NATIONAL FISHERIES CORPORATION

(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

SEPTEMBER 30, 2008 AND 2007

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INDEPENDENT AUDITORS' REPORT

The Board of Directors
National Fisheries Corporation:

We have audited the accompanying statements of net assets of the National Fisheries Corporation (NFC), a component unit of the FSM National Government, as of September 30, 2008 and 2007 and the related statements of revenues, expenses and changes in net assets and of cash flows for the year ended September 30, 2008. These financial statements are the responsibility of NFC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

NFC has historically consolidated its investment in Micronesia Longline Fishing Company, a 97%-owned corporation, and its investment in Yap Fishing Corporation, Yap Fresh Tuna, Inc., Chuuk Fresh Tuna, Inc., and Kosrae Sea Venture Inc., all 50%-owned corporations. Due to the lack of either audited or unaudited financial statements for Micronesia Longline Fishing Company, Yap Fishing Corporation, Yap Fresh Tuna, Inc., Chuuk Fresh Tuna, Inc., and Kosrae Sea Venture Inc., the amount by which this departure would affect investments and net assets at September 30, 2008 and 2007 is not reasonably determinable.

We were engaged to audit NFC's financial statements for the year ended September 30, 2007; however, the system of financial accounting and reporting for NFC for the year ended September 30, 2006 was inadequate. Because of inadequacies in NFC's accounting records and internal control over financial reporting, we were not able to satisfy ourselves about the account balances presented within the statement of net assets as of September 30, 2006, which enters into the determination of results of operations of NFC for the year ended September 30, 2007.

Because of the significance of the matter discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the statements of revenues, expenses, and changes in net assets and of cash flows for the year ended September 30, 2007.

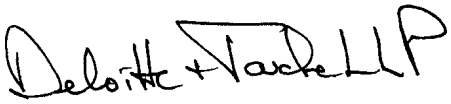
Member of
Deloitte Touche Tohmatsu

In our opinion, except for the effects on the financial statements of such adjustments, if any, as might have been determined to be had financial statements to support NFC's investment in Micronesia Longline Fishing Company, Yap Fishing Corporation, Yap Fresh Tuna, Inc., Chuuk Fresh Tuna, Inc., and Kosrae Sea Venture Inc. been available, the financial statements referred to in the first paragraph presents fairly, in all material respects, the financial position of NFC as of September 30, 2008 and 2007, and the changes in its net assets and its cash flows for the year ended September 30, 2008 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that NFC will continue as a going concern. As discussed in note 7 to the financial statements, NFC has incurred substantial losses from operations. This condition raises substantial doubt about its ability to continue as a going concern.

The Management's Discussion and Analysis on pages 3 through 6 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This information is the responsibility of NFC's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 16, 2009, on our consideration of NFC's internal control over financial reporting and on our tests of its compliance with certain laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.



September 16, 2009

NATIONAL FISHERIES CORPORATION
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Management Discussion and Analysis
September 30, 2008 and 2007

This section of the National Fisheries Corporation's (NFC) annual audit report presents the Management's Discussion and Analysis (MD&A) for the fiscal year ended September 30, 2008. The MD&A is supplementary information required by the new Government Accounting Standards Board Statement 34 (GASB 34) on reporting model. The preparation of the MD&A is the responsibility of the management of NFC, and it is designed to help the readers in understanding the accompanying financial statements and notes to the financial statements.

Background

The National Fisheries Corporation is a government owned corporation, created under Public Law No. 3-14 by the 3rd Congress of the Federated States of Micronesia. The main purpose of NFC is to promote the development of fishing industry in the FSM. NFC is also involved in ancillary activities that support commercial fishing activities. It is for this purpose that NFC initially engaged itself with its subsidiaries; Yap Fresh Tuna Inc. (YFTI), Chuuk Fresh Tuna Inc.(CFTI), Kosrae Sea Ventures Inc. (KSVI) and Micronesia Longline Fishing CO. (MLFC). However, due to the drastic decline in the number of vessels utilizing YFTI and CFTI, NFC was forced to venture into actual operation of longline fishing vessels, trading of fishing supplies and an airfreight business.

