FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION

(A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA NATIONAL GOVERNMENT)

FINANCIAL STATEMENTS, ADDITIONAL INFORMATION AND INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2019 and 2018

FEDERATED STATES OF MICRONESIA TELECOMMUNICATIONS CORPORATION (A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA NATIONAL GOVERNMENT)

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Years Ended September 30, 2019 and 2018

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Federated States of Micronesia
Telecommunications Corporation:

Report on the Financial Statements

We have audited the accompanying financial statements of the Federated States of Micronesia (FSM) Telecommunications Corporation (the Corporation), a component unit of the FSM National Government, which comprise the statements of net position as of September 30, 2019 and 2018, and the related statements of revenues, expenses, and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Corporation as of September 30, 2019 and 2018, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 9 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. This supplementary information is the responsibility of the Corporation's management. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Other Supplementary Information listed in the accompanying table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of the Corporation's management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Other Supplementary Information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2019 on our consideration of the Corporation'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 financing reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Corporation's internal control over financial reporting and compliance.

Deloitte & Touche LLP

December 20, 2019

Management's Discussion and Analysis
Years Ended September 30, 2019 and 2018

Our discussion and analysis of the Federated States of Micronesia Telecommunications Corporation (FSMTC) financial performance provides an overview of the FSMTC financial activities for the fiscal year ended September 30, 2019. This discussion has been prepared by the FSMTC management to further provide an introduction and understanding of the basic financial statements for the year ended September 30, 2019. Please read it in conjunction with the financial statements and the notes thereto, which follow this discussion and analysis. Fiscal year 2018 and 2017 comparative information has been included, where appropriate.

The FSMTC is a public corporation of the Federated States of Micronesia National Government and is the primary provider of telecommunications services throughout the Federated States of Micronesia (FSM) and to points outside of the FSM. The FSMTC also provides Cable TV in the State of Kosrae, and Digital Broadcast Television (DBTV) to both Yap and Chuuk States. Pohnpei, Chuuk and Yap state are now connected to submarine fiber optic cable and soon to be connected is Kosrae. Pohnpei's submarine fiber optic cable was funded by a loan from Rural Utilities Corporation (RUS-USDA), whereas the submarine fiber optic cable for Chuuk, Yap and Kosrae are being funded by grants from World Bank.

The FSMTC is under the governance of an appointed 5-member Board of Directors by the President of the FSM and the Governors of each State, which has oversight over both the FSMTC, Cable TV in Pohnpei, Cable TV in Kosrae and DBTV in Yap and Chuuk. The President/Chief Executive Officer (CEO) is also an ex-officio non-voting member of the Board.

The FSMTC provides telecommunications services which include Plain Old Telephone Services (POTS) to **6,941** active subscribers (Pohnpei – **3,537**, Chuuk – **1,019**, Yap - **1,392** and Kosrae - **993**). Other telecommunications services provided are National and International Overseas Calls, Internet Services, Mobile Cellular Services with **21,364** active subscribers (Pohnpei –**9,588**, Chuuk –**7,235**, Yap –**3,656** and Kosrae - **885**), Cable Television in the State of Kosrae with **186** active subscribers, DBTV in the State of Chuuk with **231** active subscribers and DBTV in the State of Yap with **279** active subscribers.

In the past, FSMTC relied on calls made to and from outside of the FSM and calls within the FSM, which account for **5.04%** of FSMTC's FY2019 operating revenues as compared with **7.39%** of FSMTC's FY2018 operating revenues. During FY2019, FSMTC realized a **decrease** in Overseas and Domestic Call Revenue of **$261,880** (or –**24.88%**) as compared to FY2018. Management believes that the decrease was caused by the increase in internet usage and the increase in ADSL Internet subscribers in FY2019. With the introduction of smart phones and accessibilities to unlimited internet, subscribers were able to utilize such technology to place overseas calls thru the use of applications available in the internet in which most of these applications are free. Accessing internet thru mobile infrastructure using 3G, 4G and LTE technologies further makes it more convenient for the subscribers to use various apps to bypass traditional voice calls. The availability of so many OTTs (Over the Top Applications) in the internet which are continuously being developed to be more efficient is really hurting overseas toll revenue.

Internet Services (Wi-Fi, Dial Up, ADSL and FM Domain) account for **38.87%** of FSMTC's FY2019 operating revenues as compared with **39.46%** of FSMTC'S FY 2018 operating revenues. During FY2019, FSMTC realized an **increase** in Internet service revenues of **$475,116** (or **8.46%**) as compared to FY2018. More and more customers are moving to unlimited internet service by subscribing to ADSL which contributed to the increase in internet revenue. It is expected that data services will continue to dominate the telecom services in terms of revenue contribution. With the cost of bandwidth getting cheaper and cheaper, more and more customers are moving to data services.

Mobile services account for **37.33%** of FSMTC's FY2019 operating revenues as compared with **30.33%** of FSMTC'S FY2018 operating revenues. During FY2019, FSMTC realized an **increase** in mobile service revenues of **$1,533,352** (or **35.52%**) as compared to FY2018. Mobile phones are now considered as a major personal and business accessory. With the introduction of more voice/data plans, more and more customers are enticed to register to save some money and enjoy the internet and mobile services. Data and voice roaming made a significant contribution to this positive annual change of **$685,570** or **119%** increase from prior year.

Net inbound carrier (external carriers) revenue account for **4.18%** of FSMTC's FY2019 operating revenues as compared with **7.13%** of FSMTC's FY2018 operating revenues. During FY2019, FSMTC realized a **decrease** in net carrier revenues of **$359,343** (or **-35.44%**) as compared to FY2018. Significant drop in settlement revenue can be attributed to upgrades on OTTS (Over the top services) on INTERNET such as Skype, Facebook messenger, Viber, Whatsapp, etc.

Statement of Net Position

The statement of net assets presents the assets, liabilities, and net position as of the end of the fiscal year. This statement is a point of time financial statement. The purpose of the statement of net position is to present to the readers of the financial statements a fiscal snapshot of the FSMTC. The statement of net position presents end-of-year data concerning assets (current and noncurrent), liabilities (current and noncurrent), and net position (assets minus liabilities).

From the data presented, readers of the statements of net position are able to determine the assets available to continue the operations of the FSMTC. They also are able to determine how much the FSMTC owes vendors and lending institutions. Finally, the statement of net position provides a picture of the net position (assets minus liabilities), which is a useful indicator of whether the financial position of the FSMTC is improving or deteriorating.

