

**POHNPEI STATE HOUSING AUTHORITY  
(A COMPONENT UNIT OF THE STATE OF POHNPEI)**

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**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2018 and 2017**

**POHNPEI STATE HOUSING AUTHORITY  
(A COMPONENT UNIT OF THE STATE OF POHNPEI)**

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Years Ended September 30, 2018 and 2017

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## **INDEPENDENT AUDITORS' REPORT**

Board of Directors  
Pohnpei State Housing Authority:

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

We have audited the accompanying financial statements of the Pohnpei State Housing Authority (the "Authority"), a component unit of the State of Pohnpei, which comprise the statements of net position as of September 30, 2018 and 2017, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pohnpei State Housing Authority as of September 30, 2018 and 2017, and the results of its operations and its cash flows, for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matters**

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 to 5 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated June 27, 2019, on our consideration of the Authority'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 solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's 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 Authority's internal control over financial reporting and compliance.

*Deloitte & Touche LLP*

June 27, 2019

**POHNPEI STATE HOUSING AUTHORITY  
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Management's Discussion and Analysis  
Years Ended September 30, 2018 and 2017

Our discussion and analysis of the Pohnpei Housing Authority's (the Authority) financial performance provides an overview of the Authority's financial activities for the fiscal years ended September 30, 2018 and 2017. Please read it in conjunction with the Authority's financial statements, which follows this section.

**FINANCIAL HIGHLIGHTS**

- For fiscal year ended September 30, 2018, the Authority's net operating revenues decreased by \$45,490 or 17% from prior year's \$271,497. The decrease in revenues was mainly due to the reduction of \$42,406 or 20% from the interest and fees on loans.
- During the year, the Authority's total expenses increased by \$15,053 or 9% to \$183,433 from prior year.
- For fiscal year 2018, the Authority collected an aggregate amount of \$194,222 representing the actual interest and fees paid by customers on loans.

**Overview of the Financial Statements**

The financial statements presented herein include all of the activities of the Authority included in this report are the statement of net position and the statement of revenues, expenses, and changes in net position. These financial statements present the complete financial picture of the Authority from the economic measurement focus substantially using the accrual basis of accounting. The Authority operated on an annual budget appropriated by the Legislature, which accounted for by the Pohnpei State Department of Treasury.

Financial Analysis

**Net Position**

The statement of net position presents the financial position or condition of the Authority and it shows the information on all of the Authority's assets and liabilities, with the difference between the two reported as net position. This financial statement communicates the lending ability of the Authority through the turnover of its receivables. The passage of time and/or increases or decreases in net position may serve as a usual indicator whether the financial position of the Authority is improving or deteriorating.

The following table summarizes the Statements of Net Position for FY2018, FY2017, and FY2016:

