FEDERATED STATES OF MICRONESIA TELECOMMUNICATIONS CORPORATION

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

FINANCIAL STATEMENTS, ADDITIONAL INFORMATION AND INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2014 AND 2013

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

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Years Ended September 30, 2014 and 2013

Deloitte & Touche LLP
361 South Marine Corps Drive
Tamuning, GU 96913-3911
USA
Tel: (671)646-3884
Fax: (671)649-4932
www.deloitte.com

INDEPENDENT AUDITORS' REPORT

Board of Directors
Federated States of Micronesia
Telecommunications Corporation:

Report on the Financial Statements

We have audited the accompanying financial statements of the Federated States of Micronesia (FSM) Telecommunications Corporation (the Corporation), a component unit of the FSM National Government, which comprise the statements of net position as of September 30, 2014 and 2013, and the related statements of revenues, expenses, and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Corporation as of September 30, 2014 and 2013, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. This supplementary information is the responsibility of the Corporation's management. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Other Supplementary Information listed in the accompanying table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The Other Supplementary Information is the responsibility of the Corporation's management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standard generally accepted in the United States of America. In our opinion, the Other Supplementary Information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated December 30, 2014 on our consideration of the Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financing reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Corporation's internal control over financial reporting and compliance.

Deloitte + Touche LLP

December 30, 2014

Our discussion and analysis of the Federated States of Micronesia Telecommunications Corporation (FSMTC) financial performance provides an overview of the FSMTC financial activities for the fiscal year then ended September 30, 2014. This discussion has been prepared by the FSMTC management to further provide an introduction and understanding of the basic financial statements for the year ended September 30, 2014. Please read it in conjunction with the financial statements and the notes thereto, which follow this discussion and analysis. Fiscal years 2013 and 2012 comparative information has been included, where appropriate.

The FSMTC is a public corporation of the Federated States of Micronesia National Government and is the primary provider of telecommunications services throughout the Federated States of Micronesia (FSM) and to points outside of the FSM. The FSMTC also provides Cable TV in the State of Kosrae, and Digital Broadcast Television (DBTV) to both Yap and Chuuk States. Yap's former Wireless TV broadcasting, which was analog in nature, was replaced by DBTV in FY2012.

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

The FSMTC provides telecommunications services which include Plain Old Telephone Services (POTS) to 13,037 active subscribers. Other telecommunications services provided are National and International Overseas Calls, Internet Services, Mobile Cellular Services, Cable Television in the State of Kosrae with 206 active subscribers, DBTV in the State of Chuuk with 305 active subscribers and DBTV in the State of Yap with 221 active subscribers.

The FSMTC relies on calls made to and from outside of the FSM and calls within the FSM, which account for 16.43% of FSMTC's FY2014 operating revenues as compared with 19.05% of the FSMTC's FY2013 operating revenues. During FY2014, FSMTC realized a decrease in Call revenue of $418,011 (or -15.78%) as compared to FY2013. Management believes that the decrease was caused by the increase in internet usage and the increase in ADSL Internet subscribers in FY2014. With the introduction of smart phones and accessibilities to unlimited internet, subscribers were able to utilize such technology to place overseas calls through the use of applications available on the internet.

Internet Services (Wifi, Dial Up, ADSL & FM Domain) account for 32.48% of FSMTC's FY2014 operating revenues as compared with 30.26% of FSMTC'S FY 2013 operating revenues. During FY2014, FSMTC realized an increase in Internet service revenues of $204,234 (or 4.86%) as compared to FY2013. More and more customers are moving to unlimited internet service by subscribing to ADSL, which contributed to the increase in internet revenue. It is expected that data services will continue to dominate the telecom services in terms of revenue contribution.

Mobile services account for 25.35% of FSMTC's FY2014 operating revenues as compared with 23.87% of FSMTC'S FY2013 operating revenues. During FY2014, FSMTC realized an increase in mobile service revenues of $124,585 (or 3.75%) as compared to FY2013. This increase can be attributed to the increasing demand for smart phones and cellphone accessories.

Statement of Net Position

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

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

The following summarizes the financial condition and operations of the FSMTC for FY2014, FY2013 and FY2012:

	2014	2013	2012
Assets:			
Cash and cash equivalents	$ 1,451,756	$ 1,198,227	$ 1,254,195
TCD's and investments in securities	1,857,641	1,731,714	1,468,405
Receivables and prepayments	1,257,884	1,474,229	1,495,375
Inventory	763,722	784,681	680,442
Total current assets	5,331,003	5,188,851	4,898,417
Capital assets	44,541,583	43,978,307	48,169,976
Other non-current assets	2,998,167	3,144,419	3,290,671
	$ 52,870,753	$ 52,311,577	$ 56,359,064
Liabilities:			
Current liabilities	3,335,702	3,032,890	3,426,175
Non-current liabilities	28,512,361	27,399,546	28,987,140
Total liabilities	31,848,063	30,432,436	32,413,315
Net Position:			
Net investment in capital assets	17,359,448	18,136,421	20,962,941
Restricted	-	-	85,866
Unrestricted	3,663,242	3,742,720	2,896,942
Total net position	21,022,690	21,879,141	23,945,749
	$ 52,870,753	$ 52,311,577	$ 56,359,064

The total liabilities of FSMTC increased by $1,415,627 (or 4.65%) compared with prior year. This increase in total liabilities can be attributed to the remaining unpaid amount from cellular infrastructure upgrade. Such liability was incurred due to the cellular network upgrade with 3G capabilities.