The following summarizes the financial condition and operations of the FSMTC for FY2019, FY2018 and FY2017:

	2019	2018	2017
Assets:			
Cash and cash equivalents	$ 2,295,300	$ 969,672	$ 1,589,393
TCD's and investments in securities	1,825,714	2,268,944	2,089,322
Receivables and prepayments	1,464,676	1,238,145	1,725,090
Inventory	895,302	971,237	734,893
Total current assets	6,480,992	5,447,998	6,138,698
Advance payment to vendor	1,077,758	711,939	201,250
Property, plant and equipment	30,646,368	31,879,267	34,371,230
Other non-current assets	2,486,907	2,649,159	2,559,411
	$ 40,692,025	$ 40,688,363	$ 43,270,589
Liabilities:			
Current liabilities	$ 2,906,485	$ 5,353,577	$ 5,022,672
Non-current liabilities	18,776,805	18,125,719	20,216,133
Total liabilities	21,683,290	23,479,296	25,238,805

Net Position:			
Net investment in capital assets	13,158,597	12,758,061	10,637,875
Restricted	0	0	0
Unrestricted	5,850,138	4,451,006	7,393,909
Total net position	19,008,735	17,209,067	18,031,784
	$ 40,692,025	$ 40,688,363	$ 43,270,589

The total liabilities of FSMTC **decreased** by **$1,796,006** (or **–7.65%**) compared with prior year. This decrease is due to RUS loan, 3G revenue sharing repayments and updated payments with major vendors and suppliers.

The 2019 equity of FSMTC was affected by the change in both assets and liabilities and **increased** by net **income** before capital contributions of **$1,799,668.**

During FY2019, total cash received from telecommunications services exceeded amounts paid to vendors and employees for goods and services. This resulted in net cash provided by operating activities of **$4,564,354** as compared with **$3,528,309** in FY2018.

Cash and cash equivalents at the end of FY2019 are **$2,295,300** as compared to **$969,672** at the end of the prior year. The **increase** in cash and cash equivalents can be attributed to a RUS loan payment break that commenced in June 2019 and the positive results in operations for FY2019.

Statement of Revenues, Expenses and Changes in Net Position

Changes in total net assets as presented on the statement of net position are based on the activity presented in the statements of revenues, expenses and changes in net position. The purpose of this statement is to present the revenues received by the FSMTC, both operating and non-operating, and expenses incurred by the FSMTC, operating and non-operating, any other revenues, expenses, gains and losses received or spent by the FSMTC.

Generally speaking, operating revenues are generated from the provision of telecommunications goods and services to various customers. Operating expenses are those expenses incurred to acquire or produce the goods or services provided in return for the operating revenues, and to carry out the mission of the FSMTC. Non-operating revenues are revenues received for which goods or services are not provided. For example, investment income is non-operating because it is earned without providing telecommunications goods or services.

The following table summarizes the financial operations of the FSMTC for the years ended September 30, 2019, 2018 and 2017.

	2019	**2018**	**2017**
Operating revenues	$ 15,670,199	$ 14,232,283	$ 14,159,193
Operating expenses	14,812,835	14,959,436	14,144,129
Net operating –loss/income	857,364	-727,153	15,064
Operating grants	0	795,228	559,979
Interest income and others	56,486	179,317	185,497
Interest expense	-962,379	-1,070,109	-1,249,545
Net non-operating –loss/income	-905,893	-822,717	-395,456
Capital grants	1,848,197	0	93,549
Net position beginning of year	17,209,067	18,031,784	18,427,240
Net position, end of year	$ 19,008,735	$ 17,209,067	$ 18,031,784

Total operating revenue in FY2019 **increased** by **$1,437,916** (or **10.10%**) compared to FY2018. Although international voice and carrier revenue continues to decrease, data, mobile and roaming revenue are now the new bloodline for the Company. Operating expenses in FY2019 **decreased** by **$146,601** (or **-0.98%**) compared to FY2018 operating expenses. This decrease can be attributed to a shift in the cost of Fiber Optic connectivity versus the cost of satellite connectivity.

The FSMTC investments in property, plant and equipment, net of accumulated depreciation, amounted to **$29,150,000** in FY2019 and **$31,139,080** in FY2018. This decrease of **$1,989,080** (or **–6.39%**) is primarily due to depreciation expense. For additional information concerning capital assets, please refer to note 4 to the accompanying financial statements.

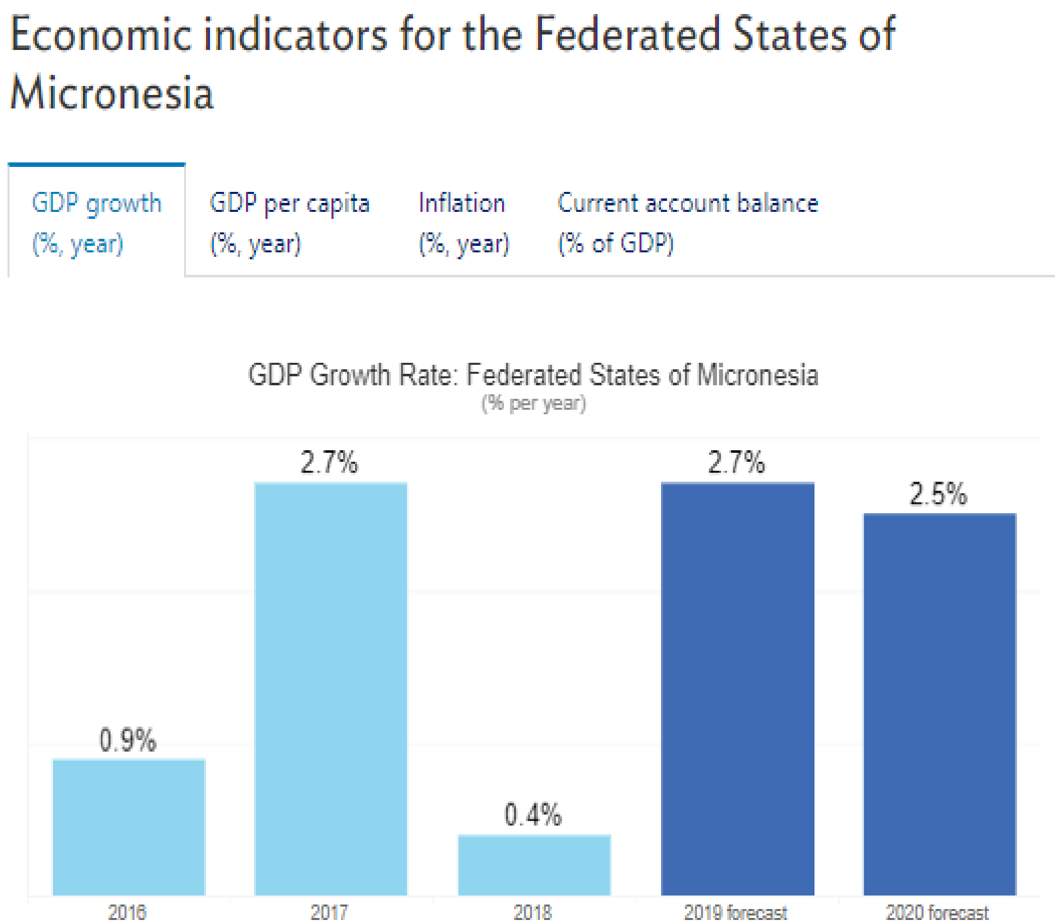
FSMTC's notes payable with the US Department of Agriculture (Rural Utilities Services) amounted to **$18,776,805** of which **$0** is classified as the current portion as of September 30, 2019 because of the 2-year loan deferment or principal payment break that commenced June 2019 until May 2021. For additional information concerning the FSMTC's long-term debt, please refer to note 7 to the accompanying financial statements.

