2009 Annual Report

Federated States of Micronesia Development Bank

Table of Contents

LETTERS TO SHAREHOLDERS

Dear Shareholders,

On behalf of the Board of Directors, we are very pleased to submit the annual report for the year ended December 31, 2009 and the audited financial statements of the FSM Development Bank for the years ended December 31, 2009 and 2008.

2009 was a very busy and productive year. A net profit of $ 2.6 million was earned, which was attributed largely to the successful launch of the new line of credit program and also the recovery in the investment market. Total revenue and expenses were $4.4 million and $1.8 million, respectively. Furthermore, $ 2.2 million in loan interest income was generated and covered the operating expenses in full. Total assets were $37 million, an increase of 8% from $34 million at the end of 2008. A total of 61 new loans were approved for $10.7 million compared to last year's approval of 52 loans with a total value of $4.6 million. About $3.2 million of loans were undisbursed at the end of the year.

With the new line of credit program, and through innovative team efforts, we will continue to maintain our commitment and focus on our primary mandate to actively promote the growth of micro, small and medium enterprises in the FSM.

In general, we anticipate 2010 another good year with potentials to further improving our performance upon 2009 good results. We foresee an increase in lending activities particularly in the construction and mining sector. Potential lending activities might also come from support services and government businesses that are involved in the infrastructure projects that are funded from the Compact. Tourism is likely to improve after the completion of the Pohnpei runway project. Furthermore, real estate sector might also improve due to these compact funded projects and the continued presence of some international and regional organizations in Pohnpei.

In closing, we wish to acknowledge and extend our sincere gratitude and appreciation for the continued support and confidence in the FSMD. We further extend the same to our esteemed colleagues, members of the Board of Directors, for their unwavering commitments and valuable insights that they have contributed throughout the years toward the betterment of this institution. We wish to also thank our employees for their hard work and their firm commitments to put our words into actions. And finally, we thank our customers for their continued loyalty and confidence in the FSMDB. We thank you for giving us the opportunity to serve you. It is our hope that you will continue to allow us to serve you while extending the opportunities to other aspiring entrepreneurs. As always, we shall remain "Your Partner in Business."

Sincerely,

Anna Mendiola, President/CEO

Ihlen Joseph, Chairman of the Board

PART I: BACKGROUND INFORMATION

About The Bank

The Federated States of Micronesia Development Bank (FSMDB) is a component unit of the National Government of the Federated States of Micronesia (FSM). It was chartered in 1979 by the First Congress of the FSM through Public Law 1-37. The bank opened in 1980 but lending did not start until 1982. In 1994, the enabling law that created the bank was amended to reorganize the structure of the bank to reflect that of a normal corporation.

The primary function of FSMDB is to provide financing to commercial businesses mainly in the FSM. Over the years, the bank has added new lending programs to meet its strategic objectives and customer needs. In 2008, the bank created its residential home loan program to help locals build their homes.

The Bank Headquarters is located in the State of Pohnpei, the capital of the FSM. It has four branch offices in all the four (4) FSM states, Chuuk, Kosrae, Pohnpei and Yap.

Vision and Mission

Vision:

The FSM DEVELOPMENT BANK is a key player in the development of the private sector in the Federated States of Micronesia that enjoys the confidence of the national and state leaders, its customers, regulators and stakeholders. FSMDB services and performance are comparable to the best-managed development financial institutions in the Pacific region.

Mission:

FSM Development Bank actively promotes the growth of micro, small and medium enterprises in the Federates States of Micronesia and supports programs designed to help business achieve greater efficiency in their operations.

The policies of the FSMDB are constantly aligned with the overall socio-economic goals of the nation and it continues to coordinate closely with the governments and community leaders in defining its strategic directions.

FSMDB processes are designed to deliver efficient and timely services to its customers, and ensure effective exchange of information at all levels of the organization.

The FSMDB organization is characterized by a high level of teamwork and morale. FSMDB supports its people with appropriate equipment and technology, ensures that its compensation and reward program are competitive within the industry, and implements a conscious program for the continuous professional growth and personal development of its people.

FSMDB maintain a consistently healthy and growing financial portfolio and continues to earn the respect and support of the general public, the various governments, donor agencies and the international financial community.

Shareholders

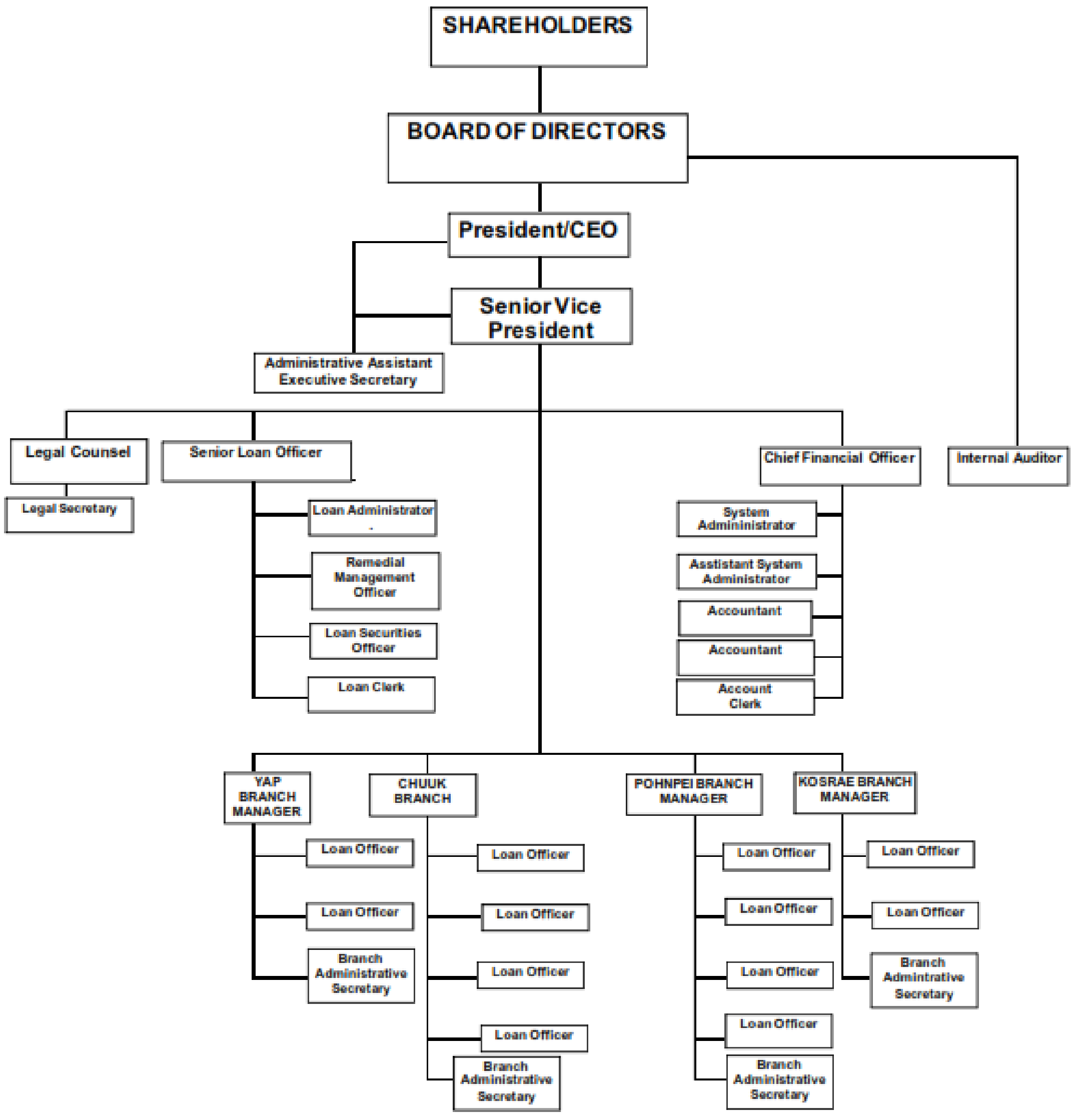
The FSM National Government is the principal shareholder of the bank. It owns 98.7% of the outstanding shares. The States of Chuuk and Kosrae each own 1.0% and 0.3% of the bank's outstanding shares respectively. The States of Pohnpei and Yap are not shareholders but they are given representation on the Bank's Board of Directors as a courtesy.