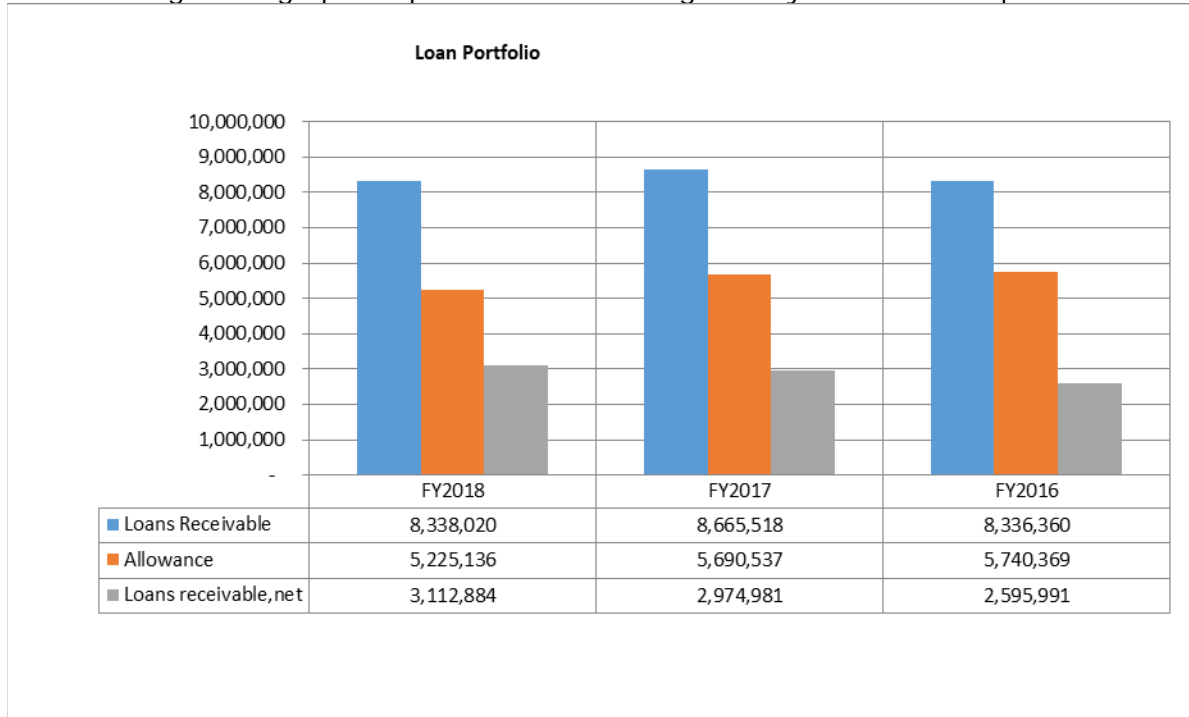
	<u>2018</u>	<u>2017</u>	<u>2016</u>
Other assets	\$ 3,560,052	\$ 3,359,808	\$ 3,089,333
Capital assets, net	<u>44,047</u>	<u>52,706</u>	<u>61,344</u>
Total assets	<u>\$ 3,604,099</u>	<u>\$ 3,412,514</u>	<u>\$ 3,150,677</u>
Liabilities	<u>\$ 145,812</u>	<u>\$ 113,752</u>	<u>\$ 69,919</u>
Net position:			
Net investment in capital assets	44,047	52,706	61,344
Restricted	<u>3,414,240</u>	<u>3,246,056</u>	<u>3,019,414</u>
	<u>3,458,287</u>	<u>3,298,762</u>	<u>3,080,758</u>
Total liabilities and net position	<u>\$ 3,604,099</u>	<u>\$ 3,412,514</u>	<u>\$ 3,150,677</u>

Total net position increased by \$159,525 or 5% during fiscal year 2018. In addition, other major account changes compared from prior year were as follows: Other assets increased by \$200,244 or 6% due to higher net loan balances. For additional information concerning capital assets, please refer to Note 4 to the financial statements.

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Management's Discussion and Analysis  
Years Ended September 30, 2018 and 2017

The following is the graphical presentation showing the 3-year trend loan portfolio of PSHA:



**OVERVIEW OF THE FINANCIAL STATEMENTS**

**Changes in Net Position**

The statement of revenues, expenses, and changes in net position shows the result of operation of the Authority. It reports the revenues earned and expenses incurred and it indicated the effect on the net position of the Authority.

The table below shows the changes in net position for the year ended September 30, 2018, 2017 and 2016:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Operating revenues:			
Interest and fees on loans	\$ 165,151	\$ 207,557	\$ 192,363
Other	<u>6,825</u>	<u>7,914</u>	<u>10,523</u>
Total operating revenues	171,976	215,471	202,886
Recovery of loan losses	<u>54,031</u>	<u>56,026</u>	<u>177,162</u>
Net operating revenues	<u>226,007</u>	<u>271,497</u>	<u>380,048</u>
Operating expenses:			
Salaries	100,397	92,014	90,913
Travel and transportation	20,910	14,942	10,666
Depreciation	17,643	16,184	16,027
Contractual services	10,500	15,702	8,198
Utilities	6,292	5,082	3,532
Repairs and maintenance	5,466	5,623	4,153
Supplies and materials	5,077	4,710	3,785
Training	4,650	-	-
Communication	3,641	3,773	2,295

