

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2011

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

YEAR ENDED SEPTEMBER 30, 2011

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FEDERATED STATES OF MICRONESIA**

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**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2011

INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei (the State) as of and for the year ended September 30, 2011, which collectively comprise the State's basic financial statements as set forth in Section II of the foregoing table of contents. These financial statements are the responsibility of the management of the State. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation, which represents 4%, 1% and 3%, respectively, of the assets, net assets and operating revenues of the State's discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation, is based solely on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

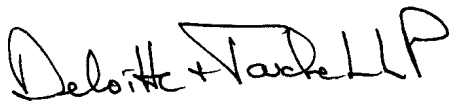
In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei as of September 30, 2011, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, during the year ended September 30, 2011, the State adopted Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 25, 2012, 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* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis, on pages 3 through 10, as well as the Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund and notes thereto, as set forth in Section III of the foregoing table of contents, are not a required part of the basic financial statements but are supplementary information required by GASB. This supplementary information is the responsibility of the management of the State. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the State's respective financial statements that collectively comprise the State's basic financial statements. The combining and individual fund financial statements, as set forth in Section IV of the foregoing table of contents, which are also the responsibility of the management of the State, are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such additional information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

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

June 25, 2012

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011

This section of the Pohnpei State's financial report presents our Management's Discussion and Analysis (MD&A) for the fiscal year ended September 30, 2011. This MD&A is prepared in compliance with the GASB 34 requirement. Readers are requested to read this MD&A in conjunction with the State's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The Pohnpei State's primary government's total net assets for this year are \$39,982,553.
- The net change in government fund balance is a decrease of \$2,627,091. Total revenues reported are \$30,812,334 against total expenditures of \$33,439,425.
- Actual revenues for the general fund were \$825,650 higher than budgeted revenues. The total expenditures-budgetary basis showed a favorable variance of \$745,214. The general fund reported an unassigned fund balance of \$1,605,147 for the fiscal year.

OVERVIEW OF THE FINANCIAL STATEMENTS

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

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

Government-Wide Financial Statements

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

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

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

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

Fund Financial Statements

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011

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

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

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

	<u>Government Activities</u>	
	<u>2011</u>	<u>2010</u>
Current and other assets	\$ 13,147,163	\$ 15,199,269
Capital assets	25,021,890	26,375,497
Other noncurrent assets	<u>13,811,519</u>	<u>13,537,676</u>
Total assets	<u>51,980,572</u>	<u>55,112,442</u>
Current liabilities	5,693,761	4,844,205
Long-term debt and other liabilities	<u>6,304,258</u>	<u>6,545,171</u>
Total liabilities	<u>11,998,019</u>	<u>11,389,376</u>
Net assets:		
Invested in capital assets, net of related debt	25,021,890	26,375,497
Restricted	19,002,982	19,870,850
Unrestricted	<u>(4,042,319)</u>	<u>(2,523,281)</u>
Total net assets	\$ <u>39,982,553</u>	\$ <u>43,723,066</u>

Changes in net assets. The State's Statement of Changes in Net Assets for the fiscal year ended September 30 follows:

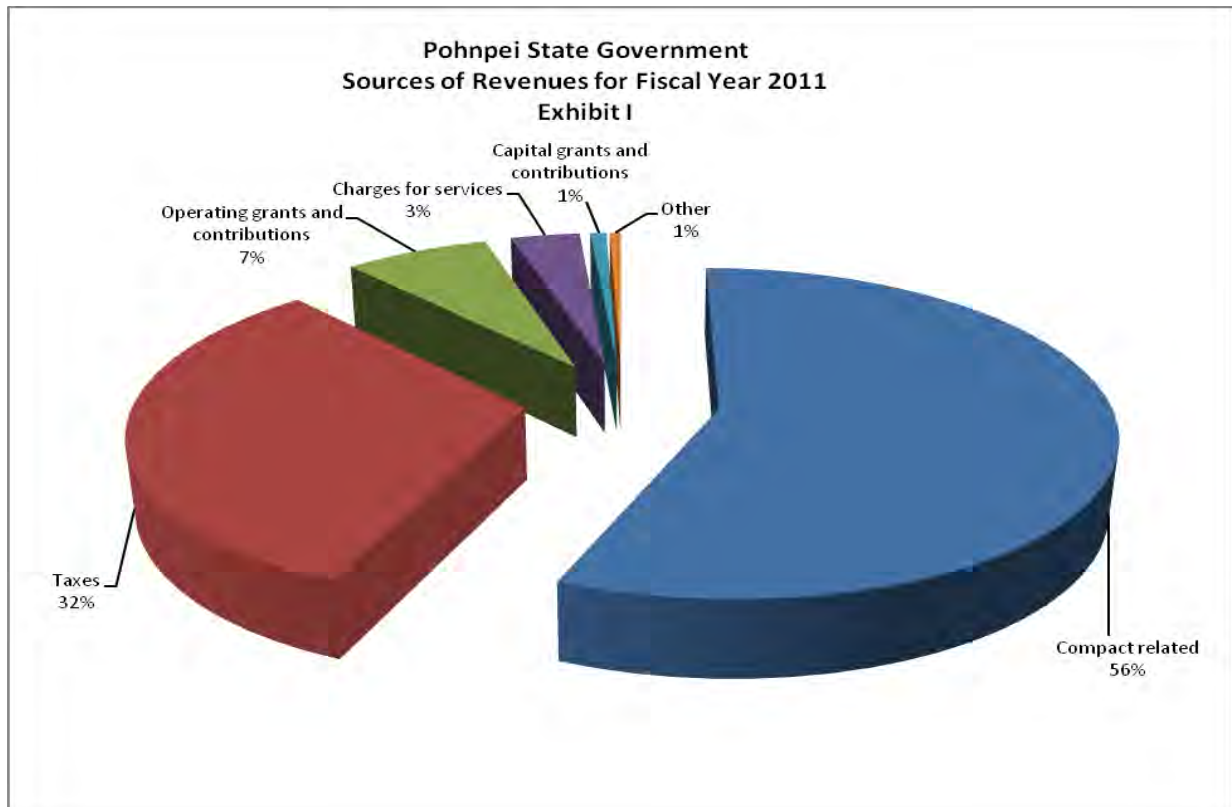
	<u>Government Activities</u>	
	<u>2011</u>	<u>2010</u>
Revenues:		
Program revenues:		
Charges for services	\$ 1,037,338	\$ 1,226,274
Operating grants and contributions	2,158,214	4,352,898
Compact related	17,421,510	17,680,454
Capital grants and contributions	239,825	4,039,825

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011

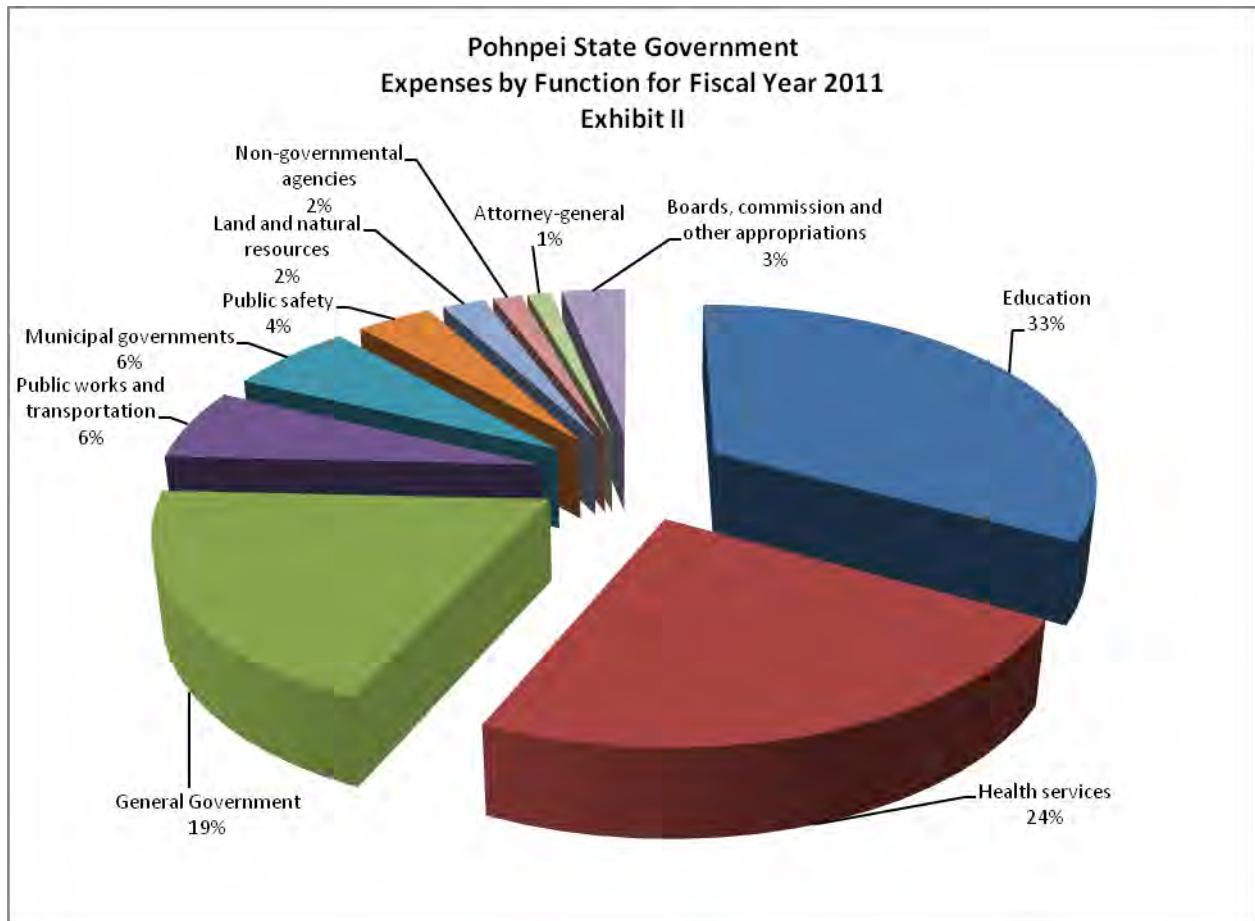
General revenues:		
Taxes	9,890,775	9,815,533
Investment earnings (loss)	(99,063)	574,823
Other	<u>163,735</u>	<u>574,651</u>
Total revenues	<u>30,812,334</u>	<u>38,264,458</u>
Expenses:		
General Government	6,537,413	6,792,085
Education	11,447,386	12,047,239
Health services	8,162,052	7,128,173
Land and natural resources	740,744	431,471
Public works and transportation	2,181,453	2,404,162
Public safety	1,323,370	1,362,735
Boards, commission and other appropriations	<u>4,160,429</u>	<u>4,455,681</u>
Total expenses	<u>34,552,847</u>	<u>34,621,546</u>
Change in net assets	\$ <u>(3,740,513)</u>	\$ <u>3,642,912</u>

Exhibit I, below, showed that 56% of the State's revenues were derived from Compact II while 32% came from taxes and licenses. Exhibit II, next page, illustrated that Education represented 33% of the State's total expenses followed by Health Services at 24%.



**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011



FINANCIAL ANALYSIS OF THE STATE'S GOVERNMENTAL FUNDS

The State's governmental fund changes in fund balances for the year ended September 30, 2011 are shown below.

	General Fund		Grants Assistance		Compact Trust		Other Funds	
	2011	2010	2011	2010	2011	2010	2011	2010
Revenues:								
Taxes	\$ 9,313,288	\$ 9,285,034	\$ -	\$ -	\$ -	\$ -	\$ 577,487	\$ 530,499
Compact	-	-	17,421,510	17,680,454	-	-	-	-
Other/transfers in	<u>158,154</u>	<u>1,357,890</u>	<u>2,651,076</u>	<u>2,609,123</u>	<u>(113,182)</u>	<u>1,790,787</u>	<u>1,420,543</u>	<u>1,345,688</u>
Total revenues	9,471,442	10,642,924	20,072,586	20,289,577	(113,812)	1,790,787	1,998,030	1,876,187
Expenditures/transfers out	<u>11,079,734</u>	<u>10,921,737</u>	<u>20,082,302</u>	<u>20,127,564</u>	-	-	<u>2,893,931</u>	<u>1,392,939</u>
Net change in fund balances	<u>\$ (1,608,292)</u>	<u>\$ (278,813)</u>	<u>\$ (9,716)</u>	<u>\$ 162,013</u>	<u>\$ (113,182)</u>	<u>\$ 1,790,787</u>	<u>\$ (895,901)</u>	<u>\$ 483,248</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011

General Fund

Revenues decreased by \$1,171,482 or 11% compared to fiscal year 2010. The decrease was caused by lower Other Revenues by \$497,149 and a decrease in fair value of investments by \$673,886. Expenditures decreased by \$150,984 or 1.4% compared to fiscal year 2010; however, the State recorded transfers out of \$308,981 in 2011 as local match under the Compact IMF program compared with none in fiscal year 2010.

Grants Assistance Fund

As mentioned in the preceding paragraph, Compact II/Sector Grants were the major sources of Pohnpei State's operating grants for fiscal year 2011. The total Compact II/Sector funding amounted to \$17,421,510 while total expenditures are in the amount of \$17,421,510, which is discussed below:

- The education sector grant that shall support and improve the educational system of the Federated States of Micronesia, including, without limitation, the systems for primary, secondary, and post-secondary education. Total revenues are \$7,649,066 against total expenditures of the same amount, an increase of \$241,804 or 3% compared to fiscal year 2010.
- The health sector grant that shall support and improve the delivery of preventive, curative and environmental care, and develop the human and material resources necessary for the Federated States of Micronesia to perform these services. Total revenue equals total expenditures in the amount of \$5,869,580, an increase of \$58,474 or 1% compared to fiscal year 2010.
- The sector grant for private sector development shall support the efforts of the Federated States of Micronesia to attract new foreign investment and increase indigenous business activity. Priorities will be in advancing the private development of fisheries, tourism and agriculture; employing new telecommunications technologies; and analyzing and developing new systems, laws, and policies to foster private sector development, to facilitate investment by potential private investors, and develop business and entrepreneurial skills. For fiscal years 2011 and 2010, Pohnpei State did not receive funding from private sector development.
- The sector for capacity building shall support the efforts of the Federated States of Micronesia to build effective, accountable and transparent national and local government and other public sector institutions and systems. Total grant revenues and expenditures are \$457,654, a decrease of \$31,762 or 6% compared to fiscal year 2010.
- The environment sector shall support the efforts of the Federated States of Micronesia to protect the Nation's land and marine environment and to conserve and achieve sustainable use of its natural resources. Total revenue is \$433,771 with the same total expenditures, an increase of \$107,842 or 33% compared to fiscal year 2010.
- Public Infrastructure grant shall give priority to primary and secondary education capital projects and programs that directly affect health and safety including water and wastewater projects, solid waste disposal projects and health care facilities. Total revenue is \$1,751 with the same total of expenditures, a decrease of \$373,249 and \$238,074, respectively, compared to fiscal year 2010.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011

- The Supplemental Education Grant (SEG) is considered the seventh-sector grant. SEG has been offered in lieu of grants that were formerly available from various federal agencies. The federal programs that were incorporated into SEG are Territories and Freely Associated States Education Grant, Adult Education & Family Literacy, Workforce Investment Act, Pacific Vocational Education Improvement Program and Early Childhood Program (formerly Head Start). For the year, total revenues and expenditures amounted to \$3,009,688, a decrease of \$262,053 or 8% compared to fiscal year 2010.