Shareholder	No. of Shares	Amount
FSM National Government	2,997,883.00	$14,989,415
State of Kosrae	9,000.00	$45,000
State of Chuuk	30,000.00	$150,000
Total Shares Outstanding	3,036,883.00	$15,184,415

The Bank's fiscal year runs on a calendar year basis. The shareholder meets annually normally during the second Quarter of the Bank's fiscal year.

Organizational Chart

The bank organizational chart is illustrated below:



Board of Directors

The board is comprised of seven members. Six of them are elected by the shareholders. The seventh member is the President and Chief Executive Officer (CEO), who serves as the Ex-Officio to the board. Aside from the Ex-Officio, all board members serve a term of 3 years on a staggering basis. The composition and representation of the board as of December 31, 2009 were as follows:

Name	*Position*	*Representation*
Ihlen Joseph	Chairman	FSM National Government
Hilary Tacheliol	Vice Chairman	Yap State
Ramon Falcam	Member	FSM National Government
John Sohl	Member	Pohnpei State
Wilson Waguk	Member	Kosrae State
Sisinio Willy	Member	Chuuk State
Anna Mendiola	Ex-Officio	President/CEO FSMDB

Management

The bank is managed by a management team comprised of a President/Chief Executive Officer (CEO), a Senior Vice President/Chief Operating Officer (COO), Chief Financial Officer (CFO) and a Senior Loan Officer (SLO). The composition of the Senior Management of the Bank as of December 31, 2009 was as follows:

Name	*Position*	*E-mail*
Anna Mendiola	President/CEO	annam@fsmdb.fm
Stevenson Joseph	Senior Vice President/COO	stevej@fsmdb.fm
Sihna Lawrence	Chief Financial Officer	sihnal@fsmdb.fm
Peter Aldis	Senior Loan Officer	petera@fsmdb.fm

PART 2: MANAGEMENT REPORT

Lending Activity

The Bank has approved 61 loans worth $10.7 million as of December 31, 2009. See below for details:

Table 1: 2012 Loans Approved by Sector

Sector	**No.**	**Value in $**
Agr/Fish/Forest	8	$ 3,037,616.00
Services	11	$ 2,442,792.00
Manufacturing	5	$ 138,295.00
Real Estate	4	$ 429,953.00
Wholesales/Retail	15	$ 2,413,792.00
Tourism	1	$ 700,000.00
Transportation	3	$ 282,944.00
Cons/Mining	3	$ 750,000.00
Home Loan	11	$ 481,606.00
Totals	61	$ 10,676,998.00

Figure 1:2009 Loans Approved by Sector

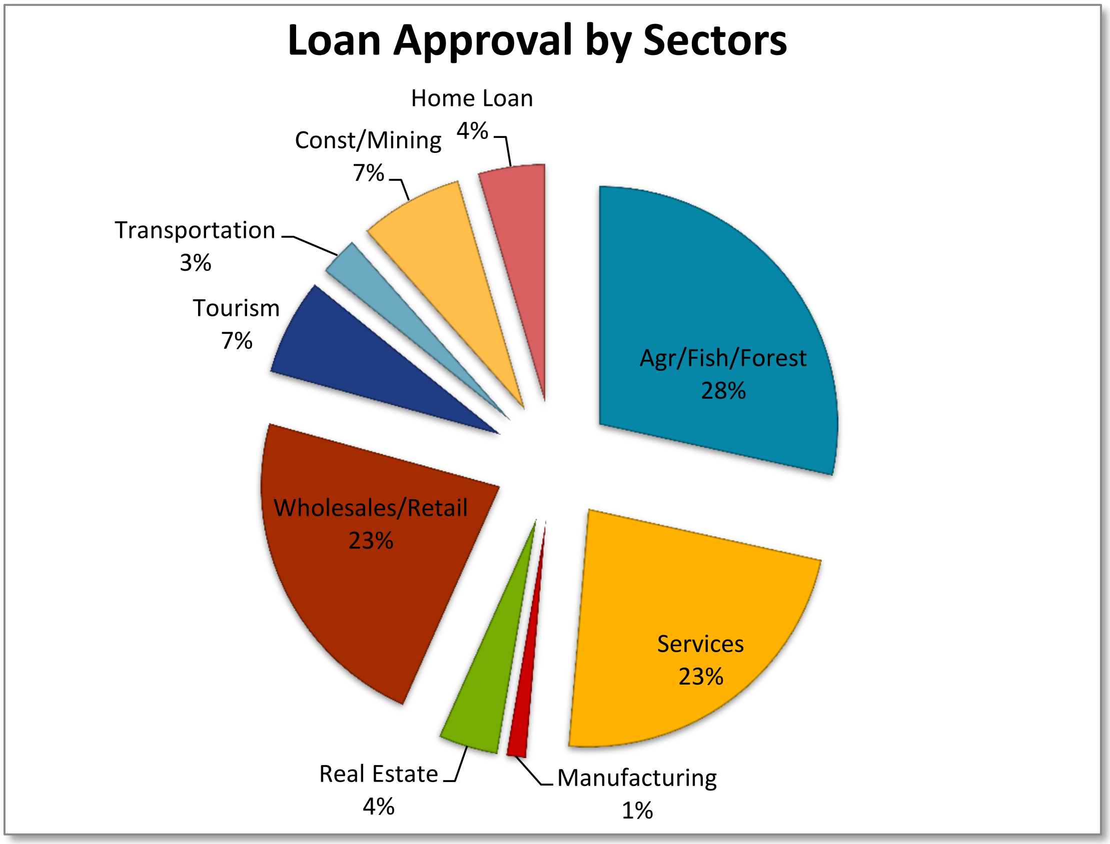
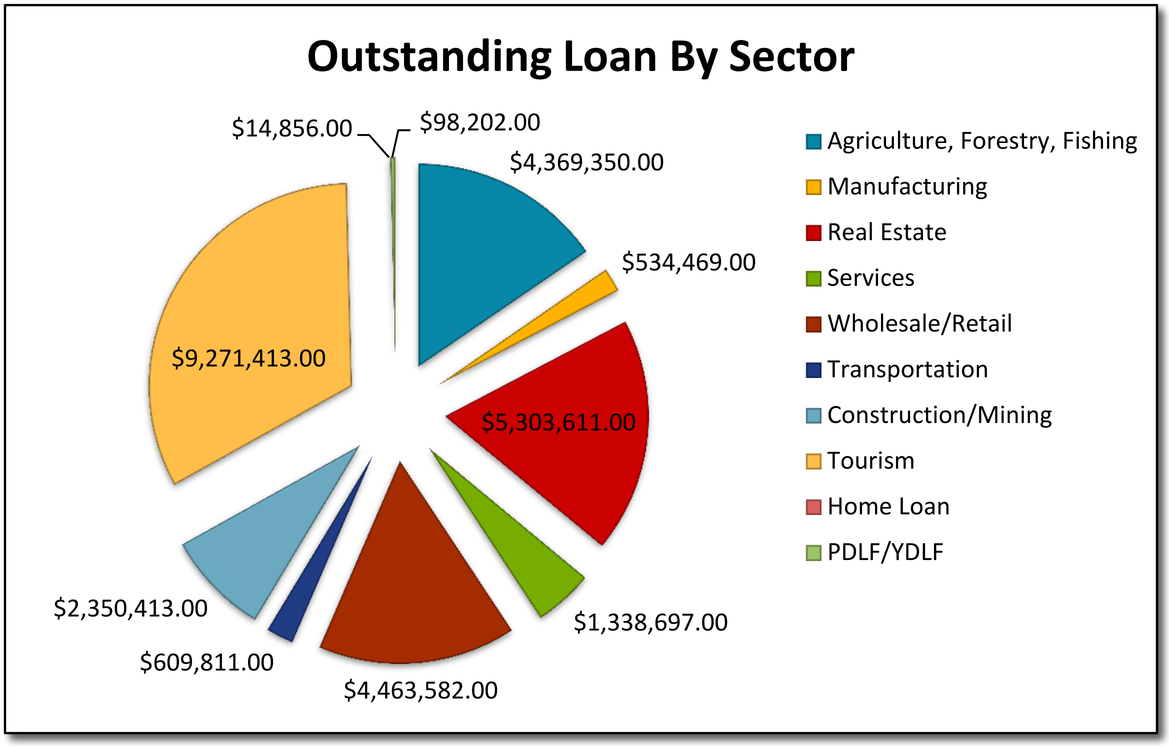