Due to drastic economic conditions, NFC's subsidiaries, namely CFTI, YFTI, KSVI and MLFC, failed to submit audited financial statements. The latest financial statements received from CFTI were dated September 1998. In FY2006, MLFC's board of directors declared the company (MLFC) to be bankrupt. NFC started the non-inclusion of MLFC's financial data in NFC's consolidated financial statements in fiscal year 2004. That company is now in trust or receivership and a new trustee has been appointed by the FSM Supreme Court.

Because of the unavailability of financial data from NFC subsidiaries, balances from these investee's has been excluded from NFC's financial statements. NFC started the non-inclusion of MLFC's financial data in NFC's consolidated financial statements in fiscal year 2004. The investment balance in CFTI amounting to $486k was also written-off in 2007.

The financial statements of NFC are presented as balances combining and including the balances of Corporate, Fishing operations, Airfreight operations, Transshipment operations and Baitfish services from previous years until FY 2006.

Overview of Fiscal Year 2008

The accounts of NFC are organized as a propriety fund. Propriety funds are used by the governmental units that are operated in a manner similar to private business enterprises. For the current year, NFC corporate office activities include consolidated activities from licensing of foreign boats, leasing of two fishing vessels, fish grading and regular corporate and administrative functions.

Revenue sources of NFC operations are from a FSM National Government subsidy of $135k, licensing fees from vessels licensed under NFC/NORMA agreements of $72k, vessel lease of $29k, fish grading of $21k, and sales of fishing gear and supplies of $7k. During the year, NFC generated $670k from licensing fees of which $598k or 89% was remitted to National Oceanic Resources Management Authority (NORMA).

NFC's budget is prepared by management with the concurrence of the Board of Directors. The budget is then forwarded to the President's budget committee which in turn submits it to Congress for approval.

Financial Highlights

NFC started implementing the new financial reporting standards in accordance with Government Accounting Standards Board (GASB) principles in fiscal year 2003. Adopting the GASB principles provide the new financial reporting of the following basic financial statements:

1. Statement of Net Assets (SNA)

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

Comparative Statements of Net Assets at September 30, 2008, 2007 and 2006 are summarized below:

	FY 2008	FY2007	FY2006
Assets:			
Current assets	$ 131,183	$ 129,425	$ 187,239
Noncurrent assets	160,377	111,704	719,758
Total Assets	$ 291,560	$ 241,129	$ 906,997
Liabilities:			
Current Liabilities	$ 3,852,285	$ 3,862,942	$ 4,880,694
Noncurrent Liabilities	-	-	-
Total Liabilities	3,852,285	3,862,942	4,880,694
Net assets:			
Invested in capital assets, net of related debt	160,377	111,704	(232,904)
Unrestricted	(3,721,102)	(3,733,517)	(4,206,601)
	(3,560,725)	(3,621,813)	(3,973,697)
Total Liabilities and net assets	$ 291,560	$ 241,129	$ 906,997

Assets: Company total assets of $291k comprise of $131k or 45% of current assets and $160k or 55% of fixed assets.

Current assets: The major portion of the $131k current assets is in inventory, which accounts for 63% or $84k. Cash is $44k or 33% of current assets and the remaining is account receivable of $3k.

Noncurrent assets: Total noncurrent assets of $160k are comprised of the Company's property and equipment, net of accumulated depreciation.

Liabilities: NFC's liabilities of $3.852 million are all current consisting of a $3.6 million loan from the FSM National Government, which comprises 93% of the total NFC liabilities, and other accounts payable and accrued liabilities of $252k.

