

**COLLEGE OF MICRONESIA-FSM**

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**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT**

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**SEPTEMBER 30, 2004 AND 2003**

## INDEPENDENT AUDITORS' REPORT

Board of Regents  
College of Micronesia-FSM:

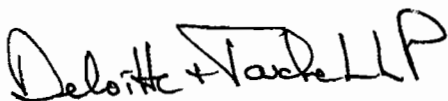
We have audited the accompanying statement of net assets of the College of Micronesia-FSM, a component unit of the FSM National Government, as of September 30, 2004 and 2003, and the related statements of revenues, expenses and changes in net assets, and of cash flows for the years then ended. These financial statements are the responsibility of the College'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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the College's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the College of Micronesia-FSM as of September 30, 2004 and 2003, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 1-8 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the College's management. We have applied certain limited procedures to such information, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 22, 2005, on our consideration of the College's internal control over financial reporting and our tests of its compliance and other matters. The purpose of that report is to describe the scope of our testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.



December 22, 2005

# **COLLEGE OF MICRONESIA-FSM**

## **Management's Discussion and Analysis September 30, 2004 and 2003**

The Management's Discussion and Analysis (MD & A) is supplementary information required by the Government Accounting Standards Board 35 (GASB 35) reporting model. The preparation of MD & A is the responsibility of the management of COM-FSM, and it is designed to help the readers in understanding the accompanying financial statements and the accompanying notes to the financial statements.

### **Institution Background**

The College of Micronesia-FSM (COM-FSM) is a multi-campus institution and serves as the only higher education facility in the Federated States of Micronesia (FSM) which has a population of over 110,000. The COM-FSM has a network of six college campuses located on four different islands in the Western Pacific. The main campus (referred to as the National campus) is located in Palikir, Pohnpei. The other college sites are state campuses on Pohnpei (Kolonias Town), Kosrae, Yap and Chuuk. FSM Fisheries and Maritime Institute (FSM – FMI), the sixth campus, is located in Yap State.

COM – FSM is a public corporation of FSM established by Public Law 7 – 79 on September 25, 1992 and considered a component unit of the FSM National Government. The governing body for the general management and control of COM – FSM is vested to a five-member Board of Regents appointed by the FSM President with the advice and consent of the FSM Congress. The President of the College, appointed by the Board of Regents, has the full charge and control of the administration and business affairs of the College.

COM – FSM is accredited by the Accrediting Commission for Community and Junior Colleges of the Western Association of Schools and Colleges, an institutional accrediting body recognized by the Commission on Recognition of Post-secondary Accreditation and the U.S. Department of Education. Accreditation was awarded to the College in 1978 and reaffirmed in 1982, 1987, 1992, 1998 and June 2005.

### **COM-FSM Mission**

During the Accrediting Commission's visit in April 2005 concerns were raised on the difficulty of assessing the College's achievement of the then mission statement. The Board of Regents tasked management to revisit the mission statement of the College. After many discussions by and evaluation of the inputs from the college community, the Board of Regents approved new mission statement for the College during its September 2005 meeting to read:

“Historically diverse, uniquely Micronesian, and globally connected, the College of Micronesia-FSM is a continuously improving and student centered institute of higher education. The college is committed to assisting in the development of the Federated States of Micronesia by providing academic, career and technical education opportunities for student learning.

### **Overview of Fiscal Year 2004**

COM – FSM offered thirty-eight degree and certificate programs: fifteen Certificates of Achievement, six degrees in Associate of Arts, nine degrees in Associate of Science, three degrees in Associate of Applied Science and five Third year Certificates. There are 5,370 students enrolled in these degree and certificate programs across all campuses for fall 03, spring 04 and summer 04. National campus enrolled 40% or 2,150 students, Pohnpei campus had 14% or 730 students, Chuuk campus had 30% or 1,610 students, Kosrae campus had 11% or 580 students and Yap campus had at 5% or 300 students. The total enrollment in fiscal year 2004 of 5,370 is lower by 7.5% or 436 students compared with fiscal year 2003 enrollment of 5,806.

# COLLEGE OF MICRONESIA-FSM

## Management's Discussion and Analysis September 30, 2004 and 2003

The College continues to administer three U.S. Federal Student Aid Programs (Pell Grant, FSEOG and Work Study). These U.S. Federal Student Aid Programs awarded to students provided more than 90% of the tuition and fees paid by the students. In the current fiscal year, the Federal Pell Grant Program has increased by \$880k, from \$7.015 million in FY 2003 to \$7.895 million. In addition, the College continues to manage U.S. government sponsored educational programs funded by Department of Education, and vocational and maintenance programs by Department of Interior.

FSM National Government continues to provide financial support to the operations of the College. The support of FSM National Government has increased by \$293K, from \$3.220 million in FY 2003 to \$3.513 million in FY 2004.

### Financial Statements Analysis

The College started implementing the new financial reporting standards for public colleges and universities in accordance with Government Accounting Standards Board (GASB) principles in FY 2003. The funds are now presented in consolidated financial statements as a whole, rather than on the fund basis used under the former accounting model. Adopting the GASB principles provide the new financial reporting of the following three basic financial statements:

#### 1. Statement of Net Assets (SNA)

SNA presents what the College owns (assets), owes (liabilities) and the net assets (the difference between total assets and total liabilities) at the end of fiscal year. The "net assets" is one indicator of the current financial condition of the College, while the change in net assets is an indicator of whether the overall financial condition has improved or worsened during the year.

Comparative Statement of Net Assets at September 30, 2004 and 2003 are summarized below:

	FY 2004 (In 000's)	FY 2003 (In 000's)
Assets:		
Current assets	\$ 11,415	\$ 10,451
Noncurrent assets	<u>15,327</u>	<u>15,800</u>
Total assets	<u>26,742</u>	<u>26,251</u>
Liabilities:		
Current liabilities	4,045	3,541
Noncurrent liabilities	<u>192</u>	<u>163</u>
Total liabilities	<u>4,237</u>	<u>3,704</u>
Net assets	\$ <u>22,505</u>	\$ <u>22,547</u>

The comparison of the statement of net assets for FY 2004 with FY 2003 indicates a slight reduction of net assets by \$42K.

**Current assets:** The current assets of \$11.415 million consist of cash and cash equivalents of \$5.408 million, receivable from FSM government of \$1.894 million, receivable from students of \$2.729 million and other current assets from inventory, other receivables and prepayments of \$1.384 million. The total current assets for FY 2004 increased by \$964K in comparison with FY 2003.

## COLLEGE OF MICRONESIA-FSM

Management's Discussion and Analysis  
September 30, 2004 and 2003

**Noncurrent assets:** The noncurrent assets of \$15.327 million consist of \$13.157 million capital assets, net of accumulated depreciation, endowment investments of \$1.948 million and \$221K grants/contracts receivable from the U.S. Government. The total noncurrent assets for FY 2004 dropped by \$473K compared with FY 2003. The market value of endowment investments increased \$271K as a result of an unrealized gain for FY 2004. However, the capital assets dropped by a net amount of \$609K, total purchased assets less depreciation expense.

**Current liabilities:** The current liabilities of \$4.045 million consist of deferred revenue of \$2.394 million and payables to vendors and affiliates of \$1.651 million. The increase in current liabilities in FY 2004 was \$504K in comparison with FY 2003. The bulk of the increase of 60% or \$306K is from deferred revenue consisting primarily of tuition and fees of students for Fall 2004.

**Noncurrent liabilities:** The noncurrent liabilities of \$192K consist of the long-term portion of the accrued annual leave.