Economic Outlook

"The economy of the Federated States of Micronesia (FSM) has performed well in recent years, with relatively high growth and low inflation. Fiscal and current account balances have recorded large surpluses since 2017, owing to the authorities' decision to save revenue windfalls. Nonetheless, the FSM faces significant medium-term uncertainty as various economic supports under the Compact Agreement with the United States are set to expire in 2023. Unless they are renewed, the FSM is expected to lose access to Compact grants, giving rise to a fiscal cliff in 2023; banking sector oversight by the Federal Deposit Insurance Corporation; and post-disaster rehabilitation assistance.

The country is highly vulnerable to climate change, while private sector activity remains anemic." *(IMF Asia and Pacific, published September 6, 2019)*

ADB projected an expected growth for 2020 of 2.5% which is slightly less than 2019 of 2.7%.

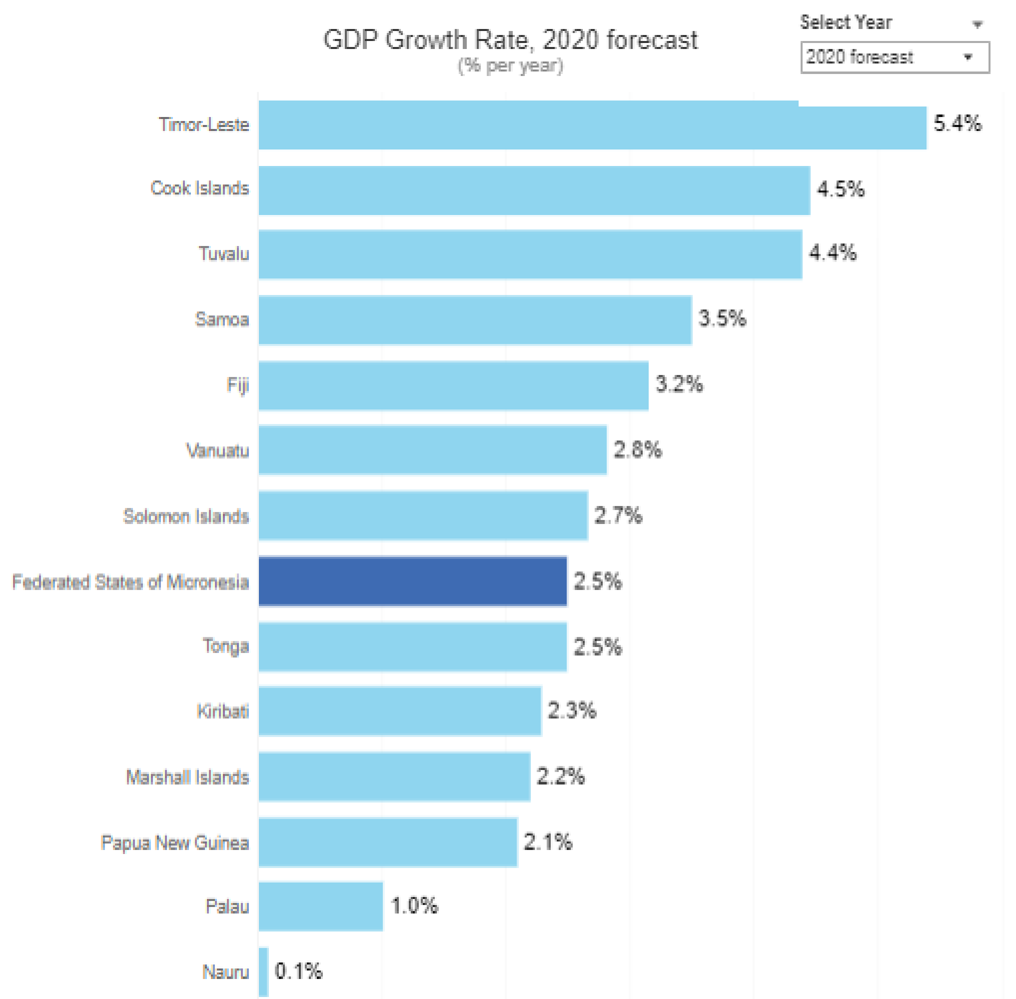


Source: Asian Development Bank. *Asian Development Outlook 2019 Update*

Comparative economic forecasts for Pacific countries

The latest available economic data for the Federated States of Micronesia compared to countries in the Pacific.

GDP growth (%, year)	GDP per capita (%, year)	Inflation (%, year)	Current account balance (% of GDP)



Source: Asian Development Bank. *Asian Development Outlook 2019 Update*

Submarine fiber optic cable landed and connected Yap state in July 2018 and also in the state of Chuuk in May 2019. With this substantial increase in broadband for the islands, telecommunications services will be better, faster and cheaper. FSMTC is committed to bring reliable and cost-effective communication services to every household in the FSM. Most of the telecommunications services provided in other more developed countries are available in the Federated States of Micronesia. These modern telecommunications services should go a long way in assisting the Federated States of Micronesia in its efforts to attract investors and to further develop our island nation. FSMTC will continue to seek improved technologies to better serve its customers and at the same time bring significant operating savings.

Over $3.7 million has already been appropriated by the FSM Congress for FSMTC for upgrades of telecommunications facilities such as cell sites in Yap and Chuuk lagoon to 4G and more cell sites to improve blind spots; improve mobile coverage in the main island of Chuuk; more cell sites in the Northwestern islands; more 3G cell sites in Kosrae and equipment services in support of the Chuuk to Pohnpei submarine cable. With all of these upgrades, the average household with superfast broadband will benefit from: Streaming HDTV programs, E-learning can be delivered at optimal speeds at any time of the day (currently much education is streamed at 'quiet' periods to avoid congestion); faster photo and video uploads, particularly when others are also accessing these services; audio and video downloads happen almost instantaneously avoiding delays and replicating the services that we are beginning to get used to in our work/school environments and better ping rates and multiple character rendering for gamers, allowing more interactivity**.** With all these new services brought about by fiber optic connectivity and new outside plant, 3G/4G LTE upgrade in Yap, Chuuk and its outer islands, FSMTC is looking forward to enhanced revenue sources.

Management's Discussion and Analysis for the year ended September 30, 2018 is set forth in FSMTC'S report on the audit of financial statements, which is dated December 20, 2018. That Discussion and Analysis explains the major factors impacting the 2018 financial statements and can be viewed at the Office of the FSM National Public Auditor's website at www.fsmopa.fm

Financial Contact

This financial report is designed to provide all interested users with a general overview of the Federated States of Micronesia Telecommunications Corporation. If you have questions about this report or need additional financial information, please contact Mr. Fredy Perman, President/CEO or Rodelio A. Pulmano, Senior Vice President/CFO at email addresses fredy.perman@fsmtc.fm and rodelio.pulmano@fsmtc.fm, respectively, or please write to us at P.O. Box 1210, Kolonia, Pohnpei FM 96941.