Financial Highlights, Continued

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

The SRECNA provides information on the financial performance of the current year in terms of revenues and expenses. It presents the operating revenues and expenses and the corresponding net operating results, as well as non-operating revenues and expenses. Comparative summary of Statements of Revenues, Expenses and Changes in Net Assets for the fiscal years ended September 30, 2008, 2007 and 2006 are summarized below:

	FY 2008	FY 2007	FY 2006
Sales	$ 138,537	$ 98,415	$ 276,808
Cost of Sales	(31,881)	(491,235)	(176,508)
Gross Profit (Loss)	106,656	(392,820)	100,300
Operating expenses	221,259	396,350	1,494,295
Loss from Operations	(114,603)	(789,170)	(1,494,295)
Other income (expense)	175,691	1,141,054	223,877
Increase (decrease) in net assets	61,088	351,884	(1,170,118)
Beginning net assets	(3,621,813)	(3,973,697)	(2,803,579)
Ending net assets	$ (3,560,725)	$ (3,621,813)	$ (3,973,697)

Sales include licensing fees from vessels licensed under the NFC/NORMA agreement of $72k, a vessel lease of $29k, fish grading of $21k, and sales of fishing gear and supplies of $7k. During the year, NFC generated $670k from licensing fees, of which $598k or 89% was remitted to NORMA.

Total sales of $132k are from NFC corporate operational activities only. The total operating expense for the year is $221k. The largest component is salaries and wages of $130k, office expense of $26k; rental expense of $24k, utilities of $12k; travel and entertainment of $12k, telephone expense of $9k, depreciation and amortization of $3k, contractual fees of $2k, representations expense of $1k, repairs and maintenance of $1k and miscellaneous expense of $642.

Other income of $176k is primarily made up of the subsidy from the FSM National Government amounting to $135k.

3. Summary Statement of Cash Flows (SCF)

The SCF presents information about changes in the 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 the activities into cash flows arising from operating activities, non capital financing and capital and related financing.

Below is the summary statement of cash flows:

	FY 2008	FY 2007	FY 2006
From operating activities	$ (104,381)	$ (94,170)	$ (114,374)
Provided by non capital financing activities	135,000	100,000	135,000
From capital and related financing activities	(11,000)	(979)	4,274
Net change in cash and equivalents	19,619	4,851	16,352
Cash and equivalents at beginning of year	24,674	19,823	3,471
Cash and equivalents at year end	$ 44,293	$ 24,674	19,823

3. Debt and Capital Asset Activities

No significant debt or capital asset activities occurred during the year ended September 30, 2008. For additional information on fixed assets, please refer to Note 4 to the financial statements. For additional information on notes payable, please refer to note 5 to the financial statements.

Management's Discussion and Analysis for the year ended September 30, 2007 is set forth in NFC's report on the audit of financial statements, which is dated February 12, 2009. That Discussion and Analysis explains the major factors impacting the 2007 financial statements and can be obtained from the FSM Office of the National Public Auditor's website at www.fsmpublicauditor.fm.

Economic Outlook

The Company has incurred substantial losses from its regular operations including investments with Micronesia Longline Fishing Company (MLFC), Kosrae Sea Ventures (KSV), Chuuk Fresh Tuna Inc. (CFTI) and Yap Fishing Corporation (YFC). The accumulated losses of NFC from its investments have severely affected NFC's regular operations. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Currently, the Company is dependent on the FSM National Government for its operating budgets. Financial assistance from FSM National Government is needed to rehabilitate and reconstruct its debt to FSM National government. NFC management is in the process of establishing a joint venture with other foreign fishing companies and anticipates commencing new joint venture operations in the late part of fiscal year 2009. The joint venture operation is expected to generate sufficient added income to render NFC to be a self supporting company in FY 2010 and thereafter.

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Statements of Net Assets
September 30, 2008 and 2007

	2008	2007
ASSETS		
Current assets:		
Cash	$ 44,293	$ 24,674
Receivables, net of allowance for uncollectible accounts of $715,783 in 2008 and 2007	3,426	15,898
Inventory	83,464	88,853
Total current assets	131,183	129,425
Investment	-	-
Property and equipment, net	160,377	111,704
	$ 291,560	$ 241,129
LIABILITIES AND NET ASSETS		
Current liabilities:		
Notes payable	$ 3,600,000	$ 3,600,000
Accounts payable	241,304	248,725
Accrued liabilities	10,981	14,217
Total current liabilities	3,852,285	3,862,942
Contingencies		
Net assets:		
Invested in capital assets	160,377	111,704
Unrestricted	(3,721,102)	(3,733,517)
Total net assets	(3,560,725)	(3,621,813)
	$ 291,560	$ 241,129

See accompanying notes to financial statements.