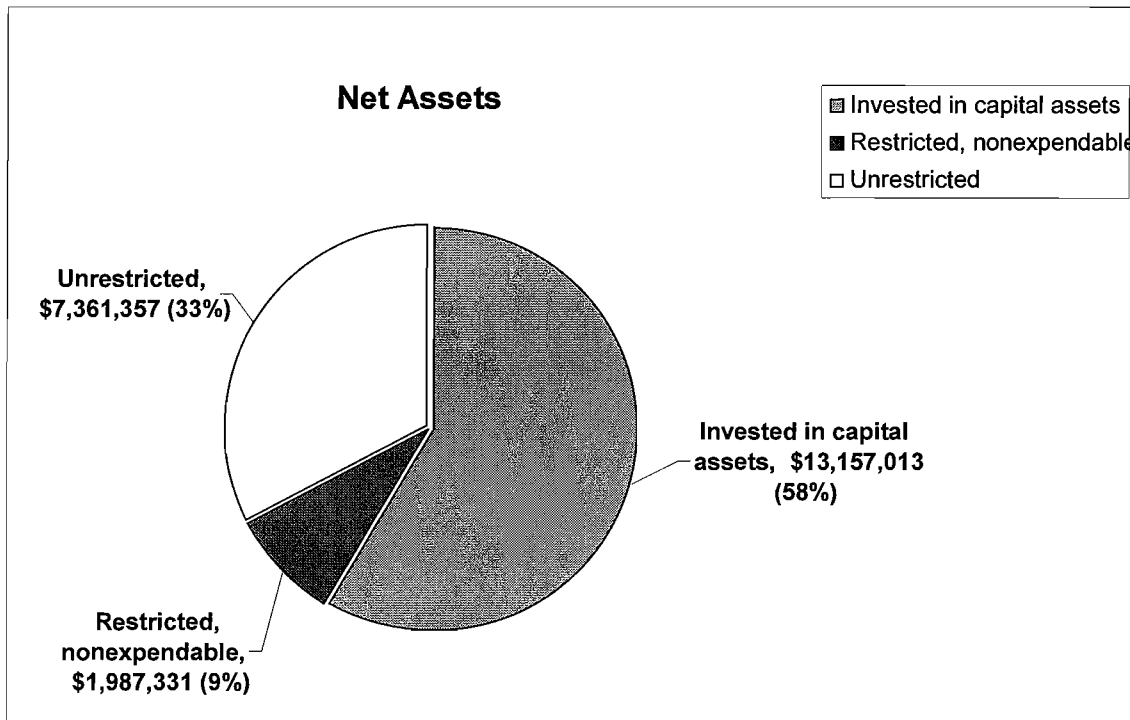
**Net Assets:** Net assets represent the residual interest in the College's assets after the liabilities are deducted. Below is the breakdown of the College's net assets as categorized in the new reporting model of GASB:

	FY 2004 (In 000's)	FY 2003 (In 000's)
Invested in capital assets	\$ 13,157	\$ 13,767
Restricted:		
Nonexpendable	1,987	1,706
Unrestricted	<u>7,362</u>	<u>7,074</u>
Total	\$ <u>22,506</u>	\$ <u>22,547</u>

Net asset invested in capital assets of \$13.157 million or 58% represents the College's capital assets net of accumulated depreciation. The restricted nonexpendable net assets of \$1.949 million or 9% represents the endowment investment which is required to be retained in perpetuity. The remaining net assets of \$7.400 million or 33% is unrestricted net assets which includes all remaining assets that can be committed or designated to support specific academic programs, capital construction projects, among other things, by the COM-FSM Board of Regents. Below is the pie graph for the College's Net Assets for fiscal year 2004:

# COLLEGE OF MICRONESIA-FSM

Management's Discussion and Analysis  
September 30, 2004 and 2003



## 2. Summary Statement of Revenues, Expenses and Changes in Net Assets (SRECNA)

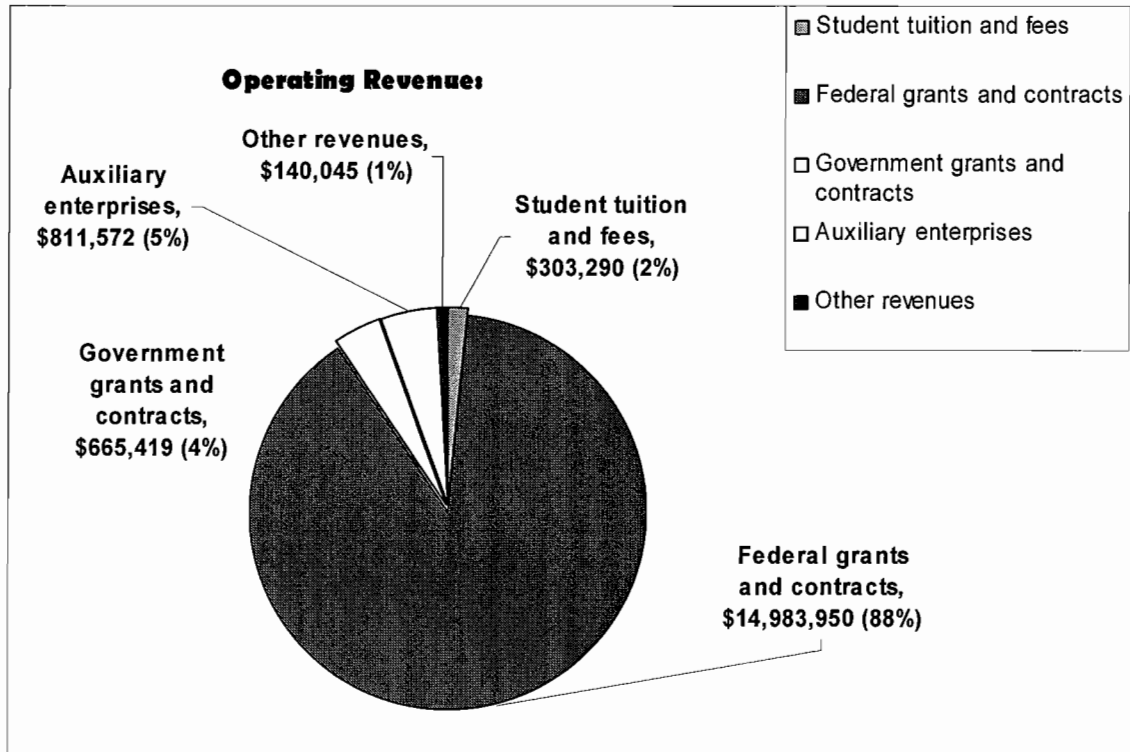
The SRECNA provides information on the College's financial performance for the current fiscal year in terms of revenues and expenses. It presents the operating revenue and expenses and the corresponding net operating results, as well as non-operating revenues and expenses for the College. Below is the comparative summary of SRECNA for the College for fiscal years ended September 30, 2004 and 2003:

	FY 2004 (In 000's)	FY 2003 (In 000's)
Operating revenues	\$ 16,904	\$ 13,102
Operating expenses	<u>18,008</u>	<u>16,819</u>
Operating loss	(1,104)	(3,717)
Net nonoperating revenue	<u>1,063</u>	<u>8,903</u>
Net increase/decrease in net assets	(41)	5,186
Net assets at beginning of year	<u>22,547</u>	<u>17,361</u>
Net assets at end of year	\$ <u>22,506</u>	\$ <u>22,547</u>

**Operating revenues:** Operating revenues consist of tuition and fees, federal grants and contracts, government contracts, sales and services of auxiliary enterprises and other revenues. About 95% of the students at the College receive U.S. Federal Student Aid, FSM National and State Governments scholarship allowances. Of the total operating revenue of \$16.904 million, 88% or \$14.894 million represents revenue from federal grants and contracts. Below is the pie graph for the composition of operating revenue for FY 2004:

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The tuition and fees of \$303K is net amount of the gross student tuition and fees of \$5.833 million less scholarship discounts and allowances of \$5.530 million.