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION
(A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA NATIONAL GOVERNMENT)

Statements of Net Position
September 30, 2019 and 2018

	2019	2018
ASSETS		
Current assets:		
Cash and cash equivalents	$ 2,295,300	$ 969,672
Time certificates of deposit	278,763	278,479
Investment in securities	1,546,951	1,990,465
Accounts receivable, net of an allowance for doubtful accounts of $866,435 and $897,940 in 2019 and 2018, respectively	528,645	486,260
Receivables from international carriers	385,574	321,729
Advances to employees	2,758	5,539
Inventory	895,302	971,237
Accrued interest and other accrued earnings	253,879	198,686
Other receivables, net of an allowance for doubtful accounts of $149,195 and $144,856 in 2019 and 2018, respectively, and prepaid expenses	293,820	225,931
Total current assets	6,480,992	5,447,998
Advance payment to vendor	1,077,758	711,939
Capital assets:		
Nondepreciable capital assets	1,496,368	740,187
Capital assets, net of accumulated depreciation	29,150,000	31,139,080
Indefeasible right of use, net	2,486,907	2,649,159
	$ 40,692,025	$ 40,688,363
LIABILITIES AND NET POSITION		
Current liabilities:		
Current maturities of long-term debt	$ -	$ 2,038,170
Current maturities of contract liability	1,197,873	1,606,476
Accounts payable, trade	61,542	266,974
Unearned income	221,107	89,499
Customer deposits	443,761	449,908
Accrued leave payable	147,602	157,626
Other accrued liabilities	834,600	744,924
Total current liabilities	2,906,485	5,353,577
Long-term debt, net of current portion	18,776,805	18,125,719
Total liabilities	21,683,290	23,479,296
Commitments and contingencies		
Net position:		
Net investment in capital assets	13,158,597	12,758,061
Unrestricted	5,850,138	4,451,006
Total net position	19,008,735	17,209,067
	$ 40,692,025	$ 40,688,363

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION
(A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA NATIONAL GOVERNMENT)

Statements of Revenues, Expenses, and Changes in Net Position
Years Ended September 30, 2019 and 2018

	2019	2018
Operating revenues:		
Internet	$ 6,091,253	$ 5,616,137
Mobile charges	5,850,072	4,316,720
Net access	2,041,357	2,066,952
Overseas tolls	790,542	1,052,422
External carriers	654,944	1,014,487
Miscellaneous	441,539	171,377
ICTV Chuuk cable charges	73,072	87,476
ICTV Yap cable charges	43,054	53,053
ICTV Kosrae cable charges	41,850	47,385
ICTV Pohnpei cable charges	1,308	-
Recovery of bad debts	45,860	44,191
Discounts	(404,652)	(237,917)
Total operating revenues	15,670,199	14,232,283
Operating expenses:		
Internet expense	2,836,858	3,242,922
Corporate operations	2,523,066	2,530,707
Plant operations	1,878,712	1,676,652
Cable and wire	1,783,317	1,840,419
Consumer operations	1,780,271	1,578,493
Wireless telephone	1,645,377	1,663,833
General support	1,149,936	1,096,391
Central office	371,701	368,213
Terminal equipment	330,907	513,053
ICTV expense	293,775	297,563
Earth station	218,915	151,190
Total operating expenses	14,812,835	14,959,436
Income (loss) from operations	857,364	(727,153)
Nonoperating revenues (expenses):		
Operating subsidy from the FSM National Government	-	795,228
Interest expense	(962,379)	(1,070,109)
Net change in fair value of investments	56,486	179,317
Total nonoperating revenues (expenses), net	(905,893)	(95,564)
Loss before capital contributions	(48,529)	(822,717)
Capital contributions	1,848,197	-
Change in net position	1,799,668	(822,717)
Net position at beginning of year	17,209,067	18,031,784
Net position at end of year	$ 19,008,735	$ 17,209,067

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION
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Statements of Cash Flows
Years Ended September 30, 2019 and 2018

	2019	2018
Cash flows from operating activities:		
Cash received from subscribers, long distance carriers and other customers	$ 15,634,237	$ 14,113,243
Cash paid to suppliers for goods and services	(7,768,123)	(7,292,245)
Cash paid to employees	(3,301,760)	(3,292,689)
Net cash provided by operating activities	4,564,354	3,528,309
Cash flows from noncapital financing activities:		
Operating subsidy received from FSM National Government	-	795,228
Cash flows from capital and related financing activities:		
Capital contributions received from FSM National Government	1,848,197	-
Additions to property, plant and equipment	(2,828,573)	(1,583,078)
Additions to indefeasible right of use	-	(240,000)
Repayments of RUS long-term debt	(1,387,084)	(1,936,706)
Interest paid on RUS long-term debt	(1,063,371)	(1,063,371)
Principal paid on equipment contract	(408,603)	(113,060)
Interest paid on equipment contract	100,708	(7,043)
Net cash used for capital and related financing activities	(3,738,726)	(4,943,258)
Cash flows from investing activities:		
Net purchases, sales and maturities of investments	500,000	-
Net change in cash and cash equivalents	1,325,628	(619,721)
Cash and cash equivalents at beginning of year	969,672	1,589,393
Cash and cash equivalents at end of year	$ 2,295,300	$ 969,672
Reconciliation of income (loss) from operations to net cash provided by operating activities:		
Income (loss) from operations	$ 857,364	$ (727,153)
Adjustments to reconcile income (loss) from operations to net cash provided by operating activities:		
Depreciation and amortization	4,223,724	4,225,293
(Increase) decrease in assets:		
Accounts receivable	(42,385)	53,200
Receivables from international carriers	(63,845)	(3,683)
Advances to employees	2,781	3,905
Inventory	75,935	123,523
Accrued interest and other accrued earnings	(55,193)	(76,126)
Other receivables and prepaid expenses	(556,208)	(235,657)
Advance payment to vendor	122,500	(125,250)
Increase (decrease) in liabilities:		
Accounts payable, trade	(205,432)	117,483
Unearned income	131,608	(72,250)
Accrued leave payable	(10,024)	16,649
Customer deposits	(6,147)	(20,181)
Other accrued liabilities	89,676	248,556
Net cash provided by operating activities	$ 4,564,354	$ 3,528,309

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

Nature of Operations

The Federated States of Micronesia (FSM) Telecommunications Corporation (the Corporation), a component unit of the FSM National Government, is a local exchange carrier (LEC) and an international exchange carrier providing local telephone service, cellular service, internet access, long distance telecommunication services, and digital wireless TV. The Corporation serves commercial and residential customers in the four States that comprise the FSM - Chuuk, Kosrae, Pohnpei and Yap.

Organization

The Corporation was established as a public corporation under the laws of the Federated States of Micronesia, the purpose of which is to provide telecommunications services, except radio and television broadcasting, throughout the FSM and to points outside the FSM and began its operations in October 1983. The Corporation is governed by a five member Board of Directors. One member is appointed by the President of the FSM with the advice and consent of the FSM Congress. The Governor of each State of the FSM appoints one member of the Board with the advice and consent of the respective State legislatures. The Chief Executive Officer of the Corporation serves as an ex officio member of the Board but has no right to vote.