Another major source of funding under Grants Assistance Fund is the US Federal Grants which supported \$2,380,002 of expenditures of the State, a decrease of \$29,412 or 1% compared to fiscal year 2010.

General Fund Budgetary Highlights

During the year, the State revised its budget several times in the aggregate amount of \$1,330,931 to accommodate supplemental funding for departments and offices requiring increases in appropriations to avoid budget overruns. These matters are not believed to have a significant effect on future services. The State conforms to the most appropriate measures of utilizing its net assets due to the current global economic crisis.

The net decrease in the State's general fund unassigned fund balance of \$2,105,956 compared with net decrease of \$178,618 in fiscal year 2010. During the year ended September 30, 2011, the State implemented GASB Statement No. 54. Refer to Note 1 for additional information regarding implementation.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

The State's capital assets at the end of fiscal year 2011 consist basically of equipment, buildings, roads and bridges. Increase in capital assets was due to purchases of machinery, equipment and others under the Infrastructure Account. The summary of capital assets at the end of September 30 is shown below:

	<u>Primary Government Governmental Activities</u>	
	<u>2011</u>	<u>2010</u>
Buildings	\$ 13,728,473	\$ 13,728,473
Infrastructure	52,446,727	52,446,727
Machinery	<u>22,199,300</u>	<u>21,467,832</u>
Total	\$ <u>88,374,500</u>	\$ <u>87,643,032</u>

Note 5 to the Financial Statements presents more information about the State's capital assets.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011

Long-Term Debt

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

	<u>Governmental Activities</u>	
	<u>2011</u>	<u>2010</u>
Asian Development Bank loans	\$ <u>5,815,013</u>	\$ <u>5,964,852</u>

Note 6 to the financial statements presents more information about the State's long-term debt.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

Funding for the operations of most of the government services in fiscal year 2012 will still come from the Compact II.

Fiscal year 2012 is the ninth year of the implementation of the economic assistance under the Compact II/Sector Grant. Sector funding replaces the funding sources from the old Compact I. Under the Compact II/Sector grant, the annual budget approved by JEMCO for fiscal year 2012 is as follows:

- For Education Sector Grant, which continues to be the funding priority, the annual budget is \$7,460,773.
- The Health Sector Grant's budget is \$5,944,305.
- The Private Sector Development Sector Grant's budget is \$136,000.
- The Public Sector Capacity Building Sector Grant budget is \$456,975.
- The Environment Sector Grant is \$453,094.
- The cumulative grants for the Public Infrastructure from fiscal years 2005 through 2011 is more than \$40,000,000. Priority projects are education, health related and private sector development. It is required that 5% of the total grant be allocated to the Infrastructure Maintenance fund for the maintenance of the existing and new projects. Local matching of the same amount is required.
- In the case of the Supplemental Education Grant (SEG), the total funding for fiscal year 2012 is \$2,978,120. The programs covered in the funding are Early Childhood Education, Education Improvement Programs, Workforce Development/Skill Training, Vocational Education and Staff Development.

For fiscal year 2012, the locally generated revenues, investment income and the revenue shares from the FSM National Government are projected at about \$10,600,000. These projected revenues were about \$1,100,000 more compared with fiscal year 2011 revenues. The increase is due mainly to projected increase in investment income of about \$700,000 and revenue share of \$300,000. In its effort to close possible shortage, the Department of Treasury and Administration will continue to intensify its collection effort to raise more revenues in the ensuing year. In addition, the final carry-over balances from the Compact II may be authorized to be used to fund other operations of the government.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Management's Discussion and Analysis
September 30, 2011

FINANCIAL CONTACT

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Net Assets
September 30, 2011

	Primary Government	Component Units
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ 3,000	\$ 3,725,165
Investments	8,230,795	174,257
Receivables, net of allowance for uncollectibles	4,319,175	4,106,846
Advances	140,302	10,832
Inventories	29,946	1,461,489
Due from component units	200,000	76,561
Restricted assets:		
Cash and cash equivalents	223,945	734,253
Total current assets	13,147,163	10,289,403
Noncurrent assets:		
Capital assets, net of accumulated depreciation	25,021,890	31,977,666
Investments	1,500,000	383,573
Receivables	-	937,773
Other	-	229,868
Restricted assets:		
Cash and cash equivalents	-	349,500
Investments	12,311,519	145,112
Total noncurrent assets	38,833,409	34,023,492
Total assets	\$ 51,980,572	\$ 44,312,895
<u>LIABILITIES</u>		
Current liabilities:		
Receivables, net	\$ -	\$ -
Current portion of long-term obligations	170,759	217,015
Note payable	-	190,000
Bank overdraft	586,647	-
Accounts payable	1,570,000	1,176,763
Current portion of compensated absences payable	400,000	-
Other liabilities and accruals	1,543,092	891,760
Due to primary government	-	1,637,001
Deferred revenues	1,423,263	184,005
Total current liabilities	5,693,761	4,296,544
Noncurrent liabilities:		
Long-term obligations, net of current portion	5,644,254	8,417,394
Compensated absences payable, net of current portion	449,036	-
Claims and judgments payable	210,968	-
Total noncurrent liabilities	6,304,258	8,417,394
Total liabilities	11,998,019	12,713,938
Contingencies and commitments		
<u>NET ASSETS</u>		
Invested in capital assets, net of related debt	25,021,890	23,672,341
Restricted for:		
Nonexpendable:		
Future operations	9,120,962	-
Expendable:		
Compact related	2,048,304	-
Capital projects	208,474	-
Debt service	3,306,657	-
Other purposes	4,318,585	3,374,814
Unrestricted	(4,042,319)	4,551,802
Total net assets	39,982,553	31,598,957
Total liabilities and net assets	\$ 51,980,572	\$ 44,312,895

See accompanying notes to basic financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Activities
Year Ended September 30, 2011

Functions/Programs	Program Revenues			Net (Expenses) Revenues and Changes in Net Assets		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government	Component Units
Primary government:						
Governmental activities:						
General government	\$ 6,537,413	362,046	\$ 784,570	\$ 239,825	\$ (5,150,972)	\$ -
Land and natural resources	740,744	57,306	123,233	-	(560,205)	-
Education	11,447,386	-	11,741,537	-	294,151	-
Health services	8,162,052	568,285	7,043,566	-	(550,201)	-
Public safety	1,323,370	49,701	-	-	(1,273,669)	-
Attorney-general	409,350	-	-	-	(409,350)	-
Public works and transportation	2,181,453	-	-	-	(2,181,453)	-
Non-governmental agencies	490,615	-	-	-	(490,615)	-
Boards, commissions and others	1,014,924	-	-	-	(1,014,924)	-
Municipal governments	2,165,719	-	-	-	(2,165,719)	-
Payments to PTA	24,771	-	-	-	(24,771)	-
Future operations	-	-	(113,182)	-	(113,182)	-
Unallocated interest on long-term debt	55,050	-	-	-	(55,050)	-
Total primary government	\$ 34,552,847	\$ 1,037,338	\$ 19,579,724	\$ 239,825	(13,695,960)	-
Component units:						
Pohnpei Utilities Corporation	\$ 16,211,625	\$ 14,002,210	\$ -	\$ -	-	(2,209,415)
Pohnpei Port Authority	2,343,002	2,326,793	-	-	-	(16,209)
Pohnpei Transportation Authority	305,513	114,112	-	-	-	(191,401)
Small Business Guarantee and Finance Corporation	160,652	92,612	-	-	-	(68,040)
Pohnpei State Housing Authority	145,188	256,499	-	-	-	111,311
Total component units	\$ 19,165,980	\$ 16,792,226	\$ -	\$ -	-	(2,373,754)
General revenues:						
Taxes:						
FSM revenue sharing:						
Gross revenue taxes						
					2,214,811	-
					2,268,381	-
					1,976,616	-
					331,258	-
					3,099,709	-
					(99,063)	-
					163,735	544,519
					9,955,447	544,519
					(3,740,513)	(1,829,235)
					43,723,066	33,428,192
					\$ 39,982,553	\$ 31,598,957

See accompanying notes to basic financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Balance Sheet
Governmental Funds
September 30, 2011

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
ASSETS					
Cash and cash equivalents	\$ 3,000	\$ -	\$ -	\$ -	\$ 3,000
Investments	5,621,811	4,108,984	-	-	9,730,795
Receivables, net:					
Taxes	1,668,605	2,088,707	-	-	3,757,312
Other	548,870	3,928	-	9,065	561,863
Due from component units	200,000	-	-	-	200,000
Due from other funds	4,108,836	2,085,802	-	4,359,971	10,554,609
Advances	57,104	80,579	-	2,619	140,302
Inventories	-	-	-	29,946	29,946
Restricted assets:					
Cash and cash equivalents	75,096	148,849	-	-	223,945
Investments	3,190,557	-	9,120,962	-	12,311,519
Total assets	<u>\$ 15,473,879</u>	<u>\$ 8,516,849</u>	<u>\$ 9,120,962</u>	<u>\$ 4,401,601</u>	<u>\$ 37,513,291</u>

LIABILITIES AND FUND BALANCES

Liabilities:					
Bank overdraft	\$ 586,647	\$ -	\$ -	\$ -	\$ 586,647
Accounts payable	819,261	682,507	-	68,232	1,570,000
Other liabilities and accruals	1,313,308	228,756	-	1,028	1,543,092
Deferred revenues	-	1,423,263	-	-	1,423,263
Due to other funds	6,445,773	4,095,083	-	13,753	10,554,609
Total liabilities	<u>9,164,989</u>	<u>6,429,609</u>	<u>-</u>	<u>83,013</u>	<u>15,677,611</u>
Fund balances:					
Non-spendable	757,104	1,080,579	9,120,962	32,565	10,991,210
Restricted	3,306,657	2,017,900	-	-	5,324,557
Committed	357,190	-	-	4,176,213	4,533,403
Assigned	282,792	37,158	-	165,721	485,671
Unassigned:					
General fund	1,605,147	-	-	-	1,605,147
Special revenue funds	-	(1,048,397)	-	(55,911)	(1,104,308)
Total fund balances	<u>6,308,890</u>	<u>2,087,240</u>	<u>9,120,962</u>	<u>4,318,588</u>	<u>21,835,680</u>
Total liabilities and fund balances	<u>\$ 15,473,879</u>	<u>\$ 8,516,849</u>	<u>\$ 9,120,962</u>	<u>\$ 4,401,601</u>	

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

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	25,021,890
Long-term liabilities, including loans payable, are not due and payable in the current period and, therefore, are not reported in the funds. The liabilities include:	
Long-term debt payable	(5,815,013)
Compensated absences payable	(849,036)
Claims and judgments payable	(210,968)
	<u>(6,875,017)</u>
Net assets of governmental activities	<u>\$ 39,982,553</u>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
Year Ended September 30, 2011

	General	Special Revenue Grants Assistance	Permanent Compact Trust	Other Governmental Funds	Total
Revenues:					
Compact funding	\$ -	\$ 17,421,510	\$ -	\$ -	\$ 17,421,510
Net change in the fair value of investments	(99,063)	-	(113,182)	-	(212,245)
CFSM grants	-	94,969	-	-	94,969
Federal contributions and other grants	-	2,416,252	-	-	2,416,252
FSM revenue sharing	6,791,066	-	-	-	6,791,066
State taxes	2,522,222	-	-	577,487	3,099,709
Fees and charges	233,337	-	-	804,001	1,037,338
Other	23,880	139,855	-	-	163,735
Total revenues	<u>9,471,442</u>	<u>20,072,586</u>	<u>(113,182)</u>	<u>1,381,488</u>	<u>30,812,334</u>
Expenditures:					
Current:					
General government	3,957,133	1,173,966	-	1,440,168	6,571,267
Land and natural resources	586,335	123,233	-	-	709,568
Education	2,318	11,741,537	-	-	11,743,855
Health services	820	7,043,566	-	1,146,202	8,190,588
Public safety	1,377,929	-	-	-	1,377,929
Office of the Attorney-General	409,350	-	-	-	409,350
Public works	535,950	-	-	-	535,950
Payments to non-governmental agencies	490,615	-	-	-	490,615
Boards, commissions and other	1,014,924	-	-	-	1,014,924
Grants to local governments	2,165,719	-	-	-	2,165,719
Pohnpei Transportation Authority	24,771	-	-	-	24,771
Debt service	204,889	-	-	-	204,889
Total expenditures	<u>10,770,753</u>	<u>20,082,302</u>	<u>-</u>	<u>2,586,370</u>	<u>33,439,425</u>
Deficiency of revenues under expenditures	(1,299,311)	(9,716)	(113,182)	(1,204,882)	(2,627,091)
Other financing sources (uses):					
Operating transfers in	-	-	-	616,542	616,542
Operating transfers out	(308,981)	-	-	(307,561)	(616,542)
Other financing sources (uses), net	<u>(308,981)</u>	<u>-</u>	<u>-</u>	<u>308,981</u>	<u>-</u>
Net change in fund balances	(1,608,292)	(9,716)	(113,182)	(895,901)	(2,627,091)
Fund balances at the beginning of the year	7,917,182	2,096,956	9,234,144	5,214,489	24,462,771
Fund balances at the end of the year	<u>\$ 6,308,890</u>	<u>\$ 2,087,240</u>	<u>\$ 9,120,962</u>	<u>\$ 4,318,588</u>	<u>\$ 21,835,680</u>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Reconciliation of the Statement of Revenues, Expenditure, and Changes in Fund
Balances of Governmental Funds to the Statement of Activities
Year Ended September 30, 2011

