010 | 58,911 | - | 10,033 | AAA |
| Tennessee Valley Authority | 8,027 | - | - | 4,348 | 3,679 | AAA |
| Housing Urban Development | 34,244 | - | - | 34,244 | - | No rating |
| AID-Tunisia | 12,255 | - | 12,255 | - | - | No rating |
| Municipal Obligations | 8,005 | 8,005 | - | - | - | A2 |
| Municipal Obligations | 17,115 | - | 6,523 | 6,502 | 4,090 | Aa1 |
| Municipal Obligations | 3,131 | - | - | 3,131 | - | Aa2 |
| Corporate Bonds | 114,499 | 34,304 | 42,190 | 24,261 | 13,744 | A1 |
| | <u>\$417,243</u> | <u>\$66,319</u> | <u>\$179,244</u> | <u>\$119,180</u> | <u>\$52,500</u> | |

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(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, 2015.

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.

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, 2015, the General Fund holds 4.3% of the shares of the Pacific Islands Development Bank in the amount of \$327,000. As the fair market value of this investment is not readily available, such has been recorded at cost.

As of September 30, 2015, the Grants Assistance Fund holds 5.0% of the shares of the Bank of the Federated States of Micronesia in the amount of \$500,000 and 5.3% of the shares of the Pacific Islands Development Bank in the amount of \$400,000. As the fair market value of these investments is not readily available, such have been recorded at cost.

As of September 30, 2015, the other governmental funds hold 1.2% of the shares of the Pacific Islands Development Bank in the amount of \$93,000. As the fair market value of this investment is not readily available, such has been recorded at cost.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(2) Deposits and Investments, Continued

B. Investments, Continued

Discretely Presented Component Units

Kosrae Utilities Authority:

As of September 30, 2015, investments at fair value comprise the following:

| | |
|-------------------------|-------------------|
| Money market funds | \$ 21,019 |
| Common stock | 171,708 |
| Fixed income securities | <u>105,861</u> |
| | <u>\$ 298,588</u> |

As of September 30, 2015, the fixed income securities consist of the following:

| | | | Investment maturities (In Years) | |
|---------------------------|------|-------------------|-------------------------------------|------------------|
| | | | 1 to 5 Years | 6 to 10 Years |
| | | Fair Value | | |
| U.S. Treasury obligations | AAA | \$ 45,300 | \$ 36,996 | \$ 8,304 |
| U.S. Government agencies | AAA | 24,186 | 24,186 | - |
| Corporate notes | A1 | 3,176 | - | 3,176 |
| Corporate notes | A2 | 3,361 | - | 3,361 |
| Corporate notes | A3 | 12,473 | 6,577 | 5,896 |
| Corporate notes | BAA1 | 6,074 | - | 6,074 |
| Corporate notes | BAA2 | 3,659 | 3,659 | - |
| Corporate notes | BAA3 | 7,632 | 2,706 | 4,926 |
| | | <u>\$ 105,861</u> | <u>\$ 74,124</u> | <u>\$ 31,737</u> |

(3) Receivables

Primary Government

Receivables as of September 30, 2015, for the primary government's individual major funds and nonmajor funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

| | General | Grants Assistance | Compact Trust | Other Governmental Funds | Total |
|---|-------------------|----------------------|------------------|--------------------------------|--------------------|
| Receivables: | | | | | |
| General | \$ 102,400 | \$ - | \$ - | \$ 979,806 | \$ 1,082,206 |
| Federal agencies | - | 263,207 | - | - | 263,207 |
| Taxes | 213,143 | - | - | - | 213,143 |
| Loans | <u>30,000</u> | <u>762,630</u> | - | <u>1,822,669</u> | <u>2,615,299</u> |
| | 345,543 | 1,025,837 | - | 2,802,475 | 4,173,855 |
| Less: Allowance for uncollectible accounts | <u>(100,953)</u> | <u>(762,630)</u> | - | <u>(2,364,806)</u> | <u>(3,228,389)</u> |
| Net receivables | <u>\$ 244,590</u> | <u>\$ 263,207</u> | <u>\$ -</u> | <u>\$ 437,669</u> | <u>\$ 945,466</u> |

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(3) Receivables, Continued

Primary Government, Continued

Loans receivable of the primary government as of September 30, 2015 are as follows:

General Fund

| | |
|---|------------------|
| Loan receivable due from Tropical Waters, Inc., uncollateralized and interest free. | \$ <u>30,000</u> |
|---|------------------|

Grants Assistance Fund

| | |
|---|---------|
| Note receivable due from Pacific Tuna Ventures, Inc., payable in monthly installments of \$11,875, uncollateralized, due May 1996, interest at 3% per annum. This note has been fully provided for in the allowance for uncollectible accounts. | 367,500 |
|---|---------|

| | |
|---|----------------|
| Loans receivable from post-secondary students issued under a student financial assistance program to qualified Kosraean students, uncollateralized with interest at up to 6% per annum. These loans have been fully provided for in the allowance for uncollectible accounts. | <u>395,130</u> |
|---|----------------|

\$ 762,630

Nonmajor Governmental Funds

| | |
|---|-----------|
| Low-income housing loans, details and terms of those loans have not been compiled and such have been provided for in the allowance for uncollectible accounts in the amount of \$1,364,504. | 1,789,361 |
|---|-----------|

| | |
|---|---------------|
| Loans receivable from post-secondary students issued under a student financial assistance program to qualified Kosraean students, uncollateralized with interest at up to 6% per annum. These loans have been fully provided for in the allowance for uncollectible accounts. | <u>33,308</u> |
|---|---------------|

\$ 1,822,669

(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, 2015, are summarized as follows:

| Receivable Fund | Payable Fund | Amount |
|-----------------------------|-----------------------------|---------------------|
| Grants Assistance | General | \$ 1,504,152 |
| Nonmajor governmental funds | General | 666,067 |
| General | Nonmajor governmental funds | 20,933 |
| General | Grants Assistance | <u>59,702</u> |
| | | <u>\$ 2,250,854</u> |

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(5) Capital Assets

Capital asset activities for the year ended September 30, 2015, are as follows:

Primary Government

| | Balance October 1, 2014 | Increases | Decreases | Balance September 30, 2015 |
|--------------------------------|-------------------------------|---------------------|-----------------|----------------------------------|
| Depreciable assets: | | | | |
| Buildings | \$ 26,835,654 | \$ - | \$ - | \$ 26,835,654 |
| Infrastructure | 32,925,368 | - | - | 32,925,368 |
| Machinery, equipment, others | <u>6,679,670</u> | <u>152,671</u> | <u>(46,043)</u> | <u>6,786,298</u> |
| | <u>66,440,692</u> | <u>152,671</u> | <u>(46,043)</u> | <u>66,547,320</u> |
| Less accumulated depreciation: | | | | |
| Buildings | (13,646,430) | (583,007) | - | (14,229,437) |
| Infrastructure | (24,939,869) | (436,241) | - | (25,376,110) |
| Machinery, equipment, others | <u>(4,627,483)</u> | <u>(321,294)</u> | <u>46,043</u> | <u>(4,902,734)</u> |
| | <u>(43,213,782)</u> | <u>(1,340,542)</u> | <u>-</u> | <u>(44,508,281)</u> |
| | 23,226,910 | (1,187,871) | - | 22,039,039 |
| Nondepreciable assets: | | | | |
| Construction work-in progress | <u>-</u> | <u>692,442</u> | <u>-</u> | <u>692,442</u> |
| | <u>\$ 23,226,910</u> | <u>\$ (495,429)</u> | <u>\$ -</u> | <u>\$ 22,731,481</u> |

During the year ended September 30, 2015, depreciation expense was charged as follows:

| | |
|--------------------------------|---------------------|
| General government | \$ 55,075 |
| Economic development | 10,287 |
| Education | 459,699 |
| Health services | 100,429 |
| Public safety | 10,699 |
| Boards, commissions and others | <u>704,353</u> |
| | <u>\$ 1,340,542</u> |

