

*Financial Statements and
Required Supplementary Information*

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

*Years ended September 30, 2023 and 2022
with Report of Independent Auditors*



Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Financial Statements and Required Supplementary Information

Years ended September 30, 2023 and 2022

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Report of Independent Auditors

The Board of Directors
Kosrae Housing and Rural Development Authority

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of the business-type activities of Kosrae Housing and Rural Development Authority (the Authority), as of and for the years ended September 30, 2023 and 2022, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of Kosrae Housing and Rural Development Authority at September 30, 2023 and 2022, and the changes in financial position and its cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States (*Government Auditing Standards*). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Authority, and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

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

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Authority's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibility for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Authority's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Authority's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 8 be presented to supplement the basic financial statements. Such information is the responsibility of management and, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with GAAS, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 2, 2025, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Authority's internal control over financial reporting or on compliance . That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

Ernst + Young LLP

September 2, 2025

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Management's Discussion and Analysis

Years ended September 30, 2023 and 2022

This analysis prepared by Kosrae Housing and Rural Development Authority (Authority) offers readers of the Authority's financial statements this narrative overview and analysis of its financial activities for the year ended September 30, 2023. We encourage readers to consider the information presented here in conjunction with Authority's financial statement, which follow this section. Fiscal years 2022 and 2021 comparative information has been included where appropriate. This analysis is required by the Government Accounting Standards Board (GASB), which provides guidelines on what must be included and excluded from the analysis.

FINANCIAL HIGHLIGHTS

- For fiscal year ended September 30, 2023, the Authority's net operating revenue decrease by (\$14,042) or 13% from prior year. The decrease in net operating revenues was mainly attributed to the increased number of delinquent loans.
- The assets of the Authority exceeded its liabilities at the close of the fiscal year (FY2023) with \$475 thousand (net position), a decrease of \$103 thousand (or 18%) compared to prior year. Of this amount, \$38.3 thousand represents the Authority's investments in capital, \$436.8 thousand represents amount restricted for housing and producers' programs and services.
- During the current fiscal year (FY2023) the Authority's operational expense total up to \$288.9 thousand, a 28% increase compared to prior year. The operation of the Authority continued to rely heavily on interest, fees and charges on loans.

Overview of the Financial Statements

The financial statements presented herein interlude all of the activities of the Authority including in this report are the statement of net position and the statement of revenues, expenses, changes in net position. These financial statements present the complete financial picture of the Authority from the economic measurement focus substantially using the accrual basis of accounting. The Authority operated on an annual budget authorized by the Board of Directors. It continues to rely heavily on interest on loans, loan fees and charges.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Management's Discussion and Analysis, continued

The Authority's assets exceeded liabilities by \$475 thousand at the close of FY2023. \$38 thousands of which is restricted as to the purpose it can be used for is invested in capital assets. The Authority is using these capital assets to provide services to the citizens, consequently these asset are not available for future spending. The majority of the Authority's net position is comprised of its capital assets and current liabilities. Current assets and liabilities are amounts that are available in the current period and obligations that will be paid within one year, respectively. The current assets of the Authority amounted to \$0 thousand while current liabilities amounted to \$162.2 thousand.

The following table summarizes the Statement of Net Position for years ended September 2023, 2022, 2021:

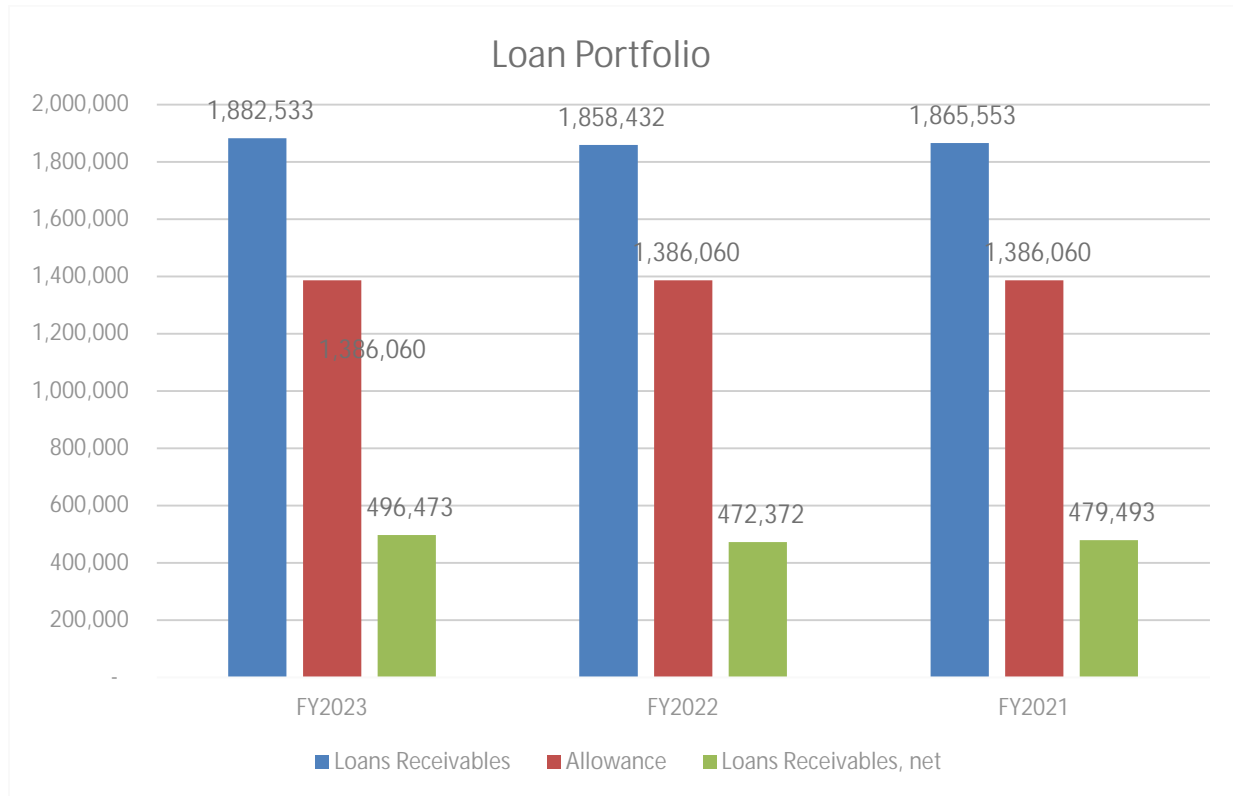
	<u>2023</u>	<u>2022</u>	<u>2021</u>
Assets			
Cash and receivables	\$496,473	\$485,987	\$526,539
Time certificates of deposit	200,000	200,000	200,000
Property and equipment, net	<u>38,255</u>	<u>45,238</u>	<u>62,005</u>
Total assets	<u>\$734,728</u>	<u>\$731,225</u>	<u>\$788,544</u>
Liabilities			
Current liabilities	\$162,375	\$137,056	\$182,231
Long term liabilities	<u>97,328</u>	<u>16,135</u>	<u>59,941</u>
Total liabilities	<u>259,703</u>	<u>153,191</u>	<u>242,172</u>
Net position			
Net investment in capital asset	38,255	45,238	62,005
Restricted	<u>436,770</u>	<u>532,796</u>	<u>484,367</u>
Total net position	<u>475,025</u>	<u>578,034</u>	<u>546,372</u>
Total liabilities & net position	<u>\$734,728</u>	<u>\$731,225</u>	<u>\$788,544</u>

The Authority's restricted net position at the close of FY23 decreased to \$436,770 (a \$96,026 decrease), a result of commitments or obligations that are more than currently available resources. The increase in current liabilities is resulted in the increase in accounts payable and accrued liabilities.

Kosrae Housing and Rural Development Authority
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Management's Discussion and Analysis, continued

The following is the graphical illustration of the 3-year trend loan portfolio of the Kosrae Housing & Rural Development Authority.