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

Net change in fund balances - total governmental funds	\$ (2,627,091)
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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	(1,353,607)
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The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction has any effect on net assets. For the current year, these amounts consist of:

Repayment of ADB Loans	149,839
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Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds. For the current year, these activities consist of:

Change in compensated absences payable	<u>90,346</u>
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Change in net assets of governmental activities	\$ (<u>3,740,513</u>)
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See accompanying notes to basic financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Combining Statement of Net Assets
Component Units
September 30, 2011

	Pohnpei Utilities Corporation	Pohnpei Port Authority	Pohnpei Transportation Authority	Small Business Guarantee and Finance Corporation	Pohnpei State Housing Authority	Total
ASSETS						
Current assets:						
Cash and cash equivalents	\$ 141,181	\$ 3,278,093	\$ -	\$ 300	\$ 305,591	\$ 3,725,165
Investments	174,257	-	-	-	-	174,257
Receivables, net	1,847,911	219,030	2,924	-	2,036,981	4,106,846
Inventories	1,444,787	-	16,702	-	-	1,461,489
Advances	-	8,517	-	2,315	-	10,832
Other	71,422	3,711	-	-	1,428	76,561
Restricted assets:	-	-	-	-	-	-
Cash and cash equivalents	-	-	-	734,253	-	734,253
Total current assets	<u>3,679,558</u>	<u>3,509,351</u>	<u>19,626</u>	<u>736,868</u>	<u>2,344,000</u>	<u>10,289,403</u>
Noncurrent assets:						
Receivables, net	-	-	-	937,773	-	937,773
Capital assets, net of accumulated depreciation	25,575,338	6,179,459	5,561	95,242	122,066	31,977,666
Long-term deposits	383,573	-	-	-	-	383,573
Restricted:	-	-	-	-	-	-
Cash and cash equivalents	349,500	-	-	-	-	349,500
Investments	145,112	-	-	-	-	145,112
Other	-	229,868	-	-	-	229,868
Total noncurrent assets	<u>26,453,523</u>	<u>6,409,327</u>	<u>5,561</u>	<u>1,033,015</u>	<u>122,066</u>	<u>34,023,492</u>
Total assets	<u>\$ 30,133,081</u>	<u>\$ 9,918,678</u>	<u>\$ 25,187</u>	<u>\$ 1,769,883</u>	<u>\$ 2,466,066</u>	<u>\$ 44,312,895</u>
LIABILITIES						
Current liabilities:						
Current portion of long-term debt	\$ 217,015	\$ -	\$ -	\$ -	\$ -	\$ 217,015
Note payable	190,000	-	-	-	-	190,000
Accounts payable	980,780	147,018	48,965	-	-	1,176,763
Other liabilities and accruals	204,894	156,878	14,134	9,751	506,103	891,760
Due to primary government	200,000	-	1,437,001	-	-	1,637,001
Deferred revenue	180,831	-	3,174	-	-	184,005
Total current liabilities	<u>1,973,520</u>	<u>303,896</u>	<u>1,503,274</u>	<u>9,751</u>	<u>506,103</u>	<u>4,296,544</u>
Noncurrent liabilities:						
Noncurrent portion of long-term debt	8,417,394	-	-	-	-	8,417,394
Total liabilities	<u>10,390,914</u>	<u>303,896</u>	<u>1,503,274</u>	<u>9,751</u>	<u>506,103</u>	<u>12,713,938</u>
NET ASSETS (DEFICIENCY)						
Invested in capital assets, net of related debt	17,401,879	6,169,659	5,561	95,242	-	23,672,341
Restricted	145,112	-	-	1,633,705	1,595,997	3,374,814
Unrestricted	2,195,176	3,445,123	(1,483,648)	31,185	363,966	4,551,802
Total net assets (deficiency)	<u>19,742,167</u>	<u>9,614,782</u>	<u>(1,478,087)</u>	<u>1,760,132</u>	<u>1,959,963</u>	<u>31,598,957</u>
	<u>\$ 30,133,081</u>	<u>\$ 9,918,678</u>	<u>\$ 25,187</u>	<u>\$ 1,769,883</u>	<u>\$ 2,466,066</u>	<u>\$ 44,312,895</u>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Combining Statement of Revenues, Expenses, and Changes in Net Assets
Component Units
Year Ended September 30, 2011

	Pohnpei Utilities Corporation	Pohnpei Port Authority	Pohnpei Transportation Authority	Small Business Guarantee and Finance Corporation	Pohnpei State Housing Authority	Total
Operating revenues:						
Charges for services	\$ 12,707,857	\$ 2,293,720	\$ 114,112	\$ 92,612	\$ 256,499	\$ 15,464,800
Sales	1,294,353	33,073	-	-	-	1,327,426
Total operating revenues	<u>14,002,210</u>	<u>2,326,793</u>	<u>114,112</u>	<u>92,612</u>	<u>256,499</u>	<u>16,792,226</u>
Operating expenses:						
Cost of services	13,025,487	-	-	-	-	13,025,487
Administration costs	971,604	1,937,094	296,572	149,421	134,098	3,488,789
Depreciation and amortization	2,214,534	405,908	8,941	11,231	11,090	2,651,704
Total operating expenses	<u>16,211,625</u>	<u>2,343,002</u>	<u>305,513</u>	<u>160,652</u>	<u>145,188</u>	<u>19,165,980</u>
Operating income (loss)	<u>(2,209,415)</u>	<u>(16,209)</u>	<u>(191,401)</u>	<u>(68,040)</u>	<u>111,311</u>	<u>(2,373,754)</u>
Nonoperating revenues (expenses):						
Contributions from the primary government	442,352	-	-	117,000	130,590	689,942
Interest income (expense)	(119,260)	8,571	-	2,855	-	(107,834)
Other	-	-	12,436	(50,025)	-	(37,589)
Total nonoperating revenues (expenses), net	<u>323,092</u>	<u>8,571</u>	<u>12,436</u>	<u>69,830</u>	<u>130,590</u>	<u>544,519</u>
Change in net assets	(1,886,323)	(7,638)	(178,965)	1,790	241,901	(1,829,235)
Net assets (deficiency) at the beginning of the year	<u>21,628,490</u>	<u>9,622,420</u>	<u>(1,299,122)</u>	<u>1,758,342</u>	<u>1,718,062</u>	<u>33,428,192</u>
Net assets (deficiency) at the end of the year	<u>\$ 19,742,167</u>	<u>\$ 9,614,782</u>	<u>\$ (1,478,087)</u>	<u>\$ 1,760,132</u>	<u>\$ 1,959,963</u>	<u>\$ 31,598,957</u>

See accompanying notes to basic financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies

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

A. Reporting Entity

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

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

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

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

Discretely Presented Component Units:

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

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

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

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

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

Discretely Presented Component Units, Continued:

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

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

B. Government-Wide Financial Statements

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

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

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

- Invested in capital assets, net of related debt 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 assets - 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 assets - expendable consists of resources in which the State is legally or contractually obligated to spend resources in accordance with restrictions either externally imposed by creditors, grantors, contributors, and the like, or imposed by law.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements, Continued

- Unrestricted net assets consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, (for example, internally restricted), to indicate that management does not consider them to be available for general operations.

The government-wide Statement of Net Assets reports \$19,002,980 of restricted net assets, of which \$4,318,585 is restricted by enabling legislation.

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

C. Fund Financial Statements

The fund financial statements present a balance sheet and a statement of revenues, expenditures, and changes in fund balances for its major and aggregated non-major funds.

Major individual governmental funds are reported as separate columns in the fund financial statements pursuant to GASB reporting standards, with nonmajor governmental funds being combined into a single column.

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

D. Measurement Focus and Basis of Accounting

Government-Wide Financial Statements:

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

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

Governmental Fund Financial Statements:

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

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

Component Unit Financial Statements:

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

The State reports the following Governmental Fund types:

i. 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.

ii. Special Revenue Funds

These funds account for specific revenue sources that have been aggregated according to enabling legislation to support specific governmental activities.

iii. Permanent Funds

These funds account for resources that are legally restricted to the extent that only earnings, and not principal, may be used to support programs for the benefit of the government.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(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:

Grants Assistance Fund, a Governmental Fund Type - Special Revenue Fund. This fund 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 Fund, a Governmental Fund Type - Permanent Fund. This fund 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. Reporting Standards

As allowed by GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the State's discretely presented component units follow all GASB pronouncements and those Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins that were issued on or before November 30, 1989, except those that conflict with a GASB pronouncement.

F. Cash and Cash Equivalents

Cash and cash equivalents include cash held in demand accounts as well as short-term investments with maturity dates within three months of the date acquired by the State.

G. Investments

Investments and related investment earnings 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 POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

H. 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 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.

I. 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.

J. Interfund Receivables/Payables

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

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

K. 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.

L. Restricted Assets

Certain assets of the primary government are classified as restricted assets because their use is completely restricted through enabling legislation and loan agreements. Specifically, the State has collateralized investments in the amount of \$3,190,557 for the Pohnpei State Early Retirement Scheme. Furthermore, investments recorded in the Compact Trust Fund of \$9,120,962 are restricted in that they are not available to be used in current operations.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

L. Restricted Assets, Continued

As of September 30, 2011, cash and cash equivalents were restricted for the following uses:

Primary Government:

Deposits with a local bank restricted for the purchase of medical supplies for the State hospital.	\$ 40,223
Savings accounts established in accordance with Section 211(d)(2) of the Compact of Free Association, as amended, for the purpose of funding the State's infrastructure maintenance plan	18,936
Deposit accounts established for the purpose of receiving payments pursuant to the Compact of Free Association, as amended	9,048
Small Business Development Center deposit account	14,589
Loan Guarantee Escrow Account established for the sole purpose of loan collateralization made through the USDA Rural Development. The escrow account may be drawn down in the event of a borrower's default on the obligation under the terms of the promissory note and the deed of trust security instrument supporting such note and for which such note is guaranteed by the Pohnpei State Housing Authority, the trustee of the Loan Guarantee Escrow Account.	<u>141,149</u>
	<u>\$ 223,945</u>

Discretely Presented Component Units:

Pohnpei Utilities Corporation:

Deposit accounts collateralizing loans payable to the FSM Development Bank and the Bank of the FSM	\$ 349,500
Self-insurance fund invested in mutual funds held by a trustee	145,112

Small Business Guarantee and Finance Corporation:

Deposit accounts restricted for various operations of the Small Business Guarantee and Finance Corporation	<u>734,253</u>
	<u>\$ 1,228,865</u>

M. Capital Assets

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

M. Capital Assets, Continued

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

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

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

N. Interfund/Intrafund Transactions

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

O. 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 the rate of 4 hours biweekly, if less than 3 years of service, 6 hours biweekly, if between 3 and 10 years of service, and 8 hours biweekly if over 10 years of service, limited to 45 working days.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

P. Deferred Revenue

In the government-wide financial statements, deferred revenue is recognized when cash, receivables or other assets are recorded prior to their being earned. In the governmental fund financial statements, deferred 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 deferred revenue in the governmental fund financial statements has primarily resulted as federal funds are received in advance of eligible expenditures.

Q. Fund Balance

GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, was implemented, effective for the fiscal year ending September 30, 2011. It establishes fund balance classifications 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. As a result of implementing this statement, there were significant changes in the State’s fund structure. Funds that did not meet the new special revenue fund definition were moved to the General Fund. Amounts previously reported as reserved and unreserved fund balance are now 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.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

R. Risk Financing

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

S. New Accounting Standards

During fiscal year 2011, the State implemented the following pronouncements:

- GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which establishes fund balance classifications that 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 the governmental funds. The Statement requires governments to disclose information in the notes about the processes through which constraints are imposed, as well as accounting policies that determine whether restricted, committed, assigned, and unassigned amounts are considered to be spent. This Statement also provides guidance for classifying stabilization amounts on the face of the balance sheet and requires disclosure of certain information about stabilization arrangements in the notes to the financial statements. As a result of implementation, the Statement of Revenues, Expenditures and Changes in Fund Balance for Governmental Funds have been restated due to reclassification of funds. Beginning fund balance for the Other Governmental Funds decreased by \$3,774,571 while the General Fund increased by the same amount. Details on the State's fund balance classifications are reflected in note 10.
- GASB Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting of certain financial instruments and external investment pools. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

S. New Accounting Standards, Continued

In December 2009, GASB issued Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which amends Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and addresses issues related to measurement of OPEB obligations by certain employers participating in agent multiple-employer OPEB plans. The provisions of Statement 57 related to the use and reporting of the alternative measurement method are effective immediately. The provisions related to the frequency and timing of measurements are effective for actuarial valuations first used to report funded status information in OPEB plan financial statements for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*, which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity*, and No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(1) Summary of Significant Accounting Policies, Continued

S. New Accounting Standards, Continued

In July 2011, GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions* (an amendment of GASB Statement No. 53), which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The provisions of this statement are effective for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

T. Estimates

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

U. 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, 2010 from which summarized information was derived.

(2) Deposits and Investments

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

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.

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:

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(2) Deposits and Investments, Continued

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

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

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

A. Deposits

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1 Deposits that are federally insured or collateralized with securities held by the State or its agent in the State's name;

Category 2 Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the State's name; or

Category 3 Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in the State's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. 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 POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(2) Deposits and Investments, Continued

A. Deposits, Continued

As of September 30, 2011, the carrying amount of the primary government's total cash and cash equivalents were \$226,945 and the corresponding bank balances were \$410,595, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2011, bank deposits were fully FDIC insured.