The net position of FSMTC was affected by the change in both assets and liabilities and decreased by a net loss from operations of $856,451.

During FY2014, total cash received from telecommunications services exceeded the amounts paid to vendors and employees for goods and services. This resulted in net cash provided by operating activities of $3,979,764 as compared with $3,800,369 in FY2013.

The cash and cash equivalents at the end of FY2014 are $1,451,756 as compared to $1,198,227 at the end of the prior year. The net cash provided during FY2014 exceeded net cash used from operations, mainly due to contribution coming from operations.

Statement of Revenues, Expenses and Changes in Net Position

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

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

The following table summarizes the financial operations of the FSMTC for the years ended September 30, 2014, 2013 and 2012.

	2014	2013	2012
Operating revenues	$ 13,579,504	$ 13,951,541	$ 13,986,609
Operating expenses	14,574,642	14,695,306	14,794,097
Net operating loss	(995,138)	(743,765)	(807,488)
Interest income and others	71,265	163,157	282,748
Interest expense	(1,326,136)	(1,486,000)	(1,513,134)
	(2,250,009)	(2,066,608)	(2,037,874)
Capital grants	1,393,558	-	360,000
Change in net position	(856,451)	(2,066,608)	(1,677,874)
Net position, beginning of year	21,879,141	23,945,749	25,623,623
Net position, end of year	$ 21,022,690	$ 21,879,141	$ 23,945,749

Total operating revenue in FY2014 decreased by $372,037 (or -2.67%) compared to FY2013. The decrease is mainly due to continuous decline in mobile and international revenue. Operating expenses in FY2014 decreased by $120,664 (or -0.82%) compared to FY2013 operating expenses. This decrease in operating expenses can be attributed to continuing cost control by the Corporation.

The FSMTC investments in property, plant and equipment, net of accumulated depreciation, amounted to $44,541,583 in FY2014 and $43,978,307 in FY2013, which included capital expenditures in FY 2014 of $4 million for 3G Mobile Services. For additional information concerning capital assets, please refer to note 4 to the accompanying financial statements.

FSMTC's notes payable with the US Department of Agriculture (Rural Utilities Services) amounted to $27,380,302 of which $1,667,941 is classified as the current portion. For additional information concerning the FSMTC's long term debt, please refer to note 7 to the accompanying financial statements.

On November 19, 2008, United States Department of Agriculture Rural Development notified the FSMTC that based on the preliminary review of it "B" loan application, the FSMTC was qualified to borrow an additional amount of $13,120,000. At September 30, 2014, the FSMTC has drawn-down $12,136,034 from RUS for the purpose of funding the Fiber Optic Cable projects. The loan proceeds were to purchase 8 wavelengths of the fiber capacity of two fibers of the Kwajealein Cable System (KCS) as a capital lease for 25 years or Indefeasible right to use (IRU). The remaining balance of the loan is for electronics, engineering and construction of the undersea facilities between Pohnpei and the KCS network branch.

Management's Discussion and Analysis for the year ended September 30, 2013 is set forth in FSMTC'S report on the audit of financial statements, which is dated December 27, 2013. That Discussion and Analysis explains the major factors impacting the 2013 financial statements and can be viewed at the Office of the FSM National Public Auditor's website at www.fsmopa.fm

Economic Outlook

The introduction of 3G service with aggressive marketing strategy can have a huge impact in increased revenue. Management is coming up with several packages to cover the majority of the market in the FSM. Should the projected revenue for FY 2015 be achieved the commitment on revenue sharing will be met. Everything rests on quality service and effective marketing strategies to achieve positive end results. Management is optimistic that all these can be accomplished with the blessing of the board of directors and concerted efforts of management as a whole. Failure to meet the projected revenue will greatly affect operations and cash flow. Should the Corporation experience difficulty in cash flows, management may have to seek assistance from the FSM National Government.

Economic indicators suggest that gross domestic product (GDP) growth this year in the Federated States of Micronesia (FSM) remains on track to meet Asian Development Outlook (ADO) 2014 projections in April. As North Pacific economies, including FSM, are small and dominated by the public sector, economic performance generally tracks public capital expenditure.