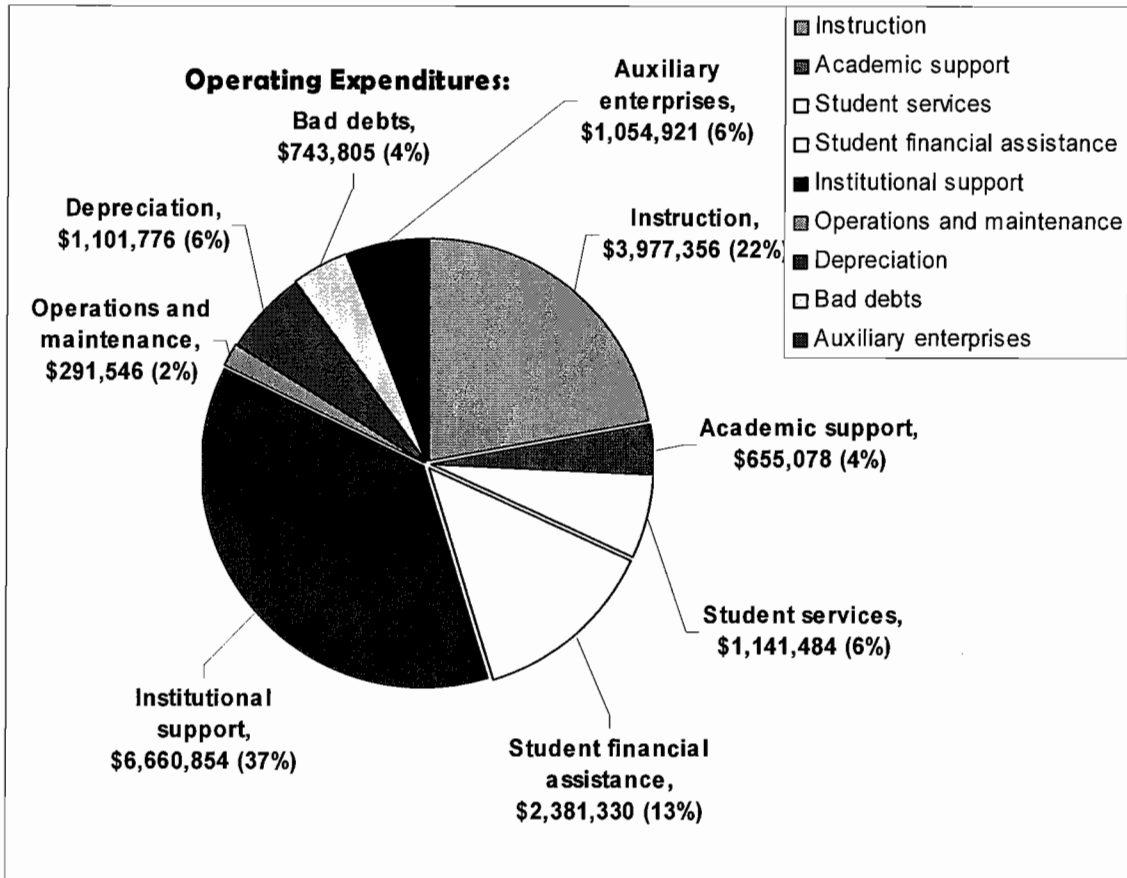
The significant increase in operating revenues by 29% or \$3.802 million is the result of the change in the presentation of the FSM National Government Appropriations funded under the Education Sector Grant of Compact II, from nonoperating revenue to operating revenue. The Compact II funds appropriated by FSM National Government to the College (\$3 million for operations, \$708K for FSM – FMI and \$84K for Board of Regents) were presented in the operating revenue and listed in the Schedule of Federal Financial Assistance instead of nonoperating revenue.

**Operating expenses:** Though operating expenses are presented based on programs and services of the College consisting of Instruction, Academic Support, Student Services, Student Financial Assistance, Institutional Support, Operations and Maintenance, Depreciation, Bad Debts and Auxiliary Enterprises, the College maintains the recording of expenses according to the general ledger classification of the operating expenses (i.e. salaries, supplies, repairs etc).

Below is the pie graph of operating expenses of \$18.008 million as presented based on programs and services per the audited financial report:

# COLLEGE OF MICRONESIA-FSM

## Management's Discussion and Analysis September 30, 2004 and 2003



Comparison of the operating expenses of FY 2004 with FY 2003 indicated an increase in operating expenses by 7% or \$1.189 million. The increases are from instruction, academic support, student services, student financial assistance, maintenance, depreciation, bad debts and auxiliary enterprises. However, there was a reduction in the institutional support operating expenditures.

**Nonoperating revenues:** The nonoperating revenue showed a significant reduction by \$7.841 million, from \$8.903 million to \$1.062 million. The two major causes for the reduction are (1) the change in the presentation of FSM appropriations for FY 2004 of \$3.792 million to operating revenue as discussed in the operating revenue portion of this report, and (2) no capital contribution was recorded in FY 2004 as compared with the \$4.168 million in FY 2003 for the recording of FSM – China Sports Complex as FSM capital contribution to the College.

**Net increase in net assets:** The College's financial performance for FY 2004 is at break even point with an insignificant net decrease in net assets of \$41K. The decrease in net assets is due to the reduction of other revenues, net investment income, and increases in noncash operating expenses from depreciation and bad debts.

### 3. Summary Statement of Cash Flows (SCF)

SCF present information about changes in the College's cash position using the direct method of reporting sources and uses of cash. The direct method reports all major cash inflows and outflows at gross amounts, differentiating these activities into cash flows arising from operating activities, noncapital financing, capital and related financing, and investing.



## COLLEGE OF MICRONESIA-FSM

### Management's Discussion and Analysis September 30, 2004 and 2003

The Summary Statement of Cash Flows indicates a balance in cash and equivalents of \$5.408 million at end of FY 2004. The FY 2004 balance reflects a net increase of 8% or \$380K in cash and equivalents compared with the balance at beginning of year of \$5.027 million.

Below is the summary statement of Cash Flows:

	FY 2004 (In 000's)	FY 2003 (In 000's)
Cash flows:		
Net cash provided by (used in) operating activities	\$ 83	\$ (2,432)
Net cash provided by noncapital financing activities	790	5,568
Net cash used in capital and related financing activities	(492)	(1,070)
Net cash used in investing activities	<u>-</u>	<u>(1)</u>
Net increase in cash and cash equivalents	\$ 381	\$ 2,065
Cash and cash equivalents at beginning of year	<u>5,027</u>	<u>2,962</u>
Cash and cash equivalents at end of year	\$ <u>5,408</u>	\$ <u>5,027</u>

### Budget Information

The College undertakes a yearly budget process as an integral part of financial planning that is linked with the Strategic Plan. The budget process includes the formulation and approval of budget guidelines, preparation of revenue and expenditure budgets by campus directors and department heads in consultation with the faculty and staffs. The prepared budgets are reviewed by Finance Committee in order to present a balanced budget. The College's budget requires endorsement by the Cabinet and approval by the Board before submitting to FSM National Government to secure financial support for the portion of the operating costs of the College, full operating budgets for FSM – FMI, Board of Regents, and Infrastructure Development Program budget.

The College's expenditures budget for operations for FY 2004 was \$9.736 million. The projected sources of funds are from tuition and fees of \$5.130 million, auxiliary enterprises of \$1.093 million and FSM National Government subsidy of \$3.513 million. In addition, FSM National Government appropriated \$708K for FSM-FMI, \$475K for scholarship to FSM students, \$84K for Board of Regents administrative budget, and \$330K for Capital Improvement Project.

### Capital Assets and Long-term Debt Activity

At September 30, 2004, the College's net investment in capital assets is \$13.157 million, net of accumulated depreciation. Depreciation for the current year totaled \$1.102 million, and capital additions for furniture and equipment, vehicles and library books totaled \$492K.

The long-term debt of the College represents the accrued annual leave. Personnel Policies and Procedures of the College provide accumulation of annual leave balance in the employees' records. However, only 180 hours of the accumulated annual leave shall be paid to the employee upon resignation/termination of employment, thus the value of the 180 hours is recorded as current liability. It should be noted that there was no additional long-term debt secured by COM – FSM in FY 2004.

## **COLLEGE OF MICRONESIA-FSM**

Management's Discussion and Analysis  
September 30, 2004 and 2003

### **Economic Outlook**

The economic position of the College is dependent on tuition fees generated from students who primarily received financial assistance from U.S. Federal Student Aid programs, and on the annual subsidy from FSM National Government. The authority for the U.S. Department of Education to award Student Financial Aid grants to the College resides in U.S. Public Law 99 – 239. If this award authority is not extended or renewed by the U.S. Congress, the result could be a significant reduction in the amount of funds available for student financial aid and accordingly a significant reduction in tuition revenue for the College. It should be noted that the U.S. Department of Education, Federal Student Aid approved the Program Participation Agreement for the College through June 30, 2008.

The accreditation of the College was reaffirmed by the Accrediting Commission for Community and Junior Colleges (ACCJC) of the Western Association of Schools and Colleges (WASC) from June 2004 to June 2010 on June 2005. The reaffirmation of the College's accreditation allows the College to continue to administer and receive US Pell grant funding for the College's eligible students, and the U.S. Department of Education competitive grants. The College administered and received \$7.912 million from the Federal Pell Grant Program and \$2.855 million from competitive grants.