Basis of Accounting

The Corporation maintains a chart of accounts in accordance with the Uniform System of Accounts for telephone companies of the United States Federal Communications Commission's Rules, and in conformity with accounting principles generally accepted in the United States of America (GAAP). Additionally, the Corporation utilizes the accrual basis of accounting.

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 - Management's Discussion and Analysis - for State and Local Governments: Omnibus*, GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, and GASB Statement No. 61, *The Financial Reporting Entity: Omnibus - an amendment of GASB Statements No. 14 and No. 34*, establish standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into the following three net position categories:

- Net investment in capital assets - capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted - net position whose use by the Corporation is subject to externally imposed stipulations that can be fulfilled by actions of the Corporation pursuant to those stipulations or that expire by the passage of time. The Corporation has no restricted net position at September 30, 2019 and 2018.

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

(1) Summary of Significant Accounting Policies, Continued

Cash and Cash Equivalents and Time Certificates of Deposit

Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity date within three months of the date acquired by the Corporation. Deposits maintained in time certificates of deposit with original maturity dates greater than three months are separately classified in the statements of net position. Certificate of deposit investment accounts established and set aside for future capital expenditure projects are classified within investment in securities.

Investments

Investments and related investment earnings are reported at fair value using quoted market prices. Fair value is the price that would be received to sell an asset or paid to transfer a liability (ie, the exit price) in an orderly transaction between market participants at the date as of which the fair value of an asset or liability is determined.

Accounts Receivable

Accounts receivable are due from businesses and individuals located within the FSM and are interest free and uncollateralized. Receivables from international carriers are due from entities within the United States and Japan.

Accounts receivable are stated at the amount management expects to collect on outstanding balances. Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection effects are written off through a charge to the valuation allowance and a credit to accounts receivable.

Inventory

Materials and supplies are valued at cost, which approximates market, using the first-in-first-out (FIFO) method.

Property, Plant and Equipment

Property, plant and equipment are stated at cost. The Corporation capitalizes buildings, land improvements and equipment that have a cost of $200 or more and an estimated useful life of at least five years. The cost of maintenance and repairs is charged to operating expenses. Depreciation is calculated on the straight-line method over the estimated useful lives of the respective assets.

Plant under Construction

Plant under construction represents the accumulated costs of unfinished capital projects. These costs are capitalized as property, plant and equipment upon completion of each project.

(1) Summary of Significant Accounting Policies, Continued

Indefeasible Right of Use

The Corporation has capitalized the cost of acquisition of the exclusive right to use a specified amount of fiber capacity for a period of time, which is amortized over the length of the term of the capacity agreement on the straight line method.

Valuation of Long-Lived Assets

The Corporation, using its best estimates based on reasonable and supportable assumptions and projections, reviews assets for impairment whenever events or changes in circumstances have indicated that the carrying amount of its assets might not be recoverable. Impaired assets are reported at the lower of cost or fair value. At September 30, 2019 and 2018, no assets had been written down.

Deferred Outflows of Resources

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

Compensated Absences

It is the Corporation's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. No liability is reported for unpaid accumulated sick leave. Vacation pay is accrued when earned.

Unearned Income

Unearned income includes amounts received for telecommunications services prior to the end of the fiscal year but related to the subsequent accounting period.

Deferred Inflows of Resources

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

Income Taxes

Corporate profits are not subject to income tax in the FSM. Instead, the FSM National Government imposes a gross revenue tax (GRT) of 3% on gross revenues earned. The Corporation is subject to GRT; however, the Corporation is specifically exempt from any other taxes in accordance with its enabling legislation for the years ended September 30, 2019 and 2018.

(1) Summary of Significant Accounting Policies, Continued

Revenue Recognition and Classification

Billings for local service revenue and basic internet service are rendered monthly in advance. Advance billings are recorded as a liability and are subsequently transferred to income in the period earned. Prepaid card revenues are recorded when the cards are sold.

Long distance network services revenues and usage-sensitive internet service revenues are based on a per-minute charge paid by the end user or other telecommunications service providers. These revenues are billed in arrears, but are recognized in the month that service is provided.

The Corporation records all revenue generated from providing telecommunications services as operating revenue, including local service, long distance, internet, and cellular services.

Non-operating revenues and expenses result from capital, financing and investing activities and consist of investment earnings, interest paid on long-term debt, and grant funds received.

Reclassification

Certain balances in 2018 presentation have been reclassified to conform to the 2019 presentation.

New Accounting Standards

During the year ended September 30, 2019, the Corporation implemented the following pronouncements:

- GASB Statement No. 83, *Certain Asset Retirement Obligations*, which addresses accounting and financial reporting for certain asset retirement obligations (AROs) associated with the retirement of a tangible capital asset.

- GASB Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*, which improves the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements.

- GASB Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, which requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. The provisions in Statement No. 89 are effective for fiscal years beginning after December 15, 2019 with early application allowed. Interest of $55,914 related to construction work in progress was recorded as an expense by the Corporation. This did not have a material effect on the Corporation's financial statements.

The implementation of these statements did not have a material effect on the Corporation's financial statements.

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

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

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

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

In May 2019, GASB issued Statement No. 91, *Conduit Debt Obligations*, which clarifies the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures. The provisions in Statement No. 91 are effective for fiscal years beginning after December 15, 2020. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

Management 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 deferred outflows of resources, liabilities and deferred inflows of resources, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(2) Investment - Island Cable Television

On December 8, 1998, the Corporation acquired a 50% ownership in Island Cable Television – Pohnpei (ICTV) for $450,000. The Corporation recorded this investment under the equity method of accounting. Goodwill of $383,062 resulting from the purchase was being amortized over a period of fifteen (15) years. The remaining goodwill balance of $325,603 as of September 30, 2002 was written-off. On June 21, 2019, the Corporation acquired the remaining 50% ownership in Island Cable Television - Pohnpei for $100,001, which was allocated to the Corporation's respective assets and are included in the accompanying financial statements as the finalization of ICTV is in process.

(3) Deposits and Investments

The deposit and investment policies of the Corporation are governed by the Board of Directors. As such, the Board of Directors is authorized to delegate certain responsibilities to third parties. Investment managers have discretion to purchase, sell, or hold the specific securities to meet the objectives set forth in the investment policy.

(3) Deposits and Investments, Continued

Generally, the Corporation can invest in bonds and other indebtedness of the U.S. and in preferred or common stock of any corporation created or existing under the laws of the U.S. or any U.S. state, territory, or commonwealth. Additionally, a maximum of 20% of the total portfolio may be invested in non-U.S. equities.

A. Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Corporation'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 but not in the Corporation's name. The Corporation does not have a deposit policy for custodial credit risk.

As of September 30, 2019 and 2018, the carrying amount of the Corporation's total cash and cash equivalents and time certificates of deposit was $2,574,063 and $1,248,151, respectively, and the corresponding bank balances were $2,602,432 and $1,314,495, respectively, all of which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2019 and 2018, bank deposits in the amount of $373,352 and $376,011, respectively, were FDIC insured. The Corporation does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk. The Corporation has not experienced any losses in such accounts and management believes it is not exposed to any significant credit risk on its deposits.