Selected economic indicators (%) - Federated States of Micronesia	2014		2015	
	ADO 2014	Update	ADO 2014	Update
GDP Growth	0.5	**0.5**	0.5	**0.5**
Inflation	2.0	**2.0**	1.5	**1.5**
Current Account Balance (share of GDP)	-9.6	**-10.3**	-9.3	**-9.9**

Source: ADB estimates.

Economic growth in FSM is expected to remain sluggish at 0.5% in Fiscal Year 2014 (ends 30 September 2014), as forecast in ADO 2014. A lack of major public infrastructure projects, and weak private investment and business activity dim prospects for stronger growth in the near term. Unutilized funds from the United States under the Compact of Free Association for infrastructure projects reached over $140 million. Sluggish private sector growth is attributed to an unfavorable business environment. Attempts to improve this through tax reform have been delayed by opposition from two of the four states.

With the recent passage of the FSM telecommunications bill into law in 2014, the impact of such is not expected to have an immediate impact on FSMTC's operations. Instead, it is expected that the impact will be felt in about 5 years as it will take time to set up regulatory boards and related agencies that will oversee the liberalization of the telecommunications industry in the FSM.

Relatively low and stable inflation is expected in FSM, in line with ADO 2014 forecasts, and expectations that international commodity prices will remain soft.

Despite higher food imports, the value of FSM's imports from the US fell by 23.0% year on year, mainly on a 42.0% drop in imports of machinery, transport equipment, and manufactured goods.

FSM's current account deficit is still expected to narrow on increases in fishing license revenue, albeit by slightly less than forecast previously. (*Source: ADB. 2014. Asian Development Outlook 2014 Update. Manila.)*

There has been no significant stimulus into the economy and none is seen in the near future. The same is being contained in the report prepared by US Graduate School. While there has been a modest increase in economic growth mostly in Pohnpei economy, the net effects from other states leave overall growth stagnant.

The Corporation had just completed the Mobile Services expansion in Pohnpei, Chuuk, Yap & Kosrae at a cost of $4 million. The upgrade calls for the introduction of 3G mobile data service to Pohnpei and soon to Chuuk, Yap & Kosrae. Because of the substantial contribution of Mobile Services to revenue, FSMTC is committed to maintaining a more reliable service to the people. The Corporation has modern, state of the art equipment and tariff rates that we feel are very reasonable compared with other telephone companies in the Pacific Region.

In addition to the mobile services investments, FSMTC has also signed up with O3B to provide better and bigger capacity. O3b's next-generation network combines the reach of satellite with the speed of fiber, providing customers with affordable, low latency, high bandwidth connectivity. Yap is the first state to experience O3B technology. O3B in Chuuk will be up in 3 months.

Most of the telecommunications services provided in other more developed countries are available in the Federated States of Micronesia. These modern telecommunications services should go a long way in assisting the Federated States of Micronesia in its efforts to attract investors and to further develop our island nation. FSMTC will continue to seek improved technologies to better serve its customers and at the same time bring significant operating savings.

Financial Contact

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

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

Statements of Net Position
September 30, 2014 and 2013

	2014	2013
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,451,756	$ 1,198,227
Time certificates of deposit	276,784	276,467
Investment in securities	1,580,857	1,455,247
Accounts receivable, net of an allowance for doubtful accounts of $947,201 and $1,076,165 in 2014 and 2013, respectively	557,728	589,337
Receivables from carriers	242,995	433,231
Advances to employees	12,700	49,559
Inventory	763,722	784,681
Accrued interest and other accrued earnings	146,903	182,398
Other receivables and prepaid expenses	297,558	219,704
Total current assets	5,331,003	5,188,851
Capital assets:		
Nondepreciable capital assets	4,724,503	23,725
Capital assets, net of accumulated depreciation	39,817,080	43,954,582
Indefeasible right of use, net	2,998,167	3,144,419
	$ 52,870,753	$ 52,311,577
LIABILITIES AND NET POSITION		
Current liabilities:		
Current maturities of long-term debt	$ 1,667,941	$ 1,586,759
Current maturities of contract liability	899,640	-
Accounts payable, trade	64,968	233,934
Unearned income	422,132	137,495
Customer deposits	355,405	445,797
Accrued leave payable	117,568	115,188
Other accrued liabilities	707,688	513,717
Total current liabilities	4,235,342	3,032,890
Contract liability, net of current portion	1,900,360	-
Long-term debt, net of current portion	25,712,361	27,399,546
Total liabilities	31,848,063	30,432,436
Commitments and contingencies		
Net position:		
Net investment in capital assets	17,359,448	18,136,421
Unrestricted	3,663,242	3,742,720
Total net position	21,022,690	21,879,141
	$ 52,870,753	$ 52,311,577

See accompanying notes to financial statements.