**COLLEGE OF MICRONESIA-FSM**

Statements of Net Assets  
September 30, 2004 and 2003

<u>ASSETS</u>	<u>2004</u>	<u>2003</u>
Current assets:		
Cash and cash equivalents	\$ 5,408,035	\$ 5,027,183
Due from FSM National Government	1,893,524	1,072,993
Tuition receivable, net	2,729,381	2,910,538
Grants and contracts receivable - U.S. Government (net of allowance for doubtful accounts of \$39,839 and \$178,437 for 2004 and 2003, respectively.)	883,645	1,186,443
Other receivables (net of allowance for doubtful accounts of \$77,807 and \$82,758 for 2004 and 2003, respectively)	386,611	85,649
Inventories	98,001	151,623
Prepaid expenses	16,250	16,250
Total current assets	<u>11,415,447</u>	<u>10,450,679</u>
Noncurrent assets:		
Endowment investments	1,948,822	1,676,404
Grants and contracts receivable - U.S. Government	221,157	357,362
Capital assets, net of accumulated depreciation	13,157,013	13,766,713
Total noncurrent assets	<u>15,326,992</u>	<u>15,800,479</u>
Total assets	<u>\$ 26,742,439</u>	<u>\$ 26,251,158</u>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Accounts payable	\$ 457,111	\$ 470,828
Payable to affiliates	302,728	331,380
Accrued liabilities	221,707	158,664
Accrued annual leave	183,240	174,848
Deferred revenue	2,393,583	2,086,834
Other current liabilities	486,196	318,342
Total current liabilities	<u>4,044,565</u>	<u>3,540,896</u>
Noncurrent liabilities:		
Long-term portion of accrued annual leave	192,173	163,143
Total liabilities	<u>4,236,738</u>	<u>3,704,039</u>
Contingencies		
Net assets:		
Invested in capital assets	13,157,013	13,766,713
Restricted:		
Nonexpendable	1,987,331	1,705,935
Unrestricted	7,361,357	7,074,471
Total net assets	<u>22,505,701</u>	<u>22,547,119</u>
Total liabilities and net assets	<u>\$ 26,742,439</u>	<u>\$ 26,251,158</u>

See accompanying notes to financial statements.

**COLLEGE OF MICRONESIA-FSM**

Statements of Revenues, Expenses and Changes in Net Assets  
Years Ended September 30, 2004 and 2003

	2004	2003
Operating revenues:		
Student tuition and fees	\$ 5,833,678	\$ 5,437,356
Less: Scholarship discounts and allowances	(5,530,388)	(5,021,041)
	303,290	416,315
Federal grants and contracts	14,983,950	10,394,938
Government grants and contracts	665,419	726,923
Sales and services of auxiliary enterprises	811,572	838,173
Other revenues	140,045	726,315
Total operating revenues	16,904,276	13,102,664
Operating expenses:		
Institutional support	6,660,854	7,487,899
Instruction	3,977,356	3,347,103
Student financial assistance	2,381,330	1,993,699
Student services	1,141,484	1,029,745
Depreciation	1,101,776	928,452
Auxiliary enterprises	1,054,921	831,036
Bad debts	743,805	650,188
Academic support	655,078	468,190
Operations and maintenance, plant	291,546	83,171
Total operating expenses	18,008,150	16,819,483
Operating loss	(1,103,874)	(3,716,819)
Nonoperating revenues (expenses):		
FSM National Government appropriations:		
Operations	790,038	4,411,000
Capital contributions	-	4,168,582
Net investment income	272,418	323,842
Net nonoperating revenues	1,062,456	8,903,424
Net change in net assets	(41,418)	5,186,605
Net assets:		
Net assets at beginning of year	22,547,119	17,360,514
Net assets at end of year	\$ 22,505,701	\$ 22,547,119

See accompanying notes to financial statements.

**COLLEGE OF MICRONESIA-FSM**

Statements of Cash Flows  
Years Ended September 30, 2004 and 2003

	2004	2003
Cash flows from operating activities:		
Student tuition and fees, net	\$ 96,043	\$ 339,999
Grants and contracts	13,937,003	11,395,450
Auxiliary services	811,572	838,173
Other receipts	(160,917)	823,813
Payments to employees for salaries and benefits	(6,721,645)	(6,303,942)
Payments to suppliers and others	(7,879,165)	(9,525,835)
Net cash provided by (used in) operating activities	82,891	(2,432,342)
Cash flows from noncapital financing activities:		
FSM National Government appropriations, grants and contracts	790,038	5,568,331
Net cash provided by noncapital financing activities	790,038	5,568,331
Cash flows from capital and related financing activities:		
Purchases of capital assets	(492,077)	(1,069,763)
Net cash used in capital and related financing activities	(492,077)	(1,069,763)
Cash flows from investing activities:		
Investment income	272,418	79,219
Purchase of investments	(272,418)	(80,000)
Net cash used in investing activities	-	(781)
Net increase in cash and cash equivalents	380,852	2,065,445
Cash and cash equivalents at beginning of year	5,027,183	2,961,738
Cash and cash equivalents at end of year	\$ 5,408,035	\$ 5,027,183
Reconciliation of operating loss to net cash provided by (used in) operating activities:		
Operating loss	\$ (1,103,874)	\$ (3,716,819)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities:		
Depreciation	1,101,776	928,452
Bad debt	743,805	650,188
Change in assets and liabilities:		
Tuition receivable	(562,648)	(693,957)
Grants and contracts receivable	(381,528)	(216,459)
Other receivables	(300,962)	587,546
Inventories	53,623	(73,649)
Prepaid expenses	-	(10,465)
Accounts payable	(13,717)	452,691
Payable to affiliates	(28,652)	331,380
Accrued liabilities	197,631	(1,132,677)
Deferred revenue	355,401	187,461
Other liabilities	22,036	273,966
Net cash provided by (used in) operating activities	\$ 82,891	\$ (2,432,342)
Summary of Noncash Investing and Financing Activities:		
Noncash increase in the fair market value of investments	\$ 272,418	\$ 252,075
Noncash increase in investment income	(272,418)	(252,075)
Noncash increase in buildings	-	4,168,582
Noncash increase in capital contribution from the FSM National Government	-	(4,168,582)
	\$ -	\$ -

See accompanying notes to financial statements.

## COLLEGE OF MICRONESIA-FSM

Notes to Financial Statements  
September 30, 2004 and 2003

### (1) Organization

The College of Micronesia-FSM (formerly Community College of Micronesia or CCM) was one of the three component campuses of the College of Micronesia (COM) prior to April 1, 1993. The COM was established on March 29, 1977, by the treaty among the governments of the Republic of the Marshall Islands, the Federated States of Micronesia (FSM), and the Republic of Palau. The treaty ended on March 31, 1993, and the COM was restructured to render autonomy to each of the three nations.

CCM and the centers for continuing education (CE) in Pohnpei, Chuuk, Yap and Kosrae were merged to form COM-FSM, a FSM public corporation established by Public Law 7-79 on September 25, 1992, under the general management and control of a seven-member Board of Regents, appointed by the FSM President with the advice and consent of the FSM Congress. This law was subsequently amended to reduce the number of Board members to five. The term of all board members is 3 years and limited to 2 consecutive terms. However, a member may serve beyond the expiration date of his/her term until a successor has been appointed. The purpose of COM-FSM is to serve the varied post-secondary and adult educational needs of the FSM.

COM-FSM is considered a component unit of the FSM National Government for the following reasons: (1) the governing body, the Board of Regents, is appointed by the FSM President with the advice and consent of FSM Congress, and (2) COM-FSM has the potential to impose financial burdens on the National Government.

### (2) Basis of Presentation

A. Financial Statement Presentation. In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*. This was followed in November 1999 by GASB Statement No. 35, *Basic Financial Statements – and Management’s Discussion and Analysis – for Public Colleges and Universities*. The financial statement presentation required by GASB No. 34 and No. 35 provides a comprehensive, entity-wide perspective of the COM-FSM assets, liabilities, net assets, revenues, expenses, changes in net assets, and cash flows, and replaces the fund-group perspective previously required.

Other GASB Statements are required to be implemented in conjunction with GASB Statements No. 34 and No. 35. Therefore, the FSM National Government and COM-FSM have also implemented Statement No. 36, *Recipient Reporting for Certain Shared Nonexchange Revenues*, Statement No. 37, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments; Omnibus*, and Statement No. 38, *Certain Financial Statement Note Disclosures*.