Table 2: Active Loans Outstanding (gross) as of December 31, 2009

SECTORS	***No***	***Original Loan***	***Out. Balance***	***% of Total***
Agriculture, Forestry, Fishing	21	$ 6,126,296.00	$ 4,369,350.00	15%
Manufacturing	22	$ 908,143.00	$ 534,469.00	2%
Real Estate	29	$ 5,988,854.00	$ 5,303,611.00	19%
Services	43	$ 2,366,711.00	$ 1,338,697.00	5%
Wholesale/Retail	80	$ 6,368,159.00	$ 4,463,582.00	16%
Transportation	11	$ 1,060,443.00	$ 609,811.00	2%
Construction/Mining	16	$ 2,593,093.00	$ 2,350,413.00	8%
Tourism	16	$ 10,003,812.00	$ 9,271,413.00	33%
Home Loan	1	$ 15,401.00	$ 14,856.00	0%
PDLF/YDLF	6	$ 229,695.00	$ 98,202.00	0%
Total	245	$ 35,660,607.00	$ 28,354,404.00	100%

Figure 2: Outstanding Loans by Sector as of December 31, 2009



At the end of 2009, Tourisms sector (33%) remains the largest portion of the outstanding loan portfolio. In terms of the number of loan, however, wholesale/retail loan have the most loans outstanding with a total of 80 loans followed by services sector (43) and real estate (29).

Figure 3: Loan Approval Trend 2005-2009

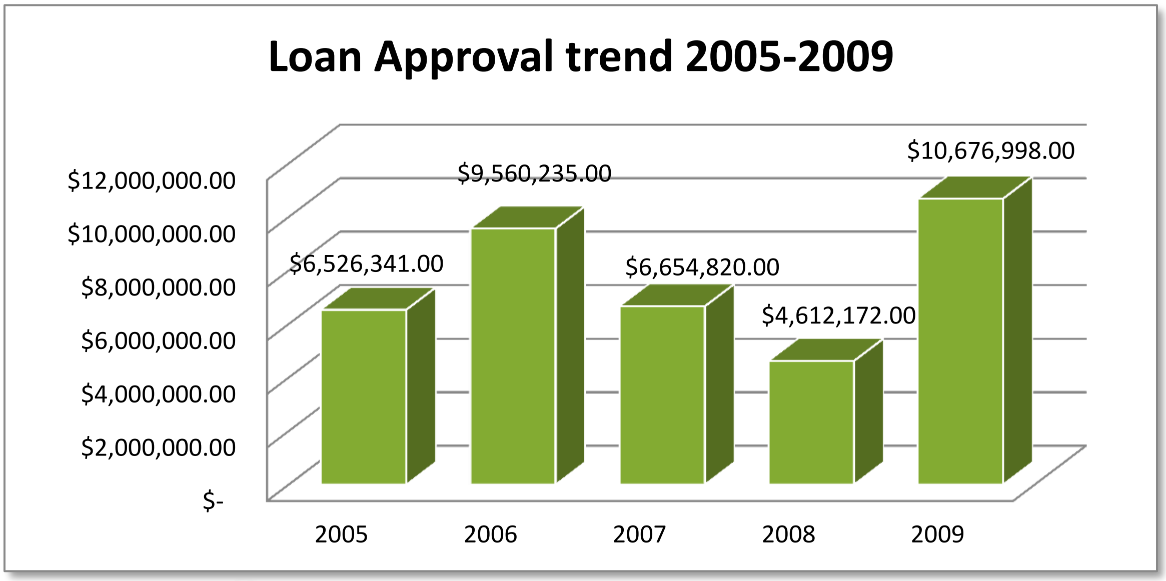
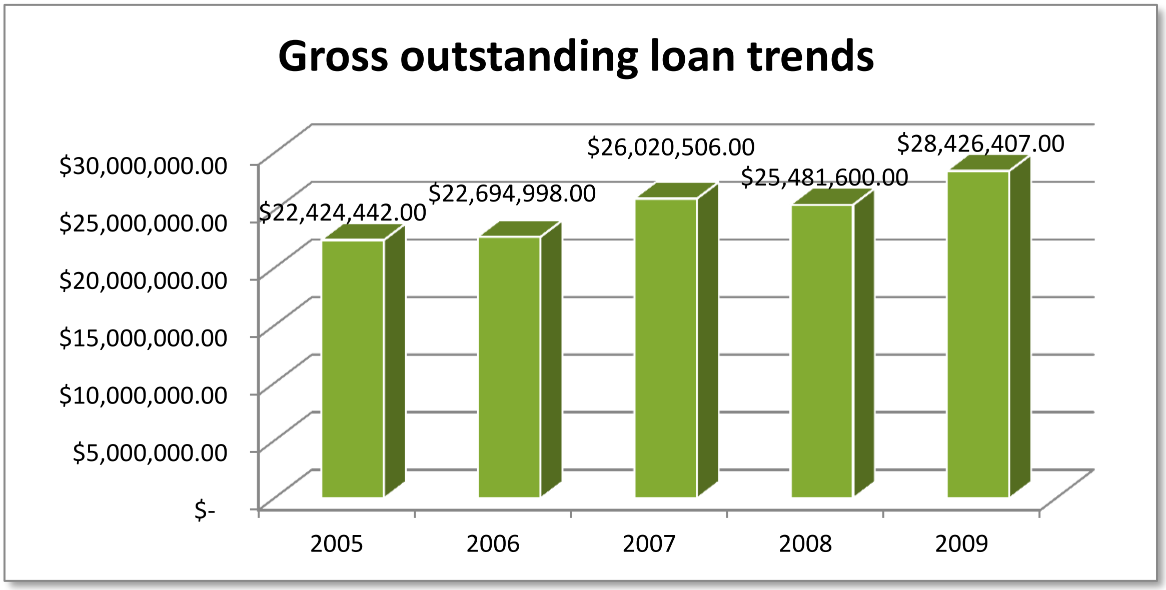


Figure 4: Gross Loan Outstanding Trend 2005-2009



Funding Source Update

Capital contribution from our principal shareholder, the FSM National Government, has not been forthcoming for the last four years of operations as it used to be in the earlier years of the bank's existence. We now rely on loan interests and other sources to fund our lending activities. As of this year, the bank has:

- Fully drawn and on-lent the $2 million loan from the China Export and Import Bank. This source has funded a total of 27 projects.
- Entered into a loan agreement with the USDA Rural Economic Development Service for $466K.
- Obtained a $5 million line of credit from the European Investment Bank (EIB).

Administered Funds Update

We manage three non-propriety type funds: 1) the Investment Development Fund (IDF), 2) the Pohnpei Development Loan Fund (PDLF) and 3) the Yap Development Loan Fund (YDLF). The detail and the current status of these funds can be found in the financial section of the report.

Loans to Women Update

We approved a total of twenty one (21) loans to women as the primary borrower as of December 31, 2009 with a combined total of $ 1,456,291.

Personnel Update

As of December 31, 2009 the bank has 35 employees. During the year, there were four newly recruited employees joining the bank. They are:

1. Masashi Mori, Loan Officer at Chuuk Branch
2. Michael Henry, Internal Auditor/Compliance Officer at Headquarters

3. Dorian Kiyoshi, Executive Secretary at Headquarters
4. Katherine Gisog, Loan Officer at Yap Branch

Training Update

Staff training focused primarily on the loan division staff. The following trainings took place in the year:

- All loan staff and officers were training on the Optimist Program by Justin Fuller. The program was also upgraded.
- Loan Officer Janet Sisam received one month OJT at the Corporate Office.
- All the Branch Managers attended the advance Development Banking training in Manila, Philippines for two weeks.