As of September 30, 2011, the carrying amount of the discretely presented component units' total cash and cash equivalents was \$4,808,918 and the corresponding bank balances were \$4,966,457, which were maintained in financial institutions subject to FDIC insurance. As of September 30, 2011, bank deposits in the amount of \$1,342,121 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

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

Category 1 Investments that are insured or registered, or securities held by the State or its agent in the State's name;

Category 2 Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in the State's name; or

Category 3 Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the State's name.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

Primary Government:

As of September 30, 2011, the State's investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	\$ <u>4,373,698</u>
Other investments:	
Domestic equities	15,628,780
Cash management account	<u>539,836</u>
	<u>16,618,616</u>
	\$ <u><u>20,542,314</u></u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(2) Deposits and Investments, Continued

B. Investments, Continued

Primary Government, Continued:

As of September 30, 2011, the State's fixed income securities, including their Moody's Investors Service credit ratings, had the following maturities:

Investment Type	Investment Maturities (In Years)					Credit Ratings
	Fair Value	Current	1-5	6-10	Over 10	
U.S. Treasury Notes and Bonds	\$ 661,848	\$17,069	\$ 263,623	\$172,267	\$ 208,889	Aaa/AAA
U.S. Government Agency Obligations:						
Federal Home Loan Banks	55,102	-	55,102	-	-	AAA
Federal Home Loan Mortgage Corporation	407,021	-	1,907	23,353	381,761	AAA
Government National Mortgage Association	679,888	-	-	-	679,888	AAA
Federal National Mortgage Association	273,080	28,101	-	14,521	230,458	AAA
Private Export Funding Corporation	92,578	-	92,578	-	-	AAA
Tennessee Valley Authority Bonds	12,285	-	-	-	12,285	AAA
Tennessee Valley Authority Fed Book Notes	69,284	-	-	-	69,284	AAA
Small Business Administration	51,020	-	-	-	51,020	No rating
Housing Urban Development	19,736	-	19,736	-	-	No rating
Financing Corporation	55,921	-	-	55,921	-	No rating
Municipal Obligations	95,546	-	-	20,004	74,542	Aa1
Municipal Obligations	45,116	-	-	-	45,116	Aa2
Municipal Obligations	34,152	-	34,152	-	-	A1/A+
Municipal Obligations	133,044	-	-	-	133,044	A
Municipal Obligations	57,021	-	-	57,021	-	Baa1/BBB+
Corporate Bonds	214,661	-	44,103	48,841	121,717	Aaa/AAA
Corporate Bonds	49,831	-	35,480	14,351	-	Aa1/AA+
Corporate Bonds	101,911	-	60,350	28,040	13,521	Aa2/AA
Corporate Bonds	75,873	-	39,190	36,693	-	Aa3/AA-
Corporate Bonds	133,264	-	65,987	28,512	38,765	A1/A+
Corporate Bonds	268,441	-	224,179	44,262	-	A2/A
Corporate Bonds	248,883	-	141,837	89,528	17,518	A3/A-
Corporate Bonds	120,749	-	110,466	10,283	-	Baa1/BBB+
Corporate Bonds	164,917	-	157,685	-	7,232	Baa2/BBB
Corporate Bonds	253,526	27,619	84,707	9,609	131,591	No rating
	<u>\$4,373,698</u>	<u>\$ 72,789</u>	<u>\$1,431,082</u>	<u>\$653,196</u>	<u>\$2,216,631</u>	

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, 2011.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(2) Deposits and Investments, Continued

B. Investments, Continued

Primary Government, Continued:

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the State. As of September 30, 2011, the State did not hold an investment in any one issuer that represented more than 5% of the State's total investments.

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

As of September 30, 2011, the Grants Assistance Fund holds 5.4% of the outstanding shares of the Bank of the Federated States of Micronesia in the amount of \$500,000 and 19% of the outstanding shares of the Pacific Islands Development Bank in the amount of \$1,000,000. As the fair market value of these investments is not readily available, such have been recorded at cost. Additionally, the State acquired an interest in an airline during fiscal year 2004 and recorded an impairment of such investment in the same period. Financial statements from the investee are not currently available.

Discretely Presented Component Units:

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

Pohnpei Utilities Corporation:	
Mutual funds	\$ <u>319,369</u>

(3) Receivables

Receivables as of September 30, 2011, for the primary government's individual major governmental funds, and nonmajor governmental funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	<u>General</u>	<u>Grants Assistance</u>	<u>Compact Trust</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Receivables:					
Taxes	\$ 1,696,084	\$ 2,542,304	\$ -	\$ 20,740	\$ 4,259,128
Other	<u>4,458,927</u>	<u>3,928</u>	<u>-</u>	<u>562,203</u>	<u>5,025,058</u>
	6,155,011	2,546,232	-	582,943	9,284,186
Allowance for uncollectible accounts	<u>(3,937,536)</u>	<u>(453,597)</u>	<u>-</u>	<u>(573,878)</u>	<u>(4,965,011)</u>
	<u>\$ 2,217,475</u>	<u>\$ 2,092,635</u>	<u>\$ -</u>	<u>\$ 9,065</u>	<u>\$ 4,319,175</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(3) Receivables, Continued

Receivables as of September 30, 2011, for the discretely presented component units, including applicable allowances for uncollectible accounts, are as follows:

	<u>Pohnpei Utilities Corporation</u>	<u>Pohnpei Port Authority</u>	<u>Pohnpei Transportation Authority</u>	<u>Small Business Guarantee and Finance Corporation</u>	<u>Pohnpei State Housing Authority</u>	<u>Total</u>
Loans	\$ -	\$ -	\$ -	\$ 960,140	\$7,026,506	\$ 7,986,646
General	4,914,602	1,905,630	853,313	2,590	-	7,676,135
Other	<u>188,463</u>	<u>-</u>	<u>-</u>	<u>35,731</u>	<u>50,287</u>	<u>274,481</u>
	5,103,065	1,905,630	853,313	998,461	7,076,793	15,937,262
Less: allowance for uncollectibles	<u>(3,255,154)</u>	<u>(1,686,600)</u>	<u>(850,389)</u>	<u>(60,688)</u>	<u>(5,039,812)</u>	<u>(10,892,643)</u>
	<u>\$ 1,847,911</u>	<u>\$ 219,030</u>	<u>\$ 2,924</u>	<u>\$ 937,773</u>	<u>\$ 2,036,981</u>	<u>\$ 5,044,619</u>

(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, 2011, are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Grants Assistance	\$ 4,095,083
General	Nonmajor governmental funds	13,753
Grants Assistance	General	2,085,802
Nonmajor governmental fund	General	<u>4,359,971</u>
		<u>\$ 10,554,609</u>

Receivables and payables between funds reflected as due to/due from components in the Statement of Net Assets at September 30, 2011, are summarized as follows:

<u>Primary Government</u>	<u>Due From</u>	<u>Due To</u>
General Fund:		
Pohnpei Utilities Corporation	\$ <u>200,000</u>	\$ <u>-</u>

The amount recorded as due from component units of the primary government of \$200,000 does not equal the corresponding due to primary government of the discretely presented component units of \$1,637,001 due to an allowance for doubtful accounts recorded by the General Fund of \$1,437,001.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(5) Fixed Assets

Capital asset activities of the primary government for the year ended September 30, 2011, are as follows:

	Balance October <u>1, 2010</u>	<u>Additions</u>	<u>Retirements</u>	Balance September <u>30, 2011</u>
Governmental activities:				
Capital assets, being depreciated:				
Buildings	\$ 13,728,473	\$ -	\$ -	\$ 13,728,473
Machinery, equipment and others	21,467,832	731,468	-	22,199,300
Infrastructure	<u>52,446,727</u>	<u>-</u>	<u>-</u>	<u>52,446,727</u>
Total capital assets, being depreciated	<u>87,643,032</u>	<u>731,468</u>	<u>-</u>	<u>88,374,500</u>
Less accumulated depreciation for:				
Buildings	(4,579,695)	(209,870)	-	(4,789,565)
Machinery, equipment and others	(20,581,801)	(237,391)	-	(20,819,192)
Infrastructure	<u>(36,106,039)</u>	<u>(1,637,814)</u>	<u>-</u>	<u>(37,743,853)</u>
	<u>(61,267,535)</u>	<u>(2,085,075)</u>	<u>-</u>	<u>(63,352,610)</u>
Governmental activities capital assets, net	\$ <u>26,375,497</u>	\$ <u>(1,353,607)</u>	\$ <u>-</u>	\$ <u>25,021,890</u>

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

General government	\$ 112,092
Land and natural resources	48,176
Education	157,325
Health services	107,318
Public safety	14,661
Public works and transportation	<u>1,645,503</u>
	<u>\$ 2,085,075</u>

(6) Long-Term Obligations

Primary Government

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 \$4,200,000 loan from the ADB (Loan Number 1520 (SF)) through the FSM National Government, non-interest bearing with a service charge of 1% per annum on the amount of the loan withdrawn from the Loan Account. The activities of the ERS Program are recorded in the General Fund.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(6) Long-Term Obligations, Continued

Primary Government, Continued

Asian Development Bank (ADB) Loans, Continued:

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

Funds for the repayment of the ADB loan are expected to be derived from the annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The Financing Agreement requires the State to continue to appropriate salaries for the abolished positions and deposit the appropriate funds into the ERS Trust Account. These funds had not been deposited to the Trust Account as of September 30, 2002. Of the required \$4,200,000 identified for future debt service payments, \$3,190,557 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, 2011, the balance payable on this loan amounted to \$4,457,140.

The State also entered into an agreement with the FSM National Government to borrow a portion of the proceeds of the FSM National Government Program Loans with ADB (Loan Number 1873 (SF) and Loan Number 1874 FSM (SF)) for the purpose of promoting private sector development in Pohnpei, with interest at 1% to 1.5% per annum. Principal payments shall be made in 32 equal semi-annual payments with the first payment due on May 15, 2010 and the last payment on November 15, 2025. As of September 30, 2011, the balances payable on these loans amounted to \$550,989 and \$806,884, respectively.

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

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2012	\$ 170,759	\$ 64,947	\$ 235,706
2013	170,759	62,871	233,630
2014	170,759	60,794	231,553
2015	170,759	58,717	229,476
2016	170,759	56,640	227,399
2017-2021	1,241,467	244,294	1,485,761
2022-2026	1,319,410	171,052	1,490,462
2027-2031	1,148,638	102,018	1,250,656
2032-2036	1,058,907	41,176	1,100,083
2037-2039	<u>192,796</u>	<u>1,935</u>	<u>194,731</u>
	<u>\$ 5,815,013</u>	<u>\$ 864,444</u>	<u>\$ 6,679,457</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(6) Long-Term Obligations, Continued

Discretely Presented Component Units

Pohnpei Utilities Corporation (PUC)

Loan payable to the State, facilitated by an Asian Development Bank (ADB) loan (Loan Number 1459-FSM (SF)) to the FSM National Government, original amount of \$2,118,767, due in semi-annual installments of \$33,500 from February 2007 to August 2044. The State has not imposed collateralization on PUC and has waived its rights to receive 6.82% in interest. The loan includes a 1% per annum service charge to be added to the principal until installment payments commence. This service charge was paid by the State during the year ended September 30, 2011. During 2011, an additional \$294,720 was allocated to PUC which extended the maturity date to February 2052. \$ 2,541,872

Loan payable to United States Department of Agriculture, Rural Utilities Service (RUS), original amount of \$578,000, due in monthly installments of \$2,654 from October 2006 to July 2044. The loan is collateralized by a revenue pledge. The loan bears fixed interest of 4.5%. 543,396

Loan payable to bank, original amount of \$773,122, with a 5 year term, interest at 9% per annum, collateralized by a diesel power comprehensive generator plant, two Daihatsu model 12D532 engines, building and materials, and existing and future receivables. Monthly principal and interest installments of \$9,794 from September 2008 with unpaid principal due in August 2013. 608,175

Loan payable to FSM Development Bank (FSMDB), original amount of \$481,701, with a 5 year term, interest at 9% per annum, collateralized by a \$150,000 time certificate of deposit, receivables, inventory and property, plant and equipment. In August 2011, the loan was refinanced to increase borrowing of \$310,950 which was used in operations. Monthly principal and interest installments of \$9,807 from December 31, 2011 to November 26, 2016. 421,584

Loan payable to the State, facilitated by an ADB loan (Loan Number 2099-FSM) to the FSM National Government, original amount of \$3,752,000 due in semi-annual installments of \$85,883 from January 15, 2013 to July 15, 2036. Interest is payable at 1% per annum during the grace period and at 1.5% per annum thereafter. Proceeds were used to fund the overhaul of sewage pumps, extension of sewage lines, and treatment plants. 3,397,609

Loan payable to the State, facilitated by an ADB loan (Loan Number 2100-FSM) to the FSM National Government, original amount of \$2,000,000, due in semi-annual installments of varying amounts through January 15, 2019. Interest is payable at LIBOR plus 0.6% per annum (2.1% at September 30, 2011). Proceeds were used to fund the overhaul of sewage pumps, extension of sewage lines, and treatment plants. 1,121,773

\$ 8,634,409

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(6) Long-Term Obligations, Continued

Discretely Presented Component Units, Continued

Pohnpei Utilities Corporation (PUC), Continued

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

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2012	\$ 217,015	\$ 193,882	\$ 410,897
2013	778,576	194,333	972,909
2014	299,749	140,165	439,914
2015	314,707	127,712	442,419
2016	261,560	113,467	375,027
2017-2021	1,172,757	512,914	1,685,671
2022-2026	1,398,888	405,427	1,804,315
2027-2031	1,435,392	274,422	1,709,814
2032-2036	1,183,470	168,997	1,352,467
2037-2041	398,150	96,090	494,240
2042-2046	366,702	53,928	420,630
2047-2051	301,346	33,654	335,000
2052-2056	316,757	18,243	335,000
2057-2062	<u>189,340</u>	<u>3,098</u>	<u>192,438</u>
	\$ <u>8,634,409</u>	\$ <u>2,336,332</u>	\$ <u>10,970,741</u>

(7) Note Payable

Discretely Presented Component Units

Pohnpei Utilities Corporation (PUC):

Note payable at September 30, 2011 includes borrowings of \$190,000 against a line of credit with the Bank of the Federated States of Micronesia (BFSM). The \$190,000 line is collateralized by a time certificate deposit (TCD) with the bank, bearing variable interest at 5% over the TCD rate (effective rate of 5.75% at September 30, 2011) and expires on May 13, 2012.