**POHNPEI STATE HOUSING AUTHORITY  
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Management's Discussion and Analysis  
Years Ended September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Operating expenses, Continued:			
Miscellaneous	<u>8,857</u>	<u>10,350</u>	<u>11,504</u>
Total operating expenses	<u>183,433</u>	<u>168,380</u>	<u>151,073</u>
Operating income	42,574	103,117	228,975
Non-operating revenues:			
Operating subsidy from PSG	<u>116,951</u>	<u>114,887</u>	<u>115,578</u>
Change in net position	\$ <u>159,525</u>	\$ <u>218,004</u>	\$ <u>344,553</u>

**Outlook**

It is the Authority's goal and mission to provide safe, decent and sanitary housing at low cost for the people of Pohnpei. To reduce the delinquency rate and improve customer servicing and lending in FY 2019, the Authority shall continuously pursue aggressive collection which include filing in court of delinquent accounts to foreclose its collateral.

Management's Discussion and Analysis for the year ended September 30, 2017, is set forth in the Authority's report on the audit of financial statements, which is dated June 22, 2018. That Discussion and Analysis explains the major factors impacting the 2017 financial statements and can be viewed at the Office of the Public Auditor's website at [www.fsmopa.fm](http://www.fsmopa.fm).

**Contacting the PSHA's Financial Management**

This Management's Discussion and Analysis is designed to provide our citizens, taxpayers, customers, creditors, and other interested parties, with a general overview of the Pohnpei State Housing Authority's finances and to demonstrate PSHA's accountability and transparency for the appropriations it receives. Questions concerning any of the information provided in this discussion and analysis or request for additional information should be addressed to the Executive Director, Pohnpei State Housing Authority P.O. Box 1109, Kolonia, Pohnpei FM 96941, or call (691) 320-4225 or (691) 320-2582.

**POHNPEI STATE HOUSING AUTHORITY  
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Statements of Net Position  
September 30, 2018 and 2017

<u>ASSETS</u>	<u>2018</u>	<u>2017</u>
Assets:		
Cash	\$ 406,460	\$ 319,337
Employee advances, net of an allowance for doubtful accounts of \$155,229 in 2018 and 2017	-	-
Due from primary government	17,899	20,435
Loans receivable, net	3,112,884	2,974,981
Interest receivable	21,781	44,027
Prepaid expense	1,028	1,028
Property and equipment, net	44,047	52,706
	<u>\$ 3,604,099</u>	<u>\$ 3,412,514</u>
<u>LIABILITIES AND NET POSITION</u>		
Liabilities:		
Accrued liabilities	\$ 40,985	\$ 22,088
Due to primary government	104,827	91,664
Total liabilities	<u>145,812</u>	<u>113,752</u>
Commitments and contingencies		
Net position:		
Net investment in capital assets	44,047	52,706
Restricted	3,414,240	3,246,056
Total net position	<u>3,458,287</u>	<u>3,298,762</u>
	<u>\$ 3,604,099</u>	<u>\$ 3,412,514</u>

See accompanying notes to financial statements.



**POHNPEI STATE HOUSING AUTHORITY**  
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Statements of Revenues, Expenses and Changes in Net Position  
Years Ended September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Operating revenues:		
Interest and fees on loans	\$ 165,151	\$ 207,557
Other	<u>6,825</u>	<u>7,914</u>
Total operating revenues	171,976	215,471
Recovery of loan losses	<u>54,031</u>	<u>56,026</u>
Net operating revenues	226,007	271,497
Operating expenses:		
Salaries	100,397	92,014
Travel and transportation	20,910	14,942
Depreciation	17,643	16,184
Contractual services	10,500	15,702
Utilities	6,292	5,082
Repairs and maintenance	5,466	5,623
Supplies and materials	5,077	4,710
Training	4,650	-
Communication	3,641	3,773
Miscellaneous	<u>8,857</u>	<u>10,350</u>
Total operating expenses	<u>183,433</u>	<u>168,380</u>
Operating income	42,574	103,117
Nonoperating revenues:		
Operating subsidy from primary government	<u>116,951</u>	<u>114,887</u>
Change in net position	159,525	218,004
Net position at beginning of year	<u>3,298,762</u>	<u>3,080,758</u>
Net position at end of year	<u>\$ 3,458,287</u>	<u>\$ 3,298,762</u>

See accompanying notes to financial statements.