Associations and Memberships Update

The bank is an active member of the following professional and regional associations:

- Association of Developmental Financial Institutions Asia and Pacific (ADFIAP)
- Association of Developmental Financial Institutions of the Pacific (ADFIP)
- Asia Pacific Association of Fiduciary Studies (APAFS)
- Association of the Pacific Island Public Auditors (APIPA)
- Federated States of Micronesia Executive Insurance Board (FSMEIB)
- Microfinance Pasifika Network

Acknowledgments

We extend our sincere appreciation to the FSMDB stockholders for the continued support and confidence in us.

We thank our Board of Directors for the steadfast support of our plans, programs and initiatives. Amidst all the challenges in the operating environment, the steadying hand of the Board and its collective wisdom enabled us to stay the course with focus and persistence.

We thank the hardworking staff for their perseverance and patients and for their judicious implementation of their assigned tasks. Without them nothing would have happened.

Finally, we extend our appreciation and thanks to those we serve for the trust and confidence they have in us and for allowing the FSMDB the opportunity to serve and assist in their business ventures. We shall always remain your partner in business.

PART 3: FINANCIAL REPORT

Figure 5: Total Revenue 2005-2009

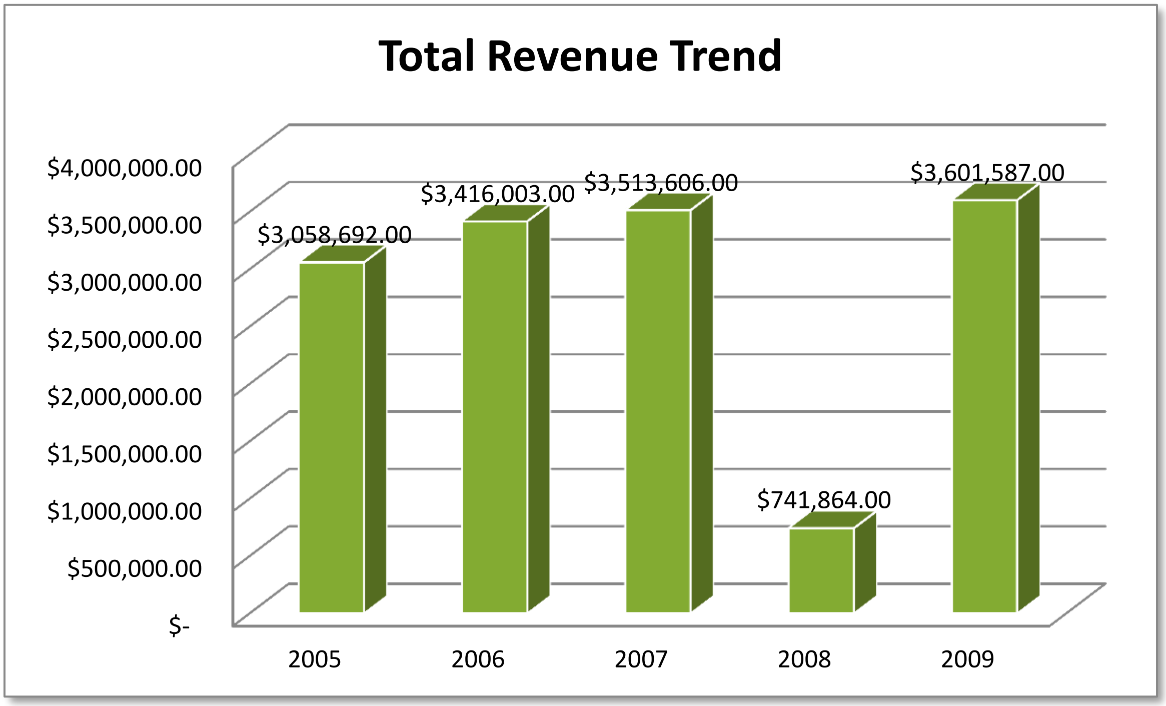


Figure 6: Total Expenditure 2005-2009

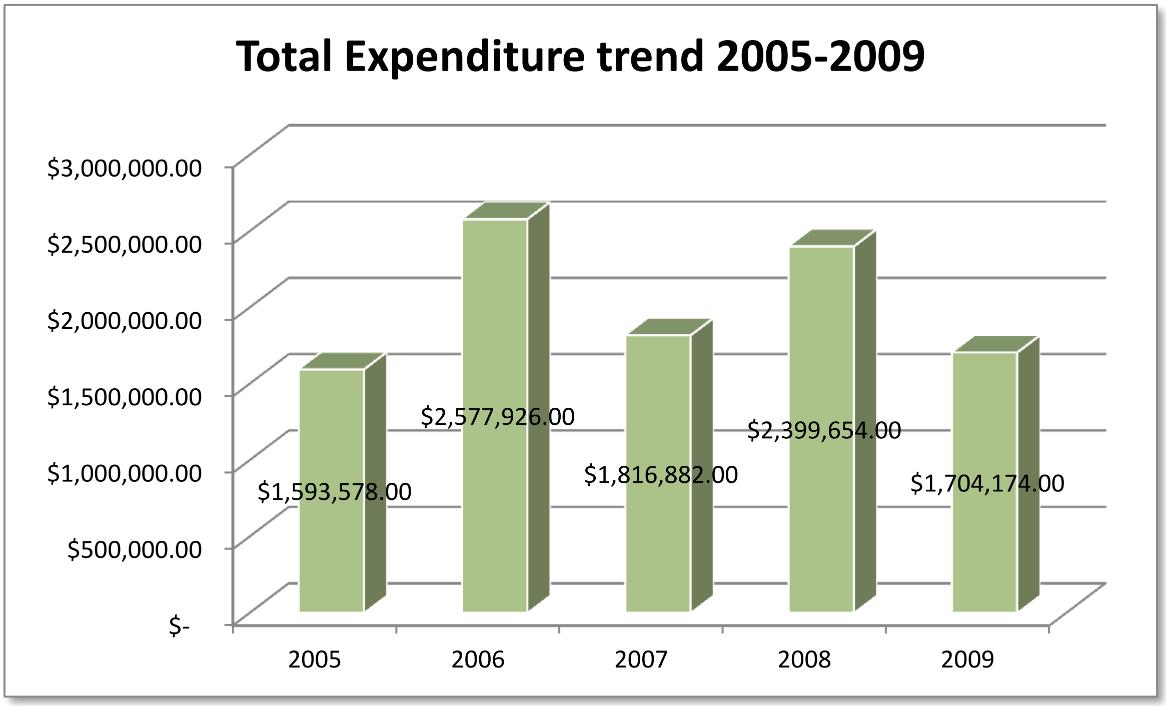


Figure 7: Net Profit Trend 2005-2009

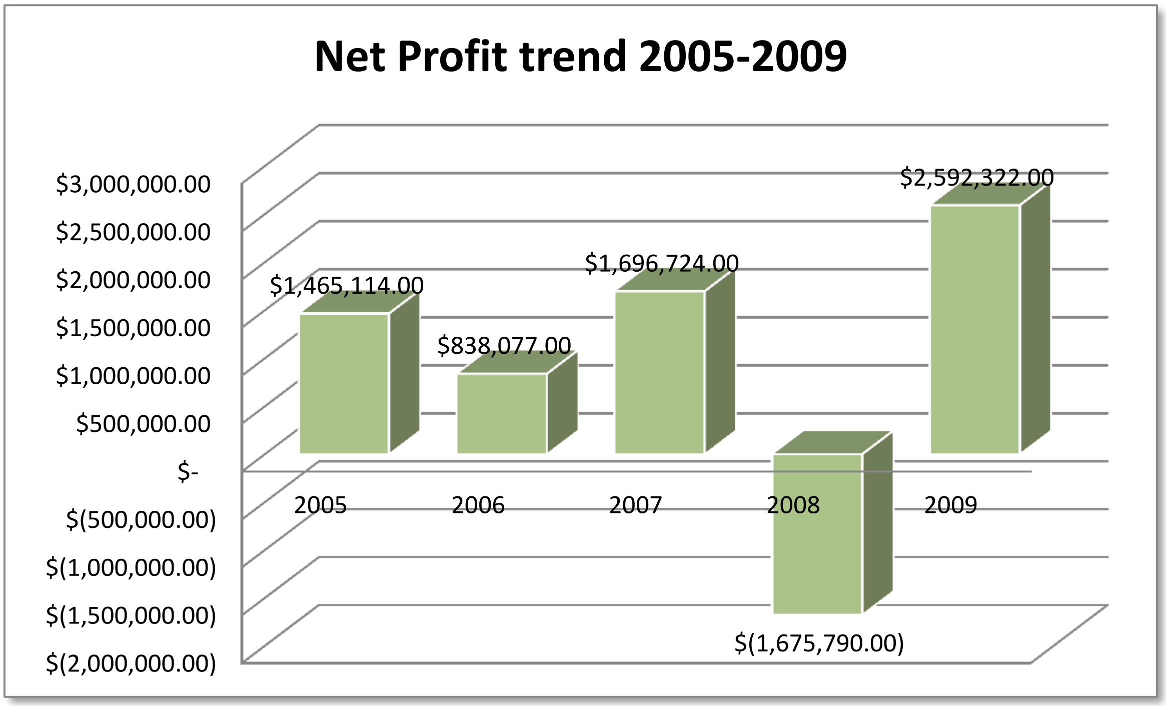
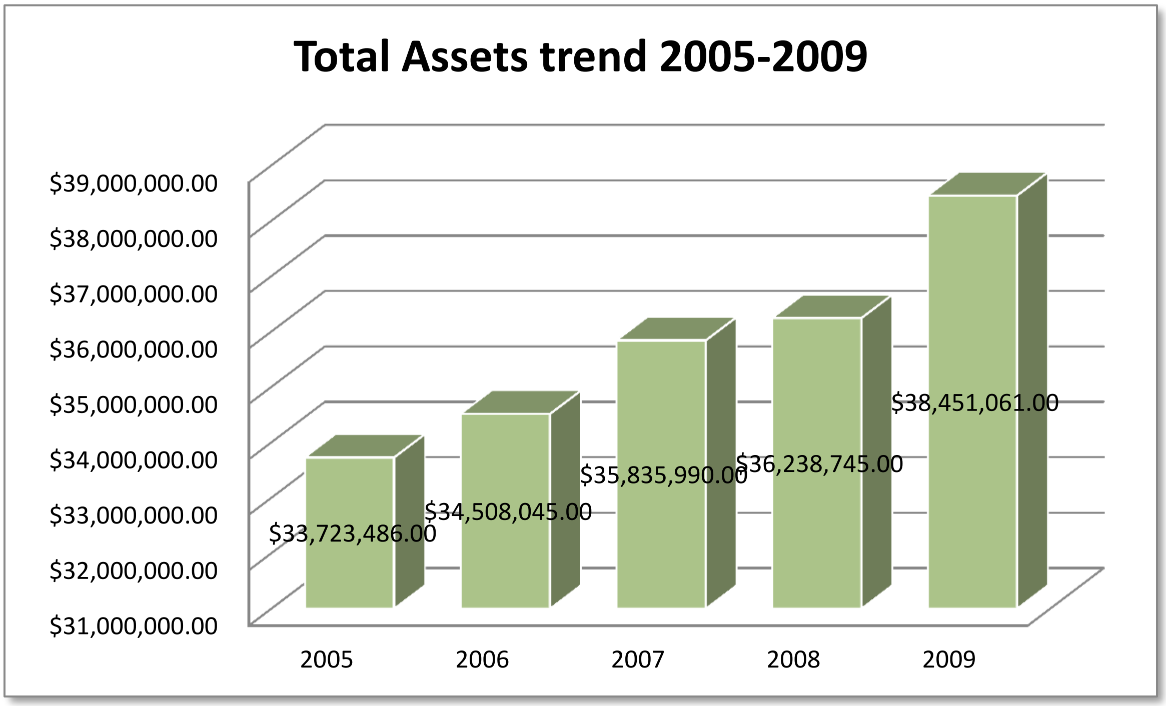


Figure 8: Total Asset Trend 2005-2009



Federated States of Micronesia
Development Bank

(A component Unit of the FSM National Government)

Financial Statements and Independent Auditors' Report

Years ended December 31, 2009 and 2008

Deloitte.

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INDEPENDENT AUDITORS' REPORT

Chairman
Board of Directors
Federated States of Micronesia
Development Bank:

We have audited the accompanying statements of net assets of the Federated States of Micronesia (FSM) Development Bank, a component unit of the FSM National Government, as of December 31, 2009 and 2008, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Federated States of Micronesia Development Bank as of December 31, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management Discussion and Analysis on pages 3-4 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Federated States of Micronesia Development Bank's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurements and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 30, 2010, on our consideration of the Bank'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.

Deloitte & Touche LLP

June 30, 2010

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

Statements of Net Assets