B. Basis of Accounting. For financial statement purposes, COM-FSM is considered a special-purpose government engaged only in business-type activities. Accordingly, COM-FSM’s financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-college transactions have been eliminated. COM-FSM reports as a business-type activity, as defined by GASB Statement No. 35. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods and services.

## COLLEGE OF MICRONESIA-FSM

Notes to Financial Statements  
September 30, 2004 and 2003

### (2) Basis of Presentation

#### B. Basis of Accounting, Continued.

COM-FSM has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. COM-FSM has elected to not apply FASB pronouncements issued after the applicable date.

### (3) Summary of Significant Accounting Policies

- A. Cash and Cash Equivalents. Cash and cash equivalents are defined as cash on hand, cash in bank and time certificates of deposit with initial maturities of ninety days or less. Time certificates of deposit with initial maturities in excess of ninety days are classified as investments.

At September 30, 2004 and 2003, COM-FSM has recorded cash balances at \$5,408,034 and \$5,027,183 with corresponding bank balances of \$5,922,855 and \$5,628,325, respectively. Of these amounts, \$200,000 and \$200,000, respectively are insured by the Federal Deposit Insurance Corporation (FDIC). The remaining balances are not insured or collateralized by securities held by a trustee in the name of the financial institution. Management elected not to require insurance or collateralization on the remaining balances based on their confidence in the financial health of the banking institutions. No losses as a result of this practice were incurred during the years ended September 30, 2004 and 2003.

- B. Investments. COM-FSM accounts for its investments at fair value in accordance with GASB Statement No. 31, *Accounting for Financial Reporting for Certain Investments and for External Investment Pools*. Unrealized gains and losses on the carrying value of investments are reported as a component of net investment income in the Statement of Revenues, Expenses and Changes in Net Assets.

- C. Accounts Receivable. Accounts receivable tuition and fees and accounts receivable employees are net of an allowance for uncollectible accounts as of September 30, 2004 are as follows:

	<u>National Campus</u>	<u>State Campuses</u>	<u>Totals</u>
Accounts receivable, gross	\$ 3,205,263	\$ 2,336,727	\$ 5,541,990
Allowance for uncollectible accounts	(1,282,927)	(1,529,682)	(2,812,609)
Accounts receivable, net	\$ <u>1,922,336</u>	\$ <u>807,045</u>	\$ <u>2,729,381</u>

Accounts receivable tuition and fees and accounts receivable employees are net of an allowance for uncollectible accounts as of September 30, 2003 are as follows:

	<u>National Campus</u>	<u>State Campuses</u>	<u>Totals</u>
Accounts receivable, gross	\$ 2,782,581	\$ 2,244,911	\$ 5,027,492
Allowance for uncollectible accounts	(1,119,918)	(997,036)	(2,116,954)
Accounts receivable, net	\$ <u>1,662,663</u>	\$ <u>1,247,875</u>	\$ <u>2,910,538</u>

**COLLEGE OF MICRONESIA-FSM**

Notes to Financial Statements  
September 30, 2004 and 2003

(3) Summary of Significant Accounting Policies, Continued

C. Accounts Receivable, Continued

The allowance for uncollectible accounts is established through a provision charged to expense. Accounts are charged against the allowance when management believes that the collection of the balance is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing balances that may be uncollectible, based on evaluations of collectibility and prior loss experience.

D. Inventory. Inventory is stated at the lower of cost (first-in, first-out) or market (net realizable value).

E. Prepaid Expenses. Payments made to vendors for goods and services that will benefit periods beyond September 30, 2004 and 2003, are recorded as prepaid expenses, an asset account. Prepaid expenses represent prepayments for laboratory supplies, textbooks and computers.

F. Capital Assets and Depreciation. All buildings and equipment transferred to COM-FSM were recorded at management's estimate of fair market value at the date of transfer. Subsequent additions have been recorded at cost and/or realizable value, as estimated and provided by COM-FSM. Depreciation is calculated using the straight-line method over estimated useful lives of three to thirty years. COM-FSM has adopted a capitalization policy of \$500. Purchases less than this threshold are expenses.

Certain real property and buildings being used by COM-FSM, were contributed to COM-FSM by the FSM National Government. No user fee or allowance has been computed or charged to COM-FSM by the FSM National Government. Therefore, such costs have been recorded neither as in-kind contributions nor expenses.

G. Deferred Revenue. Deferred revenues include amounts received for tuition and fees and certain auxiliary activities prior to the end of the fiscal year but relate to the subsequent accounting period. Deferred revenues also include amounts received from grant and contract sponsors that have not yet been earned.

H. Accrued Leave. COM-FSM recognizes as a liability all vested leave benefits accrued by its employees at the time such leave is earned.

I. Noncurrent Liabilities. Noncurrent liabilities include estimated amounts for accrued compensated absences that will not be paid within the next fiscal year.

The change in accrued compensated absences during fiscal years 2004 and 2003 is as follows:

Balance, Oct. 1, 2003	<u>Addition</u>	<u>Reduction</u>	Balance, Sept. 30, 2004	<u>Current</u>	<u>Long-Term</u>
\$337,991	\$323,380	(\$174,848)	\$375,413	\$183,240	\$192,173
Balance, Oct. 1, 2002	<u>Addition</u>	<u>Reduction</u>	Balance, Sept. 30, 2003	<u>Current</u>	<u>Long-Term</u>
\$289,519	\$ 48,472	\$ -	\$337,991	\$174,848	\$163,143



## COLLEGE OF MICRONESIA-FSM

Notes to Financial Statements  
September 30, 2004 and 2003

### (3) Summary of Significant Accounting Policies, Continued

#### J. Net Assets. COM-FSM net assets are classified as follows:

*Invested in Capital Assets* – This represents COM-FSM’s total investment in capital assets, net of outstanding debt obligations related to those capital assets.

*Restricted Net Assets – Nonexpendable* – Nonexpendable restricted net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal.

*Unrestricted Net Assets* –Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the COM-FSM, and may be used at the discretion of the governing board to meet current expenses for any purpose. These resources also include auxiliary enterprises, which are substantially self-supporting activities that provide services for student, faculty and staff.

When an expense is incurred that can be paid using either restricted or unrestricted resources, the COM-FSM’s policy is to first apply the expense towards unrestricted resources, and then toward restricted resources.

#### K. Classification of Revenues. COM-FSM has classified its revenues as either operating or nonoperating according to the following criteria:

*Operating Revenues* – Operating revenues include activities that have the characteristics of exchange transactions, such as (1) student tuition and fees, net of scholarship discounts and allowances, (2) sales and services of auxiliary enterprises, and (3) most federal, state and local grants and contracts and federal appropriations.

*Nonoperating Revenues* – Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement No. 34, such as FSM National Government appropriations and investment income.

#### L. Scholarship Discounts and Allowances. Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the Statement of Revenues, Expenses and Changes in Net Assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by COM-FSM, and the amount that is paid by students and/or third parties making payments on the students’ behalf. Certain governmental grants, such as Pell grants, and other federal, state or nongovernmental programs, are recorded as either operating or nonoperating revenues in COM-FSM’s financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, COM-FSM has recorded a scholarship discount and allowance.

**COLLEGE OF MICRONESIA-FSM**

Notes to Financial Statements  
September 30, 2004 and 2003

(3) Summary of Significant Accounting Policies, Continued

- M. New Accounting Standards. For fiscal year 2005, COM-FSM will be implementing GASB Statement No. 40, Deposit and Investment Risk Disclosures (an amendment of GASB Statement No. 3) and GASB Statement No. 42, Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries. The College has not evaluated the financial statement impact of GASB Statement Nos. 40 and 42.
- N. Risk Management. COM-FSM purchases insurance to cover its risk of losses due to fire, lightning, and other risks normal to operating an institution of higher learning. Refer to note 8 for management’s estimation of its risk exposure.
- O. 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 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.
- P. Reclassifications. Certain reclassifications have been made to correct the 2003 net asset presentation.

(4) Investments

In January 1994, COM-FSM received an endowment contribution in the amount of \$150,000 from FSM Telecommunications Corporation. The principal is to be maintained inviolate and in perpetuity.