Changes in Net Position

As noted earlier, the net position of the Authority decreased by \$103 thousand, representing an 18% decrease from the prior year's amount of \$578 thousand. This result indicates that the Authority's financial condition has experienced slight decrease from prior year. The key elements of the differences from prior year are shown in the following schedule:

Kosrae Housing and Rural Development Authority
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Management's Discussion and Analysis, continued

Revenues, Expenses and Changes in Net position

	<u>2023</u>	<u>2022</u>	<u>% change</u> <u>(2023-2022)</u>	<u>2021</u>
Operating revenue:				
Interest & fees	\$ 93,921	\$124,088	(24.3%)	\$ 95,841
(Provision for) recovery of loan loss	<u>---</u>	<u>(16,125)</u>	(100.0%)	<u>47,000</u>
Total operating revenue	<u>93,921</u>	<u>107,963</u>	(13.0%)	<u>142,841</u>
Operating expenses	<u>288,875</u>	<u>226,433</u>	28.0%	<u>196,325</u>
Non-operating revenues (expenses):				
Operating grant from US Government	101,035	131,916	(23.4%)	212,995
Other income	---	23,780	(100.0%)	---
Interest expense	<u>(9,090)</u>	<u>(5,564)</u>	63.3%	<u>(6,736)</u>
Total non-operating revenues, net	<u>91,945</u>	<u>150,132</u>	(38.8%)	<u>206,259</u>
Change in net position	(103,099)	31,662	(425.6%)	152,775
Net position at beginning of year	<u>578,034</u>	<u>546,372</u>	5.8%	<u>393,597</u>
Net position at end of year	<u>\$475,025</u>	<u>\$578,034</u>	(17.8%)	<u>\$546,372</u>

Economic Factors and Next Year's Budget

The Authority continues to face economic and financial challenges as the demands from its clients continue to increase and available resources to fill the gap of \$700 thousand and run its operation still limited. As in prior years, the Authority continues to rely heavily on interest and fees on loans to run daily operation. The Authority continues to received grant received from the US Federal Programs. It is the Authority's goal and mission to provide safe and decent housing at low cost for the people of Kosrae. To reduce the delinquency rate and improve customer servicing and lending in FY2024, the Authority shall continuously pursue aggressive collections.

The Kosrae State Law 10-115 authorized the Authority to lend toward rural development projects. The Authority after its effort and tireless work to secure more funding for the Production Loan Program and Housing Preservation Program.

The Authority has a loan portfolio of \$1.5 million and carries an updated credit classification report. The Authority expects a lower level of bad debt expense in FY2024 since the delinquency rate decreased to 18% after year end of FY2023.

Kosrae Housing and Rural Development Authority
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Management's Discussion and Analysis, continued

Management's Discussion and Analysis for the year ended September 30, 2022, is set forth in the report on the audit of financial statements, which is dated April 18, 2024. That Discussion and Analysis explains the major factors impacting the 2022 financial statements and can be viewed at the Office of the Public Auditors' website at www.fsmopa.fm

Contacting the Authority's Financial Management

This financial report is designed to provide our customers, creditors, and other interested parties a general overview of Kosrae Housing & Rural Development Authority's finances. If you have questions about this report or need additional financial information, contact the Executive Director, Kosrae State Housing Authority P.O. Box 533 Tofol, Lelu, Kosrae, FM 96944.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Statements of Net Position

	September 30, <u>2023</u>	<u>2022</u>
Assets		
Current assets:		
Cash	\$ <u>---</u>	\$ <u>13,615</u>
Total current assets	---	13,615
Loans receivable, net	496,473	472,372
Restricted time certificates of deposit	200,000	200,000
Property and equipment, net	<u>38,255</u>	<u>45,238</u>
	<u>\$734,728</u>	<u>\$731,225</u>
Liabilities and net position		
Current liabilities:		
Notes payable	\$ 50,000	\$ 50,000
Current portion of long-term debt	28,224	43,893
Accrued liabilities	41,954	31,494
Accounts payable	<u>42,197</u>	<u>11,669</u>
Total current liabilities	162,375	137,056
Long-term debt, net of current portion	<u>97,328</u>	<u>16,135</u>
Total liabilities	<u>259,703</u>	<u>153,191</u>
Commitments and contingencies		
Net position:		
Net investment in capital assets	38,255	45,238
Restricted	<u>436,770</u>	<u>532,796</u>
Total net position	<u>475,025</u>	<u>578,034</u>
	<u>\$734,728</u>	<u>\$731,225</u>