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

Statements of Revenues, Expenses, and Changes in Net Position
Years Ended September 30, 2014 and 2013

	2014	2013
Operating revenues:		
Internet	$ 4,410,783	$ 4,206,549
Mobile charges	3,442,482	3,317,897
Overseas tolls	2,230,501	2,648,512
Net access	1,816,625	1,885,607
External carriers	1,535,392	1,626,674
ICTV Chuuk cable charges	98,490	68,228
ICTV Yap cable charges	66,647	71,664
ICTV Kosrae cable charges	63,286	69,925
Recovery of bad debts	122,383	67,327
Miscellaneous	163,607	324,024
Discounts	(370,692)	(334,866)
Total operating revenues	13,579,504	13,951,541
Operating expenses:		
Corporate operations	2,605,780	2,595,174
Plant operations	2,122,211	2,063,177
Internet expense	1,898,804	1,776,888
Cable and wire	1,653,925	1,780,741
Wireless telephone	1,521,234	1,529,930
Consumer operations	1,329,284	1,187,439
Earth station	1,196,463	1,183,432
General support	1,117,378	1,144,595
Central office	404,536	378,365
Terminal equipment	338,825	449,360
ICTV expense	386,202	606,205
Total operating expenses	14,574,642	14,695,306
Loss from operations	(995,138)	(743,765)
Nonoperating revenues (expenses):		
Interest expense	(1,326,136)	(1,486,000)
Loss on fixed asset retirement	(54,345)	-
Investment income	125,610	163,157
Total nonoperating revenues (expenses), net	(1,254,871)	(1,322,843)
Capital grants	1,393,558	-
Change in net position	(856,451)	(2,066,608)
Total net position at beginning of year	21,879,141	23,945,749
Total net position at end of year	$ 21,022,690	$ 21,879,141

See accompanying notes to financial statements.

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

Statements of Cash Flows
Years Ended September 30, 2014 and 2013

	2014	2013
Cash flows from operating activities:		
Cash received from subscribers, long distance carriers and other customers	$ 14,196,047	$ 13,479,898
Cash paid to suppliers for goods and services	(6,791,591)	(6,018,253)
Cash paid to employees	(3,424,692)	(3,661,276)
Net cash provided by operating activities	3,979,764	3,800,369
Cash flows from capital and related financing activities:		
Proceeds from FSM National Government capital grant	1,393,558	-
Additions to property, plant and equipment	(2,117,418)	(758,784)
Repayments of RUS long-term debt	(1,606,003)	(1,511,401)
Interest paid on RUS long-term debt	(1,466,965)	(1,488,676)
Net cash used for capital and related financing activities	(3,796,828)	(3,758,861)
Cash flows from investing activities:		
Net purchases, sales and maturities of investments	(27,921)	(33,398)
Net investment for time deposits	-	(100,000)
Interest and dividends received on investment securities and others	28,595	35,922
Net cash provided by (used for) investing activities	674	(97,476)
Net change in cash and cash equivalents	183,610	(55,968)
Cash and cash equivalents at beginning of year	1,198,227	1,254,195
Cash and cash equivalents at end of year	$ 1,381,837	$ 1,198,227
Reconciliation of loss from operations to net cash provided by operating activities:		
Loss from operations	$ (995,138)	$ (743,765)
Adjustments to reconcile loss from operations to net cash provided by operating activities:		
Depreciation and amortization	4,515,968	4,812,965
(Increase) decrease in assets:		
Accounts receivable	31,609	(19,767)
Receivables from carriers	190,236	(104,686)
Advances to employees	36,859	(36,780)
Inventory	20,959	(104,239)
Accrued interest and other accrued earnings	35,495	2,846
Other receivables and prepaid expenses	(77,854)	179,533
Increase (decrease) in liabilities:		
Accounts payable, trade	(168,966)	(213,607)
Unearned income	284,637	(32,560)
Accrued leave payable	2,380	(17,987)
Customer deposits	(90,392)	-
Other accrued liabilities	193,971	78,416
Net cash provided by operating activities	$ 3,979,764	$ 3,800,369

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION
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Statements of Cash Flows, Continued
Years Ended September 30, 2014 and 2013

	2014	2013
Summary of disclosure for noncash activities		
Accrual of contract liability:		
Project under construction	2,800,000	-
Contract liability	(2,800,000)	-
	$ -	$ -

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

Nature of Operations

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

Organization

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

Basis of Accounting

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

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No.'s 37 and 38, establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into the following three net position categories:

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

- Restricted - net position whose use by the Corporation is subject to externally imposed stipulations that can be fulfilled by actions of the Corporation pursuant to those stipulations or that expire by the passage of time. The Corporation has no restricted net position at September 30, 2014 and 2013.

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

(1) Summary of Significant Accounting Policies, Continued

Cash and Cash Equivalents and Time Certificates of Deposit

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

Investments

Investments and related investment earnings are reported at fair value using quoted market prices. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Accounts Receivable

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

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

Inventory

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

Property, Plant and Equipment

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

Plant Under Construction

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

(1) Summary of Significant Accounting Policies, Continued

Indefeasible Right of Use

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

Valuation of Long-Lived Assets

The Corporation, using its best estimates based on reasonable and supportable assumptions and projections, reviews assets for impairment whenever events or changes in circumstances have indicated that the carrying amount of its assets might not be recoverable. Impaired assets are reported at the lower of cost or fair value. At September 30, 2014 and 2013, no assets had been written down.