In November 1995, notification was received from the U.S. Department Education that COM-FSM had been selected for a grant under the Endorsement Challenge Grant Program authorized by Title III of the Higher Education Act of 1965, as amended. Non-government funds raised for this endowment fund were matched by the U.S. Department of Education on a two-to-one basis. The Secretary of Education awarded an amount to COM-FSM equal to two times the amount of the funds raised. The College of Micronesia-FSM raised \$250,000 and the U.S. Department of Education awarded \$500,000, bringing the total of this endowment fund to \$750,000. The Endowment Challenge grant covers a period of twenty years.

In December 1997, COM-FSM adopted an investment policy, which guides current investment decisions. This policy is to be reviewed after 10 years. The policy provides that investment earnings may not be obligated until the principal has aggregated to a market value of \$20 million. During the Board of Regents meeting on March 2005, an updated investment policy recommended by the Investment Consultant and reviewed by the Administration was approved by the Board. The endowment investments are classified as restricted nonexpendable net assets in the accompanying Statement of Net Assets.

The composition of endowment assets as of September 30, 2004 and 2003, by funding source, is as follows:

<u>Donor</u>	<u>2004</u>	<u>2003</u>
FSM Telecommunications Corporation (FSMTC)	\$ 165,000	\$ 165,000
U.S. Department of Education and local match (Challenge)	<u>1,822,331</u>	<u>1,540,935</u>
	<u>\$ 1,987,331</u>	<u>\$ 1,705,935</u>

**COLLEGE OF MICRONESIA-FSM**

Notes to Financial Statements  
September 30, 2004 and 2003

**(4) Investments, Continued**

The composition of endowment assets, by type, is as follows:

Cash with local bank	\$ <u>38,509</u>	\$ <u>29,531</u>
Stock Market Investments:		
Money funds	198,726	53,099
Government and corporate bonds	424,096	466,751
U.S. securities	879,774	807,824
Foreign securities	<u>446,226</u>	<u>348,730</u>
Total investment	<u>1,948,822</u>	<u>1,676,404</u>
	\$ <u>1,987,331</u>	\$ <u>1,705,935</u>

Credit risk associated with investments is categorized into three levels generally described as follows:

Category 1 - Insured or registered, or securities held by COM-FSM or its agent in COM-FSM's name.

Category 2 - Uninsured and unregistered, or securities held by a party other than COM-FSM or its agent, but in COM-FSM's name.

Category 3 - Uninsured and unregistered, with securities held by a party other than COM-FSM and not in COM-FSM's name.

All investments held by COM-FSM have been classified as Category 2 investments.

**(5) Due from Grantor Agencies**

COM-FSM administers student financial aid (SFA) for the U.S. Department of Education SFA funds related to Pell Grants, College Work-Study and Supplemental Educational Opportunity Grants, Talent Search Program, Upward Bound Program, and Strengthening Institution Program. In addition, COM-FSM also administers Land Grant Programs on behalf of COM Land Grant College. The grants and contracts receivable – U.S. Government are comprised of the following uncollected grants as of September 30, 2004 and 2003:

	<u>2004</u>	<u>2003</u>
Due from U.S. Department of Education	\$ 622,373	\$ 923,253
Due from COM-Land Grant, net	<u>482,429</u>	<u>620,552</u>
	1,104,802	1,543,805
Classified as current	<u>883,645</u>	<u>1,186,443</u>
Noncurrent receivables	\$ <u>221,157</u>	\$ <u>357,362</u>

## COLLEGE OF MICRONESIA-FSM

Notes to Financial Statements  
September 30, 2004 and 2003

### (6) Capital Assets

Capital assets at September 30, 2004 and 2003 consist of the following:

	Balance October 1, 2003	<u>Additions</u>	<u>Retirements</u>	Balance September 30, 2004
Non-depreciable assets:				
Land	\$ <u>1,455,685</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>1,455,685</u>
Depreciable assets:				
Building	13,661,263	-	-	13,661,263
Furniture and equipment	5,103,211	385,265	-	5,488,476
Vehicles	549,329	30,914	-	580,243
Library books	<u>412,557</u>	<u>75,898</u>	<u>-</u>	<u>488,455</u>
	19,726,360	492,077	-	20,218,437
Less accumulated depreciation	<u>(7,415,332)</u>	<u>(1,101,777)</u>	<u>-</u>	<u>(8,517,109)</u>
	<u>12,311,028</u>	<u>(609,700)</u>	<u>-</u>	<u>11,701,328</u>
Net investment in capital assets	\$ <u>13,766,713</u>	\$ <u>(609,700)</u>	\$ <u>-</u>	\$ <u>13,157,013</u>
	Balance October 1, 2002	<u>Additions</u>	<u>Retirements</u>	Balance September 30, 2003
Non-depreciable assets:				
Land	\$ <u>1,455,685</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>1,455,685</u>
Depreciable assets:				
Building	9,492,681	4,168,582	-	13,661,263
Furniture and equipment	4,232,409	870,802	-	5,103,211
Vehicles	463,351	85,978	-	549,329
Library books	<u>299,574</u>	<u>112,983</u>	<u>-</u>	<u>412,557</u>
	14,488,015	5,238,345	-	19,726,360
Less accumulated depreciation	<u>(6,266,872)</u>	<u>(1,148,460)</u>	<u>-</u>	<u>(7,415,332)</u>
	<u>8,221,143</u>	<u>4,089,885</u>	<u>-</u>	<u>12,311,028</u>
Net investment in capital assets	\$ <u>9,676,828</u>	\$ <u>4,089,885</u>	\$ <u>-</u>	\$ <u>13,766,713</u>

### (7) Related Party Transactions

COM-FSM receives annual appropriations from the FSM National Government for its operational needs, student financial assistance and other programs. At September 30, 2004 and 2003, receivables from the FSM National Government amounted to \$1,893,524 and \$1,072,993, respectively, net of an allowance for doubtful accounts of \$0 and \$45,821, respectively.

**COLLEGE OF MICRONESIA-FSM**

Notes to Financial Statements  
September 30, 2004 and 2003

(7) Related Party Transactions, Continued

Payable to affiliates is comprised of the following at September 30, 2004 and 2003:

	<u>2004</u>	<u>2003</u>
FSM National Government	\$ 125,911	\$ 137,622
FSM Social Security Administration	176,817	130,406
FSM Telecommunications Corporation	-	37,387
Pohnpei Utilities Corporation	<u>-</u>	<u>25,965</u>
	\$ <u>302,728</u>	\$ <u>331,380</u>

(8) Contingencies

COM-FSM purchases commercial insurance to cover its potential risks from fire and property damage on some of its building and contents. At September 30, 2004 and 2003, three State Campus assets (Chuuk, Kosrae, and Yap), amounting to \$495,772, were not protected by insurance policies. COM-FSM is also substantially self-insured for all other risks. In the event of a catastrophe, COM-FSM may be self-insured to a material extent.

COM-FSM is party to various legal proceedings. Legal counsel is of the opinion that the probable outcome of these proceedings is not predictable but will have no material impact on the accompanying financial statements.

COM-FSM is subject to annual compliance audits. Unresolved questioned costs from these audits currently aggregate \$17,712. Management is of the opinion that resolution of this matter will not result in a material impact on the accompanying financial statements and accordingly, no liability for this matter has been recorded in the accompanying financial statements.

During fiscal year ended September 30, 2004, unreconciled differences aggregating \$101,665 exist between the College's and COM Land Grant's financial records. The College is resolving this matter with its counterpart and such reconciliation is not expected to have a material impact on the accompanying financial statements.

COM-FSM is negotiating with FSM Telecommunications Corporation on a settlement involving \$76,812 in outstanding charges for internet services. No liability has been recorded in the accompanying financial statements for any portion of this amount pending conclusion of negotiations, which resolution is not expected to have a material impact on the accompanying financial statements.

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER  
FINANCIAL REPORTING AND COMPLIANCE AND OTHER MATTERS  
BASED UPON THE AUDIT PERFORMED IN ACCORDANCE WITH  
GOVERNMENT AUDITING STANDARDS**

Board of Regents  
College of Micronesia-FSM:

We have audited the financial statements of the College of Micronesia-FSM as of and for the year ended September 30, 2004, and have issued our report thereon dated December 22, 2005. 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.