See accompanying notes.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Statements of Revenues, Expenses and Changes in Net Position

	Year ended September 30,	
	<u>2023</u>	<u>2022</u>
Operating revenues:		
Interest and fees on loans	\$ 93,921	\$124,088
Bad debt	<u>---</u>	<u>(16,125)</u>
Net operating revenues	<u>93,921</u>	<u>107,963</u>
Operating expenses:		
Salaries	173,567	181,631
Supplies and materials	46,544	5,310
Repairs and maintenance	17,746	679
Depreciation	10,545	16,767
Travel and transportation	8,264	---
Contractual services	8,225	3,995
Fuel	6,268	3,711
Utilities	5,680	4,640
Food	5,071	2,346
Communication	3,827	4,719
Meetings	1,738	2,635
Trainings	<u>1,400</u>	<u>---</u>
Total operating expenses	<u>288,875</u>	<u>226,433</u>
Operating loss	<u>(194,954)</u>	<u>(118,470)</u>
Non-operating revenues (expenses):		
Operating grant from U.S. Government	101,035	131,916
Other income	---	23,780
Interest expense	<u>(9,090)</u>	<u>(5,564)</u>
Total non-operating revenues, net	<u>91,945</u>	<u>150,132</u>
Change in net position	<u>(103,009)</u>	<u>31,662</u>
Net position at beginning of year	<u>578,034</u>	<u>546,372</u>
Net position at end of year	<u>\$475,025</u>	<u>\$578,034</u>

See accompanying notes.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Statements of Cash Flows

	Year ended September 30,	
	<u>2023</u>	<u>2022</u>
Cash flows from operating activities:		
Cash received from customers	\$ 93,921	\$ 124,088
Cash paid to suppliers for goods and services	(74,235)	(60,434)
Cash paid to employees	(163,107)	(172,483)
Net cash used in operating activities	(143,421)	(108,829)
Cash flows from noncapital financing activities:		
Operating grant from U.S. Government	101,035	131,916
Proceeds on long-term debt	150,000	---
Principal repayment on long-term debt	(84,476)	(41,900)
Interest payment on long-term debt	(9,090)	(5,564)
Net cash provided by noncapital financing activities	<u>157,469</u>	<u>84,452</u>
Cash flows from capital and related financing activities:		
Acquisition of fixed assets	(3,562)	---
Cash flows from investing activities:		
Loan originations and principal collections, net	(24,101)	<u>7,221</u>
Net change in cash	(13,615)	(17,156)
Cash at beginning of year	<u>13,615</u>	<u>30,771</u>
Cash at end of year	<u>\$ ---</u>	<u>\$ 13,615</u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$(194,954)	\$(118,470)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation	10,545	16,767
Bad debt	---	16,125
Decrease in advance to employees	---	50
Increase in accrued liabilities	10,460	9,098
Increase (decrease) in accounts payable	<u>30,528</u>	(32,399)
Net cash used in operating activities	<u>\$(143,421)</u>	<u>\$(108,829)</u>

See accompanying notes.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Notes to Financial Statements

Years ended September 30, 2023 and 2022

1. Organization

The Kosrae Housing and Rural Development Authority (the "Authority"), formerly named Kosrae Housing Authority, was established in October 2015 by Kosrae State Public Law 10-113 with the name change in June 2017 by Kosrae State Public Law 11-115. The purpose of the Authority is to manage and invest funds of Kosrae Home Improvement Program and other funds of the Authority and to lend money to qualified Kosraeans who wish to build and maintain residential homes in Kosrae.

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

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

2. Summary of Significant Accounting Policies

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America as applicable to governmental entities, specifically proprietary funds. The Governmental Accounting Standards Board (GASB) establishes financial reporting standards for governmental entities, which require that management's discussion and analysis of the financial activities be included with the basic financial statements and notes and modifies certain other financial statement disclosure requirements.

Net Position

Net position represents the residual interest in the Authority's assets after liabilities are deducted and consist of three sections: net investment in capital assets, restricted and unrestricted. Net position classified as net investment in capital assets include capital assets, restricted and unrestricted, net of accumulated depreciation and reduced by outstanding debt, net of debt service reserve. Net position is reported as restricted when constraints are imposed by third parties or enabling legislation. At September 30, 2023 and 2022, all of the Authority's restricted assets are expendable, and are restricted for loan programs.

Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and deferred outflows of resources, and liabilities and deferred inflows of resources associated with the operation of the fund are included in the statements of net position. Proprietary fund operating statements present increases and decreases in net position. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Accounting Estimates

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

Cash and Time Certificate of Deposits

For the purposes of the statements of net position and of cash flows, cash is defined as cash in checking accounts, savings accounts and cash on hand. Time certificates of deposit with original maturity term over ninety-days or restricted for specific purposes are separately presented. At September 30, 2023 and 2022, the Authority's time certificate of deposit is restricted as pledges for USDA Rural Development loan guarantees (note 3), a line of credit (note 5) and a long-term debt (note 6).

As of September 30, 2023 and 2022, the carrying amount of the Authority's total cash and time certificates of deposit was \$200,000 and \$213,615, respectively, and the corresponding bank balance was \$208,889 and \$224,419, respectively, which is maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2023 and 2022, total bank deposits in the amount of \$208,889 and \$224,419, respectively, covered under the FDIC insurance limit.

Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Authority does not have a deposit policy for custodial credit risk.

Property and Equipment

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

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Loans and Allowance for Loan Losses

Loans receivable are stated at unpaid principal balance less the allowance for loan losses. A majority of the Authority's loans has a maturity term of 10 years or over, and as such, loans, net have been presented as non-current asset in the accompanying statements of net position.

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

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

Deferred Outflows of Resources

In addition to assets, the statements 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. As of September 30, 2023 and 2022, the Authority has no items that qualify for reporting in this category.

Deferred Inflows of Resources

In addition to liabilities, the statements of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element 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. As of September 30, 2023 and 2022, the Authority has no items that qualify for reporting in this category.

Compensated Absences

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

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Taxes

The Authority exists and operates solely for the benefit of the public and shall be exempted from any State or Municipal taxes or assessments on any of its property, operations or activities. The Authority shall be liable for employees' contributions to the National Social Security System or other employees' benefits of the State or FSM National Governments, if any, in such manner as provided by law.

Operating and Non-operating Revenues and Expenses

Proprietary funds 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 proprietary fund's principal ongoing operations, which is lending. Operating expenses include the cost to provide services, including cost of funds, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Authority enters into off-balance sheet financial instruments consisting of commitments to extend credit and loan guarantees. Such financial instruments are recorded in the financial statements when they become payable.

Recently Adopted Accounting Pronouncements

In May 2019, GASB issued Statement No. 91, *Conduit Debt Obligations*. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying 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.

In March 2020, GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The primary objective of this statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements. This statement also provides guidance for accounting and financial reporting for availability payment arrangements.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Recently Adopted Accounting Pronouncements, Continued

In May 2020, GASB issued Statement No. 96, *Subscription-Based Information Technology Arrangements*. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset - an intangible asset - and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA.

The adoption of these GASB statements did not have a material effect on the financial statements.

Upcoming Accounting Pronouncements

In June 2022, GASB issued Statement No. 100, *Accounting Changes and Error Corrections – An Amendment of GASB Statement No. 62*. The primary objective of this Statement is to enhance accounting and financial reporting requirements for accounting changes and error corrections to provide more understandable, reliable, relevant, consistent, and comparable information for making decisions or assessing accountability. The requirements of this Statement will improve the clarity of the accounting and financial reporting requirements for accounting changes and error corrections, which will result in greater consistency in application in practice. In turn, more understandable, reliable, relevant, consistent, and comparable information will be provided to financial statement users for making decisions or assessing accountability. In addition, the display and note disclosure requirements will result in more consistent, decision useful, understandable, and comprehensive information for users about accounting changes and error corrections. GASB Statement No. 100 will be effective for fiscal year ending September 30, 2024.