**POHNPEI STATE HOUSING AUTHORITY**  
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Statements of Cash Flows  
Years Ended September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Cash received from customers	\$ 194,222	\$ 193,224
Cash paid to suppliers for goods and services	(46,496)	(53,431)
Cash paid to employees	(100,397)	(92,014)
Net cash provided by operating activities	<u>47,329</u>	<u>47,779</u>
Cash flows from noncapital financing activities:		
Increase in due to primary government	13,163	37,082
Operating subsidy received from primary government	124,779	116,464
Net cash provided by noncapital financing activities	<u>137,942</u>	<u>153,546</u>
Cash flows from capital and related financing activities:		
Acquisition of fixed assets	(14,276)	(7,546)
Cash flows from investing activities:		
Loan originations and principal collections, net	(83,872)	(322,964)
Net change in cash	87,123	(129,185)
Cash at beginning of year	<u>319,337</u>	<u>448,522</u>
Cash at end of year	<u>\$ 406,460</u>	<u>\$ 319,337</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 42,574	\$ 103,117
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	17,643	16,184
Recovery of loan losses	(54,031)	(56,026)
Decrease (increase) in interest receivable	22,246	(22,247)
Increase in accrued liabilities	18,897	6,751
Net cash provided by operating activities	<u>\$ 47,329</u>	<u>\$ 47,779</u>

See accompanying notes to financial statements.

**POHNPEI STATE HOUSING AUTHORITY  
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Notes to Financial Statements  
September 30, 2018 and 2017

(1) Organization and Summary of Significant Accounting Policies

Organization

The Pohnpei State Housing Authority (the "Authority" or "PSHA") was established in 1988 by Pohnpei State Public Law 2L-81-88. The purpose of the Authority is to facilitate, through low-interest loans, the construction of safe and sanitary residential housing for low income families of Pohnpei State. Additionally, the Authority monitors the Housing Preservation Grant (HPG) loan funds extended by the United States Department of Agriculture (USDA) Rural Development through the Housing and Community Facilities Program.

The affairs of the Authority are managed by a five-member Board of Directors, consisting of representatives of the Pohnpei State Government appointed by the Governor to four-year terms. Daily operation of the Authority is delegated to an executive director, who is also appointed by the Governor and serves at the pleasure of the Board.

The Authority's financial statements are incorporated into the financial statements of the Pohnpei State Government as a component unit.

Basis of Accounting

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America as applicable to governmental entities, specifically proprietary funds.

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments: Omnibus*, and modified by Statement No. 38, *Certain Financial Statement Note Disclosures*, establishes financial reporting standards for governmental entities which require that management's discussion and analysis of the financial activities be included with the financial statements and notes and modifies certain other financial statement disclosure requirements.

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of the fund are included in the statements of net position. Proprietary fund operating statements present increases and decreases in net position. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Authority considers interest income and costs that are directly related to lending operations to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

Net Position

Net position represents the residual interest in the Authority's assets after liabilities are deducted and consist of three sections: net investment in capital assets; restricted and unrestricted. Net position classified as net investment in capital assets, include capital assets, restricted and unrestricted, net of accumulated depreciation and reduced by outstanding debt net of debt service reserve. Net position are reported as restricted when constraints are imposed by third parties or enabling legislation. The Authority's restricted assets are expendable, and are restricted for loan programs.

**POHNPEI STATE HOUSING AUTHORITY  
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Notes to Financial Statements  
September 30, 2018 and 2017

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

Budget

The Authority operates on an annual budget appropriated by the Legislature which is accounted for by the Pohnpei State Department of Treasury. Appropriation Acts require that funds be administered in accordance with the provisions of the Financial Management Act. The enabling legislation does provide the Authority the power to expend revenues generated by projects maintained by the Authority. Such expenditures must, however, be in accordance with the provisions of the Financial Management Act and other applicable laws and regulations.

Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses.

Cash

Custodial credit risk is the risk that in the event of a bank failure, the Authority'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 Authority does not have a deposit policy for custodial credit risk.

For the purposes of the statements of net position and cash flows, cash is defined as cash in checking accounts, savings accounts and cash on hand. As of September 30, 2018 and 2017, cash carrying value was \$406,460 and \$319,337, respectively, which corresponding bank balances of \$413,639 and \$339,618, respectively, maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2018 and 2017, \$374,681 and \$320,170, respectively, in total banks deposits were FDIC insured. The Authority has not experienced any losses in such accounts and management believes it is not exposed to any significant credit risk on its deposits.