Discretely Presented Component Units

| | Balance October 1, 2014 | Increases | Decreases | Balance September 30, 2015 |
|-------------------------------|-------------------------------|--------------------|---------------------|----------------------------------|
| Depreciable assets: | | | | |
| Buildings | \$ 11,941,369 | \$ - | \$ - | \$ 11,941,369 |
| Utility plant | 12,197,362 | 164,132 | (1,523,633) | 10,837,861 |
| Infrastructure | 37,972,012 | - | - | 37,972,012 |
| Machinery, equipment, others | <u>924,968</u> | <u>-</u> | <u>-</u> | <u>924,968</u> |
| | 63,035,711 | 164,132 | (1,523,633) | 61,676,210 |
| Less accumulated depreciation | <u>(41,843,636)</u> | <u>(1,167,854)</u> | <u>1,389,537</u> | <u>(41,621,953)</u> |
| | 21,192,075 | (1,003,722) | (134,096) | 20,054,257 |
| Nondepreciable assets: | | | | |
| Construction work-in-progress | <u>70,065</u> | <u>124,411</u> | <u>(127,504)</u> | <u>66,972</u> |
| | <u>\$ 21,262,140</u> | <u>\$ 879,311</u> | <u>\$ (261,600)</u> | <u>\$ 20,121,229</u> |

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(6) Short-Term Debt

Discretely Presented Component Units

Kosrae Utilities Authority (KUA):

KUA has a short-term \$200,000 line of credit facility from a bank with interest at 7% per annum, due October 15, 2015 collateralized by a time certificate of deposit. Changes in this short-term borrowing were as follows:

| <u>October 1, 2014</u> | <u>Additions</u> | <u>Reductions</u> | <u>September 30, 2015</u> |
|----------------------------|-------------------|---------------------|-------------------------------|
| \$ <u> -</u> | \$ <u>150,000</u> | \$ <u>(150,000)</u> | \$ <u> -</u> |

(7) Long-Term Obligations

Primary Government

Malem Wastewater System Project (MWSP) Loan:

The State borrowed \$145,000 from the U.S. Department of Agriculture Rural Utilities Services for the Malem Wastewater System Project, payable in annual installments of \$8,119 commencing September 28, 2001, interest at 4.5% per annum, due September 28, 2040. As of September 30, 2015, the balance payable on this loan amounted to \$114,726.

Asian Development Bank (ADB) Loans:

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 \$2,000,000 loan from the ADB (Loan Number 1520 (SF)) through the FSM National Government, non-interest bearing with a service charge of 1% per annum on the amount of the loan withdrawn from the Loan Account. The activities of the ERS Program are recorded in the General Fund.

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

Funds for the repayment of the ADB loan are expected to be derived from the annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The Financing Agreement requires the State to continue to appropriate salaries for the abolished positions and deposit the appropriated funds into the ERS Trust Account. These funds had not been deposited to the Trust Account as of September 30, 2002. Of the required \$2,000,000 identified for future debt service payments, \$1,100,470 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, 2015, the balance payable on this loan amounted to \$1,681,923.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(7) Long-Term Obligations, Continued

Primary Government, Continued

Asian Development Bank (ADB) Loans, Continued:

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government Program Loan with ADB (Loan Number 1816 FSM (SF)) for the purpose of funding the Basic Social Services Project, with interest at 1% to 1.5% per annum. Principal payments shall be made semiannually commencing February 1, 2009, with a maturity date of August 1, 2032. As of September 30, 2015, the balance payable on this loan amounted to \$117,429.

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 Kosrae, 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, 2015, the balances payable on these loans amounted to \$486,711 and \$524,972, respectively.

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government Program Loan with ADB (Loan Number 2099 FSM (SF)) for the purpose of funding the Omnibus Infrastructure Development Project, with interest at 1% to 1.5% per annum. Principal payments shall be made semiannually commencing 2013, with a maturity date of 2037. As of September 30, 2015, the balance payable on this loan amounted to \$1,018,606.

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> |
|--------------------------------------|---------------------|-------------------|---------------------|
| 2016 | \$ 178,471 | \$ 54,223 | \$ 232,694 |
| 2017 | 178,701 | 51,656 | 230,357 |
| 2018 | 218,825 | 48,283 | 267,108 |
| 2019 | 218,970 | 46,103 | 265,073 |
| 2020 | 219,121 | 43,118 | 262,239 |
| 2021 – 2025 | 1,098,131 | 170,553 | 1,268,684 |
| 2026 – 2030 | 895,022 | 100,272 | 995,294 |
| 2031 – 2035 | 754,205 | 40,887 | 795,092 |
| 2036 – 2039 | <u>182,921</u> | <u>4,463</u> | <u>187,384</u> |
| | <u>\$ 3,944,367</u> | <u>\$ 559,558</u> | <u>\$ 4,503,925</u> |

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(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, 2015, 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 <u>1, 2014</u> | <u>Additions</u> | <u>Reductions</u> | Balance September <u>30, 2015</u> | Due Within <u>One Year</u> |
|----------------|--------------------------------------|-------------------|---------------------|---|-------------------------------|
| Loans payable: | | | | | |
| ADB loans: | | | | | |
| Loan 1520 | \$ 1,995,070 | \$ - | \$ (313,147) | \$ 1,681,923 | \$ 39,986 |
| Loan 1816 | 191,779 | - | (74,350) | 117,429 | 6,939 |
| Loan 1873 | 625,616 | - | (138,905) | 486,711 | 46,371 |
| Loan 1874 | 694,689 | - | (169,717) | 524,972 | 28,332 |
| Loan 2099 | 463,733 | 692,442 | (137,569) | 1,018,606 | 53,989 |
| MWSP loan | <u>118,435</u> | <u>-</u> | <u>(3,709)</u> | <u>114,726</u> | <u>2,854</u> |
| | 4,089,322 | 692,442 | (837,397) | 3,944,367 | 178,471 |
| Other: | | | | | |
| Claims | <u>166,800</u> | <u>-</u> | <u>(46,800)</u> | <u>120,000</u> | <u>-</u> |
| | <u>\$ 4,256,122</u> | <u>\$ 692,442</u> | <u>\$ (884,197)</u> | <u>\$ 4,064,367</u> | <u>\$ 178,471</u> |

When the ADB extends credit to a particular country, the loan is booked in Special Drawing Rights (SDRs) but the actual loan is delivered in the currency of the borrower, at the current exchange rate between the currency and the SDR. The value of the SDR is subject to periodic review by the International Monetary Fund, which may result in the recognition of a foreign exchange gain or loss. During the year ended September 30, 2015, the State recognized a foreign exchange gain of \$643,534 associated with valuation of the SDR, which is presented as a special item in the accompanying financial statements, and which results in a reduction in ADB loans payable.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(9) Fund Balances

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 | \$ 33,230 | \$ 3,431 | \$ - | \$ - | \$ 36,661 |
| Economic development | 30,000 | - | - | - | 30,000 |
| Home improvement program | - | - | - | 424,857 | 424,857 |
| Pacific Islands Development Bank | 327,000 | 400,000 | - | 93,000 | 820,000 |
| Bank of the FSM | - | 500,000 | - | - | 500,000 |
| Permanent fund principal | - | - | 3,949,315 | - | 3,949,315 |
| Restricted for: | | | | | |
| General government | - | 495,214 | - | - | 495,214 |
| Debt service | 1,100,470 | - | - | - | 1,100,470 |
| Housing renovation program | 84,142 | - | - | - | 84,142 |
| USDA development loans | 200,000 | - | - | - | 200,000 |
| Capital projects | - | 48,979 | - | 84,522 | 133,501 |
| Housing improvement program | - | - | - | 88,530 | 88,530 |
| Scholarships | - | - | - | 388,704 | 388,704 |
| Committed for: | | | | | |
| Education | - | - | - | 7,179 | 7,179 |
| Health services | - | - | - | 353,979 | 353,979 |
| Environment protection | - | - | - | 93,011 | 93,011 |
| Board, commissioners, others | 3,889 | - | - | 20,286 | 24,175 |
| Unassigned | <u>(746,970)</u> | <u>(59,702)</u> | <u>-</u> | <u>(22,739)</u> | <u>(829,411)</u> |
| | \$ <u>1,031,761</u> | \$ <u>1,387,922</u> | \$ <u>3,949,315</u> | \$ <u>1,531,329</u> | \$ <u>7,900,327</u> |

(10) Commitments and Contingencies

Encumbrances

The State utilizes encumbrance accounting to identify fund obligations. Encumbrances represent commitments related to unperformed contracts for goods. At September 30, 2015, 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>38,024</u> | \$ <u>1,123,114</u> | \$ <u>211,707</u> | \$ <u>1,372,845</u> |

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2015

(10) Commitments and Contingencies, Continued

Sick Leave

It is the policy of the State to record expenditures for sick leave when leave is actually taken. Sick leave is compensated time for absence during working hours arising from employee illness or injury. The estimated accumulated amount of unused sick leave as of September 30, 2015 is \$505,192.