NATIONAL FISHERIES CORPORATION
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Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2008 and 2007

	2008	2007
Sales	$ 138,537	$ 98,415
Cost of sales	(31,881)	(491,235)
Gross profit (loss)	106,656	(392,820)
Operating expenses:		
Salaries and wages	130,401	105,845
Office expense	25,552	12,785
Rent	23,702	29,118
Utilities	12,244	28,375
Travel and entertainment	11,645	5,239
Telephone and communication	8,912	10,631
Depreciation and amortization	3,018	181,238
Contractual services	2,410	13,250
Representation	1,479	1,211
Repairs and maintenance	1,254	1,530
Payroll and other taxes	-	6,766
Miscellaneous	642	362
Total operating expenses	221,259	396,350
Loss from operations	(114,603)	(789,170)
Other income (expense):		
FSM National Government operating subsidy	135,000	100,000
Other income, net	-	1,586,967
Gain (loss) on disposal of fixed assets	40,691	(59,059)
Loss on investment in subsidiary	-	(486,854)
Total other income (expense), net	175,691	1,141,054
Change in net assets	61,088	351,884
Net assets at beginning of year	(3,621,813)	(3,973,697)
Net assets at end of year	$ (3,560,725)	$ (3,621,813)

See accompanying notes to financial statements.

NATIONAL FISHERIES CORPORATION
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Statements of Cash Flows
Years Ended September 30, 2008 and 2007

	2008	2007
Cash flows from operating activities:		
Cash received from customers	$ 151,009	$ 305,358
Cash paid to suppliers for goods and services	(121,753)	(295,142)
Cash paid to employees for services	(133,637)	(104,386)
Net cash used in operating activities	(104,381)	(94,170)
Cash flows from noncapital financing activities:		
FSM National Government operating subsidies	135,000	100,000
Net cash provided by noncapital financing activities	135,000	100,000
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(11,000)	(979)
Net cash used for capital and related financing activities	(11,000)	(979)
Net change in cash	19,619	4,851
Cash at beginning of year	24,674	19,823
Cash at end of year	$ 44,293	$ 24,674
Reconciliation of loss from operations to cash flows used in operating activities:		
Loss from operations	$ (114,603)	$ (789,170)
Adjustments to reconcile loss from operations to net cash used in operating activities:		
Depreciation and amortization	3,018	181,238
Bad debts	-	475,920
(Increase) decrease in assets:		
Accounts receivable	12,472	78,057
Advances	-	128,886
Inventory	5,389	(58,105)
Increase (decrease) in liabilities:		
Accounts payable	(7,421)	(119,221)
Accrued liabilities	(3,236)	8,225
Net cash used in operating activities	$ (104,381)	$ (94,170)

See accompanying notes to financial statements.

(1) Reporting Entity

The National Fisheries Corporation (NFC) was created under FSM Public Law No. 3-14 by the third Congress of the Federated States of Micronesia (FSM).

The purpose of NFC is to promote the development of commercial pelagic fisheries and related industries within the Federated States of Micronesia's 200 mile Exclusive Economic Zone. NFC is also involved in ancillary activities that support commercial fishery activities. These activities include technical and infrastructure services, manpower training and other related activities promoting commercial fisheries development.

NFC is a discretely presented component unit of the FSM National Government. The financial statements of NFC are incorporated into those of the FSM National Government. Debts and obligations of NFC are not obligations of the FSM National Government unless specifically authorized by the FSM National Government. To date, no such authorization has been made.

(2) Summary of Significant Accounting Policies

The accounting policies of NFC conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds. Governmental 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. NFC has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

GASB issued Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and modified by Statement No. 38, *Certain Financial Statement Note Disclosures*. These statements establish financial reporting standards for governmental entities which require that management's discussion and analysis of the financial activities be included with the basic financial statements and notes and modify certain other financial statement disclosure requirements.

