FEDERATED STATES OF MICRONESIA
COCONUT DEVELOPMENT AUTHORITY

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2001 AND 2000

Deloitte & Touche LLP
361 South Marine Drive
Tamuning, Guam 96913-3911

Tel: (671)646-3884
Fax: (671)649-4932
www.dttguam.com

Deloitte
Touche
Tohmatsu

INDEPENDENT AUDITORS' REPORT

Chairman
Board of Directors
Federated States of Micronesia
Coconut Development Authority:

We have audited the accompanying balance sheets of Federated States of Micronesia (FSM) Coconut Development Authority, a component unit of the National Government of FSM, as of September 30, 2001 and 2000, and the related statements of (loss) earnings and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the FSM Coconut Development Authority's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of Federated States of Micronesia Coconut Development Authority as of September 30, 2001 and 2000, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 6 to the financial statements, the Authority changed its method of accounting for nonexchange transactions to conform with Government Accounting Standards Board Statement No. 33 and has restated the 2000 financial statements to reflect the change.

In accordance with *Government Auditing Standards,* we have also issued our report dated November 28, 2001 on our consideration of the FSM Coconut Development Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Deloitte + Touche LLP

November 28, 2001

FEDERATED STATES OF MICRONESIA
COCONUT DEVELOPMENT AUTHORITY

Balance Sheets
September 30, 2001 and 2000

ASSETS		2001		2000
Current assets:				
Cash and equivalents	$	83,556	$	144,938
Investments		169,607		213,840
Copra buyers' revolving fund, net		53,609		42,500
Accounts receivable, net		69,106		4,318
Due from other funds		-		247
Travel advances		-		6,437
Interest receivable		843		886
Prepayments		1,251		1,133
Copra bags inventory		13,413		30,315
Copra inventory, net		19,925		5,233
Total current assets		411,310		449,847
Property, plant and equipment, net (note 2)		198,371		216,410
	$	609,681	$	666,257

LIABILITIES AND FUND EQUITY		2001		2000
Current liabilities:				
Accounts payable	$	61,059	$	19,334
Accrued payroll and others		-		5,327
Total current liabilities		61,059		24,661
Fund equity:				
Retained earnings:				
Public assets (note 4)		646,616		646,616
Operations		(97,994)		(5,020)
Total equity		548,622		641,596
Contingency (note 5)				
	$	609,681	$	666,257

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA
COCONUT DEVELOPMENT AUTHORITY

Statements of (Loss) Earnings and Retained Earnings
Years Ended September 30, 2001 and 2000

	2001	2000
Copra sales	$ 82,614	$ 115,747
Cost of copra sold	(153,032)	(219,716)
Gross loss	(70,418)	(103,969)
Operating expenses:		
Personnel services	60,246	62,582
Contractual services	39,134	26,357
Ocean freight	32,589	26,742
Depreciation	25,120	22,939
Travel	21,233	19,301
Bad debts	17,229	19,861
Consumables and others	17,143	16,995
Damaged bags expense	10,285	8,884
Handling	7,213	3,967
Per diem and transportation	360	441
Laboratory division	320	22,943
Stevedoring	67	7,530
Inventory shrinkage	-	17,839
Agency fees	-	6,718
Miscellaneous	3,966	8,759
Total expenses	234,905	271,858
Loss from operations	(305,323)	(375,827)
Nonoperating revenues (expenses), net:		
Loss from fire (note 5)	(145,714)	-
Interest	8,925	4,276
Grants and subsidies (note 3)	348,953	399,573
Miscellaneous	185	25,110
Total nonoperating revenues (expenses), net	212,349	428,959
Net (loss) earnings	(92,974)	53,132
Retained earnings at beginning of year	641,596	588,464
Retained earnings at end of year	$ 548,622	$ 641,596

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA
COCONUT DEVELOPMENT AUTHORITY