Loans and Allowance for Loan Losses

Loans receivable are stated at unpaid principal balance less the allowance for loan losses.

Management maintains the allowance for loan losses at a level adequate to absorb probable losses. Management determines the adequacy of the allowance based upon reviews of individual loans, recent loss experience, current economic conditions, the risk characteristics of the various categories of loans and other pertinent factors. Loans deemed uncollectible are written off and charged to the allowance. Provisions for losses and recoveries on loans previously charged off are added to the allowance.

Interest on loans is accrued and credited to income based on the principal amount outstanding. The accrual of interest on loans is discontinued when, in the opinion of management, there is an indication that the borrower may be unable to meet payments as they become due. Upon such discontinuance, all unpaid accrued interest is reversed.

**POHNPEI STATE HOUSING AUTHORITY  
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Notes to Financial Statements  
September 30, 2018 and 2017

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

Property and Equipment

Property and equipment are stated at cost. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the respective assets, which range from three to ten years. The Authority capitalizes all fixed assets, irrespective of value, that have estimated useful lives of more than one year.

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefit accrues to employees. No liability is recorded for nonvesting accumulating rights to receive sick leave pay benefits. The related sick leave pay expense is recorded when the benefit is actually taken.

New Accounting Standards

During the year ended September 30, 2018, PSHA implemented the following pronouncements, which did not have a material effect on the accompanying financial statements:

- GASB 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.
- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement.
- GASB Statement No. 85, *Omnibus 2017*, which addresses practice issues that have been identified during implementation and application of certain GASB Statements including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits).
- GASB Statement No. 86, *Certain Debt Extinguishment Issues*, which improves consistency in accounting and financial reporting for in-substance defeasance of debt.

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which addresses accounting and financial reporting for certain asset retirement obligations (AROs) associated with the retirement of a tangible capital asset. The provisions in Statement No. 83 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

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Notes to Financial Statements  
September 30, 2018 and 2017

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

New Accounting Standards, Continued

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*, which establishes criteria for identifying fiduciary activities of all state and local governments. The provisions in Statement No. 84 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2017, GASB issued Statement No. 87, *Leases*, which establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. The provisions in Statement No. 87 are effective for fiscal years beginning after December 15, 2019. Management has yet to determine whether the implementation of this statement will have a material effect on the financial statements.

In April 2018, GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*, which improves the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. The provisions in Statement No. 88 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2018, GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, which requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. The provisions in Statement No. 89 are effective for fiscal years beginning after December 15, 2019. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In August 2018, GASB issued Statement No. 90, *Majority Equity Interests – an Amendment of GASB Statements No. 14 and No. 61*, which improves the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and the relevance of financial statement information for certain component units. The provisions in Statement No. 90 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

(2) Due From (To) Primary Government

Due from primary government represents the accumulation of the unobligated portion of the State of Pohnpei (the State) appropriations. Due to primary government represents loans provided to the Authority by the State as a result of loan guarantees issued by the State to USDA (note 3).

**POHNPEI STATE HOUSING AUTHORITY  
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Notes to Financial Statements  
September 30, 2018 and 2017

(3) Loans Receivable

The Authority's loan portfolio is comprised of three loan funds - Pohnpei State Housing Authority (PSHA) loan fund, the Housing Preservation Grant (HPG) loan fund, and USDA Rural Development ("USDA RD") loans.

The PSHA loans derive from the capital contributions of Compact of Free Association Capital Account Funds - Capital Projects by Pohnpei State to fund the Housing Development Loan Fund. The HPG loans are from a grant extended by the United States Department of Agriculture (USDA) Rural Development through the Housing and Community Facilities Program.

During the years ended September 30, 2009 and 2010, the State of Pohnpei transferred to the Authority defaulted USDA RD loans, which the State had guaranteed. The Authority bears responsibility for collection and returning the collections to Pohnpei State Government (PSG) for approximately \$500,000 of the balance. The Authority is not responsible for the ultimate recovery of these balances and as such, no liability beyond what has been collected has been recorded in the accompanying financial statements. At September 30, 2018 and 2017, cumulative unremitted collections due to PSG were \$104,827 and \$91,664, respectively.