B. Investments

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 Corporation'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 Corporation will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. As of September 30, 2019 and 2018, the Corporation's investments are held in the name of the Corporation and are administered by investment managers subject to Securities Investor Protection Corporation insurance in accordance with the Corporation's investment policy.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The Corporation's investment policy states that all fixed income securities shall have a Moody's, Standard & Poor's and/or Fitch's credit rating of no less than "BBB."

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 Corporation. As of September 30, 2019 and 2018, there were no investments in any one issuer that exceeded 5% of total investments.

(3) Deposits and Investments, Continued

B. Investments, Continued

As of September 30, 2019 and 2018, investments at fair value are as follows:

	2019	2018
Fixed income:		
U.S. Treasury obligations	$ 206,236	$ 180,477
Corporate notes	229,717	225,804
	435,953	406,281
Other investments:		
Domestic and international equities	1,092,604	1,544,688
Money market funds	18,394	39,496
	$ 1,546,951	$ 1,990,465

As of September 30, 2019, the Corporation's investments in debt securities were as follows:

	Moody's Credit Rating	Investment Maturities (In Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Treasury obligations	Aaa/P-1	$ 48,288	$ 75,302	$ 82,646	$ -	$ 206,236
Corporate notes	A1/P-1	20,050	34,709	-	-	54,759
Corporate notes	A2/P-1	-	41,177	19,089	-	60,266
Corporate notes	A3-/P-1	10,112	20,705	10,452	-	41,269
Corporate notes	BAA1/P-2	-	30,882	10,914	-	41,796
Corporate notes	BAA2/P-2-3	-	11,210	10,330	-	21,540
Corporate notes	BAA3/P-3	-	10,087	-	-	10,087
		$ 78,450	$ 224,072	$ 133,431	$ -	$ 435,953

As of September 30, 2018, the Corporation's investments in debt securities were as follows:

	Moody's Credit Rating	Investment Maturities (In Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Treasury obligations	Aaa/P-1	$ 10,155	$ 103,895	$ 66,427	$ -	$ 180,477
Corporate notes	AA3/P-1	-	14,989	-	-	14,989
Corporate notes	A1/P-1	3,991	38,406	-	-	42,397
Corporate notes	A2/P-1	-	31,828	9,691	-	41,519
Corporate notes	A3-/P-1	10,043	30,013	9,677	-	49,733
Corporate notes	BAA1/P-2	8,052	9,730	20,185	-	37,967
Corporate notes	BAA2/P-2-3	-	20,220	18,979	-	39,199
		$ 32,241	$ 249,081	$ 124,959	$ -	$ 406,281

(3) Deposits and Investments, Continued

B. Investments, Continued

The Corporation categorizes its fair value measurements within the fair value hierarchy established by GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The Corporation has the following recurring fair value measurements as of September 30, 2019 and 2018:

		Fair Value Measurements Using		
	September 30, 2019	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level:				
Fixed income:				
U.S. Treasury obligations	$ 206,236	$ -	$ 206,236	$ -
Corporate notes	229,717	-	229,717	-
Total fixed income	435,953	-	435,953	-
Equity securities:				
U.S. equities	744,145	744,145	-	-
Non U.S. equities	348,429	348,429	-	-
Total equity securities	1,092,604	1,092,604	-	-
Total investments by fair value level	1,528,557	$ 1,528,557	$ 435,953	$ -
Investments measured at amortized cost:				
Money market funds	18,394			
	$ 1,546,951			

		Fair Value Measurements Using		
	September 30, 2018	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level:				
Fixed income:				
U.S. Treasury obligations	$ 180,477	$ -	$ 180,477	$ -
Corporate notes	225,804	-	225,804	-
Total fixed income	406,281	-	406,281	-
Equity securities:				
U.S. equities	1,129,972	1,129,972	-	-
Non U.S. equities	414,716	414,716	-	-
Total equity securities	1,544,688	1,544,688	-	-
Total investments by fair value level	1,950,969	$ 1,544,688	$ 406,281	$ -
Investments measured at amortized cost:				
Money market funds	39,496			
	$ 1,990,465			

(3) Deposits and Investments, Continued

B. Investments, Continued

Equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities. Fixed income securities classified in Level 2 of the fair value hierarchy are valued using matrix-based or model-based pricing techniques. These pricing techniques, which are obtained from various sources, assume normal market conditions and are based on large volume transactions.

(4) Capital Assets

Capital asset activities of the Corporation for the years ended September 30, 2019 and 2018 are as follows:

	Estimated Useful Lives	Balance October 1, 2018	Additions	Retirements	Balance September 30, 2019
General support	5-35 years	$ 16,796,219	$ 334,505	$ (179,451)	$ 16,951,273
Central office	20 years	12,909,002	3,624	-	12,212,626
Earth station	20 years	6,528,630	1,935	(410,257)	6,120,308
Terminal equipment	5-20 years	3,616,531	67,954	(1,946)	3,682,539
Cellular network	10-20 years	22,976,776	280,954	(4,000)	23,253,730
Internet equipment	8 years	3,556,575	8,279	-	3,564,854
Pole, cable and wiring	15-20 years	44,515,950	1,375,141	-	45,891,091
Total		110,199,683	2,072,392	(595,654)	111,676,421
Accumulated depreciation		(79,060,603)	(4,061,472)	595,654	(82,526,421)
		31,139,080	(1,989,080)	-	29,150,000
Plant under Construction		740,187	2,778,672	(2,022,491)	1,496,368
Property, plant and equipment, net		$ 31,879,267	$ 789,592	$ (2,022,491)	$ 30,646,368

	Estimated Useful Lives	Balance October 1, 2017	Additions	Retirements	Balance September 30, 2018
General support	5-35 years	$ 16,534,542	$ 393,208	$ (131,531)	$ 16,796,219
Central office	20 years	12,139,906	69,096	-	12,209,002
Earth station	20 years	6,519,918	8,712	-	6,528,630
Terminal equipment	5-20 years	3,484,038	138,451	(5,958)	3,616,531
Cellular network	10-20 years	22,730,419	246,357	-	22,976,776
Internet equipment	8 years	3,374,801	208,093	(26,319)	3,556,575
Pole, cable and wiring	15-20 years	44,385,732	130,218	-	44,515,950
Total		109,169,356	1,194,135	(163,808)	110,199,683
Accumulated depreciation		(75,147,673)	(4,075,041)	162,111	(79,060,603)
		34,021,683	(2,880,906)	(1,697)	31,139,080
Plant under Construction		349,547	856,759	(466,119)	740,187
Property, plant and equipment, net		$ 34,371,230	$ (2,024,147)	$ (467,816)	$ 31,879,267

(5) Indefeasible Right of Use (IRU)

In 2009, the Corporation entered into an IRU Capital Lease agreement with a third party for the exclusive use of eight wave lengths of fiber capacity of the two fibers of the Kwajalein Cable System (KCS) which runs between Guam and Kwajalein and which is known as the "HANTRU1 System." Under the terms of the agreement, the Corporation made certain payments of $3,656,301. The initial term of the agreement is for a period of ten years commencing on the date the Corporation is initially granted access, and which term is automatically renewable for a further 10-year period and an additional 5-year period thereafter. Prior to the tenth and twentieth anniversary dates, the Corporation has the option to terminate this agreement; however, such is subject to prior approval of the Rural Utilities Services (RUS) of the U.S. Department of Agriculture. The Corporation's policy is to amortize the right of use over the 25-year period.