Statements of Cash Flows
Years Ended September 30, 2001 and 2000

	2001	2000
Increase (decrease) in cash and equivalents:		
Cash flows from operating activities:		
Operating loss	$ (305,323)	$ (375,827)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	25,120	22,939
Bad debts	17,229	19,861
Others	185	25,110
Loss from fire	(145,714)	-
	(408,503)	(307,917)
Changes in assets and liabilities:		
Accounts receivable	(93,083)	(21,309)
Inventory and prepayments	2,092	5,535
Accounts payable	41,725	14,406
Travel advances	6,437	(4,491)
Due from other funds	247	(247)
Accrued payroll and others	(5,327)	4,307
	(47,909)	(1,799)
Net cash used for operating activities	(456,412)	(309,716)
Cash flows from noncapital financing activities:		
Congress of the FSM appropriations	348,953	399,573
Cash flows from capital and related financing activities:		
Acquisition of property, plant and equipment	(7,081)	(56,787)
Cash flows from investing activities:		
Liquidation (acquisition) of investments	44,233	(213,840)
Interest received	8,925	3,890
Net cash used for investing activities	53,158	(209,950)
Decrease in cash	(61,382)	(176,880)
Cash and equivalents at beginning of year	144,938	321,818
Cash and equivalents at end of year	$ 83,556	$ 144,938

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

A. Reporting Entity

The Coconut Development Authority of the Federated States of Micronesia (the Authority) was established in 1981 by Public Law 1-145, as amended by Public Law 2-8, and incorporated as Chapter Two, Title 22 of the Code of the Federated States of Micronesia. The purpose of the Authority is to manufacture, process, buy, collect, market, sell, export, inspect, improve the quality, and deal with, in general, all products derived from the coconut tree. The Authority has the additional responsibility to establish prices to producers or sellers of coconut products in the Federated States of Micronesia, to collect and receive all monies derived from the sales of coconut products, and to stabilize the price of these products. The Authority is a component unit of the National Government of the Federated States of Micronesia.

The affairs of the Authority are managed by a five-member board, consisting of representatives of the four FSM states and the FSM National Government. Daily operations of the Authority are delegated to a general manager, who is hired by and serves at the pleasure of the board.

The operation of the Authority is funded by annual appropriations from the FSM Congress. The purchase of coconut products is funded by copra subsidy appropriations from the FSM Congress and revenues generated through sales of copra.

The financial statements of the Authority have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. Government Accounting Standards Board (GASB) Statement No. 20, “Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting”, requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Authority has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

B. Fund Structure and Basis of Accounting

The accounts of the Authority are organized in the same manner as a proprietary fund-component unit. A proprietary fund is used by governmental units that are operated in a manner similar to private business enterprises. The purpose of a proprietary fund is to provide periodic determination of revenues, expenses and net income, with maintenance of capital. Proprietary funds are accounted for on the flow of economic resources measurement focus, whereby all assets and liabilities associated with the operations of the funds are included on the balance sheet. This is in contrast to "governmental" fund type accounting, which has a measurement focus on the sources and uses of funds, and includes only current assets and current liabilities on the balance sheet.

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. The Authority uses the accrual basis of accounting. Revenues are recognized when they are earned and expenses are recognized when the related liabilities are incurred, regardless of when cash is received or payment is made.

(1) Summary of Significant Accounting Policies, Continued

C. Reclassification

Certain accounts in the 2000 statements have been reclassified to conform with the 2001 presentation.

D. Cash and Equivalents

For the purposes of the balance sheets and the statements of cash flows, cash and equivalents are defined as cash in checking accounts and certificates of deposit with initial maturities of ninety days or less. As of September 30, 2001 and 2000, $100,000 is subject to FDIC coverage with remaining balances being uncollateralized.

E. Investments

Investments consist of time certificates of deposits (TCDs) with original maturity dates in excess of ninety days.

F. Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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.

G. Receivables

The Authority purchases and collects copra from local vendors within the FSM states and the majority of sales is primarily derived from one customer based in Singapore.

Receivables are carried at cost, less an allowance for doubtful accounts. The allowance for doubtful accounts is estimated using the valuation method. Accounts determined to be uncollectible are charged against the allowance. Uncollectibility of accounts is determined by management based on the financial condition and responsiveness of the debtors to the Authority's collection efforts. Amounts ultimately collected could differ materially from the amounts estimated in determining the allowance for doubtful accounts.

Copra Buyers Revolving Fund. In prior years, the Authority executed contracts with local businesses within the FSM states, wherein the businesses agreed to act on behalf of the Authority as copra purchasing agents. As part of the agreements, the Authority advances $10,000 to each agent to be used for the purchase and collection of copra. The advances are treated as a revolving fund, whereby the agents purchase copra from the producers in their home states and submit voucher claims to the Authority for replenishment. There are ten designated purchasing agents of which only five were active during the year ended September 30, 2001.