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.

Federal Grants

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 Guarantee Escrow

As set forth in note 1K, the State has pledged an escrow account in support of certain housing loans. In the event of default, the State could be exposed to an amount in excess of the escrow account balance, an amount that is presently indeterminable.

Litigation

The State is party to numerous legal proceedings, many of which are normal recurrences in governmental operations. The State's Attorney General is of the opinion that the probable outcome of suits existing at September 30, 2015, is not predictable but could have a material impact on the accompanying financial statements. Such impact has currently been estimated to approximate \$120,000, which has been recorded as a liability in the accompanying government-wide financial statements.

Other

The State issued certain reduction-in-force checks to State employees without withholdings. This matter is being discussed between the State and the FSM National Government and State management believes that no adverse impact on the accompanying financial statements will result.

(11) Budgetary Compliance

For the year ended September 30, 2015, significant over-expenditures exceeded appropriations within the General Fund for the following:

| | |
|--------------|------------|
| Debt service | \$ 235,825 |
|--------------|------------|

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2015

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual
General Fund
Year Ended September 30, 2015

| | <u>Budgeted Amounts</u> | | <u>Actual - Budgetary Basis (see Note 1)</u> | <u>Variance with Final Budget -</u> |
|---|-------------------------|---------------------|--|---|
| | <u>Original</u> | <u>Final</u> | | |
| Revenues: | | | | |
| FSM revenue sharing | \$ 1,153,658 | \$ 1,153,658 | \$ 1,009,802 | \$ (143,856) |
| State taxes | 359,457 | 359,457 | 403,154 | 43,697 |
| Licenses and fees | 219,409 | 219,409 | 199,464 | (19,945) |
| Interest and dividends | 44,849 | 44,849 | 35,439 | (9,410) |
| Other | 113,912 | 113,912 | 85,101 | (28,811) |
| Total revenues | <u>1,891,285</u> | <u>1,891,285</u> | <u>1,732,960</u> | <u>(158,325)</u> |
| Expenditures: | | | | |
| Current: | | | | |
| General government | 1,023,578 | 1,027,046 | 1,020,380 | 6,666 |
| Economic development | 21,000 | 25,120 | 25,106 | 14 |
| Education | 27,532 | 27,532 | 26,140 | 1,392 |
| Public order and safety | 344,282 | 328,782 | 321,644 | 7,138 |
| Boards, commissions and other | 495,905 | 1,198,878 | 1,378,258 | (179,380) |
| Total expenditures | <u>1,912,297</u> | <u>2,607,358</u> | <u>2,771,528</u> | <u>(164,170)</u> |
| Deficiency of revenues under expenditures | <u>(21,012)</u> | <u>(716,073)</u> | <u>(1,038,568)</u> | <u>(322,495)</u> |
| Other financing sources: | | | | |
| Proceeds from issuance of long-term debt | <u>-</u> | <u>692,442</u> | <u>692,442</u> | <u>-</u> |
| Net change in fund balance | (21,012) | (23,631) | (346,126) | (322,495) |
| Encumbrances | 21,012 | 21,012 | (910) | (21,922) |
| Fund balance at the beginning of the year | <u>1,378,797</u> | <u>1,378,797</u> | <u>1,378,797</u> | <u>-</u> |
| Fund balance at the end of the year | <u>\$ 1,378,797</u> | <u>\$ 1,376,178</u> | <u>\$ 1,031,761</u> | <u>\$ (344,417)</u> |

See accompanying notes to required supplementary information - budgetary reporting.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting
September 30, 2015

(1) Budgetary Information

The Governor presents to the Kosrae 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 Kosrae State Legislature reviews and approves these estimates making changes, as it deems appropriate. The Appropriation Committee of the Kosrae State Legislature, during the regular session of the Kosrae State Legislature, holds public hearings at which time Departments and Offices are required to justify their budget estimates. During the regular session of the Kosrae State Legislature, an appropriation bill, as required by the Constitution, is introduced and budget estimates are then legally enacted by the Kosrae State Legislature.

Formal budget integration is employed as a management control device during the year for all funds. The Kosrae State Legislature has the authority to reprogram budgeted estimates in accordance with the Constitution. All annual appropriations lapse at fiscal year end 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 KOSRAE
FEDERATED STATES OF MICRONESIA**

OTHER SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2015

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account
Governmental Funds
Year Ended September 30, 2015

| | | Special Revenue | Permanent | | |
|-------------------------------------|---------------------|----------------------|------------------|--------------------------------|----------------------|
| | General | Grants Assistance | Compact Trust | Other Governmental Funds | Total |
| Expenditures: | | | | | |
| Salaries and wages: | | | | | |
| Regular | \$ 1,175,343 | \$ 3,842,637 | \$ - | \$ 88,304 | \$ 5,106,284 |
| Overtime | 27,009 | 107,211 | - | 12,500 | 146,720 |
| Fringe benefits | 148,049 | 505,426 | - | 11,011 | 664,486 |
| Other personnel costs | 70 | 6,960 | - | - | 7,030 |
| Travel and transportation | 88,535 | 253,961 | - | 75,541 | 418,037 |
| Communications | 38,076 | 78,889 | - | 5,688 | 122,653 |
| Dues, membership, and subscriptions | 5 | 4,055 | - | - | 4,060 |
| Food stuffs | 24,552 | 41,154 | - | 1,640 | 67,346 |
| Port charges | - | 10,832 | - | - | 10,832 |
| Office supplies and materials | 71,248 | 791,195 | - | 75,763 | 938,206 |
| POL | 16,278 | 119,410 | - | 19,673 | 155,361 |
| Printing and reproduction | 1,733 | 14,630 | - | 14,280 | 30,643 |
| Rental services | 3,172 | 13,203 | - | 1,538 | 17,913 |
| Repairs and maintenance | 2,287 | 23,657 | - | 502 | 26,446 |
| Utilities | 103,124 | 340,232 | - | 10,985 | 454,341 |
| Subsidies and contributions | 4,585 | - | - | - | 4,585 |
| Medical referral | - | 100,242 | - | - | 100,242 |
| Medical supplies | - | 398,358 | - | 237,395 | 635,753 |
| Contractual services | 748,421 | 1,005,923 | - | 52,828 | 1,807,172 |
| Professional services | - | 7,174 | - | - | 7,174 |
| Scholarships and allowances | 7,070 | 238,538 | - | - | 245,608 |
| Training | 10,722 | 278,802 | - | - | 289,524 |
| Leased housing, buildings and land | 16,630 | 109,951 | - | - | 126,581 |
| Nonpayroll compensation | - | 10,446 | - | - | 10,446 |
| Equipment | 21,684 | 296,826 | - | 66,014 | 384,524 |
| Principal repayment | 193,863 | - | - | - | 193,863 |
| Interest payments | 41,962 | - | - | - | 41,962 |
| Miscellaneous | 28,020 | 20,391 | - | 24,354 | 72,765 |
| | <u>\$ 2,772,438</u> | <u>\$ 8,620,103</u> | <u>\$ -</u> | <u>\$ 698,016</u> | <u>\$ 12,090,557</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function,
and Changes in Fund Balance
General Fund
Year Ended September 30, 2015
(with comparative totals for the year ended September 30, 2014)