A summary of loans receivable as of September 30, 2018 and 2017, is presented below:

	<u>2018</u>	<u>2017</u>
Pohnpei State Housing Authority loans	\$ 6,874,788	\$ 7,128,922
HPG loans	325,170	399,449
USDA RD loans	<u>1,138,062</u>	<u>1,137,147</u>
	8,338,020	8,665,518
Less allowance for loan losses	<u>(5,225,136)</u>	<u>(5,690,537)</u>
Loans receivable, net	\$ <u>3,112,884</u>	\$ <u>2,974,981</u>

Recovery of loan losses of \$54,031 and \$56,026 for the years ended September 30, 2018 and 2017, respectively, represents change in assessed requirements of allowance for loan losses. During the years ended September 30, 2018 and 2017, loan charge-offs totalled \$387,386 and \$0, respectively.

All loans, other than the USDA RD loans, bear interest rate fixed substantially at 4.5% with terms ranging from 3 to 25 years. The USDA RD loans are non-interest bearing.

(4) Property and Equipment

Capital asset activities for the years ended September 30, 2018 and 2017, is as follows:

	Estimated <u>Useful Life</u>	Balance at October <u>1, 2017</u>	Additions and <u>Transfers</u>	Deletions and <u>Transfers</u>	Balance at September <u>30, 2018</u>
Depreciable:					
Building	10 years	\$ 126,408	\$ -	\$ -	\$ 126,408
Machinery and equipment	3-5 years	212,181	7,899	(123,793)	96,287
Other equipment	2 years	12,409	-	-	12,409
Improvements	10 years	<u>9,447</u>	<u>6,377</u>	<u>-</u>	<u>15,824</u>
		360,445	14,276	(123,793)	250,928
Less accumulated depreciation		<u>(307,739)</u>	<u>(17,643)</u>	<u>118,501</u>	<u>(206,881)</u>
		\$ <u>52,706</u>	\$ <u>(3,367)</u>	\$ <u>(5,292)</u>	\$ <u>44,047</u>

**POHNPEI STATE HOUSING AUTHORITY  
(A COMPONENT UNIT OF THE STATE OF POHNPEI)**

Notes to Financial Statements  
September 30, 2018 and 2017

(4) Property and Equipment, Continued

Depreciable:	<u>Estimated Useful Life</u>	Balance at October <u>1, 2016</u>	Additions and <u>Transfers</u>	Deletions and <u>Transfers</u>	Balance at September <u>30, 2017</u>
Building	10 years	\$ 126,408	\$ -	\$ -	\$ 126,408
Machinery and equipment	3-5 years	204,635	7,546	-	212,181
Other equipment	2 years	12,409	-	-	12,409
Improvements	10 years	<u>9,447</u>	<u>-</u>	<u>-</u>	<u>9,447</u>
		352,899	7,546	-	360,445
Less accumulated depreciation		<u>(291,555)</u>	<u>(16,184)</u>	<u>-</u>	<u>(307,739)</u>
		\$ <u>61,344</u>	\$ <u>(8,638)</u>	\$ <u>-</u>	\$ <u>52,706</u>

(5) Commitments and Contingencies

Loan Commitments

The Authority has loan commitments aggregating \$250,864 as of September 30, 2018. These loan commitments represent undisbursed balances of approved loans for housing projects.

Litigation

The Authority is party to various legal proceedings. The Attorney General of the Pohnpei State Government is of the opinion that the probable outcome of such cases existing at September 30, 2018, is not predictable. No provision for any liability has been made in the accompanying financial statements because management believes that no unfavorable outcome is likely to occur.

Risk Management

The Authority is essentially self-insured for potential losses. Management is of the opinion that no material losses during the past three years have resulted from this practice.

(6) Related Parties

As of September 30, 2018 and 2017, the Authority has \$151,319 and \$158,749, respectively, of loans receivable from employees. Additionally, outstanding advances to former and current employees totaling of \$155,229 are fully provided with an allowance.