December 31, 2009 and 2008

	2009	2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 3,485,431	$ 3,425,012
Time certificates of deposit	1,906,333	891,275
Accounts receivable	11,034	6,593
Receivable from trust funds	358,844	225,017
Prepaid expenses	2,500	2,700
Interest and other receivables	160,323	244,252
Current portion of loans receivable	7,697,812	2,542,990
Total current assets	13,622,277	7,337,839
Noncurrent assets:		
Fixed assets, net	224,450	226,565
Investments	9,002,812	10,369,201
Equity investment, at cost	662,188	662,188
Loans receivable, net of current portion and allowance for loan losses	14,939,334	17,642,961
Total noncurrent assets	24,828,784	28,900,915
Total assets	$ 38,451,061	$ 36,238,754
LIABILITIES		
Current liabilities:		
Current portion of long-term debt	$ 400,000	$ 400,000
Accounts payable	129,902	111,049
Accrued interest payable	52,732	69,902
Credit life payable	8,322	10,425
Payable to trust funds	36,243	15,838
Total current liabilities	627,199	607,214
Noncurrent liabilities:		
Long-term debt, net of current portion	1,200,000	1,600,000
Total liabilities	1,827,199	2,207,214
Commitments and contingencies		
Net assets:		
Invested in capital assets	224,450	226,565
Unrestricted	36,399,412	33,804,975
Total net assets	36,623,862	34,031,540
Total liabilities and net assets	$ 38,451,061	$ 36,238,754

See accompanying notes to financial statements.

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

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended December 31, 2009 and 2008

	2009	2008
Operating revenues:		
Interest income on loans	$ 2,212,585	$ 2,130,965
Interest income on time certificates of deposit	44,982	49,572
Loan fees	190,949	71,057
Miscellaneous	51,491	81,632
Total operating revenues	2,500,007	2,333,226
Recovery of (provision for) loan losses	365,582	(722,000)
Net operating revenues	2,865,589	1,611,226
Operating expenses:		
Interest expense:		
Interest on long-term debt	120,090	103,349
General and administrative expenses:		
Personnel services	941,549	892,372
Rent	121,967	122,016
Contractual services	113,015	79,857
Depreciation	80,936	80,564
Travel	76,734	101,031
Training	60,501	15,354
FSM retirement plan	51,395	54,035
Communications	36,840	37,174
Supplies	18,601	14,606
Printing	6,730	7,639
Insurance	5,265	4,303
Miscellaneous expenses	190,641	165,357
Total general and administrative expenses	1,704,174	1,574,308
Earnings (loss) from operations	1,041,325	(66,431)
Non-operating revenues (expenses):		
IDF reimbursement	250,000	250,000
Allocations from managed funds	13,734	25,582
Investment earnings (loss)	1,286,632	(1,873,134)
Other income	631	6,190
Total non-operating revenues (expenses), net	1,550,997	(1,591,362)
Change in net assets	2,592,322	(1,657,793)
Net assets at beginning of year	34,031,540	35,689,333
Net assets at end of year	$ 36,623,862	$ 34,031,540

See accompanying notes to financial statements.