To conform to the requirements of GASB Statement 34, retained earnings are presented in the following net asset categories:

- Investment in capital assets; capital assets, net of accumulated depreciation, plus construction or improvement of those assets.

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

(2) Summary of Significant Accounting Policies, Continued

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.

Basis of Accounting

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

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

Cash

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

As of September 30, 2008 and 2007, the carrying amount of NFC's total cash and cash equivalents and time certificates of deposit were $44,293 and $24,674, respectively, and the corresponding bank balances were $44,463 and $28,931, respectively, all of which were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2008 and 2007, all bank deposits were FDIC insured. NFC does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk. NFC has not experienced any losses in such accounts and management believes it is not exposed to any significant credit risk on its deposits.

(2) Summary of Significant Accounting Policies, Continued

Investments and Business Development

NFC, in prior years, has invested in various joint ventures with respective agencies in the four states which are directly involved in the exploitation and development of the FSM's fisheries industry. The NFC involvement in these joint ventures varies in nature.

NFC has previously been directly involved in the management of certain joint ventures through management and marketing agreements entered into with the respective parties. The investment in Micronesia Longline Fishing Company (MLFC), Yap Fishing Corporation (YFC), Yap Fresh Tuna, Inc. (YFTI), Chuuk Fresh Tuna, Inc. (CFTI), and Kosrae Sea Venture Inc. (KSVI) are accounted for using the equity method and, accordingly, the carrying values of these investments have been reduced to $0. In 2008 and 2007, financial statements for these joint ventures were not available and, therefore the financial position and results of operations of these joint ventures has not been consolidated with NFC's financial statements.

Receivables

Receivables from fishing and ancillary activities are based on contracted prices, which are both interest free and uncollateralized and are primarily due from government agencies, businesses and individuals located within the FSM. The allowance for doubtful accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. The allowance is established through a provision for uncollectible receivables recorded in the statement of revenues, expenses and changes in net assets.

Inventory

Inventory of fishing supplies is valued at the lower of cost (first-in, first-out) or market.

Property and Equipment

Property and equipment are stated at cost or estimated historical cost, less accumulated depreciation. Donated fixed assets are recorded at estimated fair market value at the date received. The provision for depreciation is computed by the straight line method over the estimated useful lives of the assets, ranging from 3 to 15 years depending on the nature of the asset. A singular piece of equipment, vehicles, office equipment, etc. that equals or exceeds $5,000 is capitalized, except for those assets of the investees, where no set threshold for capitalization of fixed assets has been established.

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. No liability is recorded for nonvesting accumulating rights to receive sick pay benefits.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During fiscal year 2008, NFC implemented the following pronouncements:

- GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which establishes uniform financial reporting for other postemployment benefit plans by state and local governments.

- GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues*, which establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing, and includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components.

- GASB Statement No. 50, *Pension Disclosures an amendment of GASB Statements No. 25 and 27*, which more closely aligns the financial reporting requirements for pensions with those for other post-employment benefits.

The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other post-employment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of NFC.

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB Statement No. 49 provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of NFC.

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. GASB Statement No. 51 addresses whether and when intangible assets should be considered capital assets for financial reporting purposes. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of NFC.

In November 2007, GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. GASB Statement No. 52 improves the quality of financial reporting by requiring endowments to report their land and other real estate investments at fair value, creating consistency in reporting among similar entities that exist to invest resources for the purpose of generating income. The provisions of this statement are effective for periods beginning after June 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of NFC.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. GASB Statement No. 53 is intended to improve how state and local governments report information about derivative instruments - financial arrangements used by governments to manage specific risks or make investments - in their financial statements. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of NFC.

(3) Related Party Transactions

NFC has entered into various transactions with the FSM National Government. Various loans have been obtained from the FSM National Government or the FSM Development Bank, a component unit of the FSM National Government. These loans are disclosed in note 5.