**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**

The Board of Directors  
Pohnpei State Housing Authority:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Pohnpei State Housing Authority (the "Authority"), which comprise the statements of net position as September 30, 2018, and the related statements of revenues, expenses and changes in net position and of cash flows for the year then ended and the related notes to the financial statements, and have issued our report thereon dated June 27, 2019.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Authority'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority'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 have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in accompanying Schedule of Findings and Responses as items 2018-001 and 2018-002 that we consider to be significant deficiencies.

## Compliance and Other Matters

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

## The Authority's Response to Findings

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

## Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results 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.

*Deloitte & Touche LLP*

June 27, 2019

**POHNPEI STATE HOUSING AUTHORITY  
(A COMPONENT UNIT OF THE STATE OF POHNPEI)**

Schedule of Findings and Responses  
Year Ended September 30, 2018

Finding No.: 2018-001

Loan Receivable

Criteria: Measures and actions should be strengthened to improve the collection of delinquent loans and maintenance of loan portfolio.

Condition: The following loan receivable matters were noted:

- At September 30, 2018, a significant portion of the Authority's loan portfolio represent delinquent loans. Specifically, of the Authority's total housing and HPG loans of approximately \$7.20 million, \$3.47 million relate to loans that have no transactions (payments or disbursements) during the year. Additionally, \$0.32 million of the remaining loans are six months or over past due.
- Adjustments by the Authority's consultant to decrease the allowance by \$962,654 for the year ended September 30, 2018 has no evidence of review and approval.

Cause: The cause of the above condition appears to be the lack of adequate controls over loan collections and the lack of appropriate loan origination controls to eligible and qualified borrowers in the past years which contributed to loan defaults.

Effect: The effect of the above condition is the accumulation of uncollectible receivables and misstatement of loans receivable.

Recommendation: The Authority should perform a review of existing collection measures and strategies, including policies over loan write-offs. Additionally, the Authority should strengthen its procedures over maintenance of the loan portfolio.

Identification as a Repeat Finding: Finding 2017-001

Auditee Response and Corrective Action Plan: We agree with your finding. With a Collection Officer on board and monthly meetings with the Attorney General's Office, we will see some improvement but we are not sure we will be able have significant impact on old delinquent accounts due to the purpose of lending to low income families and legal prohibition on property sales.

**POHNPEI STATE HOUSING AUTHORITY  
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Schedule of Findings and Responses  
Year Ended September 30, 2018

Finding No.: 2018-002

Loan Application

Criteria: All loan applications and disbursements should adhere to the Authority's Rules and Regulations.

Condition: Nine of seventeen new loan accounts (loan nos. 1670, 1651, 1680, 1666, 1673, 1693, 1695, 1649 and 1701) tested did not have one or more of the following documents in file as required by the Authority's Rules and Regulations:

- Property inspection;
- Development plan;
- Property map;
- Scope of work;
- Contractor agreements;
- Power of attorney;
- Mortgage agreement; or
- Land-certificate of title.

Additionally, for three of the seventeen new loans (loan no. 1683, 1693 and 1695) and for seven of the fifty-seven prior year loans (loan nos. 1477, 1476, 600,1640, 1584, 1442 and 1386) tested, the total loan disbursements per the disbursements journal exceeded approved loan amount. The Authority was not able to provide a reconciliation on the differences.

Cause: The cause of the above condition is potentially ineffective loan package monitoring and filing system.

Effect: The effect of the above condition is potential noncompliance with the Authority's Rules and Regulations, which may contribute to insufficient loan documentation to support future loan collection efforts.

Recommendation: The Authority should take reasonable steps to document compliance with loan application rules and regulations.

Identification as a Repeat Finding: Finding 2017-002

Auditee Response and Corrective Action Plan: We disagree with the finding because we always ensure that loan approval conditions are met prior to disbursement. It is the filing of loan documents that needs improvement.

Auditor Response: The Auditee may be correct but until the unlocated documentation is located, the finding remains.

**POHNPEI STATE HOUSING AUTHORITY  
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Unresolved Prior Year Findings  
Year Ended September 30, 2018

Summary Schedule of Prior Audit Findings

<u>Finding Number</u>	<u>Finding Title</u>	<u>Status</u>
2017-001	Loan Receivable	Partially Corrected
2017-002	Loan Application	Not Corrected or Resolved