(1) Summary of Significant Accounting Policies, Continued

G. Receivables, Continued

A summary of the copra revolving fund at September 30, 2001 and 2000, is presented below:

	2001	2000
Copra revolving funds advanced	$ 111,609	$ 91,000
Allowance for doubtful accounts	(58,000)	(48,500)
Copra revolving funds, net	$ 53,609	$ 42,500

Accounts Receivable. Accounts receivable substantially arise from local copra sales, of which one entity is considered to be a related party. The Chairman of the Board of Directors of Coconut Development Authority is also the General Manager of the Pohnpei Coconut Products, from whom the total related party receivable is due. A summary at September 30, 2001 and 2000, is as follows:

	2001	2000
Trade accounts receivable	$ 85,334	$ 99,014
Related party accounts receivable	104,921	99,360
	190,255	198,374
Allowance for doubtful accounts	(121,149)	(194,056)
Accounts receivable, net	$ 69,106	$ 4,318

H. Inventory

Inventory consists of dried copra and copra bags which are collected and stored at designated warehouses located within the four FSM states. Copra inventory is carried at cost determined through use of average costs. Cost may ultimately exceed market value, a factor which is offset by subsidies for this purpose which are received from the FSM National Government (note 3).

Ending copra inventory at September 30, 2001 and 2000, is valued at a cost of $260 per short ton ($.13 per pound).

The inventory of bags is recorded at cost. Provision for damaged bags and deterioration in value of usable bags is made at the end of each fiscal year.

I. Property, Plant and Equipment

Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation expense is calculated by the straight-line method over the estimated useful life of the assets.

(2) Property, Plant and Equipment

A summary of the Authority's property, plant and equipment at September 30, 2001 and 2000, is as follows:

	Estimated Useful Life	2001	2000
Buildings	20 years	$ 238,333	$ 238,333
Vehicles	5 years	28,082	28,082
Furniture and fixtures	5-10 years	84,656	77,591
Leasehold improvements	20 years	11,255	11,255
Water tank	10 years	3,489	3,489
		365,815	358,750
Accumulated depreciation		(167,444)	(142,340)
Property, plant and equipment, net		$ 198,371	$ 216,410

(3) Grants and Subsidies

During the years ended September 30, 2001 and 2000, the Authority recognized grants and contributions from FSM Congressional appropriations as follows:

	2001	2000
Copra subsidy funds	$ 200,000	$ 200,000
Operational grants:		
FSM Food Division contribution	12,364	-
Administrative expenses	129,205	142,014
Capital asset additions	7,384	57,559
Total grants and subsidies	$ 348,953	$ 399,573

(4) Public Assets

At September 30, 2001 and 2000, public assets include the net assets of $575,116 transferred from the Trust Territory of the Pacific Islands on the dissolution of the old Coconut Stabilization Board. Additionally, the Authority received a $71,500 appropriation from the FSM National Government in fiscal year 1990 for the construction of a warehouse and office at Dekehtik, Pohnpei.

(5) Risk Management

The Company purchases insurance to cover risks associated with its warehouses ($96,500 of coverage) and its inventory and office contents ($130,000 of coverage). The Company is self insured for all other risks. During the year ended September 30, 2001, the Company’s inventory in Yap was completely destroyed by fire resulting in an estimated loss of $145,714 which was charged to operations during 2001. No other such losses occurred in the prior two years.

(6) Adoption of New Accounting Principle

Effective October 1, 2000, the Authority adopted GASB Statement No. 33, "Accounting and Financial Reporting for Nonexchange Transactions." GASB No. 33 establishes more uniform revenue recognition criteria and financial reporting standards regarding the timing of recognition of the results of nonexchange transactions involving cash and other financial and capital resources. The provisions of GASB No. 33 were applied to all periods presented. Implementation of GASB No. 33 had no material impact on the 2000 financial statements.

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Tamuning, Guam 96913-3911

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Deloitte
Touche
Tohmatsu

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

Chairman
Board of Directors
Federated States of Micronesia
Coconut Development Authority:

We have audited the financial statements of Federated States of Micronesia Coconut Development Authority (FSMCDA), as of and for the year ended September 30, 2001, and have issued our report thereon dated November 28, 2001. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether FSMCDA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 the objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered FSMCDA's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

However, we noted two matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operations of the internal control over financial reporting that, in our judgment, could adversely affect FSMCDA's ability to record, process, summarize and report financial data consistent with assertions of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as item 2001-01 through 2001-04.