Changes in short-term debt of the discretely presented component units is as follows:

	<u>Balance October 1, 2010</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2011</u>
Note payable:				
PUC	\$ _____ -	\$ <u>190,000</u>	\$ _____ -	\$ <u>190,000</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(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, 2011, the following changes occurred in liabilities reported as part of the primary government's long-term liabilities in the statement of net assets:

	Balance October 1, 2010	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2011	Due Within <u>One Year</u>
Loans payable:					
ADB loans:					
Loan 1520	\$ 4,544,810	\$ -	\$ (87,670)	\$ 4,457,140	\$ 96,918
Loan 1873	588,643	-	(37,654)	550,989	37,949
Loan 1874	<u>831,399</u>	<u>-</u>	<u>(24,515)</u>	<u>806,884</u>	<u>35,892</u>
	5,964,852	-	(149,839)	5,815,013	170,759
Other:					
Compensated absences	939,382	509,969	(600,315)	849,036	400,000
Claims	<u>210,968</u>	<u>-</u>	<u>-</u>	<u>210,968</u>	<u>-</u>
	\$ <u>7,115,202</u>	\$ <u>509,969</u>	\$ <u>(750,154)</u>	\$ <u>6,875,017</u>	\$ <u>570,759</u>

Discretely Presented Component Units

During the year ended September 30, 2011, the following changes occurred in long-term obligations of the discretely presented component units:

	Balance October 1, 2010	<u>Additions</u>	<u>Reductions</u>	Balance September 30, 2011	Due Within <u>One Year</u>
Loans payable:					
Pohnpei Utilities Corporation	\$ <u>3,683,912</u>	\$ <u>5,125,052</u>	\$ <u>(174,555)</u>	\$ <u>8,634,409</u>	\$ <u>217,015</u>

(9) Contingencies and Commitments

Sick Leave

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

Encumbrances

The State utilizes encumbrance accounting to identify fund obligations. Encumbrances represent commitments related to unperformed contracts for goods. At September 30, 2011, the State has significant encumbrances summarized as follows:

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(9) Contingencies and Commitments, Continued

Encumbrances, Continued

	<u>General</u>	<u>Grants Assistance</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Encumbrances	\$ <u>282,007</u>	\$ <u>1,906,521</u>	\$ <u>295,355</u>	\$ <u>2,483,883</u>

Federal Grants

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

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

Loan Guarantees

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

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

Litigation

The State is party to several legal proceedings arising from governmental operations. Claims are filed with the State's Attorney General. Approved claims are usually paid under general appropriations to the affected government agency. The State Attorney General is of the opinion that the probable outcome of suits existing at September 30, 2011, is not predictable but could have a material impact on the accompanying financial statements. Such impact has currently been estimated to approximate \$210,968.

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.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(9) Contingencies and Commitments, Continued

Other

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

(10) Fund Balance

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

	General <u>Fund</u>	Grants Assistance <u>Fund</u>	Compact Trust <u>Fund</u>	Nonmajor <u>Funds</u>	Total Governmental <u>Funds</u>
Non-spendable:					
General government	\$ 57,104	\$ 36,694	\$ -	\$ 1,000	\$ 94,798
Economic development	-	-	-	31,565	31,565
Education	-	39,213	-	-	39,213
Health services	-	4,672	-	-	4,672
Pohnpei Utilities Corporation loan	200,000	-	-	-	200,000
Pacific Islands Development Bank	-	1,000,000	-	-	1,000,000
Bank of the FSM	500,000	-	-	-	500,000
Permanent fund principal	-	-	9,120,962	-	9,120,962
Restricted for:					
Debt service	3,306,657	-	-	-	3,306,657
USDA development loans	-	141,149	-	-	141,149
Capital projects	-	1,832,648	-	-	1,832,648
Education	-	43,988	-	-	43,988
Health services	-	115	-	-	115
Committed:					
General government	148,716	-	-	1,973,314	2,122,030
Economic development	-	-	-	404,768	404,768
Environment protection	-	-	-	34,589	34,589
Health services	-	-	-	1,760,414	1,760,414
Boards, commissioner, others	-	-	-	3,128	3,128
ADB private sector development	208,474	-	-	-	208,474
Assigned	282,792	37,158	-	165,721	485,671
Unassigned	<u>1,605,147</u>	<u>(1,048,397)</u>	<u>-</u>	<u>(55,911)</u>	<u>500,839</u>
	<u>\$ 6,308,890</u>	<u>\$ 2,087,240</u>	<u>\$ 9,120,962</u>	<u>\$ 4,318,588</u>	<u>\$ 21,835,680</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Financial Statements
September 30, 2011

(11) Self-Insurance Fund - Component Units

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

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

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

(12) FSM Development Bank Loan Funds

Compact Capital Account funds in an aggregate amount of \$1.7 million were transferred to the control of the FSM Development Bank (FSMDB) (a component unit of the FSM National Government) to be loaned out to borrowers from the State mainly for economic development projects. The loan fund is administered by FSMDB in a Trust capacity. All loan decisions are made by management of the State. These loans are not controlled by the State and are not currently recorded in the accompanying financial statements. As of December 31, 2011 (FSMDB fiscal year end), the outstanding fund balance aggregated \$724,646.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

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

YEAR ENDED SEPTEMBER 30, 2011

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual
General Fund
Year Ended September 30, 2011

	<u>Budgeted Amounts</u>		Actual - Budgetary	Variance with <u>Final Budget -</u>
	<u>Original</u>	<u>Final</u>	Basis (see Note 1)	
Revenues:				
FSM revenue sharing	\$ 5,769,824	\$ 5,769,824	\$ 6,791,066	\$ 1,021,242
State taxes	2,369,055	2,369,055	2,522,222	153,167
Fees and charges	-	-	233,337	233,337
Net change in the fair value of investments	250,000	250,000	(190,976)	(440,976)
Other	165,000	165,000	23,880	(141,120)
Total revenues	<u>8,553,879</u>	<u>8,553,879</u>	<u>9,379,529</u>	<u>825,650</u>
Expenditures:				
Current:				
General government	3,911,646	4,015,246	3,931,104	84,142
Department of Land and Natural Resources	345,516	435,676	589,722	(154,046)
Department of Education	7,318	13,400	3,281	10,119
Department of Health Services	188	165,188	833	164,355
Department of Public Safety	1,310,298	1,378,451	1,390,734	(12,283)
Office of the Attorney-General	405,422	405,422	429,228	(23,806)
Department of Public Works	1,114,736	1,058,759	633,124	
Boards, Commissions and Other	979,286	1,569,879	1,060,077	509,802
Payments to Non-governmental Agencies	304,651	526,363	495,154	31,209
Grants to local governments	2,184,604	2,184,604	2,165,719	18,885
Pohnpei Transportation Authority	-	141,608	24,771	116,837
Total expenditures	<u>10,563,665</u>	<u>11,894,596</u>	<u>10,723,747</u>	<u>745,214</u>
Deficiency of revenues under expenditures	<u>(2,009,786)</u>	<u>(3,340,717)</u>	<u>(1,344,218)</u>	<u>1,996,499</u>
Other financing uses:				
Operating transfers out	-	-	(308,981)	(308,981)
Net change in fund balance	<u>(2,009,786)</u>	<u>(3,340,717)</u>	<u>(1,653,199)</u>	<u>1,687,518</u>
Other changes in fund balance:				
GASB 54 implementation:				
Early Retirement Program Fund			3,306,657	3,306,657
Student Vocational Arts Program Revolving Fund			67	67
Airport Operations Fund			22,273	22,273
Health Education Projects Fund			208,474	208,474
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes	282,792	282,792	282,007	(785)
	<u>(1,726,994)</u>	<u>(3,057,925)</u>	<u>2,166,279</u>	<u>5,224,204</u>
Fund balance at the beginning of the year	<u>4,142,611</u>	<u>4,142,611</u>	<u>4,142,611</u>	<u>-</u>
Fund balance at the end of the year	<u>\$ 2,415,617</u>	<u>\$ 1,084,686</u>	<u>\$ 6,308,890</u>	<u>\$ 5,224,204</u>

See accompanying notes to required supplementary information - budgetary reporting.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Required Supplementary Information – Budgetary Reporting
September 30, 2011

(1) Budgetary Information

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

Formal budget integration is employed as a management control device during the year for all funds. The Pohnpei State Legislature has the authority to reprogram budgeted estimates in accordance with the Constitution. All annual appropriations lapse at 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.

(2) GASB 54 Implementation

During the year ended September 30, 2011, the State implemented GASB Statement No. 54, which resulted in funds not meeting the special revenue fund definition being moved to the General Fund. Accordingly, the Early Retirement Program Fund, the Student Vocational Arts Program Revolving Fund, the Airport Operations Fund, and the Health Education Projects Fund that were previously presented as special revenue funds have been moved to the General Fund. The effect on the fund balance of the General Fund is as follows:

	Early Retirement Program	Student Voc. Arts Program Revolving	Airport Operations	Health Education Projects	Total
Fund balance, beginning of the year	\$ 3,543,757	\$ 67	\$ 22,273	\$ 208,474	\$ 3,774,571
Revenues	91,913	-	-	-	91,913
Expenditures	<u>(329,103)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(329,103)</u>
	<u>(237,100)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(237,100)</u>
Fund balance, end of the year	\$ <u>3,306,657</u>	\$ <u>67</u>	\$ <u>22,273</u>	\$ <u>208,474</u>	\$ <u>3,537,471</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

OTHER SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2011

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Combining Schedule of Expenditures by Account
Governmental Funds
Year Ended September 30, 2011

	General	Special Revenue	Permanent	Other	Total
		Grants Assistance	Compact Trust	Governmental Funds	
Expenditures:					
Salaries and wages					
Regular	\$ 4,681,847	\$ 9,656,417	\$ -	\$ 70,404	\$ 14,408,668
Overtime	128,391	160,057	-	7,287	295,735
Fringe benefits	919,078	2,070,750	-	18,935	3,008,763
Travel and transportation	336,625	521,026	-	7,710	865,361
Books and instructional materials	-	664,175	-	-	664,175
Communications	104,769	103,108	-	5,370	213,247
Customs and taxes	955	15,355	-	177	16,487
Dues, membership, and subscriptions	31,769	8,200	-	-	39,969
Food stuffs	104,496	565,818	-	251	670,565
Port charges	4,856	36,572	-	648	42,076
Non-capitalized equipment	44,583	164,155	-	3,215	211,953
Capital outlays	87,230	822,268	-	-	909,498
Office supplies and materials	300,561	531,197	-	87,297	919,055
POL	234,723	234,642	-	20,091	489,456
Printing and reproduction	44,950	81,791	-	2,421	129,162
Rental services	9,223	15,691	-	50	24,964
Repairs and maintenance	39,914	118,043	-	935	158,892
Utilities	300,295	809,173	-	46,811	1,156,279
Miscellaneous goods and services	38,977	6,228	-	330	45,535
Subsidies and contributions	301,085	68,250	-	-	369,335
Medical referrals	820	441,727	-	-	442,547
Medical supplies	-	1,216,329	-	1,120,875	2,337,204
Contractual services	370,859	939,321	-	1,175,721	2,485,901
Professional services	-	105,221	-	-	105,221
Housing allowance	54,765	84,260	-	-	139,025
Non-payroll compensation	3,500	177,936	-	-	181,436
Court settlements	79,605	-	-	-	79,605
Scholarships and allowances	-	437,783	-	-	437,783
Insurance	36,182	-	-	-	36,182
Training	4,564	4,339	-	-	8,903
Official allowance	115,000	-	-	-	115,000
Meeting allowance	3,190	12,598	-	3,904	19,692
Leased housing, buildings and land	2,318	6,300	-	-	8,618
Principal repayment	149,839	-	-	-	149,839
Interest payments	55,050	-	-	-	55,050
Payments to municipalities	2,165,719	-	-	-	2,165,719
Miscellaneous	50	3,422	-	13,938	17,410
Bank charges	14,965	150	-	-	15,115
	<u>\$ 10,770,753</u>	<u>\$ 20,082,302</u>	<u>\$ -</u>	<u>\$ 2,586,370</u>	<u>\$ 33,439,425</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function,
and Changes in Fund Balance
General Fund
Year Ended September 30, 2011
(with comparative totals for the year ended September 30, 2010)

	2011	2010
Revenues:		
FSM revenue sharing:		
Gross revenue taxes	\$ 2,214,811	\$ 2,055,637
Import taxes	2,268,381	2,447,558
Income taxes	1,976,616	1,971,942
Other taxes	331,258	306,480
	6,791,066	6,781,617
State taxes:		
Sales tax	2,438,271	2,425,260
Hotel tax	83,951	78,157
	2,522,222	2,503,417
Fees and charges:		
Licenses and fees:	233,337	262,038
Net change in the fair value of investments	(99,063)	574,823
Other revenues	23,880	521,029
Total revenues	9,471,442	10,642,924
Expenditures:		
Current:		
General government:		
Governor and Staff	645,588	566,950
Department of Treasury and Administration	961,774	891,761
Office of Pohnpei Public Auditor	1,802	388
Judiciary Branch	702,593	670,122
Legislative Branch	1,645,376	1,793,815
	3,957,133	3,923,036
Department of Land and Natural Resources:		
Office of the Director	83,839	16,173
Divison of Public Land	57,392	-
Land Use Planning and Zoning Commission	(165)	346
Division of Surveying and Mapping	179,652	187,060
Division of Forestry and Marine Conservation	124,450	84,309
Division of Historic Preservation	66,417	71,923
Division of Parks and Recreation	74,750	75,224
	586,335	435,035
Department of Education:		
Division of Primary Education	2,318	2,318
Office of the Director	-	4,918
	2,318	7,236
Department of Health:		
Medical referrals	820	164,180
Department of Public Safety:		
Office of the Director	85,218	114,552
Search and Rescue	32,030	19,481
Hazard Mitigation	1,000	15,650
Fish & Wildlife	42,163	-
Police Commission	24,987	26,107
Division of Police and Security	936,496	827,993
Division of Correction and Rehabilitation	256,035	266,468
	1,377,929	1,270,251
Office of the Attorney-General	409,350	299,181
Public Works	535,950	705,014

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function,
and Changes in Fund Balance, Continued
General Fund
Year Ended September 30, 2011
(with comparative totals for the year ended September 30, 2010)