(4) Property and Equipment

Capital asset activity for the years ended September 30, 2008 and 2007 follows:

	October 1, 2007	Additions	Deletions	September 30, 2008
Machinery and equipment	$ 13,750	$ 11,000	$ -	$ 24,750
Fishing vessels – donated	1,497,618	-	-	1,497,618
Office furniture and equipment	32,315	-	(5,254)	27,061
	1,543,683	11,000	(5,254)	1,549,429
Less accumulated depreciation	(1,431,979)	(3,018)	45,945	(1,389,052)
	$ 111,704	$ 7,982	$ 40,691	$ 160,377

	October 1, 2006	Additions	Deletions	September 30, 2007
Machinery and equipment	$ 28,424	$ -	$ (14,674)	$ 13,750
Fishing vessels – purchased	543,423	-	(543,423)	-
Fishing vessels – donated	2,351,454	-	(853,836)	1,497,618
Fishing equipment – purchased	89,055	-	(89,055)	-
Fishing equipment – donated	464,099	-	(464,099)	-
Office furniture and equipment	212,745	979	(181,409)	32,315
Vehicles	12,745	-	(12,745)	-
	3,701,945	979	(2,159,241)	1,543,683
Less accumulated depreciation	(3,469,041)	(181,238)	2,218,300	(1,431,979)
	$ 232,904	$ (180,259)	$ 59,059	$ 111,704

(5) Notes Payable

Notes payable consist of the following at September 30, 2008 and 2007:

	2008	2007
Loan payable to the FSM National Government due in annual installments of $44,153, non-interest bearing, collateralized by NFC's shares in YFC, with a term of 16 years, beginning March 1994, ending March 2010.	$ 750,640	$ 750,640
Loan payable to the FSM National Government due in annual installments of $86,639, non-interest bearing, with a term of 13 years, beginning July 1994, ending July 2007.	1,212,940	1,212,940
Loan payable to the FSM National Government due in annual installments of $23,363, non-interest bearing, with a term of 16 years, beginning September 1994, ending September 2010.	397,176	397,176
Loan payable to FSM National Government due in annual installments of $29,412, non-interest bearing, with a term of 17 years, beginning October 1995, ending October 2011.	500,000	500,000
Loan payable to the FSM National Government due in annual installments of $5,000, non-interest bearing, with a term of 20 years, beginning April 1995, ending April 2014.	100,000	100,000
Loan payable to the FSM National Government due in annual installments of $1,962, non-interest bearing, with a term of 20 years, beginning April 1995, ending April 2014.	39,244	39,244
Loan payable to the FSM National Government due in annual installments of $5,000, non-interest bearing, with a term of 20 years, beginning November 1994, ending April 2013.	100,000	100,000
Loan payable to the FSM National Government with no terms.	500,000	500,000
	$ 3,600,000	$ 3,600,000

NFC is in default on its notes payable and, therefore, all related debt has been classified as current.

Changes in debt during the years ended September 30, 2008 and 2007 are as follows:

Balance at Beginning of Year 2008	Additions	Deletions	Balance at End of Year 2008
$ 3,600,000	$ -	$ -	$ 3,600,000

(5) Notes Payable, Continued

Balance at Beginning of Year 2007	Additions	Deletions	Balance at End of Year 2007
$ 3,600,000	$ -	$ -	$ 3,600,000

(6) Contingencies

NFC is party to various legal proceedings arising from operations. External legal counsel represents that the ultimate outcome of the lawsuits cannot be predicted at this time; therefore, no provision for any related liability has been made in the financial statements.

NFC is liable for Micronesia Longline Fishing Company's (MLFC) loans payable to the Asian Development Bank. MLFC has defaulted on this loan; however, the FSM National Government has been making required debt service payments on behalf of NFC and it is not possible to predict the ultimate outcome of this matter. No provision for this matter has been made in the accompanying financial statements. The MLFC debt is, instead, recorded in the financial statements of the FSM National Government.

(7) Going Concern

NFC has incurred substantial losses from operations. This condition raises substantial doubt about the Corporation's ability to continue as a going concern. NFC, as a component unit of the FSM National Government, is dependent on the FSM National Government for its cash flows.

(8) Risk Management

NFC is substantially self-insured for all risks. Management is of the opinion that no material losses have been sustained as a result of this practice during the past three years.