In June 2022, GASB issued Statement No. 101, *Compensated Absences*. The objective of this Statement is to better meet the information needs of financial statement users by updating the recognition and measurement guidance for compensated absences. That objective is achieved by aligning the recognition and measurement guidance under a unified model and by amending certain previously required disclosures. The unified recognition and measurement model in this Statement will result in a liability for compensated absences that more appropriately reflects when a government incurs an obligation. In addition, the model can be applied consistently to any type of compensated absence and will eliminate potential comparability issues between governments that offer different types of leave. The model also will result in a more robust estimate of the amount of compensated absences that a government will pay or settle, which will enhance the relevance and reliability of information about the liability for compensated absences. GASB Statement No. 101 will be effective for fiscal year ending September 30, 2025.

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In December 2023, GASB issued Statement No. 102, *Certain Risk Disclosures*. The objective of this Statement is to provide users of government financial statements with essential information about risks related to a government's vulnerabilities due to certain concentrations or constraints. This Statement defines a concentration as a lack of diversity related to an aspect of a significant inflow of resources or outflow of resources. A constraint is a limitation imposed on a government by an external party or by formal action of the government's highest level of decision-making authority. Concentrations and constraints may limit a government's ability to acquire resources or control spending. This Statement requires a government to assess whether a concentration or constraint makes the primary government reporting unit or other reporting units that report a liability for revenue debt vulnerable to the risk of a substantial impact. Additionally, this Statement requires a government to assess whether an event or events associated with a concentration or constraint that could cause the substantial impact have occurred, have begun to occur, or are more likely than not to begin to occur within 12 months of the date the financial statements are issued. GASB Statement No. 102 will be effective for fiscal years ending September 30, 2025.

3. Loans Receivable

The Authority's loan portfolio is comprised of Kosrae Home Improvement Program, USDA Rural Development ("USDA RD") loans and Economic Development Administration Revolving Loan Fund ("EDA RLF") loans.

The State of Kosrae transferred defaulted USDA Rural Development (RD) loans to the Authority. The Authority guarantees USDA RD loans and bears responsibility for collection. As of September 30, 2023 and 2022, the balance of USDA Rural Development loans is \$32,360 and \$32,311, respectively. The Authority has pledged an escrow account in support of USDA RD loans. As of September 30, 2023 and 2022, \$200,000 of time certificates of deposit has been pledged for this purpose. Per the USDA RD agreement with the State, \$300,000 is to be so pledged.

The Authority administers EDA RLF loans and bears responsibility for collection. As of September 30, 2023 and 2022, the balance of EDA Revolving Loan Fund loans is \$389,610 and \$271,348, respectively. The EDA RLF funds were established through a \$400,000 grant award from the United States Department of Commerce Economic Development Administration in July 2020. The grant requires a non-federal matching at 20% of total project expense, or \$100,000. The Authority provides its non-Federal Matching Share contribution for eligible project expenses in proportion to the Federal share requested for such project expenses.

Kosrae Housing and Rural Development Authority
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Notes to Financial Statements, continued

3. Loans Receivable, continued

A summary of loans receivable as of September 30, 2023 and 2022, is presented below:

	<u>2023</u>	<u>2022</u>
Kosrae Home Improvement Program loans	\$1,448,335	\$1,554,773
EDA Revolving Loan Fund loans	389,610	271,348
USDA Rural Development loans	32,360	32,311
Other loans receivable	<u>12,228</u>	<u>---</u>
	1,882,533	1,858,432
Less allowance for loan losses	<u>(1,386,060)</u>	<u>(1,386,060)</u>
Loans receivable, net	\$ <u>496,473</u>	\$ <u>472,372</u>

There are no recorded loan loss provisions, charge-offs or recoveries during the years ended September 30, 2023 and 2022.

4. Notes payable

The Authority maintains a \$50,000 bank Line of Credit for working capital, which may be subject to annual renewal. The line is secured by a \$200,000 time certificate of deposit (TCD) maintained with the same Bank. Borrowing against the line bears interest floating at 3.5% plus the TCD interest rate (effective rate of 3.51% at September 30, 2022), with interest payable monthly and principal due upon maturity of February 1, 2023. On February 20, 2023, the note was rolled over to mature on February 20, 2024. The note contains the same TCD collateral, now bears interest at a fixed rate of 4%. Accrued interest and outstanding principal are due and payable upon maturity.