	2011	2010
Expenditures, continued:		
Current:		
Boards, Commissions and Other:		
Office of Economic Affairs	308,166	304,092
Office of Social Affairs	113,729	237,842
Election Commissioner's Office	57,891	153,140
Pohnpei Public Broadcasting Corporation	106,199	124,400
Foreign Investment Board	60,399	59,733
Pohnpei Housing Authority	130,000	129,072
Sports and Recreation	118,517	-
Office of Fisheries and Aquaculture	120,023	42,509
	1,014,924	1,050,788
Payments to Non-governmental Agencies:		
Small Business Guarantee and Finance Corporation	117,000	117,000
Pohnpei Public Library	58,000	52,463
Micronesia Legal Services Corporation	38,280	38,280
U.S.D.A. Rural Development	93,267	94,317
Pohnpei Visitors' Bureau	130,840	123,899
Economic Planning Commission	-	15,431
Small Business Development	50,000	50,000
Micro Games	-	209,911
ALMS	-	56
Constitutional Convention	597	62,490
Other	2,631	463
	490,615	764,310
Grants to local governments	2,165,719	2,185,869
Pohnpei Transportation Authority	24,771	116,837
Debt Service:		
Principal payments	149,839	-
Interest charges	55,050	-
	204,889	-
Total expenditures	10,770,753	10,921,737
Deficiency of revenues under expenditures	(1,299,311)	(278,813)
Other financing uses:		
Operating transfers out	(308,981)	-
Net change in fund balance	(1,608,292)	(278,813)
Fund balance at the beginning of the year	7,917,182	4,421,424
Fund balance at the end of the year	\$ 6,308,890	\$ 4,142,611

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function and Changes in Fund Balance
Budget and Actual - General Fund
Year Ended September 30, 2011

	Budgeted Amounts		Actual - Budgetary Basis (see Note 1)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues:				
FSM revenue sharing	\$ 5,769,824	\$ 5,769,824	\$ 6,791,066	\$ 1,021,242
State taxes:				
Sales tax	2,369,055	2,369,055	2,438,271	69,216
Hotel tax	-	-	83,951	83,951
	<u>2,369,055</u>	<u>2,369,055</u>	<u>2,522,222</u>	<u>153,167</u>
Fees and charges:				
Licenses and fees	-	-	233,337	233,337
Net change in the fair value of investments	250,000	250,000	(190,976)	(440,976)
Other	165,000	165,000	23,880	(141,120)
Total revenues	<u>8,553,879</u>	<u>8,553,879</u>	<u>9,379,529</u>	<u>825,650</u>
Expenditures:				
Current:				
General government:				
Governor and Staff	564,747	569,247	679,774	(110,527)
Department of Treasury and Administration	760,302	798,802	851,775	(52,973)
Office of the Pohnpei Public Auditor	3,300	2,000	1,802	198
Judiciary Branch	741,754	761,254	713,010	48,244
Legislative Branch	1,841,543	1,883,943	1,684,743	199,200
	<u>3,911,646</u>	<u>4,015,246</u>	<u>3,931,104</u>	<u>84,142</u>
Department of Land and Natural Resources:				
Office of the Director	18,022	18,022	84,009	(65,987)
Division of Public Land	-	-	57,392	(57,392)
Land Use Planning and Zoning Commission	1,346	1,346	(165)	1,511
Soil and Water Conservation District	1,000	1,000	-	1,000
Division of Surveying and Mapping	181,261	184,014	180,164	3,850
Division of Forestry and Marine Conservation	74,189	80,600	125,065	(44,465)
Division of Historic Preservation	69,698	69,698	68,359	1,339
Division of Parks and Recreation	-	80,996	74,898	6,098
	<u>345,516</u>	<u>435,676</u>	<u>589,722</u>	<u>(154,046)</u>
Department of Education:				
Division of Primary Education	7,318	13,400	3,281	10,119
Department of Health Services:				
Division of Medical Services	188	165,188	833	164,355
Department of Public Safety:				
Office of the Director	186,803	186,803	85,317	101,486
Search and Rescue	20,387	20,387	32,030	(11,643)
Police Commission	26,800	26,800	26,272	528
Division of Police and Security	812,644	812,644	943,268	(130,624)
Division of Correction and Rehabilitation	263,664	263,664	259,868	3,796
Matching RUS Grant	-	54,810	-	54,810
Fish and Wildlife	-	-	42,389	(42,389)
Hazard Mitigation Project	-	13,343	1,590	11,753
	<u>1,310,298</u>	<u>1,378,451</u>	<u>1,390,734</u>	<u>(12,283)</u>
Office of the Attorney-General	405,422	405,422	429,228	(23,806)
Department of Public Works:				
Office of Transportation and Infrastructure	1,114,736	1,058,759	633,124	425,635

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Statement of Revenues, Expenditures by Function and Changes in Fund Balance, Continued
Budget and Actual - General Fund
Year Ended September 30, 2011

	Budgeted Amounts		Actual - Budgetary Basis (see Note 1)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Expenditures, continued:				
Boards, Commissions and Other:				
Office of Economic Affairs	324,868	280,242	333,932	(53,690)
Office of Social Affairs	244,338	130,605	114,093	16,512
Election Commissioner's Office	53,328	158,689	59,544	99,145
Pohnpei Public Broadcasting Corporation	151,641	151,641	106,265	45,376
Ethics Commission	1,500	1,500	-	1,500
Foreign Investment Board	67,595	67,595	62,413	5,182
Pohnpei Housing Authority	131,102	131,102	130,000	1,102
Sports & Recreation	-	-	128,700	(128,700)
Board of Residential Properties and Public Utilities	750	750	-	750
Matching for Traffic project	-	35,500	-	35,500
Pohnpei Sports Commission	-	128,091	-	128,091
PUC Parts & Equipment	-	200,000	-	200,000
Task Force 2011	-	10,000	-	10,000
Economic Planning Conference	-	30,000	-	30,000
Micro Games	-	210,000	-	210,000
Office of Fisheries and Aquaculture	4,164	34,164	125,130	(90,966)
	<u>979,286</u>	<u>1,569,879</u>	<u>1,060,077</u>	<u>509,802</u>
Payments to Non-Governmental Agencies:				
Small Business Guarantee and				
Finance Corporation	117,000	117,000	117,000	-
Small Business Development Center	-	50,000	50,000	-
Pohnpei Public Library	52,463	52,463	58,000	(5,537)
Micronesian Legal Services Corporation	38,280	38,280	38,280	-
U.S.D.A. Rural Development	95,483	95,483	94,750	733
Pohnpei Visitors Bureau	136	132,888	133,525	(637)
Constitutional Convention	-	38,960	597	38,363
Other	1,289	1,289	3,002	(1,713)
	<u>304,651</u>	<u>526,363</u>	<u>495,154</u>	<u>31,209</u>
Grants to local governments	<u>2,184,604</u>	<u>2,184,604</u>	<u>2,165,719</u>	<u>18,885</u>
Pohnpei Transportation Authority	<u>-</u>	<u>141,608</u>	<u>24,771</u>	<u>116,837</u>
Total expenditures	<u>10,563,665</u>	<u>11,894,596</u>	<u>10,723,747</u>	<u>1,170,849</u>
Deficiency of revenues under expenditures	<u>(2,009,786)</u>	<u>(3,340,717)</u>	<u>(1,344,218)</u>	<u>1,996,499</u>
Other financing uses:				
Operating transfers out	<u>-</u>	<u>-</u>	<u>(308,981)</u>	<u>(308,981)</u>
Net change in fund balance	<u>(2,009,786)</u>	<u>(3,340,717)</u>	<u>(1,653,199)</u>	<u>1,687,518</u>
Other changes in unreserved fund balance:				
GASB 54 implementation (note 2):				
Early Retirement Program Fund			3,306,657	3,306,657
Student Vocational Arts Program Revolving Fund			67	67
Airport Operations Fund			22,273	22,273
Health Education Projects Fund			208,474	208,474
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary purposes but in the year the supplies are received for financial reporting purposes	<u>282,792</u>	<u>282,792</u>	<u>282,007</u>	<u>(785)</u>
	<u>(1,726,994)</u>	<u>(3,057,925)</u>	<u>2,166,279</u>	<u>5,224,204</u>
Fund balance at the beginning of the year	<u>4,142,611</u>	<u>4,142,611</u>	<u>4,142,611</u>	<u>-</u>
Fund balance at the end of the year	<u>\$ 2,415,617</u>	<u>\$ 1,084,686</u>	<u>\$ 6,308,890</u>	<u>\$ 5,224,204</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Balance Sheet
September 30, 2011

	Alien Registration Revolving	Pohnpei State Farmers' Revolving	Fisheries Enforcement and Development	Recycling Revolving	Paved Road Maintenance	Medical Supplies Revolving	Public Broadcasting Corporation	Health Care Premium	Department of Public Safety Fees	Environmental Quality	Infrastructure Maintenance	Public Lands Trust	Total
ASSETS													
Receivables:													
Other	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 9,065	\$ -	\$ -	\$ -	\$ -	\$ 9,065
Due from other funds	145,175	10,671	408,844	22,899	1,592,988	-	6,186	1,751,349	140,464	11,690	180,873	88,832	4,359,971
Advances	-	-	1,619	-	-	-	-	-	-	-	1,000	-	2,619
Inventories	-	29,946	-	-	-	-	-	-	-	-	-	-	29,946
Total assets	<u>\$ 145,175</u>	<u>\$ 40,617</u>	<u>\$ 410,463</u>	<u>\$ 22,899</u>	<u>\$ 1,592,988</u>	<u>\$ -</u>	<u>\$ 6,186</u>	<u>\$ 1,760,414</u>	<u>\$ 140,464</u>	<u>\$ 11,690</u>	<u>\$ 181,873</u>	<u>\$ 88,832</u>	<u>\$ 4,401,601</u>
LIABILITIES AND FUND BALANCES (DEFICIT)													
Liabilities:													
Accounts payable	\$ -	\$ 3,521	\$ 5,211	\$ -	\$ -	\$ 42,158	\$ 1,659	\$ -	\$ -	\$ -	\$ 15,383	\$ 300	\$ 68,232
Other liabilities and accruals	100	-	-	-	-	-	-	-	-	-	-	928	1,028
Due to other funds	-	-	-	-	-	13,753	-	-	-	-	-	-	13,753
Total liabilities	<u>100</u>	<u>3,521</u>	<u>5,211</u>	<u>-</u>	<u>-</u>	<u>55,911</u>	<u>1,659</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>15,383</u>	<u>1,228</u>	<u>83,013</u>
Fund balances (deficit):													
Non-spendable	-	29,946	1,619	-	-	-	-	-	-	-	1,000	-	32,565
Restricted	-	-	-	-	-	-	-	-	-	-	-	-	-
Committed	124,281	7,150	397,618	22,899	1,571,892	-	3,128	1,760,414	139,862	11,690	49,825	87,454	4,176,213
Assigned	20,794	-	6,015	-	21,096	-	1,399	-	602	-	115,665	150	165,721
Unassigned	-	-	-	-	-	(55,911)	-	-	-	-	-	-	(55,911)
Total fund balances (deficit)	<u>145,075</u>	<u>7,150</u>	<u>405,252</u>	<u>22,899</u>	<u>1,592,988</u>	<u>(55,911)</u>	<u>4,527</u>	<u>1,760,414</u>	<u>140,464</u>	<u>11,690</u>	<u>166,490</u>	<u>87,604</u>	<u>4,318,588</u>
Total liabilities and fund balances (deficit)	<u>\$ 145,175</u>	<u>\$ 10,671</u>	<u>\$ 410,463</u>	<u>\$ 22,899</u>	<u>\$ 1,592,988</u>	<u>\$ -</u>	<u>\$ 6,186</u>	<u>\$ 1,760,414</u>	<u>\$ 140,464</u>	<u>\$ 11,690</u>	<u>\$ 181,873</u>	<u>\$ 88,832</u>	<u>\$ 4,401,601</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS

Combining Statement of Revenues, Expenditures By Function,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2011

	Alien Registration Revolving	Pohnpei State Farmers' Revolving	Fisheries Enforcement and Development	Recycling Revolving	Paved Road Maintenance	Medical Supplies Revolving	Public Broadcasting Corporation	Health Care Premium	Department of Public Safety Fees	Environmental Quality	Infrastructure Maintenance	Public Lands Trust	Total
Revenues:													
Excise tax	\$ -	\$ -	\$ -	\$ -	\$ 457,047	\$ -	\$ -	\$ 120,440	\$ -	\$ -	\$ -	\$ -	\$ 577,487
Fees and charges	74,550	57,306	-	-	-	568,285	17,400	-	49,701	-	-	36,759	804,001
Total revenues	74,550	57,306	-	-	457,047	568,285	17,400	120,440	49,701	-	-	36,759	1,381,488
Expenditures by function:													
Current:													
General government	-	75,154	148,059	-	111,710	-	46,912	-	(26,579)	12,676	1,039,870	32,366	1,440,168
Health services	-	-	-	-	-	1,146,202	-	-	-	-	-	-	1,146,202
Total expenditures	-	75,154	148,059	-	111,710	1,146,202	46,912	-	(26,579)	12,676	1,039,870	32,366	2,586,370
Excess (deficiency) of revenues over (under) expenditures	74,550	(17,848)	(148,059)	-	345,337	(577,917)	(29,512)	120,440	76,280	(12,676)	(1,039,870)	4,393	(1,204,882)
Other financing sources (uses):													
Operating transfers in	-	-	-	-	-	-	-	-	-	-	616,542	-	616,542
Operating transfers out	-	-	-	-	(307,561)	-	-	-	-	-	-	-	(307,561)
Total other financing sources (uses), net	-	-	-	-	(307,561)	-	-	-	-	-	616,542	-	308,981
Net change in fund balances (deficit)	74,550	(17,848)	(148,059)	-	37,776	(577,917)	(29,512)	120,440	76,280	(12,676)	(423,328)	4,393	(895,901)
Fund balances at the beginning of the year	70,525	54,944	553,311	22,899	1,555,212	522,006	34,039	1,639,974	64,184	24,366	589,818	83,211	5,214,489
Fund balances (deficit) at the end of the year	\$ 145,075	\$ 37,096	\$ 405,252	\$ 22,899	\$ 1,592,988	\$ (55,911)	\$ 4,527	\$ 1,760,414	\$ 140,464	\$ 11,690	\$ 166,490	\$ 87,604	\$ 4,318,588

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

**NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS**

Combining Statement of Revenues, Expenditures By Account,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2011