Internal Control Over Financial Reporting

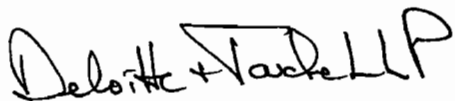
In planning and performing our audit, we considered College of Micronesia-FSM's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we considered 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 College of Micronesia-FSM's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Two reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs (pages 28 through 30) as items 2004-3 and 2004-4.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud 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 over financial reporting 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, of the reportable conditions described above, we consider none to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the College of Micronesia-FSM's general purpose 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 an objective of our audit and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards*, which are described in the accompanying Schedule of Findings and Questioned Costs as items 2004-1 and 2004-2.

This report is intended solely for the information and use of the College of Micronesia-FSM, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

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

December 22, 2005

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND INTERNAL CONTROL  
OVER COMPLIANCE APPLICABLE TO EACH MAJOR FEDERAL AWARD PROGRAM  
AND ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

Board of Regents  
College of Micronesia-FSM:

Compliance

We have audited the compliance of College of Micronesia-FSM with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2004. College of Micronesia-FSM's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (page 25). Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of College of Micronesia-FSM's management. Our responsibility is to express an opinion on College of Micronesia-FSM's compliance based on our audit.

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

As described in items 2004-1 and 2004-2 in the accompanying Schedule of Findings and Questioned Costs, the College of Micronesia-FSM did not comply with requirements regarding procurement and suspension and debarment and reporting. Compliance with such requirements is necessary, in our opinion, for the College of Micronesia-FSM to comply with requirements applicable to its major federal programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the College of Micronesia-FSM complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended September 30, 2004.



## Internal Control Over Compliance

The management of the College of Micronesia-FSM is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the College of Micronesia-FSM's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

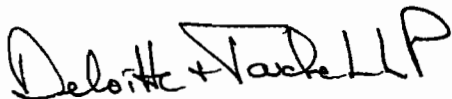
We noted matters involving the internal control over compliance and its operations that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the College of Micronesia-FSM's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 2004-1 through 2004-4.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program 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 over compliance 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. We consider none of the reportable conditions set forth above to be material weaknesses.

## Schedule of Expenditures of Federal Awards

We have audited the financial statements of the College of Micronesia-FSM, as of and for the year ended September 30, 2004, and have issued our report thereon dated December 22, 2005. Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. This schedule is the responsibility of the management of the College of Micronesia-FSM. Such information has been subjected to the auditing procedures applied in our audit of the financial statements and, in our opinion, is fairly stated, in all material respects when considered in relation to the financial statements taken as a whole.

This report is intended solely for the information and use of the College of Micronesia-FSM, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.



December 22, 2005

**COLLEGE OF MICRONESIA-FSM**

Schedule of Expenditures of Federal Awards  
Year Ended September 30, 2004

<u>Grantor/Program Title</u>	<u>CFDA Number</u>	<u>Expenditures</u>
<u>U.S. Department of Education:</u>		
Federal Pell Grant Program	84.063	\$ 7,895,301
Federal Work-Study Program	84.033	167,471
TRIO: Upward Bound	84.047	1,020,808
TRIO: Talent Search	84.044	254,269
TRIO: Student Support Services	84.042	250,760
Bilingual Education: Professional Development	84.195	796,803
Gaining Early Awareness and Readiness for Undergraduate Programs	84.334	481,366
Special Education: Parent Information Centers	84.328	22,315
Special Education: Personnel Preparation to Improve Services and Results for Children with Disabilities	84.325	<u>28,745</u>
Total U.S. Department of Education		\$ <u>10,917,838</u>
 <u>U.S. Department of the Interior:</u>		
Compact II	15.875	\$ 3,792,852
Operation and Maintenance Technical Assistance	15.875	<u>154,253</u>
Total U.S. Department of the Interior		\$ <u>3,947,105</u>
Total Federal Awards		\$ <u>14,864,943</u>

Notes: The above grants are received in a direct capacity from the U.S. Department of Education and the U.S. Department of the Interior. The Schedule of Expenditures of Federal Awards is prepared on the accrual basis of accounting.

Reconciliation to financial statements:

Total federal awards expenditures	\$ 14,864,943
Bad debt	743,805
Depreciation	1,101,776
Non-federal awards	<u>1,297,626</u>
Total expenditures per financial statements	\$ <u>18,008,150</u>

**COLLEGE OF MICRONESIA-FSM**

Schedule of Findings and Questioned Costs  
Year Ended September 30, 2004

**Part I - Summary of Auditors' Results**

1. The Independent Auditors' Report on the financial statements expressed an unqualified opinion.
2. Reportable conditions in internal control over financial reporting were identified, none of which is considered to be a material weakness.
3. Instances of noncompliance considered material to the financial statements were not disclosed by the audit.
4. Reportable conditions in internal control over compliance with requirements applicable to major federal awards programs were identified, none of which were considered to be material weaknesses.
5. The Independent Auditors' Report on compliance with requirements applicable to major federal award programs expressed a qualified opinion.
6. The audit disclosed findings required to be reported by OMB Circular A-133.
7. COM-FSM's major programs were:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>	<u>Expenditures</u>
<u>U.S. Department of Education:</u>		
	Student Financial Aid Cluster:	
84.063	Federal Pell Grant Program	\$7,895,301
84.033	Federal Work-Study Program	\$ 167,471
84.195	Bilingual Education: Professional Development	\$ 796,803
15.875	Compact II	\$3,792,852

8. A threshold of \$445,948 was used to distinguish between Type A and Type B programs, as those terms are defined in OMB Circular A-133.
9. COM-FSM did not qualify as a low-risk auditee as that term is defined in OMB Circular A-133.

**Part II – Federal Award Findings and Questioned Cost Section**

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>	<u>Refer Page #</u>
2004-1	Procurement and suspension and debarment	\$ 17,712	26
2004-2	Reporting	\$ -	27

**Part III - Financial Statement Findings Section**

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>	<u>Refer Page #</u>
2004-3	Accounts Receivable and Accounts Payable	\$ -	28
2004-4	Timeliness of Financial Statement Reconciliations	\$ -	29-30

## COLLEGE OF MICRONESIA-FSM

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2004

Finding No.: 2004-01  
CFDA No.: 84.195E Career Ladder Program  
Grantor Agency: U.S. Department of Education  
Program/Area: Procurement, Suspension and Debarment  
Questioned Costs: \$17,712

Criteria: The entity should utilize competitive procurement procedures as prescribed by the federal government or local procedures that either meet or exceed the federal requirements.

Condition: Of 23 expenditures tested aggregating \$144,587, informal procurement procedures were not evident for two purchases (PO04-1089 and PO04-2066, \$3,022 and \$14,690). It appears that sole source procurement procedures occurred without appropriate justification.

Cause: The cause of the above condition is a noncompliance with appropriate procurement procedures.

Effect: The effect of the above condition is questioned costs of \$17,712.

Recommendation: We recommend that COM-FSM review its procurement policy to ensure it incorporates provisions which conform with federal requirements for costs charged to federal programs.

Auditee Response and Corrective Action Plan: The questioned costs comprised of the following purchases:

1. PO04-2066 in the amount of \$14,689

This is for the procurement of 5 desktop computers at \$2,103, 5 scanners at \$196, 5 battery back-up at \$125 and 1 notebook at \$1,865 documented in a duly signed Purchase Order on April, 2004. Due to geographical location of the College and the limited technical services in the island, the College considered the corresponding vendor as the most reliable vendor for computer at Chuuk due to its compliance with the minimum requirements set by our Information Technology Office and the ability to provide the required service warranties.

2. PO04-1089 in the amount of \$3,021

This is for the procurement of various office supplies with unit prices ranging from \$1 to \$114 on January, 2004. In the island, availability of supplies is limited and only this vendor carries a wide variety of office supplies. Other vendors could not provide all the needed items.

Prior to January 19, 2005, the College policy on procurement does not require formal documentation for price solicitation due to geographical location of our island and the limited available items in the island. However, in most cases the College is performing informal price solicitations from local and off-island vendors.

With the Auditor's recommendation from the FY 2003 audit, the management has reviewed the procurement policy and implemented the policy that all procurement transactions shall be conducted in a manner to provide, to the maximum extent practical, open and free competition despite the scarcity of supplies and materials in the island. A memorandum was issued by the Comptroller through the Office of the President on January 19, 2005 requiring all procurement with a total of \$500 and \$24,999 per Purchase Order per Vendor be supported by price comparison from three vendors. In addition, Purchase Order in the amount of \$25,000 and above shall follow the policy and procedures of competitive sealed bidding or formal bidding.