Changes in short-term debt during the years ended September 30, 2023 and 2022 are as follows:

	<u>Balance October 1, 2022</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2023</u>	<u>Due Within One Year</u>
Short-term debt	\$ <u>50,000</u>	\$ <u>50,000</u>	\$(<u>50,000</u>)	\$ <u>50,000</u>	\$ <u>50,000</u>

	<u>Balance October 1, 2021</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2022</u>	<u>Due Within One Year</u>
Short-term debt	\$ <u>50,000</u>	\$ <u>50,000</u>	\$(<u>50,000</u>)	\$ <u>50,000</u>	\$ <u>50,000</u>

Kosrae Housing and Rural Development Authority
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Notes to Financial Statements, continued

5. Long-Term Debt

In March 2019, a \$200,000 bank term-loan was obtained to fund operations. The line is secured by the \$200,000 time certificate of deposit (TCD). The loan bears an interest floating at 5.0% plus the TCD interest rate (effective rate of 5.01% at September 30, 2022).

In November 2022, a \$150,000 bank term-loan was obtained to pay off the 2019 term-loan and to fund operations. The line is secured by the \$200,000 time certificate of deposit (TCD). The loan bears an interest floating at 5.0% plus the TCD interest rate (effective rate of 5.75% at September 30, 2023). The loan requires a monthly principal and interest payment of \$2,831 beginning December 2022 for sixty months ending in November 2027.

Changes in long-term debt during the years ended September 30, 2023 and 2022 are as follows:

	Balance October <u>1, 2022</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2023</u>	Due Within <u>One Year</u>
Long-term debt	<u>\$60,028</u>	<u>\$150,000</u>	<u>\$(84,476)</u>	<u>\$125,552</u>	<u>\$28,224</u>
	Balance October <u>1, 2021</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2022</u>	Due Within <u>One Year</u>
Long-term debt	<u>\$101,928</u>	<u>\$ ---</u>	<u>\$(41,900)</u>	<u>\$60,028</u>	<u>\$43,893</u>

As of September 30, 2023, the scheduled payments of the above long-term debt are as follows:

<u>Year Ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2024	\$ 28,224	\$ 5,753	\$ 33,977
2025	29,679	4,298	33,977
2026	31,197	2,780	33,977
2027	32,797	1,180	33,977
2028	<u>3,655</u>	<u>34</u>	<u>3,689</u>
	<u>\$125,552</u>	<u>\$14,045</u>	<u>\$139,597</u>

Kosrae Housing and Rural Development Authority
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Notes to Financial Statements, continued

6. Property and Equipment

Capital asset activities for the years ended September 30, 2023 and 2022 are as follows:

	<u>Estimated Useful Life</u>	<u>Balance at October 1, 2022</u>	<u>Additions and Transfers</u>	<u>Deletions and Transfers</u>	<u>Balance at September 30, 2023</u>
Depreciable:					
Building	10 years	\$ 79,000	\$ ---	\$ ---	\$ 79,000
Office equipment	1-5 years	7,594	---	---	7,594
Furniture and fixtures	1-5 years	9,610	---	---	9,610
Vehicles	1-5 years	<u>18,970</u>	<u>3,562</u>	<u>---</u>	<u>22,532</u>
		115,174	3,562	---	118,736
Less accumulated depreciation		(69,936)	(10,545)	---	(80,481)
		<u>\$ 45,238</u>	<u>\$ (6,983)</u>	<u>\$ ---</u>	<u>\$ 38,255</u>
	<u>Estimated Useful Life</u>	<u>Balance at October 1, 2021</u>	<u>Additions and Transfers</u>	<u>Deletions and Transfers</u>	<u>Balance at September 30, 2022</u>
Depreciable:					
Building	10 years	\$ 79,000	\$ ---	\$ ---	\$ 79,000
Office equipment	1-5 years	7,594	---	---	7,594
Furniture and fixtures	1-5 years	9,610	---	---	9,610
Vehicles	1-5 years	<u>18,970</u>	<u>---</u>	<u>---</u>	<u>18,970</u>
		115,174	---	---	115,174
Less accumulated depreciation		(53,169)	(16,767)	---	(69,936)
		<u>\$ 62,005</u>	<u>\$ (16,767)</u>	<u>\$ ---</u>	<u>\$ 45,238</u>

7. Related Parties

Except when a loan is under EDA RLF and is specifically approved by the Board because it is determined that the Authority is a sole provider, the Authority is generally prohibited from lending money to its employees or their immediate relatives pursuant to Kosrae State Public Law 10-113. As of September 30, 2023 and 2022, the Authority has \$143,358 and \$135,099, respectively of loans receivable from employee family members, who are eligible under the EDA RLF program.