	Alien Registration Revolving	Pohnpei State Farmers' Revolving	Fisheries Enforcement and Development	Recycling Revolving	Paved Road Maintenance	Medical Supplies Revolving	Public Broadcasting Corporation	Health Care Premium	Department of Public Safety Fees	Environmental Quality	Infrastructure Maintenance	Public Lands Trust	Total
Revenues:													
Excise tax	\$ -	\$ -	\$ -	\$ -	\$ 457,047	\$ -	\$ -	\$ 120,440	\$ -	\$ -	\$ -	\$ -	\$ 577,487
Fees and charges	74,550	57,306	-	-	-	568,285	17,400	-	49,701	-	-	36,759	804,001
Total revenues	74,550	57,306	-	-	457,047	568,285	17,400	120,440	49,701	-	-	36,759	1,381,488
Expenditures by account:													
Salaries and wages:													
Regular	-	-	68,063	-	-	-	287	-	(21,986)	-	-	24,040	70,404
Overtime	-	-	-	-	-	-	-	-	(4,593)	11,880	-	-	7,287
Fringe benefits	-	-	14,315	-	-	-	55	-	-	638	-	3,927	18,935
Travel	-	-	7,710	-	-	-	-	-	-	-	-	-	7,710
Communications	-	760	610	-	-	-	4,000	-	-	-	-	-	5,370
Custom and tax	-	177	-	-	-	-	-	-	-	-	-	-	177
Food stuff	-	-	51	-	-	-	200	-	-	-	-	-	251
Port charges	-	-	71	-	-	577	-	-	-	-	-	-	648
Non-capital equipment and furnitures	-	285	2,930	-	-	-	-	-	-	-	-	-	3,215
Office supplies and materials	-	54,116	6,155	-	-	24,750	1,158	-	-	158	-	960	87,297
POL	-	5,340	13,082	-	-	-	1,669	-	-	-	-	-	20,091
Printing and reproduction	-	-	1,946	-	-	-	400	-	-	-	-	75	2,421
Rental	-	-	-	-	-	-	50	-	-	-	-	-	50
Repairs and maintenance	-	174	30	-	-	-	731	-	-	-	-	-	935
Utilities	-	4,087	24,968	-	-	-	17,756	-	-	-	-	-	46,811
Miscellaneous goods and services	-	330	-	-	-	-	-	-	-	-	-	-	330
Medical supplies	-	-	-	-	-	1,120,875	-	-	-	-	-	-	1,120,875
Contractual services	-	3,535	8,128	-	111,710	-	12,478	-	-	-	1,039,870	-	1,175,721
Meeting allowance	-	-	-	-	-	-	540	-	-	-	-	3,364	3,904
Equipment	-	6,350	-	-	-	-	7,588	-	-	-	-	-	13,938
Total expenditures	-	75,154	148,059	-	111,710	1,146,202	46,912	-	(26,579)	12,676	1,039,870	32,366	2,586,370
Excess (deficiency) of revenues over (under) expenditures	74,550	(17,848)	(148,059)	-	345,337	(577,917)	(29,512)	120,440	76,280	(12,676)	(1,039,870)	4,393	(1,204,882)
Other financing sources (uses):													
Operating transfers in	-	-	-	-	-	-	-	-	-	-	616,542	-	616,542
Operating transfers out	-	-	-	-	(307,561)	-	-	-	-	-	-	-	(307,561)
Total other financing sources (uses), net	-	-	-	-	(307,561)	-	-	-	-	-	616,542	-	308,981
Net change in fund balances (deficit)	74,550	(17,848)	(148,059)	-	37,776	(577,917)	(29,512)	120,440	76,280	(12,676)	(423,328)	4,393	(895,901)
Fund balances at the beginning of the year	70,525	54,944	553,311	22,899	1,555,212	522,006	34,039	1,639,974	64,184	24,366	589,818	83,211	5,214,489
Fund balances (deficit) at the end of the year	\$ 145,075	\$ 37,096	\$ 405,252	\$ 22,899	\$ 1,592,988	\$ (55,911)	\$ 4,527	\$ 1,760,414	\$ 140,464	\$ 11,690	\$ 166,490	\$ 87,604	\$ 4,318,588

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUNDS

**Combining Balance Sheet
September 30, 2011**

	Section 211(a)(1) Education Sector	Section 211(a)(2) Health Sector	Section 211(a)(5) Environment	Section 211(a)(3) Private Sector Development	Section 211(a)(4) Capacity Building	Section 211(a)(1) Supplemental Education	Section Infrastructure Maintenance	Section 221(b) Special Block Grant	Compact I Other Grants	U.S. Federal Grants	Non-U.S. Grants	CFSM Grants	Compact I Capital Grant	Total
ASSETS														
Investment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 223,856	\$ 1,195,803	\$ -	\$ -	\$ -	\$ 2,689,325	\$ 4,108,984
Grants receivable from FSM, net	-	-	11,174	-	-	1,428,526	1,751	-	-	588,304	8,749	50,203	-	2,088,707
Other receivable	-	-	-	-	-	-	-	-	-	-	-	3,928	-	3,928
Due from other funds	1,024,609	786,600	-	66,032	92,493	-	17,218	-	-	-	98,850	-	-	2,085,802
Advances	7,715	4,672	288	1,760	28,899	12,384	-	-	-	19,114	1,778	3,969	-	80,579
Restricted cash	-	7,700	-	-	-	-	-	-	-	-	-	-	141,149	148,849
	<u>\$ 1,032,324</u>	<u>\$ 798,972</u>	<u>\$ 11,462</u>	<u>\$ 67,792</u>	<u>\$ 121,392</u>	<u>\$ 1,440,910</u>	<u>\$ 18,969</u>	<u>\$ 223,856</u>	<u>\$ 1,195,803</u>	<u>\$ 607,418</u>	<u>\$ 109,377</u>	<u>\$ 58,100</u>	<u>\$ 2,830,474</u>	<u>\$ 8,516,849</u>
LIABILITIES AND FUND BALANCES														
(DEFICIT)														
Liabilities:														
Accounts payable	\$ 312,465	\$ 159,399	\$ 11,751	\$ -	\$ 5,041	\$ 137,015	\$ -	\$ -	\$ -	\$ 41,254	\$ 10,786	\$ 4,796	\$ -	\$ 682,507
Other liabilities and accruals	113,123	48,813	4,841	-	4,407	23,737	-	-	-	29,136	-	4,699	-	228,756
Deferred revenue	599,620	585,973	-	67,255	110,760	-	-	-	-	-	59,655	-	-	1,423,263
Due to other funds	-	-	21,056	-	-	1,272,665	-	179,868	1,160,215	537,028	-	48,605	875,646	4,095,083
Total liabilities	<u>1,025,208</u>	<u>794,185</u>	<u>37,648</u>	<u>67,255</u>	<u>120,208</u>	<u>1,433,417</u>	<u>-</u>	<u>179,868</u>	<u>1,160,215</u>	<u>607,418</u>	<u>70,441</u>	<u>58,100</u>	<u>875,646</u>	<u>6,429,609</u>
Fund balances (deficit):														
Non-spendable	7,715	4,672	288	1,760	28,899	12,384	-	-	1,000,000	19,114	1,778	3,969	-	1,080,579
Restricted	-	115	-	-	-	-	18,969	43,988	-	-	-	-	1,954,828	2,017,900
Committed	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Assigned	-	-	-	-	-	-	-	-	-	-	37,158	-	-	37,158
Unassigned	(599)	-	(26,474)	(1,223)	(27,715)	(4,891)	-	-	(964,412)	(19,114)	-	(3,969)	-	(1,048,397)
Total fund balances (deficit)	<u>7,116</u>	<u>4,787</u>	<u>(26,186)</u>	<u>537</u>	<u>1,184</u>	<u>7,493</u>	<u>18,969</u>	<u>43,988</u>	<u>35,588</u>	<u>-</u>	<u>38,936</u>	<u>-</u>	<u>1,954,828</u>	<u>2,087,240</u>
Total liabilities and fund balances (deficit)	<u>\$ 1,032,324</u>	<u>\$ 798,972</u>	<u>\$ 11,462</u>	<u>\$ 67,792</u>	<u>\$ 121,392</u>	<u>\$ 1,440,910</u>	<u>\$ 18,969</u>	<u>\$ 223,856</u>	<u>\$ 1,195,803</u>	<u>\$ 607,418</u>	<u>\$ 109,377</u>	<u>\$ 58,100</u>	<u>\$ 2,830,474</u>	<u>\$ 8,516,849</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUNDS

**Combining Statement of Revenues, Expenditures by Function,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2011**

	Section 211(a)(1) Education Sector	Section 211(a)(2) Health Sector	Section 211(a)(5) Environment	Section 211(a)(3) Private Sector Development	Section 211(a)(4) Capacity Building	Section 211(a)(1) Supplemental Education	Section Infrastructure Maintenance	Section 221(b) Special Block Grant	Section Compact I Other Grants	U.S. Federal Grants	Non-U.S. Grants	CFSM Grants	Section Compact I Capital Grant	Total
Revenues:														
Compact funding	\$ 7,649,066	\$ 5,869,580	\$ 433,771	\$ -	\$ 457,654	\$ 3,009,688	\$ 1,751	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 17,421,510
CFSM grants	-	-	-	-	-	-	-	-	-	-	-	94,969	-	94,969
Federal contributions and other grants	-	-	-	-	-	-	-	-	-	2,380,002	36,250	-	-	2,416,252
Other	-	-	-	-	-	-	-	-	-	-	139,146	-	709	139,855
	<u>7,649,066</u>	<u>5,869,580</u>	<u>433,771</u>	<u>-</u>	<u>457,654</u>	<u>3,009,688</u>	<u>1,751</u>	<u>-</u>	<u>-</u>	<u>2,380,002</u>	<u>175,396</u>	<u>94,969</u>	<u>709</u>	<u>20,072,586</u>
Expenditures by function:														
Current:														
General government	-	-	433,771	-	457,654	-	1,751	-	-	-	185,821	94,969	-	1,173,966
Land and natural resources	-	-	-	-	-	-	-	-	-	123,233	-	-	-	123,233
Education	7,649,066	-	-	-	-	3,009,688	-	-	-	1,082,783	-	-	-	11,741,537
Health services	-	5,869,580	-	-	-	-	-	-	-	1,173,986	-	-	-	7,043,566
Total expenditures	<u>7,649,066</u>	<u>5,869,580</u>	<u>433,771</u>	<u>-</u>	<u>457,654</u>	<u>3,009,688</u>	<u>1,751</u>	<u>-</u>	<u>-</u>	<u>2,380,002</u>	<u>185,821</u>	<u>94,969</u>	<u>-</u>	<u>20,082,302</u>
Net change in fund balances (deficit)	-	-	-	-	-	-	-	-	-	-	(10,425)	-	709	(9,716)
Fund balances (deficit) at the beginning of the year	7,116	4,787	(26,186)	537	1,184	7,493	18,969	43,988	35,588	-	49,361	-	1,954,119	2,096,956
Fund balances (deficit) at the end of the year	<u>\$ 7,116</u>	<u>\$ 4,787</u>	<u>\$ (26,186)</u>	<u>\$ 537</u>	<u>\$ 1,184</u>	<u>\$ 7,493</u>	<u>\$ 18,969</u>	<u>\$ 43,988</u>	<u>\$ 35,588</u>	<u>\$ -</u>	<u>\$ 38,936</u>	<u>\$ -</u>	<u>\$ 1,954,828</u>	<u>\$ 2,087,240</u>

See Accompanying Independent Auditors' Report.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

GRANTS ASSISTANCE FUNDS

**Combining Statement of Revenues, Expenditures by Account,
and Changes in Fund Balances (Deficit)
Year Ended September 30, 2011**

	Section 211(a)(1) Education Sector	Section 211(a)(2) Health Sector	Section 211(a)(5) Environment	Section 211(a)(3) Private Sector Development	Section 211(a)(4) Capacity Building	Section 211(a)(1) Supplemental Education	Infrastructure	Section 221(b) Special Block Grant	Compact I Other Grants	U.S. Federal Grants	Non-U.S. Grants	CFSM Grants	Compact I Capital Grant	Total
Revenues:														
Compact funding	\$ 7,649,066	\$ 5,869,580	\$ 433,771	\$ -	\$ 457,654	\$ 3,009,688	\$ 1,751	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 17,421,510
CFSM grants	-	-	-	-	-	-	-	-	-	-	-	94,969	-	94,969
Federal contributions and other grants	-	-	-	-	-	-	-	-	-	2,380,002	36,250	-	-	2,416,252
Other	-	-	-	-	-	-	-	-	-	-	139,146	-	709	139,855
	<u>7,649,066</u>	<u>5,869,580</u>	<u>433,771</u>	<u>-</u>	<u>457,654</u>	<u>3,009,688</u>	<u>1,751</u>	<u>-</u>	<u>-</u>	<u>2,380,002</u>	<u>175,396</u>	<u>94,969</u>	<u>709</u>	<u>20,072,586</u>
Expenditures by account:														
Salaries and wages:														
Regular	4,842,767	2,165,520	196,298	-	208,360	1,018,143	-	-	-	1,205,451	322	19,556	-	9,656,417
Overtime	-	82,450	13,773	-	-	-	-	-	-	48,614	-	15,220	-	160,057
Fringe benefits	1,062,803	400,987	41,274	-	28,633	246,669	-	-	-	284,657	(147)	5,874	-	2,070,750
Travel and transportation	13,268	97,391	(33)	-	148,670	45,519	-	-	-	179,317	19,858	17,036	-	521,026
Communications	19,906	18,054	2,991	-	2,502	37,370	-	-	-	20,307	1,555	423	-	103,108
Dues, membership, and subscriptions	-	500	-	-	4,923	2,777	-	-	-	-	-	-	-	8,200
Food stuffs	260,040	95,280	60	-	56	182,602	-	-	-	4,645	9,263	13,872	-	565,818
Port charges	23,658	11,010	249	-	-	660	-	-	-	67	-	928	-	36,572
Custom and tax	5,963	9,064	104	-	-	-	-	-	-	-	224	-	-	15,355
Capital outlays	328,009	220,284	7,274	-	7,865	147,166	-	-	-	98,266	5,429	7,975	-	822,268
Office supplies and materials	97,392	98,960	25,148	-	9,310	81,346	-	-	-	149,085	70,660	(704)	-	531,197
Books and instructional supplies	377,726	-	-	-	-	280,028	-	-	-	6,421	-	-	-	664,175
POL	76,673	16,019	9,277	-	1,815	65,492	-	-	-	57,337	6,190	1,839	-	234,642
Printing and reproduction	48,472	14,591	443	-	850	9,973	-	-	-	7,462	-	-	-	81,791
Rental services	135	597	-	-	1,417	545	-	-	-	9,241	3,756	-	-	15,691
Repairs and maintenance	54,494	6,072	2,634	-	2,841	27,616	-	-	-	21,514	202	2,670	-	118,043
Utilities	120,471	609,795	10,938	-	9,181	36,375	-	-	-	17,570	3,843	1,000	-	809,173
Subsidies and contributions	68,250	-	-	-	-	-	-	-	-	-	-	-	-	68,250
Medical referrals	-	441,727	-	-	-	-	-	-	-	-	-	-	-	441,727
Medical supplies	-	1,194,569	-	-	-	1,087	-	-	-	20,673	-	-	-	1,216,329
Contractual services	24,475	299,840	121,496	-	15,974	206,463	1,751	-	-	218,357	44,449	6,516	-	939,321
Professional services	-	1,384	-	-	11,950	91,887	-	-	-	-	-	-	-	105,221
Scholarships and allowances	122,394	-	-	-	-	315,389	-	-	-	-	-	-	-	437,783
Housing allowance	-	61,801	-	-	-	20,999	-	-	-	1,460	-	-	-	84,260
Meeting allowance	358	-	280	-	-	1,260	-	-	-	9,500	1,200	-	-	12,598
Training	-	-	-	-	-	3,299	-	-	-	1,040	-	-	-	4,339
Leased housing, buildings and land	6,300	-	-	-	-	-	-	-	-	-	-	-	-	6,300
Non-capital equipment and furnitures	95,512	17,919	1,515	-	3,232	24,994	-	-	-	15,171	3,048	2,764	-	164,155
Non-payroll compensation	-	-	-	-	-	162,021	-	-	-	3,100	12,815	-	-	177,936
Miscellaneous goods and services	-	2,419	50	-	75	8	-	-	-	622	3,054	-	-	6,221
Bank charges	-	50	-	-	-	-	-	-	-	-	100	-	-	150
Miscellaneous	-	3,297	-	-	-	-	-	-	-	125	-	-	-	3,422
Total expenditures	<u>7,649,066</u>	<u>5,869,580</u>	<u>433,771</u>	<u>-</u>	<u>457,654</u>	<u>3,009,688</u>	<u>1,751</u>	<u>-</u>	<u>-</u>	<u>2,380,002</u>	<u>185,821</u>	<u>94,969</u>	<u>-</u>	<u>20,082,302</u>
Net change in fund balances (deficit)	-	-	-	-	-	-	-	-	-	-	(10,425)	-	709	(9,716)
Fund balances (deficit) at the beginning of the year	7,116	4,787	(26,186)	537	1,184	7,493	18,969	43,988	35,588	-	49,361	-	1,954,119	2,096,956
Fund balances (deficit) at the end of the year	<u>\$ 7,116</u>	<u>\$ 4,787</u>	<u>\$ (26,186)</u>	<u>\$ 537</u>	<u>\$ 1,184</u>	<u>\$ 7,493</u>	<u>\$ 18,969</u>	<u>\$ 43,988</u>	<u>\$ 35,588</u>	<u>\$ -</u>	<u>\$ 38,936</u>	<u>\$ -</u>	<u>\$ 1,954,828</u>	<u>\$ 2,087,240</u>