Compensated Absences

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

Income Taxes

Corporate profits are not subject to income tax in the FSM. Instead, the FSM National Government imposes a gross revenue tax (GRT) of 3% on gross revenues earned. The Corporation is subject to GRT; however, the Corporation is specifically exempt from any other taxes in accordance with its enabling legislation for the years ended September 30, 2014 and 2013.

Revenue Recognition and Classification

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

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

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

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

Reclassifications

Certain reclassifications have been made to the 2013 financial statements to correspond to the 2014 presentation.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During fiscal year 2014, the Corporation implemented the following pronouncements:

- GASB Statement No. 66, *Technical Corrections - 2012*, which enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 67, *Financial Reporting for Pension Plans,* which revises existing guidance for the financial reports of most pension plans. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, which requires a state or local government guarantor that offers a nonexchange financial guarantee to another organization or government to recognize a liability on its financial statements when it is more likely than not that the guarantor will be required to make a payment to the obligation holders under the agreement. The implementation of this statement did not have a material effect on the accompanying financial statements.

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions,* which revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The provisions in Statement 68 are effective for fiscal years beginning after June 15, 2014. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Corporation.

In January 2013, GASB issued Statement No. 69, *Government Combinations and Disposals of Government Operations,* which improves accounting and financial reporting for state and local governments' combinations and disposals of government operations. Government combinations include mergers, acquisitions, and transfers of operations. A disposal of government operations can occur through a transfer to another government or a sale. The provisions in Statement 69 are effective for fiscal years beginning after December 15, 2013. Management has not yet determined the effect of implementation of these statements on the financial statements of the Corporation.

In November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date - an amendment of GASB Statement No. 68,* which addresses an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or nonemployer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability. The provisions in Statement 71 are effective for fiscal years beginning after June 15, 2014. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Corporation.

(1) Summary of Significant Accounting Policies, Continued

Management Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and 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.

(2) Investment - Island Cable Television

On December 8, 1998, the Corporation acquired a 50% ownership in Island Cable Television - Pohnpei for $450,000. The Corporation recorded this investment under the equity method of accounting. Goodwill of $383,062 resulting from the purchase was being amortized over a period of fifteen (15) years. The remaining goodwill balance of $325,603 as of September 30, 2002 was written-off.

(3) Deposits and Investments

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

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

A. Deposits

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

As of September 30, 2014 and 2013, the carrying amount of the Corporation’s total cash and cash equivalents and time certificates of deposit was $1,728,540 and $1,474,694, respectively, and the corresponding bank balances were $1,867,350 and $1,537,860, respectively, all of which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2014 and 2013, bank deposits in the amount of $378,234 and $386,217, respectively, were FDIC insured. The Corporation does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk. The Corporation has not experienced any losses in such accounts and management believes it is not exposed to any significant credit risk on its deposits.

(3) Deposits and Investments, Continued

B. Investments

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. With the exception of investments in U.S. government securities, which are explicitly or implicitly guaranteed by the United States government, all other investments must be rated in accordance with the Corporation's investment policy.

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Corporation will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. As of September 30, 2014 and 2013, the Corporation's investments are held in the name of the Corporation and are administered by investment managers subject to Securities Investor Protection Corporation insurance in accordance with the Corporation's investment policy.

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

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the Corporation. As of September 30, 2014 and 2013, there were no investments in any one issuer that exceeded 5% of total investments.

As of September 30, 2014 and 2013, investments at fair value are as follows:

	2014	2013
Fixed income:		
U.S. Treasury obligations	$ 198,173	$ 181,204
U.S. Government agencies	53,112	54,353
Corporate notes	140,495	147,347
	391,780	382,904
Other investments:		
Domestic and international equities	1,112,380	978,474
Money market funds	66,697	83,869
	$ 1,570,857	$ 1,445,247

As of September 30, 2014, the Corporation's investments in debt securities were as follows:

	Moody's Credit Rating	Investment Maturities (In Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Treasury obligations	Aaa/P-1	$ 48,706	$ 92,484	$ 56,983	$ -	$ 198,173
U.S. Government agencies	Aaa/P-1	40,770	12,342	-	-	53,112
Corporate notes	AA3/P-1	-	16,814	-	-	16,814
Corporate notes	A1/P-1	15,318	35,698	-	-	51,016
Corporate notes	A2/P-1	15,266	11,365	25,772	-	52,403
Corporate notes	A3-/P-1	15,256	5,006	-	-	20,262
		$ 135,316	$ 173,709	$ 82,755	$ -	$ 391,780

(3) Deposits and Investments, Continued

B. Investments, Continued

As of September 30, 2013, the Corporation's investments in debt securities were as follows:

	Moody's Credit Rating	Investment Maturities (In Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Treasury obligations	Aaa/P-1	$ 28,609	$ 57,907	$ 94,688	$ -	$ 181,204
U.S. Government agencies	Aaa/P-1	-	54,353	-	-	54,353
Corporate notes	A1/P-1	-	41,512	-	-	41,512
Corporate notes	A2/P-1	20,417	15,740	25,328	-	61,485
Corporate notes	A2-/P-1	-	27,302	-	-	27,302
Corporate notes	Aa3/P-1	-	-	17,048	-	17,048
		$ 49,026	$ 196,814	$ 137,064	$ -	$ 382,904

C. Equity Investment, at Cost

On October 7, 2011, the Corporation invested $10,000 in Caroline Cable Corporation (CCC). The equity investment in CCC represents 10,000 shares of common stock and a 1/3 ownership interest. The primary purpose of CCC shall be to engage in the commercial enterprise of acquiring, owning, deploying, managing, maintaining, operating, and repairing a new or used underwater fiber-optic cable to the Republic of Palau with a spur running from a branching unit on the main cable to the State of Yap, Federated States of Micronesia.

(4) Capital Assets

Capital asset activities of the Corporation for the years ended September 30, 2014 and 2013 are as follows:

	Estimated Useful Lives	Balance October 1, 2013	Additions	Retirements	Balance September 30, 2014
General support	5-35 years	$ 16,605,250	$ 165,510	$ (24,948)	$ 16,745,812
Central office	20 years	12,067,074	43,695	(17,343)	12,093,426
Earth station	20 years	5,651,383	-	(29,659)	5,621,724
Terminal equipment	5-20 years	3,610,497	46,607	(221,290)	3,435,814
Cellular network	10-20 years	18,226,611	3,405	-	18,230,016
Internet equipment	8 years	3,042,301	27,342	(14,592)	3,055,051
Pole, cable and wiring	15-20 years	44,415,393	-	(92,228)	44,323,165
Total		103,618,509	286,559	(400,060)	103,505,008
Accumulated depreciation		(59,663,927)	(4,369,716)	345,715	(63,687,928)
		43,954,582	(4,083,157)	(54,345)	39,817,080
Plant under construction		23,725	4,700,778	-	4,724,503
Property, plant and equipment, net		$ 43,978,307	$ 617,621	$ (54,345)	$ 44,541,583

(4) Capital Assets, Continued

	Estimated Useful Lives	Balance October 1, 2012	Additions	Retirements	Balance September 30, 2013
General support	5-35 years	$ 17,000,113	$ 156,521	$ (551,384)	$ 16,605,250
Central office	20 years	12,065,328	1,746	-	12,067,074
Earth station	20 years	5,649,401	11,076	(9,094)	5,651,383
Terminal equipment	5-20 years	3,570,176	40,321	-	3,610,497
Cellular network	10-20 years	18,025,738	200,873	-	18,226,611
Internet equipment	8 years	2,633,389	408,912	-	3,042,301
Pole, cable and wiring	15-20 years	44,424,242	2,182	(11,031)	44,415,393
Total		103,368,387	821,631	(571,509)	103,618,509
Accumulated depreciation		(55,569,725)	(4,665,711)	571,509	(59,663,927)
		47,798,662	(3,844,080)	-	43,954,582
Plant under construction		371,314	145,214	(492,803)	23,725
Property, plant and equipment, net		$ 48,169,976	$ (3,698,866)	$ (492,803)	$ 43,978,307

(5) Capitalized Interest

Interest is capitalized on all construction-in-progress pursuant to ASC 835-20, *Capitalization of Interest*, provided that the construction period exceeds one year. Interest capitalized on qualifying construction-in-progress was $69,919 and $0 during the years ended September 30, 2014 and 2013, respectively.

(6) Indefeasible Right of Use (IRU)

On January 12, 2009, the Corporation entered into an IRU Capital Lease agreement with a third party for the exclusive use of 8 wave lengths of fiber capacity of the two fibers of the Kwajalein Cable System (KCS) which runs between Guam and Kwajalein and which is known as the “HANTRU1 System”. Under the terms of the agreement, the Corporation made certain payments of $3,656,301. The initial term of the agreement is for a period of 10 years commencing on the date the Corporation is initially granted access, and which term is automatically renewable for a further 10 year period and an additional 5 year period thereafter. Prior to the tenth and twentieth anniversary dates, the Corporation has the option to terminate this agreement; however, such is subject to prior approval of the Rural Utilities Services (RUS) of the U.S. Department of Agriculture. The Corporation’s policy is to amortize the right of use over the 25 year period. As of September 30, 2014 and 2013, accumulated amortization expense of $658,134 and $511,882, respectively, has been recorded.