| | 2015 | 2014 |
|---|------------------|------------------|
| Revenues: | | |
| FSM revenue sharing: | | |
| Gross revenue taxes | \$ 309,398 | \$ 341,545 |
| Import taxes | 301,970 | 339,360 |
| Income taxes | 325,815 | 277,104 |
| Other taxes | 72,619 | 47,699 |
| | <u>1,009,802</u> | <u>1,005,708</u> |
| State taxes: | | |
| Sales tax | <u>403,154</u> | <u>321,208</u> |
| Fees and charges: | | |
| Licenses and fees | <u>199,464</u> | <u>199,868</u> |
| Net change in fair value of investments | <u>29,495</u> | <u>191,976</u> |
| Interest and dividend income | <u>35,439</u> | <u>37,508</u> |
| Other: | | |
| Other | <u>55,606</u> | <u>8,654</u> |
| Total revenues | <u>1,732,960</u> | <u>1,764,922</u> |
| Expenditures: | | |
| Current: | | |
| General government: | | |
| Office of the Governor | 165,981 | 185,918 |
| Department of Administration and Finance | 101,805 | 97,885 |
| Judiciary Branch | 184,654 | 193,174 |
| Legislative Branch | 541,466 | 563,610 |
| Election | 30,085 | 14,870 |
| | <u>1,023,991</u> | <u>1,055,457</u> |
| Economic development: | | |
| Land management services | <u>25,231</u> | <u>77,210</u> |
| Education: | | |
| Scholarship board | <u>25,662</u> | <u>25,868</u> |
| Public order and safety: | | |
| Office of the Attorney General | 320,428 | 327,240 |
| Parole board | 400 | 500 |
| | <u>320,828</u> | <u>327,740</u> |
| Boards, Commissions and Other: | | |
| Department of Transportation and Infrastructure | 939,594 | 384,468 |
| Broadcast Authority | 46,081 | 46,262 |
| Sports Council | 15,269 | 17,165 |
| RM Small Business Development Center | 744 | 4,634 |
| Land Court | 97,885 | 111,240 |
| KPA Fire truck | - | 840 |
| Micronesia Legal Services | - | 15,000 |
| Municipal governments | 3,750 | 6,870 |
| Other | 37,578 | 41,803 |
| | <u>1,140,901</u> | <u>628,282</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function,
and Changes in Fund Balance, Continued
General Fund
Year Ended September 30, 2015
(with comparative totals for the year ended September 30, 2014)

| | 2015 | 2014 |
|---|---------------------|---------------------|
| Expenditures, continued: | | |
| Debt service: | | |
| Principal payments | 193,863 | 187,951 |
| Interest charges | 41,962 | 59,779 |
| | <u>235,825</u> | <u>247,730</u> |
| Total expenditures | <u>2,772,438</u> | <u>2,362,287</u> |
| Deficiency of revenues under expenditures | <u>(1,039,478)</u> | <u>(597,365)</u> |
| Other financing sources: | | |
| Proceeds from issuance of long-term debt | 692,442 | 104,548 |
| Operating transfers in | - | 172,629 |
| | <u>692,442</u> | <u>277,177</u> |
| Net change in fund balance | (347,036) | (320,188) |
| Fund balance at the beginning of the year | <u>1,378,797</u> | <u>1,698,985</u> |
| Fund balance at the end of the year | <u>\$ 1,031,761</u> | <u>\$ 1,378,797</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function,
and Changes in Fund Balance - Budget and Actual
General Fund
Year Ended September 30, 2015

| | Budgeted Amounts | | Actual Amounts Budgetary Basis | Variance |
|---|------------------|--------------|---|--------------|
| | Original | Final | | |
| Revenues: | | | | |
| FSM revenue sharing: | \$ 1,153,658 | \$ 1,153,658 | \$ 1,009,802 | \$ (143,856) |
| State taxes: | | | | |
| Sales tax | 359,457 | 359,457 | 403,154 | 43,697 |
| Fees and charges: | | | | |
| Licences and fees | 219,409 | 219,409 | 199,464 | (19,945) |
| Interest and dividend income | 44,849 | 44,849 | 35,439 | (9,410) |
| Other: | | | | |
| Other | 113,912 | 113,912 | 85,101 | (28,811) |
| Total revenues | 1,891,285 | 1,891,285 | 1,732,960 | (158,325) |
| Expenditures: | | | | |
| Current: | | | | |
| General government: | | | | |
| Office of the Governor | 161,928 | 166,396 | 166,331 | 65 |
| Department of Administration and Finance | 98,765 | 98,765 | 101,752 | (2,987) |
| Judiciary Branch | 201,266 | 200,266 | 182,711 | 17,555 |
| Legislative Branch | 534,839 | 534,839 | 539,888 | (5,049) |
| Election | 26,780 | 26,780 | 29,698 | (2,918) |
| | 1,023,578 | 1,027,046 | 1,020,380 | 6,666 |
| Economic development: | | | | |
| Land management and preservation | 21,000 | 25,120 | 25,106 | 14 |
| | 21,000 | 25,120 | 25,106 | 14 |
| Education: | | | | |
| Scholarship board | 27,532 | 27,532 | 26,140 | 1,392 |
| Public order and safety: | | | | |
| Office of the Attorney General | 343,532 | 328,032 | 321,244 | 6,788 |
| Parole board | 750 | 750 | 400 | 350 |
| | 344,282 | 328,782 | 321,644 | 7,138 |
| Boards, commissions and other: | | | | |
| Department of Transportation and Infrastructure | 281,712 | 969,685 | 939,522 | 30,163 |
| Broadcast Authority | 48,564 | 48,564 | 46,081 | 2,483 |
| Sports Council | 16,263 | 16,263 | 14,462 | 1,801 |
| Small Business Development Center | - | - | 111 | (111) |
| Land Court | 109,111 | 109,111 | 100,429 | 8,682 |
| Municipal governments | 18,800 | 18,800 | 3,750 | 15,050 |
| Other | 21,455 | 36,455 | 38,078 | (1,623) |
| Debt Service: | | | | |
| Principal payments | - | - | 193,863 | (193,863) |
| Interest charges | - | - | 41,962 | (41,962) |
| | 495,905 | 1,198,878 | 1,378,258 | (179,380) |
| Total expenditures | 1,912,297 | 2,607,358 | 2,771,528 | (164,170) |
| Deficiency of revenues under expenditures | (21,012) | (716,073) | (1,038,568) | (322,495) |
| Other financing sources: | | | | |
| Proceeds from issuance of long-term debt | - | 692,442 | 692,442 | - |
| Net change in fund balance | (21,012) | (23,631) | (346,126) | (322,495) |
| Encumbrances | 21,012 | 21,012 | (910) | (21,922) |
| Fund balance at the beginning of the year | 1,378,797 | 1,378,797 | 1,378,797 | - |
| Fund balance at the end of the year | \$ 1,378,797 | \$ 1,376,178 | \$ 1,031,761 | \$ (344,417) |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

**Combining Balance Sheet
September 30, 2015**

| | Scholarship Revolving Loan | Production and Development Loan | Health Care | Sports Council | Broadcasting Authority | Transportation Infrastructure Revolving | Home Improvement Program Revolving | Aluminum Recycling | CFSM Grants | Gifford Scholarship | Land Administration | Total |
|--|----------------------------------|--|-------------------|-------------------|---------------------------|---|---|-----------------------|-------------------|------------------------|------------------------|---------------------|
| ASSETS | | | | | | | | | | | | |
| Investments | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 93,000 | \$ - | \$ - | \$ 93,000 |
| Receivables: | | | | | | | | | | | | |
| General | - | - | - | - | - | - | - | - | 12,812 | - | - | 12,812 |
| Loans | - | - | - | - | - | - | 424,857 | - | - | - | - | 424,857 |
| Due from other funds | 7,179 | 10,975 | 367,121 | 182 | 7,780 | 1,349 | 92,909 | 100,476 | 78,096 | - | - | 666,067 |
| Prepaid items | - | - | 8,883 | - | - | - | - | - | - | - | - | 8,883 |
| Restricted: | | | | | | | | | | | | |
| Cash and equivalents | - | - | - | - | - | - | - | - | - | 37,298 | - | 37,298 |
| Time certificates of deposit | - | - | - | - | - | - | - | - | - | 354,383 | - | 354,383 |
| Total assets | <u>\$ 7,179</u> | <u>\$ 10,975</u> | <u>\$ 376,004</u> | <u>\$ 182</u> | <u>\$ 7,780</u> | <u>\$ 1,349</u> | <u>\$ 517,766</u> | <u>\$ 100,476</u> | <u>\$ 183,908</u> | <u>\$ 391,681</u> | <u>\$ -</u> | <u>\$ 1,597,300</u> |
| LIABILITIES AND FUND BALANCES (DEFICIT) | | | | | | | | | | | | |
| Liabilities: | | | | | | | | | | | | |
| Accounts payable | \$ - | \$ - | \$ 22,025 | \$ - | \$ - | \$ - | \$ 7 | \$ 7,465 | \$ 6,353 | \$ - | \$ - | \$ 35,850 |
| Other liabilities and accruals | - | - | - | - | - | - | 4,372 | - | - | - | 4,783 | 9,155 |
| Due to other funds | - | - | - | - | - | - | - | - | - | 2,977 | 17,956 | 20,933 |
| Unearned revenue | - | - | - | - | - | - | - | - | 33 | - | - | 33 |
| Total liabilities | <u>-</u> | <u>-</u> | <u>22,025</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>4,379</u> | <u>7,465</u> | <u>6,386</u> | <u>2,977</u> | <u>22,739</u> | <u>65,971</u> |
| Fund balances (deficit): | | | | | | | | | | | | |
| Non-spendable | - | - | - | - | - | - | 424,857 | - | 93,000 | - | - | 517,857 |
| Restricted | - | - | - | - | - | - | 88,530 | - | 84,522 | 388,704 | - | 561,756 |
| Committed | 7,179 | 10,975 | 353,979 | 182 | 7,780 | 1,349 | - | 93,011 | - | - | - | 474,455 |
| Unassigned | - | - | - | - | - | - | - | - | - | - | (22,739) | (22,739) |
| Total fund balances (deficit) | <u>7,179</u> | <u>10,975</u> | <u>353,979</u> | <u>182</u> | <u>7,780</u> | <u>1,349</u> | <u>513,387</u> | <u>93,011</u> | <u>177,522</u> | <u>388,704</u> | <u>(22,739)</u> | <u>1,531,329</u> |
| Total liabilities and fund balances | <u>\$ 7,179</u> | <u>\$ 10,975</u> | <u>\$ 376,004</u> | <u>\$ 182</u> | <u>\$ 7,780</u> | <u>\$ 1,349</u> | <u>\$ 517,766</u> | <u>\$ 100,476</u> | <u>\$ 183,908</u> | <u>\$ 391,681</u> | <u>\$ -</u> | <u>\$ 1,597,300</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Statement of Revenues, Expenditures By Function,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2015