See Accompanying Independent Auditors' Report.

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

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

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei as of and for the year ended September 30, 2011, which collectively comprise the State of Pohnpei's basic financial statements and have issued our report thereon dated June 25, 2012. Our report includes a reference to other auditors and a reference for the adoption of a new accounting standard. 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. Other auditors audited the financial statements of the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation, as described in our report on the State of Pohnpei's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those other auditors.

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

Internal Control Over Financial Reporting

Management of the State of Pohnpei is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the State of Pohnpei's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State of Pohnpei's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the State of Pohnpei's internal control over financial reporting.

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.

Our consideration of internal control over financial reporting 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 financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings and Questioned Costs (pages 70 and 71) as item 2011-1 that we consider to be significant deficiencies in internal control over financial reporting. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weaknesses, yet important enough to merit attention by those charged with governance.

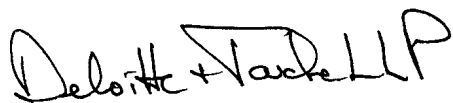
Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Pohnpei's financial statements are free of 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*.

We noted certain matters that we reported to management of the State of Pohnpei in a separate letter dated June 25, 2012.

The State of Pohnpei's response to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the State of Pohnpei's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the management of the State of Pohnpei, others within the entity, the Honorable Members of the Pohnpei State Legislature, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.



June 25, 2012

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB
CIRCULAR A-133 AND ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

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

Compliance

We have audited the State of Pohnpei's compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on the State of Pohnpei's major federal programs for the year ended September 30, 2011. The State of Pohnpei's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (pages 70 and 71). Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the State of Pohnpei's management. Our responsibility is to express an opinion on the State of Pohnpei's compliance based on our audit.

As discussed in Note 2b to the Schedule of Expenditures of Federal Awards, the State of Pohnpei's basic financial statements include the operations of certain entities whose federal awards are not included in the Schedule of Expenditures of Federal Awards for the year ended September 30, 2011. 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.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of Pohnpei's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the State of Pohnpei's compliance with those requirements.

In our opinion, the State of Pohnpei complied, in all material respects, with the 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, 2011. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as item 2011-1.

Internal Control Over Compliance

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

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.

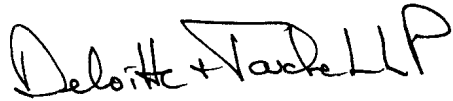
Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying Schedule of Findings and Questioned Costs as item 2011-1. 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.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Pohnpei as of and for the year ended September 30, 2011, and have issued our report thereon dated June 25, 2012. Our report includes a reference to other auditors and a reference for the adoption of a new accounting standard. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the State of Pohnpei's basic financial statements. We did not audit the financial statements of the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation which represent 4%, 1% and 3%, respectively, of the assets, net assets and operating revenues of the discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Pohnpei Transportation Authority and the Small Business Guarantee and Finance Corporation is based on the reports of the auditors. The accompanying schedule of expenditures of federal awards (pages 64 through 67) 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. This schedule is the responsibility of the management of the State of Pohnpei. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The State of Pohnpei's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the State of Pohnpei's responses and, accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of the management of the State of Pohnpei, others within the entity, the Honorable Members of the Pohnpei State Legislature, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

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

June 25, 2012

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Expenditures of Federal Awards, by Grantor
Year Ended September 30, 2011

Agency/Program	Expenditures
U.S. Department of Agriculture	\$ 62,405
U.S. Department of the Interior	17,544,743
U.S. Department of Homeland Security	-
U.S. Department of Education	1,082,783
U.S. Department of Health and Human Services	1,111,581
GRAND TOTAL	\$ 19,801,512

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

Direct from the U.S. Department of Health and Human Services:
Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, Public Housing Primary Care and School Based Health Centers)

93.224 \$ 225,430

Reconciliation to the basic financial statements:

Grants Assistance Fund	\$ 20,082,302
Less:	
Non-U.S. Grants	(185,821)
CFSM Grants	(94,969)
	\$ 19,801,512

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2011

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF AGRICULTURE		
US Grants Forest Invasive Species FY07	10.660	\$ -
Cooperative Forestry Assistance	10.664	49,905
Community Facilities Loans and Grants	10.766	<u>12,500</u>
U.S. DEPARTMENT OF AGRICULTURE TOTAL		<u><u>\$ 62,405</u></u>
U.S. DEPARTMENT OF THE INTERIOR		
Economic, Social and Political Development of the Territories:	15.875	
Compact II Education Sector		\$ 7,649,066
Compact II Health Sector		5,869,580
Compact II Capacity Building Sector		457,654
Compact II Environment Sector		433,771
Compact II Supplemental Education		3,009,688
Compact II Infrastructure Maintenance		1,751
Technical Assistance:		
Survey and Mapping		26,411
Historic Preservation Fund Grants-In-Aid	15.904	<u>96,822</u>
U.S. DEPARTMENT OF THE INTERIOR TOTAL		<u><u>\$ 17,544,743</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2011

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF HOMELAND SECURITY		
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	\$ <u> -</u>
U.S. DEPARTMENT OF HOMELAND SECURITY		\$ <u><u> -</u></u>

See accompanying notes to schedule of expenditures of federal awards.

U.S. DEPARTMENT OF EDUCATION

Special Education - Grants to States	84.027	\$ <u> 1,082,783</u>
U.S. DEPARTMENT OF EDUCATION TOTAL		\$ <u><u> 1,082,783</u></u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued
Year Ended September 30, 2011

Agency/Program	CFDA#	Expenditures
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES		
Project Grants and Cooperative Agreements for Tuberculosis		
Control Programs	93.116	\$ 39,836
Family Planning - Services	93.217	83,052
Consolidated Health Centers	93.224	225,430
Substance Abuse and Mental Health Services - Projects of Regional and National Significance	93.243	-
Immunization Grants	93.268	118,317
CDC & Prevention-Investigations & Technical Assistance	93.283	104,212
ARRA Health Center Integrated Services Development Initiative	93.703	227,014
HIV Care Formula Grants	93.917	3,069
HIV Prevention Activities-Health Department Based	93.940	86,308
Block Grants for Prevention and Treatment of Substance Abuse	93.959	107,898
Preventive Health Services - Sexually Transmitted Diseases Control Grants	93.977	2,425
Cooperative Agreements for State-Based Diabetes Control Programs and Evaluation of Surveillance Systems	93.988	12,138
Preventive Health and Health Services Block Grant	93.991	-
Maternal and Child Health Services Block Grant to the States	93.994	87,593
CCPI Cancer Program	93.UNKNOWN	10,343
Others	N/A	3,946
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES TOTAL		\$ <u>1,111,581</u>
GRAND TOTAL		\$ <u>19,801,512</u>

See accompanying notes to schedule of expenditures of federal awards.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2011

1. Scope

The State of Pohnpei is one of the four States of the Federated States of Micronesia. All significant operations of the State 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's cognizant agency for Single Audit.

A. Programs Subject to Single Audit

Schedules of expenditures of federal awards are presented for each federal program related to the following agencies:

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

2. Summary of Significant Accounting Policies

A. Basis of Accounting

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

B. Reporting Entity

For purposes of complying with The Single Audit Act of 1984, as amended in 1996, the State's reporting entity is defined in Note 1A to its September 30, 2011 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, as defined above, for the year ended September 30, 2011.

C. Subgrantees

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

D. Indirect Cost Allocation

The State does not receive any indirect cost allocation and does not charge indirect costs against federal programs.

E. CFDA #15.875

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

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Programs Selected For
Audit in Accordance with OMB Circular A-133
Year Ended September 30, 2011

<u>Grantor Program Title</u>	<u>CFDA No.</u>	<u>2011 Fiscal Year Expenditures</u>
<u>U.S. Department of the Interior</u>		
Economic, Social and Political Development of the Territories:		
Compact of Free Association Sector Grants	15.875	
Compact II Education Sector		\$ 7,649,066
Compact II Health Sector		5,869,580
Compact II Capacity Building Sector		457,654
Compact II Environment Sector		433,771
Compact II Supplemental Education		3,009,688
Compact II Infrastructure Maintenance		<u>1,751</u>
Total Major Programs Under CFDA #15.875		<u>17,421,510</u>
<u>U.S. Department of Health and Human Services</u>		
Consolidated Health Centers	93.224	225,430
Block Grants for Prevention and Treatment of Substance Abuse	93.959	107,898
Immunization Grant	93.268	118,317
ARRA Health Center Integrated Services Development Initiative	93.703	<u>227,014</u>
		<u>678,659</u>
Total U.S. Federal program expenditures selected		\$ <u>18,100,169</u>
Total U.S. Federal program expenditures		\$ <u>19,801,512</u>
% of total U.S. Federal expenditures covered by major programs		<u>91%</u>

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs
Year Ended September 30, 2011

Part I - Summary of Auditors' Results Section

Financial Statements

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

Federal Awards

Internal control over major programs:

- | | |
|---|-------------|
| 5. Material weakness(es) identified? | No |
| 6. Significant deficiency(ies) identified? | Yes |
| 7. Type of auditors' report issued on compliance for major programs | Unqualified |
| 8. Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? | Yes |
| 9. Identification of major programs: | |

<u>Name of Federal Program or Cluster</u>	<u>CFDA Numbers</u>
Economic, Social and Political Development of the Territories – Compact of Free Association Compact Sector Grants	15.875
Block Grants for Prevention and Treatment of Substance Abuse	93.959
Immunization Grants	93.268
Consolidated Health Center	93.224
ARRA Health Center Integrated Services Development Initiative	93.703

- | | |
|--|-----------|
| 10. Dollar threshold used to distinguish between Type A and Type B Programs: | \$594,045 |
| 11. Auditee qualified as a low-risk auditee? | Yes |

Part II – Financial Statements Findings Section

<u>Finding #</u>	<u>Finding</u>
2011-1	Equipment and Real Property Management

Part III - Federal Award Findings and Questioned Cost Section

<u>Finding #</u>	<u>CFDA #</u>	<u>Finding</u>	<u>Questioned Costs</u>
2011-1	15.875	Equipment and Real Property Management	\$ -

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2011

Finding No.: 2011-1
Federal Agency: U.S. Department of the Interior
CFDA Program: 15.875 Economic, Social and Political Development of the Territories
Grant Number: Compact Sector Grants
Requirement: Compliance: Equipment and Real Property Management
Questioned Cost: \$0

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

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

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

Effect: The expected life of fixed assets may be lessened. However, no questioned costs result from this finding as no specific instances came to our attention in fiscal year 2011 of unnecessary expenditures that occurred due to this condition.

Prior Year Status: Noncompliance with maintenance of fixed assets was reported as a finding in the fiscal years 2007 to 2010 single audits.

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

Auditee Response and Corrective Action Plan: We concur.

In our effort to solve this finding in previous years, our efforts in FY 2011 still did not work. To be workable, we shall implement a different approach to include strengthening our existing Maintenance of Fixed Assets policy and consistently monitoring adaption of the policy among all departments.

**STATE OF POHNPEI
FEDERATED STATES OF MICRONESIA**

Summary Schedule of Prior Audit Findings and Questioned Costs
Year Ended September 30, 2011

The following is a summary of unresolved questioned costs of the State of Pohnpei as of September 30, 2011:

Questioned Costs as of September 30, 2010	\$ -
Fiscal year 2011 questioned costs	<u>-</u>
Total questioned costs at September 30, 2011	\$ <u><u>-</u></u>

Unresolved prior year findings are set forth in the accompanying schedule of findings and questioned costs.