In 2018, the Corporation entered into another IRU Capital Lease agreement with a third party for the exclusive use of capacity of the fiber cable system which runs between Guam and mainland of United States of America. Under the terms of the agreement, the Corporation made certain payments of $240,000. The initial term of the agreement is for a period of fifteen years commencing on the date the Corporation is initially granted access, and which term is renewable on a month-to-month basis thereafter. The Corporation's policy is to amortize the right of use over the 15-year period.

As of September 30, 2019 and 2018, accumulated amortization expense of $1,409,394 and $1,247,142, respectively, has been recorded.

(6) Long-term Debt

Long-term debt at September 30, 2019 and 2018 is as follows:

	2019	2018
Loans payable to RUS, with a 35 year term, interest at 5% per annum, collateralized by the Corporation's specific ground leases and essentially all other assets. Pursuant to loan agreements dated August 1, 1990 and March 12, 2009, the Corporation is required to make monthly payments of both principal and interest to RUS. The loans were originally in the amounts of $32,000,000 and $12,136,000 and the proceeds were used for capital related purposes.	$ 18,776,805	$ 20,163,889

On May 29, 2019, the Corporation was granted a two-year principal deferral period from June 01, 2019 to May 31, 2021. The deferred principal on the loans will be re-amortized such that all outstanding RUS debt will be due and payable in full by the maturity dates. The Corporation must continue to make interest payments during the deferral period.

(6) Long-term Debt, Continued

Future minimum principal and interest payments on notes payable for subsequent years ending September 30, are as follows:

Year ending September 30,	Principal	Interest	Total
2020	$ -	$ 989,744	$ 989,744
2021	691,385	968,470	1,659,855
2022	2,144,508	855,569	3,000,077
2023	2,254,225	745,852	3,000,077
2024	2,369,555	630,521	3,000,076
2025 - 2029	9,154,255	1,450,615	10,604,870
2030 - 2032	2,162,877	138,679	2,301,556
	$ 18,776,805	$ 5,779,450	$ 24,556,255

These notes are subject to certain coverage ratio requirements. The Corporation is not in compliance with its ratio requirements as of September 30, 2019. Management is of the opinion that the lender is aware of this matter and will not call the debt. Therefore, the debt is classified in accordance with expected future payouts.

A summary of changes in long-term debt for the years ended September 30, 2019 and 2018 are as follows:

	Balance October 1, 2018	Increases	Decreases	Balance September 30, 2019	Due Within One Year
Notes payable:					
Rural Utilities Service	$ 20,163,889	$ -	$ (1,387,084)	$ 18,776,805	$ -

	Balance October 1, 2017	Increases	Decreases	Balance September 30, 2018	Due Within One Year
Notes payable:					
Rural Utilities Service	$ 22,100,595	$ -	$ (1,936,706)	$ 20,163,889	$ 2,038,170

(7) Commitments and Contingencies

Leases

The Corporation has various operating leases as of September 30, 2019. Three are for land sites for state offices beginning in 1988 for Pohnpei and Yap and 1990 for Kosrae. There is one land site lease for the southeast remote switch on Pohnpei with a 15-year term beginning in 1994. The Corporation has also entered into various circuit leases expiring through 2022.

The approximate future minimum annual lease payments payable by the Corporation are as follows:

Year ending September 30,	Total
2020	$ 240,097
2021	1,380
2022	575
	$ 242,052

(7) Commitments and Contingencies, Continued

Operation, Management and Repair (OM&R) Agreement

In 2009, the Corporation, along with the Marshall Islands National Telecommunications Authority (MINTA), entered into an OM&R agreement with a third party for the purpose of operating, maintaining, and repairing the "Micronesian Addition", which is a subset of the HANTRU1 System. The term of the agreement coincides with the term of the IRU Capital Lease agreement wherein the Corporation and MINTA are required to each make monthly payments of $6,400 less certain service credits, and which are subject to inflationary adjustments and an annual incremental increase of 3%.

Self Insurance

The Corporation purchases insurance to cover risks associated with its buildings and equipment ($10,099,944 of coverage) and vehicles (up to $1,000,000 of coverage per vehicle per incident). Additionally, the Corporation purchases fidelity insurance coverage for selected employees (total coverage of $950,000) and workmen's compensation insurance (coverage of up to $100,000 per employee). The Corporation also purchases general liability insurance in connection with operations (up to $1,000,000 per occurrence). There have been no significant reductions in coverage, and there have been no settlements in excess of insurance coverage for the past three years. The Corporation does not purchase insurance for its Outside Plant. As most of these items are underground, the Corporation is of the opinion that losses from such, if any, will be minimal. Therefore, the Corporation is self insured for Outside Plant and all other risks not encompassed in the forgoing. Management is of the opinion that no material losses have resulted from this practice.

Construction and Other Commitments

The Corporation has entered into various contracts for construction and expansion of its facilities and services. Approximately $5,795,427 is outstanding under these contracts as of September 30, 2019.

The Corporation has entered into a $4 million contract with Acclinks Communications, Inc. for a Third Generation (3G) Mobile Network Partnership Agreement signed on September 12, 2013. As of September 30, 2019 and 2018, the Corporation recognized $1,197,873 and $1,606,476, respectively, as a contract liability that will be paid through revenue sharing as agreed per payment terms. The Corporation pays 10% of total 3G revenue and 5% of 2G revenue to Acclinks as the interest and technical support fee for 5 years starting from the commencement of the 3G services.

A summary of changes in other long-term liabilities for the years ended September 30, 2019 and 2018 is as follows:

	Balance October 1, 2018	Increases	Decreases	Balance September 30, 2019	Due Within One Year
Contract liability	$ 1,606,476	$ -	$ (408,603)	$ 1,197,873	$ 1,197,873

	Balance October 1, 2017	Increases	Decreases	Balance September 30, 2018	Due Within One Year
Contract liability	$ 1,719,536	$ -	$ (113,060)	$ 1,606,476	$ 1,606,476

(7) Commitments and Contingencies, Continued

Construction and Other Commitments, Continued

Future minimum payments payable by the Corporation under this contract are as follows:

Year ending September 30,	Total
2020	$ 1,197,873

The Corporation has entered into various contract service agreements to improve internet capacity in the States of Chuuk, Kosrae and Yap.

Future minimum payments payable by the Corporation under these contracts are as follows:

Year ending September 30,	Total
2020	$ 1,869,725
2021	1,872,100
2022	1,137,000
2023	1,099,575
2024	1,097,200
2025 - 2029	5,486,000
2030 - 2033	5,303,129
	$ 17,864,729

External Carriers

External carriers located in other countries are subject to oversight policies from their respective regulatory agencies. Currently, U.S. regulatory agencies are contemplating a reduction of the tariff rate used by the Corporation for settlement with certain U.S. carriers. The ultimate outcome of this matter and the related impact on the Corporation cannot be predicted at this time.