(9) Other Income

During the year ended September 30, 2007, NFC recorded net non-operating income of $1,586,967, which represents the write-off of aircraft lease payable, totaling $992,228, and the reconciliation of various asset and liability accounts amounting to a net total of $594,739.

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

The Board of Directors
National Fisheries Corporation:

We have audited the financial statements of the National Fisheries Corporation (NFC) as of September 30, 2008 and have issued our report thereon dated September 16, 2009, which was qualified with respect to equity investments. 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 NFC's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of NFC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of NFC's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with accounting principles generally accepted in the United States of America such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Responses (pages 19 through 21) as items 2008-1 through 2008-3 to be significant deficiencies in internal control over financial reporting.

A *material weakness* is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Member of
Deloitte Touche Tohmatsu

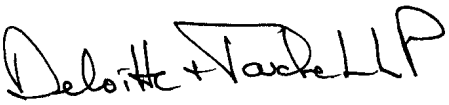
Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that the significant deficiencies described above are material weaknesses.

Compliance and Other Matters

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

NFC's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. We did not audit NFC's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Board of Directors, management, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.



September 16, 2009

NATIONAL FISHERIES CORPORATION
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Schedule of Findings and Responses
Year Ended September 30, 2008

Other Income

Finding No. 2008-1

Criteria: Adequate documentation, including subsidiary records, should be available to support amounts and items reported in the financial statements.

Condition: Detailed records supporting $14,529 of other income were not available for inspection.

Cause: The root cause of the weakness is that subsidiary records are not correctly maintained.

Effect: The effect of this condition is the possibility of misstatement of account balances.

Recommendation: We recommend that NFC ensure appropriate maintenance of all subsidiary ledgers to support amounts reported in the financial statements.

Auditee Response: As cited before, poor record keeping was a problem in prior years and the amount cited refers to previous years transaction. NFC's new management is doing its best to correct the account balances as part of the new management accounting procedures and system. In an effort to clean up the financial statements of NFC and to ensure that the balances reflected are properly supported with details and documents, all account were revisited. The cited entries were the result of this cleaning-up process.

Absence of Investee's Financial Statements

Finding No. 2008-2

Criteria: Adequate documentation, i.e. investee's audited financial statements, should be available to support amounts reported in the financial statements.

Condition: Financial statements supporting NFC's investment in Chuuk Fresh Tuna, Inc., Yap Fresh Tuna, Inc., Kosrae Sea Venture, Inc., and Micronesia Longline Fishing Company are not available for inclusion in the NFC consolidation.

Cause: The cause of this condition is that financial statements from the investees have not been provided.

Effect: The effect of this condition is a potential material misstatement of the financial statements.

Prior Year Status: This condition has been reported in prior year audits.

Recommendation: We recommend that management ensure that its investees provide audited financial statements on an annual basis.

Auditee Response: NFC subsidiaries failed to submit audited financial statements since 1997. Therefore, because of the unavailability of financial data from NFC subsidiaries, balances from these investee's were excluded from NFC's financial statement as we can not ascertain the value of these investments. NFC started the non-inclusion of MLFC's financial data in NFC's consolidated financial statement in fiscal year 2004. Investment balance from CFTI amounting to $486k was also written –off during FY 2007. Thus, balances of all NFC subsidiaries were zero since 2007.

Journal Voucher Entries

Finding No. 2008-3

Criteria: Adjustments to the general ledger should be correct and valid.

Condition: Based on nine journal voucher entries tested, we found that all were incorrect and invalid.

Cause: The root cause of the condition is that the JVs were incorrectly prepared.

Effect: Corrections were made through the audit process.

Prior Year Status: The condition has been reported in prior year audits.

Recommendation: We recommend that NFC management scrutinize each adjusting journal entry as to correctness and validity before it is entered into the accounting system.

Auditee Response: As with finding number 1, these relate to previous years erroneous balances. The cited entries are made to correct those balances.

NATIONAL FISHERIES CORPORATION
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Unresolved Prior Year Findings
Year Ended September 30, 2008

The status of unresolved prior year findings is disclosed within the Schedule of Findings and Responses section of this report (pages 19 through 21).