| | Scholarship Revolving Loan | Production and Development Loan | Health Care | Sports Council | Broadcasting Authority | Transportation Infrastructure Revolving | Home Improvement Program Revolving | Aluminum Recycling | CFSM Grants | Gifford Scholarship | Land Administration | Total |
|--|----------------------------------|--|----------------|-------------------|---------------------------|---|---|-----------------------|----------------|------------------------|------------------------|--------------|
| Revenues: | | | | | | | | | | | | |
| Fees and charges | \$ 235 | \$ 28,597 | \$ 142,921 | \$ - | \$ 837 | \$ - | \$ - | \$ 80,776 | \$ - | \$ - | \$ 2,000 | \$ 255,366 |
| CFSM grants | - | - | - | - | - | - | - | - | 141,848 | - | - | 141,848 |
| Interest income | - | 26 | 289 | - | - | - | 79,705 | 82 | - | 3,407 | - | 83,509 |
| Total revenues | 235 | 28,623 | 143,210 | - | 837 | - | 79,705 | 80,858 | 141,848 | 3,407 | 2,000 | 480,723 |
| Expenditures by function: | | | | | | | | | | | | |
| Current: | | | | | | | | | | | | |
| Health services | - | - | 308,886 | - | - | - | - | - | - | - | - | 308,886 |
| Economic development | - | - | - | - | - | - | - | - | 172,164 | - | - | 172,164 |
| Public order and safety | - | - | - | - | - | - | - | - | 26,250 | - | - | 26,250 |
| Environment, protection and sanitation | - | - | - | - | - | - | - | 57,313 | - | - | - | 57,313 |
| Boards, commissions and other | - | 23,430 | - | 280 | 867 | 1,366 | 82,721 | - | - | - | 24,739 | 133,403 |
| Total expenditures | - | 23,430 | 308,886 | 280 | 867 | 1,366 | 82,721 | 57,313 | 198,414 | - | 24,739 | 698,016 |
| Net change in fund balances | 235 | 5,193 | (165,676) | (280) | (30) | (1,366) | (3,016) | 23,545 | (56,566) | 3,407 | (22,739) | (217,293) |
| Fund balances at the beginning of the year | 6,944 | 5,782 | 519,655 | 462 | 7,810 | 2,715 | 516,403 | 69,466 | 234,088 | 385,297 | - | 1,748,622 |
| Fund balances (deficit) at the end of the year | \$ 7,179 | \$ 10,975 | \$ 353,979 | \$ 182 | \$ 7,780 | \$ 1,349 | \$ 513,387 | \$ 93,011 | \$ 177,522 | \$ 388,704 | \$ (22,739) | \$ 1,531,329 |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

**Combining Statement of Revenues, Expenditures By Account,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2015**

| | Scholarship Revolving Loan | Production and Development Loan | Health Care | Sports Council | Broadcasting Authority | Transportation Infrastructure Revolving | Home Improvement Program Revolving | Aluminum Recycling | CFSM Grants | Gifford Scholarship | Land Administration | Total |
|--|----------------------------------|--|----------------|-------------------|---------------------------|---|---|-----------------------|----------------|------------------------|------------------------|--------------|
| Revenues: | | | | | | | | | | | | |
| Fees and charges | \$ 235 | \$ 28,597 | \$ 142,921 | \$ - | \$ 837 | \$ - | \$ - | \$ 80,776 | \$ - | \$ - | \$ 2,000 | \$ 255,366 |
| CFSM Grants | - | - | - | - | - | - | - | - | 141,848 | - | - | 141,848 |
| Interest income | - | 26 | 289 | - | - | - | 79,705 | 82 | - | 3,407 | - | 83,509 |
| Total revenues | 235 | 28,623 | 143,210 | - | 837 | - | 79,705 | 80,858 | 141,848 | 3,407 | 2,000 | 480,723 |
| Expenditures by account: | | | | | | | | | | | | |
| Salaries and wages: | | | | | | | | | | | | |
| Regular | - | - | - | - | - | - | 43,604 | - | 22,866 | - | 21,834 | 88,304 |
| Overtime | - | - | - | - | - | - | - | - | 12,500 | - | - | 12,500 |
| Fringe benefits | - | - | - | - | - | - | 4,494 | - | 3,612 | - | 2,905 | 11,011 |
| Travel and transportation | - | (558) | 61,921 | - | - | - | 6,738 | - | 7,440 | - | - | 75,541 |
| Communications | - | - | - | 130 | 477 | - | 2,585 | - | 2,496 | - | - | 5,688 |
| Food stuffs | - | - | - | - | - | - | 446 | - | 1,194 | - | - | 1,640 |
| Office supplies and materials | - | 14,860 | 2,180 | - | - | 1,366 | (6,672) | 57,313 | 6,716 | - | - | 75,763 |
| POL | - | - | - | - | - | - | 320 | - | 19,353 | - | - | 19,673 |
| Contractual services | - | 9,078 | - | - | - | - | 500 | - | 43,250 | - | - | 52,828 |
| Utilities | - | - | - | 150 | - | - | 3,600 | - | 7,235 | - | - | 10,985 |
| Medical supplies | - | - | 237,395 | - | - | - | - | - | - | - | - | 237,395 |
| Rental | - | - | - | - | 390 | - | - | - | 1,148 | - | - | 1,538 |
| Equipment | - | - | 7,138 | - | - | - | 2,310 | - | 56,566 | - | - | 66,014 |
| Repairs and maintenance | - | - | - | - | - | - | 502 | - | - | - | - | 502 |
| Printing and reproduction | - | - | - | - | - | - | 280 | - | 14,000 | - | - | 14,280 |
| Miscellaneous | - | 50 | 252 | - | - | - | 24,014 | - | 38 | - | - | 24,354 |
| Total expenditures | - | 23,430 | 308,886 | 280 | 867 | 1,366 | 82,721 | 57,313 | 198,414 | - | 24,739 | 698,016 |
| Net change in fund balances | 235 | 5,193 | (165,676) | (280) | (30) | (1,366) | (3,016) | 23,545 | (56,566) | 3,407 | (22,739) | (217,293) |
| Fund balances at the beginning of the year | 6,944 | 5,782 | 519,655 | 462 | 7,810 | 2,715 | 516,403 | 69,466 | 234,088 | 385,297 | - | 1,748,622 |
| Fund balances (deficit) at the end of the year | \$ 7,179 | \$ 10,975 | \$ 353,979 | \$ 182 | \$ 7,780 | \$ 1,349 | \$ 513,387 | \$ 93,011 | \$ 177,522 | \$ 388,704 | \$ (22,739) | \$ 1,531,329 |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Balance Sheet
September 30, 2015