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

Statements of Cash Flows
Years Ended December 31, 2009 and 2008

	2009	2008
Cash flows from operating activities:		
Cash received from customers	$ 2,458,187	$ 2,210,570
Cash paid to suppliers for goods and services	(664,738)	(626,476)
Cash paid to employees for services	(941,549)	(892,372)
Interest received on time certificates of deposit	121,309	53,496
Interest paid	(137,261)	(33,447)
Net cash provided by operating activities	835,948	711,771
Cash flows from noncapital financing activities:		
Proceeds from issuance of long-term debt	-	2,000,000
Principal repayment of long-term debt	(400,000)	-
Net transfers in from (out to) trust funds	150,311	372,132
Net cash (used for) provided by noncapital financing activities	(249,689)	2,372,132
Cash flows from capital and related financing activities:		
Acquisition of fixed assets	(78,821)	(48,058)
Proceeds from sale of fixed assets	631	-
Net cash used for capital and related financing activities	(78,190)	(48,058)
Cash flows from investing activities:		
Loan origination and principal collections, net	(2,085,613)	27,435
Additions to time certificates of deposit, net	(1,015,058)	(591,275)
(Additions to) withdrawals from investments	2,600,000	(1,000,000)
Investment income received	106,290	61,474
Investment fees paid	(113,269)	(63,496)
Dividends received	60,000	65,000
Net cash used for investing activities	(447,650)	(1,500,862)
Net change in cash and cash equivalents	60,419	1,534,983
Cash and cash equivalents at beginning of year	3,425,012	1,890,029
Cash and cash equivalents at end of year	$ 3,485,431	$ 3,425,012
Reconciliation of earnings (loss) from operations to net cash provided by operating activities:		
Earnings (loss) from operations	$ 1,041,325	$ (66,431)
Adjustment to reconcile (loss) earnings from operations to net cash provided by operating activities:		
(Recovery of) provision for doubtful loans	(365,582)	722,000
Depreciation	80,936	80,564
(Increase) decrease in assets:		
Accounts receivable	(4,441)	(3,955)
Prepaid expenses	200	(200)
Interest and other receivables	83,929	(65,205)
Increase (decrease) in liabilities:		
Accounts payable	18,853	(27,062)
Accrued interest payable	(17,170)	69,902
Credit life payable	(2,102)	2,158
Net cash provided by operating activities	$ 835,948	$ 711,771

See accompanying notes to financial statements.

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

Notes to Financial Statements
December 31, 2009 and 2008

(1) Summary of Significant Accounting Policies

Reporting Entities

The Federated States of Micronesia Development Bank (the Bank) was created in 1979 by Public Law 1-37 of the First Congress of the Federated States of Micronesia. The FSM Development Bank began its operations on October 1, 1980. The Bank was reorganized in January 1994 by Public Law 8-47 of the Eighth Congress of the Federated States of Micronesia. The purpose of the FSM Development Bank is to provide loans for economic development of the FSM. Such loans may otherwise be too risky for commercial banks to underwrite. Additionally, the Bank's repayment terms tend to be longer than those offered by commercial banks. As of December 31, 2009, the Bank has issued 2,997,883 shares to the FSM National Government (98.7%), Kosrae State (0.3%) and Chuuk State (1.0%).

The Investment Development Fund (IDF) was established by Public Law 5-122 in January 1989. The purpose of the IDF is to finance projects which will (1) have their operations primarily located within the FSM; (2) improve the balance of payments position of the FSM; (3) increase the value of visible and invisible exports or result in import substitutions; (4) demonstrate positive economic returns; (5) contribute to the furtherance of close economic relations with the USA.

The Pohnpei Development Loan Fund (PDLF) and the Yap Development Loan Fund (YDLF) are administered by the Bank in a Trust capacity. All loan decisions are made by executives of the respective state governments.

The Bank is a component unit (a discretely presented proprietary fund type) of the FSM National Government. The financial statements in this report do not represent the financial position, results of operations or cash flows of the FSM National Government as a whole. The financial statements of the Bank are not obligations of the FSM National Government unless specifically authorized by the FSM National Government. To date, no such authorizations have been made.

The Bank has opted to establish itself more in line with a corporate model. The Bank, through this process, hopes to be able to attract additional capital through non-FSM sources. To that end, the Bank, in September 2007, entered into a line of credit agreement with Export and Import Bank of China for $2,000,000. As of December 31, 2009 and 2008, the amount outstanding and payable under this line was $1,600,000 and $2,000,000, respectively. Additionally, the Bank has entered into a memorandum of understanding with the U.S. Department of Agriculture's Office of Rural Economic and Community Development to provide guarantees for housing loans in the FSM. An escrow account amounting to $517,953 and $510,543, respectively, was established for the housing guarantee as of December 31, 2009 and 2008.

Fund Structure and Basis of Accounting

The accounts of the Bank are organized as a discretely presented component unit - proprietary fund of the FSM National Government. Proprietary funds are used by governmental units to account for operations that are financed and operated in a manner similar to a private business. This accounting is appropriate when costs of providing goods or services to the general public are to be financed primarily through user charges or where the periodic determination of net income is appropriate for accountability purposes. The accrual basis of accounting is utilized by proprietary funds. Under the accrual basis, revenues are recorded when earned, and expenses are recorded at the time the liabilities are incurred.

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

Notes to Financial Statements
December 31, 2009 and 2008

(1) Summary of Significant Accounting Policies

Fund Structure and Basis of Accounting, Continued

The accounts of the IDF, PDLF and YDLF are accounted for as fiduciary fund types as the amounts are to be reported on the respective entities' financial statements (the FSM National Government, Pohnpei State and Yap State, respectively).

The Bank utilizes the flow of economic resources measurement focus. Its financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to governmental units using the accrual basis of accounting. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. 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 Principle Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Bank has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

The Bank has adopted GASB Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments* (GASB 34) as amended by GASB Statement No. 37, *Basic Financial Statements – Management's Discussion and Analysis-for State and Local Governments: Omnibus* and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. GASB Statement No. 34 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 four net asset categories:

- Invested in capital assets, net of related debt:

  Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted:

  - Nonexpendable – Net assets subject to externally imposed stipulations that require the Bank to maintain them permanently. For the years ended December 31, 2009 and 2008, the Bank does not have nonexpendable restricted net assets.

  - Expendable – Net assets whose use by the Bank is subject to externally imposed stipulations that can be fulfilled by actions of the Bank pursuant to those stipulations or that expire by the passage of time.

- Unrestricted:

  Net assets that are not subject to externally imposed stipulations. Unrestricted net assets 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.

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

Notes to Financial Statements
December 31, 2009 and 2008

(1) Summary of Significant Accounting Policies, Continued

Fund Structure and Basis of Accounting, Continued

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. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Cash and Cash Equivalents

For the purposes of the statements of net assets and the statements of cash flows, cash and cash equivalents are defined as cash in bank checking and savings accounts, money market funds, and commercial paper with original maturities of three months or less from the date of acquisition.

Time certificates of deposit with original maturities of greater than three months are separately classified.

Investments

Investments and related investment earnings are recorded at fair value. 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 and is primarily determined based on quoted market values.

Loans and Allowance for Loan Losses

Loans receivable are stated at unpaid principal balance less the allowance for loan losses.

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

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

Fixed Assets

Fixed assets are stated at cost, less accumulated depreciation. Depreciation is based on the straight-line method over the estimated useful lives of the respective assets. All assets have estimated useful lives of three to five years.

The Bank's policy on fixed assets requires that assets with a purchase value of $5,000 and over are capitalized and depreciated based on its useful life. Assets with a purchase value less than $5,000 are expensed fully in the year of purchase.

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

Notes to Financial Statements
December 31, 2009 and 2008

(1) Summary of Significant Accounting Policies, Continued

Off-Balance Sheet Financial Instruments

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

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for loan losses.

Reclassifications

Certain reclassifications have been made to the 2008 financial statements in order to conform with the 2009 presentation.

New Accounting Standards

During fiscal year 2009, the Bank implemented the following pronouncements:

- GASB Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, which 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.

- GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which improves financial reporting by contributing to the GASB's efforts to codify all GAAP for state and local governments so that they derive from a single source.

- GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*, which incorporates accounting and financial reporting guidance previously only contained in the American Institute of Certified Public Accountants (AICPA) auditing literature into the GASB's accounting and financial reporting literature for state and local governments, and addresses three issues from the AICPA's literature - related party transactions, going concern considerations, and subsequent events.

- GASB Technical Bulletin No. 2008-1, *Determining the Annual Required Contribution Adjustment for Postemployment Benefits*, which clarifies the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, for calculating the annual required contribution (ARC) adjustment.

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

Notes to Financial Statements
December 31, 2009 and 2008

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

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

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, which 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 the Bank.

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which 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 the Bank.

In March 2009, GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The provisions of this statement are effective for periods beginning after June 15, 2010. Management has not evaluated the effect that the implementation of this statement will have on the financial statements of the Bank.

In December 2009, GASB issued Statement No. 57, *OPEB Measurements by Agent and Employers and Agent Multiple-Employer Plans*, and GASB Statement No. 58, *Accounting and Financial Reporting for Chapter 9 Bankruptcies*. GASB Statement No. 57 addresses issues related to the use of the alternative measurement method and the frequency and timing of measurements by employers that participate in agent multiple-employer other postemployment benefit plans. GASB Statement No. 58 establishes accounting and financial reporting guidance for governments that have petitioned for protection from creditors by filing for bankruptcy under Chapter 9 of the United States Bankruptcy Code. The provisions of these statements are effective for periods beginning after June 15, 2011 and June 15, 2009, respectively. Management does not believe that the implementation of these statements will have a material effect on the financial statements of the Bank.

(2) Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

The deposit and investment policies of the Bank are governed by its enabling legislation. The Board is required to engage one or more fund custodians to assume responsibility for the physical possession of the Bank's investments. Legally authorized investments are as follows:

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

Notes to Financial Statements
December 31, 2009 and 2008

(2) Deposits and Investments, Continued

(i) Government obligations - Obligations issued or guaranteed as to principal and interest by the National Government and/or State governments of the Federated States of Micronesia or by the Government of the United States, provided that the principal and interest on each obligation are payable in the currency of the United States.

(ii) Corporate obligations and mortgage-backed securities - Obligations of any public or private entity or corporation created or existing under the laws of the Federated States of Micronesia or of the United States or any state, territory or commonwealth thereof, or obligations of any other government or economic community which are payable in United States dollars, or other mortgage-backed securities provided that the obligation is an agency of the United States Government, the National Government of the Federated States of Micronesia, or is rated in one of the three highest categories by two nationally recognized rating agencies. No investment under this heading shall exceed ten percent of the market value of the investment fund or ten percent of the outstanding value of the issue at the time of purchase.

(iii) Preferred and common stocks - Shares of preferred or common stocks of any corporation created or existing under the laws of the Federated States of Micronesia or under the laws of the United States or any state, territory or commonwealth thereof provided that the purchase of such shares shall be considered reasonable and prudent by the Bank's investment advisor at the time of purchase, that not more than five percent of the market value of its investments shall be invested in the stock of any one corporation, and that not more than ten percent of the market value of its investments shall be invested in any one industry group.

(iv) Insurance company obligations - Contracts and agreements supplemental thereto providing for participation in one or more accounts of a life insurance company authorized to do business in the Federated States of Micronesia or in any state, territory or commonwealth of the United States provided that the total market value of these investments at no time shall exceed ten percent of all investments.

A. Deposits:

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1	Deposits that are federally insured or collateralized with securities held by the Bank or its agent in the Bank's name;
Category 2	Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the Bank's name; or
Category 3	Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in the Bank's name and non-collateralized deposits.

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

Notes to Financial Statements
December 31, 2009 and 2008

(2) Deposits and Investments, Continued

A. Deposits, Continued

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Bank's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Bank does not have a deposit policy for custodial credit risk.

As of December 31, 2009 and 2008, the carrying amount of the Bank's total cash and cash equivalents and time certificates of deposit was $5,391,764 and $4,316,287, respectively, and the corresponding bank balances were $5,412,386 and $4,411,458, respectively. Of the bank balance amounts, all are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of both December 31, 2009 and 2008, bank deposits in the amount of $500,000 were FDIC insured. The Bank 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. Management's confidence in the financial strength of their banking institutions was the basis of the decision to not require collateralization. No losses as a result of this practice were incurred for the years ended December 31, 2009 and 2008.

B. Investments:

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

Category 1 — Investments that are insured or registered, or securities held by the Bank or its agent in the Bank's name;

Category 2 — Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in the Bank's name; or

Category 3 — Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the Bank's name.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

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

Notes to Financial Statements
December 31, 2009 and 2008

(2) Deposits and Investments, Continued

B. Investments, Continued

As of December 31, 2009 and 2008, investments at fair value are as follows:

	2009	2008
Fixed income securities:		
Domestic fixed income	$ 3,019,931	$ 3,032,615
Other investments:		
Domestic equities	4,600,775	3,199,435
Money market funds	1,382,106	4,137,151
	$ 9,002,812	$ 10,369,201

As of December 31, 2009 and 2008, the Bank's fixed income securities had the following maturities:

2009	Less Than 1 Year	1 to 5 Years	6 to 10 Years	Greater Than 10 Years	Fair Value
U.S. Treasury obligations	$ 160,619	$ 1,257,781	$ 158,564	$ 73,369	$ 1,650,333
U.S. Government agency obligations	-	1,014,232	355,366	-	1,369,598
	$ 160,619	$ 2,272,013	$ 513,930	$ 73,369	$ 3,019,931

2008	Less Than 1 Year	1 to 5 Years	6 to 10 Years	Greater Than 10 Years	Fair Value
U.S. Treasury obligations	$ -	$ 1,058,189	$ 659,806	$ -	$ 1,717,995
U.S. Government agency obligations	945,651	216,962	152,007	-	1,314,620
	$ 945,651	$ 1,275,151	$ 811,813	$ -	$ 3,032,615

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

The Bank's exposure to credit risk at December 31, 2009 and 2008, was as follows:

2009	Total	Domestic	International
Moody's Rating – AAA	$ 3,019,931	$ 3,019,931	$ -
Total credit risk debt securities	$ 3,019,931	$ 3,019,931	$ -

2008	Total	Domestic	International
Moody's Rating – AAA	$ 3,032,615	$ 3,032,615	$ -
Total credit risk debt securities	$ 3,032,615	$ 3,032,615	$ -

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

Notes to Financial Statements
December 31, 2009 and 2008

(2) Deposits and Investments, Continued

B. Investments, Continued

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Bank will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Bank's investments are held and administered by trustees. Accordingly, these investments are exposed to custodial credit risk. Based on negotiated trust and custody contracts, all of these investments were held in the Bank's name by the Bank's custodial financial institutions at December 31, 2009 and 2008.

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 Bank. As of December 31, 2009, the Bank's investment in U.S. treasury notes and agency obligations of the Federal National Mortgage Association constituted 18% and 11%, respectively, of its total investments. As of December 31, 2008, the Bank's investment in agency obligations of the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association constituted 5% and 7%, respectively, of its total investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The Bank has a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

(3) Equity Investment, at Cost

The equity investment in Bank of the FSM, carried at cost, represents 100,000 common shares and approximately an 11% ownership interest. Since the book value of the shares exceeds the carrying value, management believes that the equity investment has not become impaired.