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable conditions described above are not material weaknesses.

This report is intended for the information of management and the Board of Directors. However, this report is a matter of public record and its distribution is not limited.

Deloitte + Touche LLP

November 28, 2001

Sales/Receivables

Finding No. 2001-01

Criteria: Policies and procedures should be in place to promote timely collection of receivables.

Condition: Cash advances made to copra buyer agents and other individuals are not recovered on a timely basis. The advances made to the buyer agents should be collected upon termination/expiry of the agent agreement.

Also, sales are granted to customers with accounts receivable balances greater than one year old.

Cause: Set procedures are not in place to recover advances once a contract has expired.

With respect to trade receivables, management is reluctant to cut off sales to customers (largely Pohnpei Coconut Products) because management believes the situation is inherent to this subsidized industry.

Effect: Excessively aged accounts receivable balances increase the likelihood of large balances becoming uncollectible.

Prior Year Status: This condition was reported as an internal control finding in the audit of the Authority for the years ended September 30, 2000 and 1999.

Recommendation: We recommend that prior to termination of a buyer agency agreement and while there are still purchases from the buyer agent, such payments for copra purchases be off set against the advance for that buyer agent. This will ensure the recovery of these advances on a timely basis.

With respect to trade receivables, we recommend that further deterioration of accounts receivable aging be avoided by attempting to collect receivables on a timely basis. If management believes this situation is a form of subsidizing the industry, a less risky method of helping customers would be to grant discounts for early payment. In addition, if management does not believe these amounts are recoverable, an adequate provision or write-off should be made.

Auditee Response dated October 7, 2002: The Authority has begun to receive payments of old accounts from the previous Copra Buyers. Currently Trans Co., Susumu Enterprises, Pattiew Development Authority are making monthly payments on their accounts. Whenever there are delays the Authority makes an effort to remind them of their payments. Still there are other old buyers that are now insolvent and are unable to pay back what they owed the Authority. These will be brought to the attention of the Board for decision. The Authority will also follow your recommendation to accumulate reasonable amount to be offset against the advance for the buyer.

Ponape Coconut Product Inc. (PCPI) has made arrangement with the Authority to pay addition 10% on top of their current purchases to be applied to their old account. Currently PCPI is purchasing on cash basis. This practice has been going on and have been proven to be successful.

Fixed Assets

Finding No. 2001-02

Criteria: Policies and procedures should be in place to dispose of fixed assets.

Condition: Fixed assets are currently being disposed of without any documented approval or authorization.

Cause: Procedures are not in place to properly dispose of fixed assets.

Effect: Fixed assets may be overstated as a result of this condition.

Recommendation: We recommend that all disposals of assets be documented by the authorized approval of either the Board of Directors or General Manager.

Auditee Response dated October 7, 2002: This is an oversight and the Authority will make sure that all disposals of assets be documented and disposed of by the proper authority.

Expenses

Finding No. 2001-3

Criteria: Policies and procedures should be in place to promote adequate maintenance of supporting documentation.

Condition: During tests of FSM Food Division expenses, supporting invoices for two out of six selections were not provided.

Cause: The cause of this condition is that the necessary documents were not available for our inspection.

Effect: A possible overstatement of expenses may exist as a result of this condition.

Recommendation: We recommend that invoices be properly maintained and made readily available for review.

Auditee Response dated October 7, 2002: This is also an oversight and the Authority will make certain that such an error does not appear again in the future.

FSM Food Division

Finding No. 2001-4

Criteria: The Authority should account for all of its activities in its financial statements.

Condition: The Authority has not combined the Food Division in its financial statements.

Cause: The Authority appears to have been uncertain as to the correct manner of reporting the results of the Food Division.

Effect: The effect is that without the Food Division, an incomplete financial presentation results.

Recommendation: The Authority should combine the Food Division operation in its financial statements.

Auditee Response dated October 7, 2002: When the Authority launched its Food Division Project it was the intention of the Authority to deposit all moneys collected from the sales of products manufactured by this division and all other daily transactions and prepare a financial statement that will show every details and prepare separate financial statements. We thought it would be more appropriate to go that direction. Since your recommendation recommends to combine the Food Division operation in our financial statement of the Authority we will follow your recommendation beginning this fiscal year so it can be reflected in the next audit of FY 2002.