The Authority initiated an Employee Pay Advance Program in May 2018. The Authority requires employees to repay the amount of the advance with 10.5% interest within a one-year term. As of September 30, 2023 and 2022, the balance of advances to employees of \$16,125 was fully provided with allowance due to lack of collection.

Kosrae Housing and Rural Development Authority
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Notes to Financial Statements, continued

8. Grants and Subsidies

The Authority receives grants from the United States Government and other foreign governments and organization either as a direct or as a sub-recipient from the Kosrae State Government or the FSM National Government. During the years ended September 30, 2023 and 2022, the Authority recorded grant revenue of \$50,335 and \$131,916, respectively under the \$400,000 EDA RLF grant (note 3). There is no remaining EDA RLF grant balance as September 30, 2023.

On September 3, 2021, the Authority was awarded a grant with a sum not to exceed \$147,750 from USDA through Housing Preservation Grant (HPG), which has a September 3, 2024 completion date, as extended. During the year ended September 30, 2023, the Authority recorded grant revenue of \$50,700 under the HPG grant. Remaining USDA HPG grant balance was \$97,050 at September 30, 2023.

9. Commitments and Contingencies

Loan Commitments

As of September 30, 2023 and 2022, the Authority has loan commitments aggregating \$310,710 and \$493,791, respectively. The loan commitments represent undisbursed balances of approved loans for housing projects.

Risk Management

The Authority does not purchase insurance to cover risks associated with potential losses. Management is of the opinion that no material losses during the years ended September 30, 2023 and 2022, respectively, have resulted from this practice.

Litigation

The Authority is a party to various legal proceedings, the ultimate impact of which is not currently predictable. Therefore, no liability has been recorded in the accompanying financial statements due to management's inability to predict the ultimate outcome of these proceedings.

Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board of Directors
Kosrae Housing and Rural Development Authority:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Kosrae Housing and Rural Development Authority (the “Authority”), which comprise the statement of net position as September 30, 2023, 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 September 2, 2025.

Report on Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify a certain deficiency in internal control, described in the accompanying Schedule of Findings and Questioned Costs, that we consider to be a material weakness as item 2023-001.

Report on Compliance and Other Matters

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

The Authority's Responses to Findings

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

Purpose of this Report

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

Ernst + Young LLP

September 2, 2025

Kosrae Housing and Rural Development Authority
(A Component Unit of the State of Kosrae)

Schedule of Findings and Responses

Year Ended September 30, 2023

Finding No.: 2023-001
Area: Loan Receivable

Criteria: The Authority should maintain an adequate system of accounting to facilitate the reconciliation of its general ledger with supporting schedules, including individual loan account history reports.

Condition: Because of inadequacies in the accounting records, detailed records regarding loans and the allowance for loan losses were not substantiated by underlying supporting documentation evidencing the validity of loans. The Authority did not utilize accounting or loan software and did not maintain an adequate system of accounting.

USDA loan collections were recorded in the incorrect GL account.

Cause: The cause of this condition is primarily due to inadequate accounting assistance, the absence of closing procedures and review and the lack of adequate filing and document maintenance systems.

Effect: The effect of this condition is an inability to substantiate certain financial statement balances, financial statement transactions and compliance with laws and regulations.

Identification as a Repeat Finding: 2021-001

Recommendation: The Authority should acquire adequate accounting assistance, should prepare monthly financial statements that are supported by its books and records, and should maintain an adequate filing and retention system and be able to demonstrate compliance with laws and regulations.

Auditee Response and Corrective Action Plan: The Authority agrees with this finding as a repeat finding. The office has revived contract discussions with software company and will procure the loan and accounting system likely in FY2024. Funding is the primary cause of delays.