| | Section 211(a)(1) Education Sector | Section 211(a)(2) Health Sector | Section 211(a)(3) Private Sector Development | Section 211(a)(4) Capacity Building | Section 211(a)(5) Environment | Section 211(a)(6) Infrastructure |
|---|---|--|---|--|-------------------------------------|--|
| <u>ASSETS</u> | | | | | | |
| Investments | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - |
| Receivables: | | | | | | |
| Federal agencies | 77,176 | - | - | - | 684 | - |
| Advances | - | 19,590 | 9,382 | 9,754 | - | - |
| Prepayments | 23,312 | 77,725 | 1,264 | - | - | - |
| Due from other funds | <u>209,654</u> | <u>238,330</u> | <u>61,754</u> | <u>81,896</u> | <u>28,268</u> | <u>122,262</u> |
| Total assets | <u>\$ 310,142</u> | <u>\$ 335,645</u> | <u>\$ 72,400</u> | <u>\$ 91,650</u> | <u>\$ 28,952</u> | <u>\$ 122,262</u> |
| <u>LIABILITIES AND FUND BALANCES</u> | | | | | | |
| Liabilities: | | | | | | |
| Accounts payable | \$ 6,779 | \$ 84,997 | \$ 3,743 | \$ 484 | \$ 2,503 | \$ - |
| Other liabilities and accruals | 119,400 | 71,125 | 19,499 | 14,400 | 8,301 | - |
| Due to other funds | - | - | - | - | - | - |
| Unearned revenues | <u>183,963</u> | <u>179,523</u> | <u>49,158</u> | <u>76,766</u> | <u>18,148</u> | <u>73,283</u> |
| Total liabilities | <u>310,142</u> | <u>335,645</u> | <u>72,400</u> | <u>91,650</u> | <u>28,952</u> | <u>73,283</u> |
| Fund balances: | | | | | | |
| Non-spendable | - | - | - | - | - | - |
| Restricted | - | - | - | - | - | 48,979 |
| Unassigned | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| Total fund balances | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>48,979</u> |
| Total liabilities and fund balances | <u>\$ 310,142</u> | <u>\$ 335,645</u> | <u>\$ 72,400</u> | <u>\$ 91,650</u> | <u>\$ 28,952</u> | <u>\$ 122,262</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Balance Sheet, Continued
September 30, 2015

| | Section 211(a)(7) Supplemental Education | Enhanced Reporting Accountability | U.S. Federal Grants | Compact Capital Projects | Foreign Assistance | Total |
|---|---|---|---------------------------|--------------------------------|-----------------------|-------------------------|
| <u>ASSETS</u> | | | | | | |
| Investments | \$ - | \$ - | \$ - | \$ 800,000 | \$ 100,000 | \$ 900,000 |
| Receivables: | | | | | | |
| Federal agencies | 80,617 | 262 | 104,468 | - | - | 263,207 |
| Advances | 3,098 | - | 3,093 | - | 3,431 | 48,348 |
| Prepayments | 45,045 | - | - | - | - | 147,346 |
| Due from other funds | <u>184,649</u> | <u>13,346</u> | <u>15,099</u> | <u>-</u> | <u>548,894</u> | <u>1,504,152</u> |
| Total assets | <u>\$ 313,409</u> | <u>\$ 13,608</u> | <u>\$ 122,660</u> | <u>\$ 800,000</u> | <u>\$ 652,325</u> | <u>\$ 2,863,053</u> |
| <u>LIABILITIES AND FUND BALANCES</u> | | | | | | |
| Liabilities: | | | | | | |
| Accounts payable | \$ 16,142 | \$ - | \$ 40,019 | \$ - | \$ 828 | \$ 155,495 |
| Other liabilities and accruals | 12,524 | 13,608 | 48,278 | - | - | 307,135 |
| Due to other funds | - | - | - | 59,702 | - | 59,702 |
| Unearned revenues | <u>284,743</u> | <u>-</u> | <u>34,363</u> | <u>-</u> | <u>52,852</u> | <u>952,799</u> |
| Total liabilities | <u>313,409</u> | <u>13,608</u> | <u>122,660</u> | <u>59,702</u> | <u>53,680</u> | <u>1,475,131</u> |
| Fund balances: | | | | | | |
| Non-spendable | - | - | - | 800,000 | 103,431 | 903,431 |
| Restricted | - | - | - | - | 495,214 | 544,193 |
| Unassigned | <u>-</u> | <u>-</u> | <u>-</u> | <u>(59,702)</u> | <u>-</u> | <u>(59,702)</u> |
| Total fund balances | <u>-</u> | <u>-</u> | <u>-</u> | <u>740,298</u> | <u>598,645</u> | <u>1,387,922</u> |
| Total liabilities and fund balances | <u>\$ 313,409</u> | <u>\$ 13,608</u> | <u>\$ 122,660</u> | <u>\$ 800,000</u> | <u>\$ 652,325</u> | <u>\$ 2,863,053</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances
Year Ended September 30, 2015

| | Section 211(a)(1) Education Sector | Section 211(a)(2) Health Sector | Section 211(a)(3) Private Sector Development | Section 211(a)(4) Capacity Building | Section 211(a)(5) Environment | Section 211(a)(6) Infrastructure |
|--|---|--|---|--|-------------------------------------|--|
| Revenues: | | | | | | |
| Compact funding | \$ 2,621,557 | \$ 2,085,492 | \$ 626,270 | \$ 447,451 | \$ 179,193 | \$ 26,717 |
| Federal contributions | - | - | - | - | - | - |
| Other grants | - | - | - | - | - | - |
| Total revenues | <u>2,621,557</u> | <u>2,085,492</u> | <u>626,270</u> | <u>447,451</u> | <u>179,193</u> | <u>26,717</u> |
| Expenditures by function: | | | | | | |
| Current: | | | | | | |
| General government | - | - | - | 447,451 | - | 26,717 |
| Economic development | - | - | 626,270 | - | - | - |
| Education | 2,621,557 | - | - | - | - | - |
| Health services | - | 2,085,492 | - | - | - | - |
| Environment protection and sanitation | - | - | - | - | 179,193 | - |
| Total expenditures | <u>2,621,557</u> | <u>2,085,492</u> | <u>626,270</u> | <u>447,451</u> | <u>179,193</u> | <u>26,717</u> |
| Net change in fund balances | - | - | - | - | - | - |
| Fund balances at the beginning of the year | - | - | - | - | - | 48,979 |
| Fund balances at the end of the year | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 48,979</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances, Continued
Year Ended September 30, 2015

| | Section 211(a)(7) Supplemental Education | Enhanced Reporting Accountability | U.S. Federal Grants | Compact Capital Projects | Foreign Assistance | Total |
|--|---|---|---------------------------|--------------------------------|-----------------------|---------------------|
| Revenues: | | | | | | |
| Compact funding | \$ 1,207,973 | \$ 174,819 | \$ - | \$ - | \$ - | \$ 7,369,472 |
| Federal contributions | - | - | 1,128,679 | - | - | 1,128,679 |
| Other grants | - | - | - | - | 248,153 | 248,153 |
| Total revenues | <u>1,207,973</u> | <u>174,819</u> | <u>1,128,679</u> | <u>-</u> | <u>248,153</u> | <u>8,746,304</u> |
| Expenditures by function: | | | | | | |
| Current: | | | | | | |
| General government | - | 174,819 | 53,606 | - | 66,731 | 769,324 |
| Economic development | - | - | - | - | - | 626,270 |
| Education | 1,207,973 | - | 536,669 | - | 2,860 | 4,369,059 |
| Health services | - | - | 479,642 | - | 13,420 | 2,578,554 |
| Environment protection and sanitation | - | - | 58,762 | - | 38,941 | 276,896 |
| Total expenditures | <u>1,207,973</u> | <u>174,819</u> | <u>1,128,679</u> | <u>-</u> | <u>121,952</u> | <u>8,620,103</u> |
| Net change in fund balances | - | - | - | - | 126,201 | 126,201 |
| Fund balances at the beginning of the year | - | - | - | 740,298 | 472,444 | 1,261,721 |
| Fund balances at the end of the year | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 740,298</u> | <u>\$ 598,645</u> | <u>\$ 1,387,922</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Account,
and Changes in Fund Balances
Year Ended September 30, 2015