Litigation

In the ordinary course of business, claims have been filed against the Corporation. Management does not believe that the plaintiffs will prevail and the ultimate outcome is currently not determinable. Therefore, no provision has been recorded in the accompanying financial statements for losses, if any, that may result.

(8) Related Party Transactions

The Corporation's services are provided to its affiliates at the same rates as are charged to third parties. The Corporation is a component unit of the FSM National Government. As of September 30, 2019 and 2018, receivables from the FSM National Government amounted to $65,096 and $43,939, respectively.

During the years ended September 30, 2019 and 2018, the Corporation received capital contributions and operating subsidies of $1,848,197 and $795,228, respectively, from the FSM National Government for the purpose of upgrading network services in all four states.

(8) Related Party Transactions, Continued

Cable System in Chuuk and Yap State

On March 15, 2019, FSM National Government transferred to FSM Telecommunications Cable Corporation (FSMT Cable Corporation), a component unit of the FSM National Government, the custody and maintenance of new submarine cable systems constructed under the financial agreement namely Yap Spur and Chuuk-Pohnpei Cable. The Corporation pays monthly charges for the services provided by FSMT Cable Corporation based on actual costs incurred. During the years ended September 30, 2019 and 2018, the Corporation recognized expenses of $210,795 and $120,702, respectively, for services provided by FSMT Cable Corporation.

(9) Retirement Plan

The Corporation's retirement plan (the Plan) is a self-administered program established to pay retirement, disability and survivor income to employees and their survivors to supplement similar benefits that employees received from the FSM Social Security System. The Plan is a contributory plan in which the Corporation contributes 10 percent of the participant's annual salary, and the participant contributes 3 or more percent from his or her annual salary. Participation is optional. The Corporation's controller is the designated Plan administrator. Employer contributions to the Plan during the years ended September 30, 2019, 2018 and 2017 were $220,735, $224,352, and $217,010, respectively, and employee contributions were $141,963, $138,811 and $132,009, respectively. Management is of the opinion that the plan does not represent an asset or liability of the Corporation. At September 30, 2019 and 2018, plan assets were $4,985,095 and $4,796,596, respectively.

(10) Subsequent Event

The Telecommunication Regulation Authority (TRA) has assessed the Corporation a fee of 1.25% starting in fiscal year 2020. The fee will be based on latest gross revenue available.

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION
(A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA NATIONAL GOVERNMENT)

Schedule of Operating Expenses
Years Ended September 30, 2019 and 2018

	2019	2018
Depreciation and amortization	$ 4,223,724	$ 4,225,293
Salaries and wages	3,305,089	3,323,815
Circuit lease	2,346,792	2,762,999
Utilities	1,171,738	1,117,077
Repairs and maintenance	968,756	881,831
Cost of sales	877,556	598,906
Taxes	387,613	396,208
Travel	257,580	268,871
Rental expenses	204,743	144,037
Petroleum and lubricants	162,756	142,704
Contractual services	155,249	268,891
Communications	92,967	106,811
Training	72,663	86,815
Freight	71,723	75,119
Advertising	65,118	113,675
ICTV affiliated	63,491	59,608
Professional fees	61,317	59,167
Insurance	55,338	50,658
Supplies	41,601	70,411
Publications and printing	26,604	19,217
Representation	22,177	36,117
Land lease	21,746	19,764
Miscellaneous	156,494	131,442
	$ 14,812,835	$ 14,959,436

See accompanying Independent Auditors' Report.

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION
(A COMPONENT UNIT OF THE FEDERATED STATES OF MICRONESIA NATIONAL GOVERNMENT)

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2019

U.S. Department of Agriculture

Rural Utilities Service Loan Funding:

Approved Purposes	Loan Proceeds Approved as of September 30, 2019	Loan Proceeds Received During FY 2019	Total Disbursements on Contracts During FY 2019
F/A 1	$ 411,584	$ -	$ -
Work Orders	422,905	-	-
CT. A-4	90,688	-	-
CT. A-5	1,191,004	-	-
CT. A-6	650,676	-	-
CT. A-7	3,108,615	-	-
CT. A-8	3,500,000	-	-
CT. A-9	1,108,149	-	-
CT. A-10	636,505	-	-
CT. A-11	1,193,317	-	-
CT. A-12	1,422,800	-	-
CT. A-13	19,440,795	-	-
CT. A-14X	1,988,002	-	-
CT. B-15	8,206,857	-	-
CT. B-16E	274,500	-	-
CT. A-1E	275,625	-	-
CT. A-2E	4,008,263	-	-
CT. A-3A	304,109	-	-
Operating Equipment	387,263	-	-
Pre-Loan	55,000	-	-
IRU Capital Lease	3,656,301	-	-
	$ 52,332,958	$ -	$ -

See accompanying Independent Auditors' Report.

Deloitte.

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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*

Board of Directors
Federated States of Micronesia
Telecommunications Corporation:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Federated States of Micronesia (FSM) Telecommunications Corporation (the Corporation), which comprise the statement of net position as of September 30, 2019, and the related statements of revenues, expenses, and changes in net position and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 20, 2019.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Corporation's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as item 2019-001.

The Corporation's Response to Findings

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

Purpose of this Report

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

Deloitte & Touche LLP

December 20, 2019

Loan Noncompliance

Finding No. 2019-001

Criteria: Section 5.12, *TIER Requirement*, of the RUS Loan Agreements state the required Times Interest Earned Ratio (TIER) rate that is to be maintained. Such provision has also been stated under the preliminary review of “B” Loan letter dated November 19, 2008 requiring at least 1.5 commencing December 31, 2012.

Condition: Per examination of RUS Form 479 for the year ended December 31, 2018, submitted by the Corporation on February 18, 2019, the TIER rate reported was (0.09), which is less than the criteria.

Cause: The cause of the above condition is insufficient earnings to cover interest on funded debt as of December 31, 2018, the RUS loan reporting period, which resulted in a TIER rate less than the minimum requirement.

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

Prior Year Status: Noncompliance with Section 5.12 of the RUS Loan Agreements was reported as a finding in the audits of the Corporation for fiscal years 2013 through 2018.

Recommendation: We recommend compliance with the criteria.

Views of Auditee and Planned Corrective Actions:

See the auditee-prepared corrective action plan.

FSM Telecommunications Corporation

Unresolved Prior Year Findings
Year Ended September 30, 2019

Summary Schedule of Prior Audit Findings

Finding Number	Finding Title	Status
2018-001	Loan Noncompliance	Not Corrected or Resolved. See corrective action plan - Finding 2019-001

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FSM TC
FSM Telecommunications Corporation

CORRECTIVE ACTION PLAN
2 CFR § 200.511(c)
Year Ended September 30, 2019

Finding Number	Corrective Action Plan	Anticipated Completion Date	Responsible Person (Contact details)
2019-001	Based on the audited result in operations for fiscal year 2019, FSM Telecom have already met RUS TIER requirement as of September 30, 2019. By December 31, 2019, which is RUS reporting date, FSM Telecom, without a doubt will meet such requirement.	Ongoing	Fredy Perman/CEO

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