(7) Long-term Debt

	2014	2013
Loans payable to RUS, with a 35 year term, interest at 5% per annum, collateralized by the Corporation's specific ground leases and essentially all other assets. Pursuant to loan agreements dated August 1, 1990 and March 12, 2009, the Corporation is required to make monthly payments of both principal and interest to RUS. The loans were originally in the amounts of $32,000,000 and $12,136,000 and the proceeds were used for capital related purposes.	$ 27,380,302	$ 28,986,305

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

Year ending September 30,	Principal	Interest	Total
2015	$ 1,667,941	$ 1,332,136	$ 3,000,077
2016	1,752,305	1,247,772	3,000,077
2017	1,843,782	1,156,295	3,000,077
2018	1,937,258	1,062,819	3,000,077
2019	2,036,372	963,705	3,000,077
2020 - 2024	11,854,850	3,145,533	15,000,383
2025 - 2027	6,287,794	370,600	6,658,394
	$ 27,380,302	$ 9,278,860	$ 36,659,162

These notes are subject to certain coverage ratio requirements. The Corporation is not in compliance with its ratio requirements as of September 30, 2014. Management is of the opinion that the lender is aware of this matter and will not call the debt. Therefore, the debt is classified per the expected future payouts.

A summary of changes in long-term debt for the years ended September 30, 2014 and 2013 are as follows:

	Balance October 1, 2013	Increases	Decreases	Balance September 30, 2013	Due Within One Year
Notes payable:					
Rural Utilities Service	$ 28,986,305	$ -	$ (1,606,003)	$ 27,380,302	$ 1,667,941

	Balance October 1, 2012	Increases	Decreases	Balance September 30, 2013	Due Within One Year
Notes payable:					
Rural Utilities Service	$ 30,497,706	$ -	$ (1,511,401)	$ 28,986,305	$ 1,586,759

(8) Commitments and Contingencies

Leases

The Corporation has fourteen operating leases as of September 30, 2014. Five are residential real estate leases for contract employees, which have a term of one or two years. Three are for land sites for state offices with 25-35 year terms beginning in 1988 for Pohnpei and Yap and 1990 for Kosrae. There is one land site lease for the southeast remote switch on Pohnpei with 15-year term beginning in 1994. The Corporation has also entered into various circuit leases expiring through 2016.

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

Year ending September 30;	Total
2015	1,295,949
2016	30,407
2017	9,816
2018	8,101
2019	5,252
2020 - 2024	17,640
2025	1,764
	$ 1,368,929

Operation, Management and Repair (OM&R) Agreement

On March 2, 2009, the Corporation, along with the Marshall Islands National Telecommunications Authority (MINTA), entered into an OM&R agreement with a third party for the purpose of operating, maintaining, and repairing the “Micronesian Addition”, which is a subset of the HANTRU1 System. The term of the agreement coincides with the term of the IRU Capital Lease agreement wherein the Corporation and MINTA are required to each make monthly payments of $6,400 less certain service credits, and which are subject to inflationary adjustments and an annual incremental increase of 3%.

Self Insurance

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

(8) Commitments and Contingencies, Continued

Construction and Other Commitments

During the year ended September 30, 2014, the Corporation entered into various contracts for construction and expansion of its facilities and services. Approximately $3,259,146 is outstanding under these contracts as of September 30, 2014.

The Corporation entered into a $4 million contract with Acclinks Communications, Inc. for a Third Generation (3G) Mobile Network Partnership Agreement signed on September 12, 2013. As of September 30, 2014, the Corporation recognized $2,800,000 as a contract liability that will be paid through revenue sharing as agreed per payment terms. No amount has yet been paid as the project has not been completed as of September 30, 2014. A total of $149,940 has been billed to the Corporation for 3G network services as of September 30, 2014. Management is of the opinion that the billed amount is not payable as the service has yet to be implemented.

As summary of changes in other long-term liabilities for the year ended September 30, 2014 is as follows:

	Balance October 1, 2013	Increases	Decreases	Balance September 30, 2014	Due Within One Year
Contract liability	$ -	$4,000,000	$ (1,200,000)	$ 2,800,000	$ 899,642

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

Year ending September 30;	Total
2015	$ 899,642
2016	701,283
2017	502,924
2018	502,924
2019	193,227
	$ 2,800,000

External Carriers

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

Litigation

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

(9) Related Party Transactions

The Corporation's services are provided to its affiliates at the same rates as are charged to third parties. The Corporation is a component unit of the FSM National Government. As of September 30, 2014 and 2013, receivables from the FSM National Government amounted to $55,528 and $33,439, respectively.

During the year ended September 30, 2014, the Corporation received a $1,393,558 subsidy from the FSM National Government for the purposes of financing Third Generation (3G) upgrade and O3B Network projects.