| | Section 211(a)(1) Education Sector | Section 211(a)(2) Health Sector | Section 211(a)(3) Private Sector Development | Section 211(a)(4) Capacity Building | Section 211(a)(5) Environment | Section 211(a)(6) |
|--|---|--|---|--|-------------------------------------|----------------------|
| Revenues: | | | | | | |
| Compact funding | \$ 2,621,557 | \$ 2,085,492 | \$ 626,270 | \$ 447,451 | \$ 179,193 | \$ 26,717 |
| Federal contributions | - | - | - | - | - | - |
| Other grants | - | - | - | - | - | - |
| Total revenues | <u>2,621,557</u> | <u>2,085,492</u> | <u>626,270</u> | <u>447,451</u> | <u>179,193</u> | <u>26,717</u> |
| Expenditures by account: | | | | | | |
| Salaries and wages: | | | | | | |
| Regular | 1,498,161 | 832,384 | 259,138 | 185,647 | 102,673 | - |
| Overtime | - | 96,819 | 7,655 | - | 57 | - |
| Fringe benefits | 207,737 | 104,825 | 36,838 | 17,117 | 14,941 | - |
| Other personnel costs | - | 6,960 | - | - | - | - |
| Travel and transportation | 3,768 | 16,056 | 27,617 | 34,107 | 3,039 | - |
| Communications | 11,422 | 2,708 | 14,339 | 14,019 | 4,529 | - |
| Dues, membership, and subscriptions | - | 1,100 | 1,375 | 1,580 | - | - |
| Food stuffs | 534 | 28,735 | - | - | - | - |
| Port charges | 7,068 | 544 | 968 | - | 54 | - |
| Office supplies and materials | 205,976 | 72,700 | 71,991 | 22,357 | 14,843 | - |
| POL | 46,625 | 10,236 | 14,833 | 2,946 | 4,348 | - |
| Printing and reproduction | 2,592 | 4,272 | 176 | - | 2,978 | - |
| Rental services | 849 | 1,275 | 140 | - | 304 | - |
| Repairs and maintenance | 11,567 | 2,300 | 1,659 | 175 | 5,427 | - |
| Utilities | 85,795 | 178,160 | 19,458 | 3,300 | 4,055 | - |
| Medical referral | - | 100,242 | - | - | - | - |
| Medical supplies | - | 396,037 | - | - | - | - |
| Contractual services | 124,721 | 89,646 | 145,650 | 86,309 | 19,588 | 26,717 |
| Professional services | - | 7,174 | - | - | - | - |
| Scholarships and allowances | 236,318 | - | 440 | - | 1,260 | - |
| Training | - | 63,793 | 15,404 | 52,457 | - | - |
| Leased housing, buildings and land | 33,466 | 29,370 | - | 13,574 | 1,097 | - |
| Nonpayroll compensation | - | - | - | - | - | - |
| Equipment | 144,377 | 40,076 | 5,871 | 13,863 | - | - |
| Miscellaneous | 581 | 80 | 2,718 | - | - | - |
| Total expenditures | <u>2,621,557</u> | <u>2,085,492</u> | <u>626,270</u> | <u>447,451</u> | <u>179,193</u> | <u>26,717</u> |
| Net change in fund balances | - | - | - | - | - | - |
| Fund balances at the beginning of the year | - | - | - | - | - | 48,979 |
| Fund balances at the end of the year | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 48,979</u> |

See Accompanying Independent Auditors' Report.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUND

Combining Statement of Revenues, Expenditures by Account,
and Changes in Fund Balances, Continued
Year Ended September 30, 2015

| | Section 211(a)(7) <u>Supplemental</u> | Enhanced Reporting <u>Accountability</u> | U.S. <u>Federal</u> | Compact <u>Capital</u> | <u>Foreign</u> | <u>Total</u> |
|--|---|--|------------------------|---------------------------|-------------------|---------------------|
| Compact funding | \$ 1,207,973 | \$ 174,819 | \$ - | \$ - | \$ - | \$ 7,369,472 |
| Federal contributions | - | - | 1,128,679 | - | - | 1,128,679 |
| Other grants | - | - | - | - | 248,153 | 248,153 |
| Total revenues | <u>1,207,973</u> | <u>174,819</u> | <u>1,128,679</u> | <u>-</u> | <u>248,153</u> | <u>8,746,304</u> |
| Expenditures by account: | | | | | | |
| Salaries and wages: | | | | | | |
| Regular | 169,234 | 153,311 | 625,121 | - | 16,968 | 3,842,637 |
| Overtime | - | 2,680 | - | - | - | 107,211 |
| Fringe benefits | 20,315 | 18,828 | 83,052 | - | 1,773 | 505,426 |
| Other personnel costs | - | - | - | - | - | 6,960 |
| Travel and transportation | 49,251 | - | 105,852 | - | 14,271 | 253,961 |
| Communications | 16,660 | - | 13,380 | - | 1,832 | 78,889 |
| Dues, membership, and subscriptions | - | - | - | - | - | 4,055 |
| Food stuffs | - | - | 1,320 | - | 10,565 | 41,154 |
| Port charges | 2,165 | - | 33 | - | - | 10,832 |
| Office supplies and materials | 252,755 | - | 140,586 | - | 9,987 | 791,195 |
| POL | 14,594 | - | 24,668 | - | 1,160 | 119,410 |
| Printing and reproduction | 1,172 | - | 2,598 | - | 842 | 14,630 |
| Rental services | 3,048 | - | 4,608 | - | 2,979 | 13,203 |
| Repairs and maintenance | 573 | - | 1,256 | - | 700 | 23,657 |
| Utilities | 37,493 | - | 10,121 | - | 1,850 | 340,232 |
| Medical referral | - | - | - | - | - | 100,242 |
| Medical supplies | - | - | 2,321 | - | - | 398,358 |
| Contractual services | 373,906 | - | 82,920 | - | 56,466 | 1,005,923 |
| Professional services | - | - | - | - | - | 7,174 |
| Scholarships and allowances | (5,000) | - | 5,520 | - | - | 238,538 |
| Training | 142,551 | - | 4,597 | - | - | 278,802 |
| Leased housing, buildings and land | 32,444 | - | - | - | - | 109,951 |
| Nonpayroll compensation | 10,446 | - | - | - | - | 10,446 |
| Equipment | 81,945 | - | 10,694 | - | - | 296,826 |
| Miscellaneous | 4,421 | - | 10,032 | - | 2,559 | 20,391 |
| Total expenditures | <u>1,207,973</u> | <u>174,819</u> | <u>1,128,679</u> | <u>-</u> | <u>121,952</u> | <u>8,620,103</u> |
| Net change in fund balances | - | - | - | - | 126,201 | 126,201 |
| Fund balances at the beginning of the year | - | - | - | 740,298 | 472,444 | 1,261,721 |
| Fund balances at the end of the year | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 740,298</u> | <u>\$ 598,645</u> | <u>\$ 1,387,922</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 Lyndon Jackson
Governor, State of Kosrae
Federated States of Micronesia:

We have audited, 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, the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of State of Kosrae as of and for the year ended September 30, 2015, and the related notes to the financial statements, which collectively comprise State of Kosrae's basic financial statements, and have issued our report thereon dated June 17, 2016.

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 Kosrae Port Authority and the Kosrae Utilities 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. 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 State of Kosrae'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 State of Kosrae's internal control. Accordingly, we do not express an opinion on the effectiveness of State of Kosrae'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. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Questioned Costs as item 2015-001, that we consider to be material weaknesses.

Compliance and Other Matters

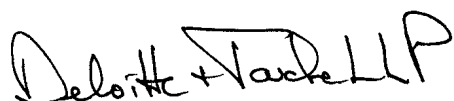
As part of obtaining reasonable assurance about whether State of Kosrae's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material 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*.

State of Kosrae's Response to Findings

State of Kosrae's response to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. State of Kosrae's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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.

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is stylized, with the "D" and "T" being particularly prominent.

June 17, 2016

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 Lyndon Jackson
Governor, State of Kosrae
Federated States of Micronesia:

Report on Compliance for Each Major Federal Program

We have audited State of Kosrae's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of State of Kosrae's major federal programs for the year ended September 30, 2015. State of Kosrae'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, State of Kosrae's basic financial statements include the operations of certain entities whose federal awards are not included in the accompanying Schedule of Expenditures of Federal Awards for the year ended September 30, 2015. 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 State of Kosrae'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 State of Kosrae'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 State of Kosrae's compliance.

Opinion on Each Major Federal Program

In our opinion, State of Kosrae 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 major federal programs for the year ended September 30, 2015.

Report on Internal Control Over Compliance

Management of State of Kosrae 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 State of Kosrae'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 State of Kosrae's internal control over compliance.