**COLLEGE OF MICRONESIA-FSM**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding No.: 2004-02  
CFDA No.: 15.875 Compact II  
Grantor Agency: U.S. Department of the Interior  
Program/Area: Reporting  
Questioned Costs: \$0

Criteria: Recipients of federal funds should comply with the applicable federal reporting agreements.

Condition: Both the SF269 and SF272 reports were not submitted in the current fiscal year.

Cause: COM-FSM as a subrecipient of Compact II federal grants was not made aware of the reporting requirements.

Effect: COM-FSM appears to be in noncompliance with federal reporting requirements.

Recommendation: We recommend that COM-FSM ensure compliance with federal requirement applicable to the Compact II federal grant.

Auditee Response and Corrective Action Plan: In FY 2004, we were advised that preparation of SF 269 and SF 272 reports are to be handled by FSM. It was only in the beginning of fiscal year 2005 that the College was asked to prepare and submit SF 269 and SF 272 reports covering the period October 01 to December 31, 2004 to FSM. Currently, the College is updated in the preparation and submission of SF 269 and SF 272 reports to FSM.

**COLLEGE OF MICRONESIA-FSM**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2004

Finding No.: 2004-03  
Area: Accounts Receivable and Accounts Payable

Criteria: All general ledger balances should be reconciled at year-end.

Condition: As of September 30, 2004, there exists an unreconciled difference of \$100,409 between COM-FSM and COM Land Grant receivable and payable balances.

COM-FSM	\$ 481,173
COM Land Grant	<u>380,764</u>
Unreconciled Difference	\$ <u>100,409</u>

Cause: The cause of this condition is lack of timely reconciliations.

Effect: The effect of the condition is a possible misstatement of the financial statements.

Recommendation: We recommend that COM-FSM reconcile its account with COM Land Grant.

Auditee Response and Corrective Action Plan: Since fiscal year 2003, the College has been handling reconciliation with COM-Land Grant. The reconciliation efforts provided significant improvements in reducing the difference between the two records, from \$500K to \$100K. The discrepancy from COM-Land Grant were from prior years since fiscal year 1997, thus reconciliation from prior records was a tough challenge. The College is fully aware of the discrepancy and in the continuous process of doing the reconciliation with COM Land Grant to establish a reconciled balance.

## COLLEGE OF MICRONESIA-FSM

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2004

Finding No.: 2004-04  
Area: Financial Statement Reconciliation

Criteria: A functioning system of internal control requires timely reconciliation of financial statements.

Condition: The final trial balance for the fiscal year ended September 30, 2004 was received on August 23, 2005, fifty-four days after the June 30, 2005 report submission deadline. In addition, a reconciliation of receivables and fund balance for the restricted fund was not received until September 14, 2005.

Cause: The cause of this condition is that reconciliations were not performed in a timely manner.

Effect: The effect of the condition is noncompliance with reporting requirements.

Recommendation: We recommend that timely reconciliations and periodic review of the financial statements for accuracy occur so any misstatement identified during such process can be corrected in a timely manner.

Auditee Response and Corrective Action Plan: The College acknowledged that the College provided the final trial balance to Auditor on August 23, 2005. However, the College does not agree with the cause of this condition because the College has performed reconciliations in a timely manner and has given top priority in providing the schedules and analyses requested by the auditors. In the College's opinion, the following events that transpired in the conduct of the FY2004 audit are the contributing causes for the condition of the audit finding.

- The FY2003 audit was completed only on the third week of January, 2005, and final audit report was issued on February, 2005. The delay in the completion of the FY2003 audit was due to the upgrading of the College's accounting system which required familiarization of the staffs in the new system and building of database (students and vendors records, fixed assets, organization and administration set-ups).
- Despite the delay in the completion of FY 2003 audit, the College provided a tentative trial balance before the auditor started the field audit on April 18, 2005. During the field audit, the College has provided all the schedules and working papers requested by the field auditors.
- When the field auditors left on the first week of June, 2005, no advice was received for any open items of the audit and we were made to understand that the field audit has been completed. Since then, we have not received any words from the auditor as to the status of the audit.
- On June 17, 2005, the College emailed the auditor to check the status of the FY 2004 audit. A meeting with the auditor occurred on June 21, 2005 to discuss the audit status. In the meeting, the Auditor provided a list of open items for the FY 2004 audit. The College is wondering why the list of open items was not provided during the field audit or before the auditor has concluded the field work. Providing the list of open items during the fieldwork or right after the fieldwork would help in preventing the occurrence of the condition of the audit finding.
- On June 22, 2005, the College emailed the responses on the list of open items of the audit as requested in the meeting of June 21, 2005.
- On June 23, 2005, the College received a call from FSM National Government-Finance Department checking the status of the FY 2004 audit. Called-up the auditor and checked the percentage of completion of FY2004 audit. The auditor advised that the audit is about 90% completed.
- On June 29, 2005, the College likewise received a call from FSM Public Auditor inquiring the status of FY 2004 audit. Communicated again with auditor to check the status. In the follow-up status with the auditor, the auditor provided the College with another list of open items. The College could not understand why the lists of open items were being asked on piecemeal basis and at the time when the College is following-up on the status of the audit.

## COLLEGE OF MICRONESIA-FSM

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2004

Finding No.: 2004-04, Continued  
Area: Financial Statement Reconciliation

#### Auditee Response and Corrective Action Plan, Continued:

- The College worked on the open items and submitted it to the auditor on June 30, 2005, a day after the list was received from the auditor. After submitting the requested items, the College has not received any communication from the auditor.
- On July 26, 2005, the College called-up the office of the auditor to follow-up again the draft of audit report. We were advised that our message will be relayed to the auditor-in-charge. No communication was received from the auditor until August 11, 2005.
- On August 11, 2005, an email was received from the auditor transmitting another list of items that need to be done in the audit. Additional list was likewise transmitted the following day.
- On August 18, 2005, the College called up the auditor for a meeting for the College to submit the documents requested per emails dated August 11 and 12, 2005, and to solve all other open items of the audit. The meeting was set on August 22, 2005.
- On August 22, 2005, the College met with the auditor to provide the requested items to complete the audit. In the discussion, the auditor advised the College to record the adjustments discussed in the meeting, and to provide the auditor copies of the journal vouchers and the revised Trial Balance.
- On August 23, 2005, the College transmitted the revised Trial Balance as stated in the condition of the audit finding.

With respect to the condition that the reconciliation of receivables and fund balances for the restricted fund was not received until September 14, 2005, the College does not agree with this finding. The auditor requested clarification on fund balances and receivables, and not the submission of reconciliation of these accounts on September 14, 2005. Again, these clarifications could have been done in the early part of the audit and not after the first draft report has been provided to the College on September 12, 2005, and this finding was not included in the first draft of the audit report.

#### Auditor Response:

The auditee has the sole responsibility in making corrections to its financial statements in a timely manner for the financial statements to conform with accounting principles accepted in the United States of America. Final material corrections to the financial statements were not made until August 22, 2005 through Journal Voucher numbers 04-121, 04-122, 04-123, 04-124, 04-125, 04-126, and 04-127. In addition, the Restricted Fund's opening fund balance was not corrected until September 14, 2005 through Journal Voucher 04-0114r and 04-0116r. These journal vouchers were for normal recurring corrections relating to misstatements uncovered by the auditee through the general ledger reconciliation process.



**COLLEGE OF MICRONESIA-FSM**

Schedule of Unresolved Prior Year Questioned Costs  
Year Ended September 30, 2004

The following is a summary of unresolved federal questioned costs for the College of Micronesia-FSM:

	Questioned Costs Set Forth in the Audit Report <u>2003</u>	Questioned Costs Resolved in Fiscal Year <u>2004</u>	Questioned Costs at <u>September 30, 2004</u>
Unresolved Questioned Costs FY02	\$ 147,139	\$ 147,139 (1)	\$ -
Unresolved Questioned Costs FY03	60,005	60,005 (1)	-
Costs questioned during the year ended September 30, 2004	-	-	<u>17,712</u>
Total questioned costs outstanding as of September 30, 2004			\$ <u>17,712</u>

(1) These costs were resolved based on resolution issued by the grantor agency.