(10) Retirement Plan

The Corporation's retirement plan (the Plan) is a self-administered program established to pay retirement, disability and survivor income to employees and their survivors to supplement similar benefits that employees received from the FSM Social Security System. The Plan is a contributory plan in which the Corporation contributes 10 percent of the participant's annual salary, and the participant contributes 3 or more percent from his or her annual salary. Participation is optional. The Corporation's controller is the designated Plan administrator. Contributions to the Plan during the years ended September 30, 2014 and 2013 were $351,238 and $377,768, respectively. Management is of the opinion that the plan does not represent an asset or liability of the Corporation. At September 30, 2014 and 2013, plan assets were $4,621,148 and $4,463,870, respectively.

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

Schedule of Operating Expenses
Years Ended September 30, 2014 and 2013

	2014	2013
Depreciation and amortization	$ 4,515,968	$ 4,812,965
Salaries and wages	3,470,296	3,616,549
Circuit lease	2,226,881	2,107,537
Utilities	1,338,142	1,378,967
Repairs and maintenance	634,228	628,424
Cost of sales	465,117	328,254
Taxes	359,546	362,164
Travel	329,421	261,634
Petroleum and lubricants	186,683	157,641
Rental expenses	149,076	138,025
Contractual services	132,580	144,411
Communications	131,790	121,390
ICTV affiliated	116,429	127,773
Supplies	101,916	130,738
Professional fees	93,973	45,546
Insurance	70,595	79,239
Freight	27,653	44,906
Publications and printing	26,986	26,430
Representation	25,108	19,104
Land lease	23,617	32,132
Advertising	22,532	12,875
Training	15,351	12,055
Miscellaneous	110,754	106,547
	$ 14,574,642	$ 14,695,306

See Accompanying Independent Auditors' Report.

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

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2014

U.S. Department of Agriculture

Rural Utilities Service Loan Funding:

Approved Purposes	Loan Proceeds Approved as of September 30, 2014	Loan Proceeds Received During FY 2014	Total Disbursements on Contracts During FY 2014
F/A 1	$ 411,584	$ -	$ -
Work Orders	422,905	-	-
CT. A-4	90,688	-	-
CT. A-5	1,191,004	-	-
CT. A-6	650,676	-	-
CT. A-7	3,108,615	-	-
CT. A-8	3,500,000	-	-
CT. A-9	1,108,149	-	-
CT. A-10	636,505	-	-
CT. A-11	1,193,317	-	-
CT. A-12	1,422,800	-	-
CT. A-13	19,440,795	-	-
CT. A-14X	1,988,002	-	-
CT. B-15	8,206,857	-	-
CT. B-16E	274,500	-	-
CT. A-1E	275,625		
CT. A-2E	4,008,263	-	-
CT. A-3A	304,109	-	-
Operating Equipment	387,263	-	-
Pre-Loan	55,000	-	-
IRU Capital Lease	3,656,301	-	-
Interest Income	-	-	-
	$ 52,332,958	$ -	$ -

See Accompanying Independent Auditors' Report.

Deloitte.

Deloitte & Touche LLP
361 South Marine Corps Drive
Tamuning, GU 96913-3911
USA
Tel: (671)646-3884
Fax: (671)649-4932
www.deloitte.com

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

Board of Directors
Federated States of Micronesia
Telecommunications Corporation:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Federated States of Micronesia (FSM) Telecommunications Corporation (the Corporation), which comprise the statement of net position as of September 30, 2014 and the related statements of revenues, expenses, and changes in net position and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 30, 2014.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Corporation's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as item 2014-001.

The Corporation's Response to Findings

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

Purpose of this Report

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

Deloitte + Touche LLP

December 30, 2014

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION

Schedule of Findings and Responses
Year Ended September 30, 2014

Loan Noncompliance

Finding No. 2014-001

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

Condition: Per examination of RUS Form 479 ending December 31, 2013, submitted by the Corporation on February 11, 2014, the TIER rate reported was -0.41, which is less than the criteria.

Cause: The cause of the above condition is net losses incurred as of December 31, 2013, the RUS loan reporting period, which resulted in a negative TIER rate.

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

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

Recommendation: We recommend compliance with the criteria.

Auditee Response and Corrective Action Plan: Management is fully aware of the situation as to non-compliance with the TIER required by RUS, due to the fact that the Corporation has suffered continuous losses since 2007. For FY2014, FSMTC received a $1.3 million subsidy from the FSM National Government which had brought down the losses to $800k. Management will continue to request for subsidy for additional capital funding and operations.

We have continued to request RUS for a loan payment break and utilize the fund for other projects that could contribute to the increase in revenue. We had completed the upgrade on cellular infrastructure to expand data thru 3G technology which is currently one of the hottest products in telecommunications industry. The board of directors is challenging management to come up with a marketing plan making sure that the projected revenue for FY2015 is achieved. Management is optimistic that with this new service plus the marketing plan RUS TIER requirement will be achieved.

FEDERATED STATES OF MICRONESIA
TELECOMMUNICATIONS CORPORATION

Unresolved Prior Year Findings
Year Ended September 30, 2014

The status of unresolved prior year findings is disclosed within the Schedule of Findings and Responses section of this report.