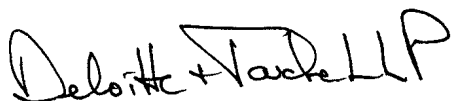
A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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 State of Kosrae as of and for the year ended September 30, 2015, and the related notes to the financial statements, which collectively comprise State of Kosrae's basic financial statements. We issued our report thereon dated June 17, 2016, which contained unmodified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. 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 stylized, with the "D" and "T" being particularly prominent.

June 17, 2016

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Expenditures of Federal Awards, by Grantor
Year Ended September 30, 2015

| Agency/Program | Expenditures |
|--|---------------------|
| U.S. Department of Agriculture | \$ 85,138 |
| U.S. Department of the Interior | 7,396,705 |
| U.S. Department of Education | 536,669 |
| U.S. Department of Health and Human Services | <u>479,639</u> |
| GRAND TOTAL | <u>\$ 8,498,151</u> |

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

| | | |
|---|--------|---------------------|
| U.S. Department of Agriculture: | | |
| Cooperative Forestry Assistance | 10.664 | 7,550 |
| Urban and Community Forestry Program | 10.675 | 14,463 |
| Forest Legacy Program | 10.676 | 115 |
| Forest Stewardship Program | 10.678 | 8,900 |
| Community Facilities Loans and Grants | 10.766 | <u>26,374</u> |
| | | <u>57,402</u> |
| Reconciliation to the basic financial statements: | | |
| Grants Assistance Fund expenditures | | \$ 8,620,103 |
| Less: | | |
| Foreign Assistance Fund expenditures | | <u>(121,952)</u> |
| | | <u>\$ 8,498,151</u> |

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2015

| Agency/Program | CFDA# | Expenditures |
|---|---------------------|---------------------|
| U.S. DEPARTMENT OF AGRICULTURE | | |
| Cooperative Forestry Assistance | 10.664 | 19,366 |
| Urban and Community Forestry Program | 10.675 | 22,618 |
| Forest Legacy Program | 10.676 | 115 |
| Forest Stewardship Program | 10.678 | 16,665 |
| Community Facilities Loans and Grants | 10.766 | 26,374 |
| Total U.S. Department of Agriculture | | <u>\$ 85,138</u> |
| U.S. DEPARTMENT OF THE INTERIOR | | |
| Economic, Social and Political Development of the Territories: | | |
| Compact of Free Association Sector Grants: | 15.875 | |
| Compact Special Block | | \$ - |
| Compact Special Development | | - |
| Compact Energy Block Grant | | - |
| Compact Health & Medical | | - |
| Compact II Education Sector | | 2,621,557 |
| Compact II Health Sector | | 2,085,494 |
| Compact II Private Sector Development | | 626,270 |
| Compact II Capacity Building | | 447,451 |
| Compact II Environment | | 179,193 |
| Compact II Infrastructure Sector | | 26,717 |
| Supplemental Education Grant | | 1,207,973 |
| Compact II ERA | | 174,819 |
| Historic Preservation Fund Grants-In Aid | 15.904 | 27,231 |
| Total U.S. Department of the Interior | | <u>\$ 7,396,705</u> |
| U.S. DEPARTMENT OF EDUCATION | | |
| Special Education - Grants to States | 84.027A | \$ 536,669 |
| Total U.S. Department of Education | | <u>\$ 536,669</u> |
| U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES | | |
| Affordable Care Act (ACA) Personal Responsibility Education Program | 93.092 | \$ 44,179 |
| Maternal and Child Health Federal Consolidated Programs | 93.110 | 6,294 |
| Project Grants and Cooperative Agreements for Tuberculosis Control Programs | 93.116 | 30,329 |
| Family Planning - Services | 93.217 | 22,280 |
| Consolidated Health Centers (Community Health Centers, MHC, HCH and PHPC) | 93.224 | 4,833 |
| Affordable Care Act (ACA) Abstinence Education Program | 93.235 | 4,020 |
| Grants to States to Support Oral Health Workforce Activities | 93.236 | 1,861 |
| Substance Abuse and Mental Health Services - Projects of Regional and National Significance | 93.243 | 78,047 |
| Universal Newborn Hearing Screening | 93.251 | 4,768 |
| Immunization Cooperative Agreements | 93.268 | 40,901 |
| Centers for Disease Control and Prevention Investigations and Technical Assistance | 93.283 | 68,191 |
| Early Hearing Detection and Intervention Information System Surveillance Program | 93.314 | 1,572 |
| Affordable Care Act-Coordinated Chronic Disease Prevention & Health Promotion | 93.544 | - |
| Preventive Health & Health Services Block Grant funded solely with PPHF | 93.758 | 11,708 |
| Assistance Programs for Chronic Disease Prevention and Control | 93.945 | 40,099 |
| Block Grants for Community Mental Health Services | 93.958 | 3,265 |
| Block Grants for Prevention and Treatment of Substance Abuse | 93.959 | 57,689 |
| Preventive Health and Health Services Block Grant-14 | 93.991 | 5,523 |
| Maternal and Child Health Services Block Grant to the States | 93.994 | 39,519 |
| Cancer Prevention and Control Program (See Note) | 93.U55/CCU923887.02 | 14,561 |
| Total U.S. Department of Health and Human Services | | <u>\$ 479,639</u> |
| TOTAL FEDERAL AWARDS | | <u>\$ 8,498,151</u> |

Note: The grant is received through the University of Hawaii and the grant number is U55/CCU923887.02.

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2015

1. Scope

The State of Kosrae is one of the four States of the Federated States of Micronesia. All significant operations of the State of Kosrae 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 Kosrae'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 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 Kosrae's reporting entity is defined in Note 1A to its September 30, 2015 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 Kosrae, as defined above, for the year ended September 30, 2015.

The federal award totals for the excluded component units as of September 30, 2015, are as follows:

| | | |
|----------------------------|----|---------|
| Kosrae Port Authority | \$ | 0 |
| Kosrae Utilities Authority | \$ | 175,000 |

C. Subgrantees

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

D. Indirect Cost Allocation

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

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2015

2. Summary of Significant Accounting Policies, Continued

E. CFDA #15.875

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

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs
Year Ended September 30, 2015

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? | Yes |
| 3. Significant deficiency(ies) identified? | None reported |
| 4. Noncompliance material to financial statements noted? | No |

Federal Awards

Internal control over major federal programs:

- | | |
|---|------------|
| 5. Material weakness(es) identified? | No |
| 6. Significant deficiency(ies) identified? | None noted |
| 7. Type of auditors' report issued on compliance for major federal programs: | Unmodified |
| 8. Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? | No |
| 9. Identification of major federal programs: | |

| | |
|--------------------|---|
| <u>CFDA Number</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: | \$300,000 |
| 11. Auditee qualified as low-risk auditee? | Yes |

Section II – Financial Statements Findings

| | |
|--------------------|---------------|
| <u>Finding No.</u> | <u>Area</u> |
| 2015-001 | Housing Loans |

Section III - Federal Award Findings and Questioned Cost

No matters were reported.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2015

Finding No.: 2015-001
Area: Housing Loans

Criteria:

Housing loan records of Kosrae Housing Authority should be periodically reconciled and timely recorded. A loan portfolio must be maintained that includes loan account information which is consistent with records from prior years.

Condition:

There was significant variance in prior year account information in the housing loan portfolio. Housing loan records are not timely updated.

Cause:

The cause of this condition is the lack of formal record-keeping procedures for housing loans.

Effect:

The effect of the above condition is noncompliance with the criteria.

Recommendation:

We recommend that the State establish policies and procedures to facilitate appropriate record keeping of housing loans. Kosrae Housing Authority became a component unit in October 2015 and therefore, recorded loan information should be reconciled with the State's books.

Auditee Response and Corrective Action Plan:

Kosrae Housing Authority accepts the finding as provided by the review of the auditors and shall endeavor to make the following actions to correct the deficiencies.

1. With KHA operating its own financial affairs, the reconciliation and records beginning balances FY 2016 shall resolve issues with timelines on account updates. KHA has begun the periodic updates for FY 2016.
2. KHA to engage loan staff to review all loan files and ensure files are complete with all documents.
3. KHA to proceed to purchase new loan software to improve record keeping and accounts reporting.

**STATE OF KOSRAE
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Prior Audit Findings
Year Ended September 30, 2015

There are no unresolved prior audit findings.