(4) Loans Receivable

A summary of loans receivable at December 31, 2009 and 2008 follows:

	2009	2008
Unpaid principal balance	$ 28,426,407	$ 25,481,600
Allowance for loan losses	(5,789,261)	(5,295,649)
	$ 22,637,146	$ 20,185,951

Movements in the allowance for loan losses during the years ended December 31, 2009 and 2008, are as follows:

	2009	2008
Balance at beginning of year	$ 5,295,649	$ 5,085,120
Other loan loss recoveries	(365,582)	-
Provision for loan losses	-	722,000
Loans charged off	-	(772,684)
Loan recoveries from previously charged off loans	610,094	261,213
Loan reactivations from previously charged off loans	249,100	-
Balance at end of year	$ 5,789,261	$ 5,295,649

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

Notes to Financial Statements
December 31, 2009 and 2008

(5) Fixed Assets

A summary of fixed assets as of December 31, 2009 and 2008, is as follows:

	Beginning Balance January 1, 2009	Additions	Deletions	Ending Balance December 31, 2009
Office furniture, fixtures and equipment	$ 150,964	$ -	$ -	$ 150,964
Home furniture, fixtures and equipment	13,123	-	-	13,123
Vehicles	232,104	-	-	232,104
Computers and software	520,637	78,821	-	599,458
	916,828	78,821	-	995,649
Less accumulated depreciation	(690,263)	(80,936)	-	(771,199)
Net fixed assets	$ 226,565	$ (2,115)	$ -	$ 224,450

	Beginning Balance January 1, 2008	Additions	Deletions	Ending Balance December 31, 2008
Office furniture, fixtures and equipment	$ 144,996	$ 5,968	$ -	$ 150,964
Home furniture, fixtures and equipment	13,123	-	-	13,123
Vehicles	232,104	-	-	232,104
Computers and software	478,547	42,090	-	520,637
	868,770	48,058	-	916,828
Less accumulated depreciation	(609,699)	(80,564)	-	(690,263)
Net fixed assets	$ 259,071	$ (32,506)	$ -	$ 226,565

(6) Related Party Transactions

As of December 31, 2009 and 2008, the Bank has direct loans with outstanding balances of $186,647 and $238,941, respectively, to employees of the Bank and project loans extended to businesses owned by or affiliated with employees of $2,424,869 and $2,625,840, respectively. These loans were made under similar terms and conditions as exist with other borrowers. Officers and Board members are not eligible to borrow from the Bank.

(7) Commitments and Contingencies

Guaranty

The Bank, from time-to-time, is contingently liable on loan guarantees ranging from 50% to 90% of the outstanding loan balances for commercial projects within the FSM. There were no outstanding guaranteed loan balances as of December 31, 2009 and 2008.

Loan Commitments

The Bank has entered into loan commitments for loans approved but undisbursed in the amount of $3,255,189 at December 31, 2009.

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

Notes to Financial Statements
December 31, 2009 and 2008

(7) Commitments and Contingencies, Continued

Litigation

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

Self Insurance

The FSM Development Bank carries insurance to cover its potential risks from vehicle usage. FSM Development Bank is substantially self-insured for all other risks. Management is of the opinion that no material losses have been sustained as a result of this practice.

Lease Commitments

The Bank has six operating leases as of December 31, 2009. Two are residential real estate leases for contract employees. Four leases are for the branch offices in each State (one with a lease term of two years, two for five years and one for fifteen years). All leases have an attached option allowing FSMDB to renew the lease upon expiration of the current term. It is likely that these options will be exercised by the Bank and the leases renewed. The approximate future minimum annual lease payments payable by the Bank, assuming all options are exercised, are as follows:

Fiscal year ending December 31,	Total
2010	$ 116,016
2011	116,016
2012	116,016
2013	116,016
2014	116,016
2015 – 2019	580,080
2020 – 2024	580,080
2025 – 2029	580,080
2030 – 2034	580,080
	$ 2,900,400

(8) Note Payable

On September 29, 2007, the Bank entered into a line of credit agreement with Export and Import Bank of China in the amount of $2,000,000, due July 21, 2013, for the purpose of funding its loan programs. The loan is uncollateralized, bears interest at 7.38% per annum. Repayment of principal and interest commenced January 21, 2008 in semi-annual installments of $200,000. As of December 31, 2009 and 2008, the amount outstanding and payable was $1,600,000 and $2,000,000, respectively.

The Bank has also entered into a $466,254 USDA RECD Intermediary Relending Program loan. Interest is at 1%, the term is for thirty years, and cash collateral of $500,000 is pledged. No drawdowns have occurred through December 31, 2009.

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

Notes to Financial Statements
December 31, 2009 and 2008

(8) Note Payable, Continued

Annual debt service requirements to maturity for principal and interest are as follows:

Year ending December 31,	Principal	Interest	Total
2010	$ 400,000	$ 110,700	$ 510,700
2011	400,000	81,180	481,180
2012	400,000	51,660	451,660
2013	400,000	22,140	422,140
	$ 1,600,000	$ 265,680	$ 1,865,680

Long-term debt changes during the years ended December 31, 2009 and 2008 are as follows:

	Balance January 1,	Additions	Reductions	Balance December 31,	Due Within One Year
2009:					
Loan payable	$ 2,000,000	$ -	$ (400,000)	$ 1,600,000	$ 400,000
	Balance January 1,	Additions	Reductions	Balance December 31,	Due Within One Year
2008:					
Loan payable	$ -	$ 2,000,000	$ -	$ 2,000,000	$ 400,000

(9) Contribution from the FSM National Government

The Bank was reimbursed for expenses incurred in administering the IDF program from the IDF Private Sub Account for $250,000 for each of the years ended December 31, 2009 and 2008.

(10) Retirement Plan

The Bank'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 receive from the FSM Social Security System. The Plan is a contributory plan in which the Bank matches 100% of the participants' contributions up to a maximum of 10 percent of the participant's annual salary, if the participant contributes 3 or more percent from his or her annual salary. Employee participation is optional. The Bank's CFO is the designated Plan Administrator. Matching contributions to the Plan during the years ended December 31, 2009, 2008, and 2007 were $51,395, $54,035, and $52,733, respectively. Management is of the opinion that the Plan does not represent an asset or a liability of the Bank.

(11) Staff Loan Revolving Fund

In July 2007, the Bank's Board of Directors approved the establishment of a Staff Loan Revolving Fund. In September 2007, a savings account was established for this purpose. As of December 31, 2009 and 2008, the account has a balance of $81,428 and $16,423, respectively.

TRUST FUNDS ADMINISTERED BY THE
FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

DECEMBER 31, 2009

Deloitte.

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INDEPENDENT AUDITORS' REPORT

Chairman
Board of Directors
Federated States of Micronesia
Development Bank:

We have audited the accompanying statement of fiduciary net assets of the Investment Development Fund (IDF), the Pohnpei Development Loan Fund (PDLF), and the Yap Development Loan Fund (YDLF) (the Funds) as of December 31, 2009, and the related statement of changes in fiduciary net assets for the year then ended. The Funds are administered by the Federated States of Micronesia Development Bank (FSMDB), a component unit of the National Government of the Federated States of Micronesia. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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 the Bank'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.

In our opinion, such financial statements present fairly, in all material respects, the respective financial status of the Investment Development Fund, the Pohnpei Development Loan Fund and the Yap Development Loan Fund at December 31, 2009, and the changes in their respective financial status for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have issued our report dated June 30, 2010, on our consideration of the Bank'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.

Deloitte & Touche LLP

June 30, 2010

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

Trust Funds
Statement of Fiduciary Net Assets
December 31, 2009

	IDF	PDLF	YDLF	Total
ASSETS				
Held by FSMDB:				
Cash in bank and on hand	$ -	$ 172,792	$ 25,810	$ 198,602
Time certificates of deposit	1,408,739	566,520	140,282	2,115,541
Held by trustee:				
Investments	2,478,665	-	-	2,478,665
Total cash and equivalents	3,887,404	739,312	166,092	4,792,808
Receivable from FSMDB	-	-	25,449	25,449
Interest and other receivables	25,207	7,355	852	33,414
Loans receivable, net	6,854,533	46,335	50,619	6,951,487
Total receivables	6,879,740	53,690	76,920	7,010,350
	$ 10,767,144	$ 793,002	$ 243,012	$ 11,803,158
LIABILITIES AND NET ASSETS				
Liabilities:				
Payable to FSMDB	$ 281,211	$ 66,840	$ -	$ 348,051
Commitments				
Net assets:				
Restricted	6,854,533	46,335	50,619	6,951,487
Unrestricted	3,631,400	679,827	192,393	4,503,620
Total net assets	10,485,933	726,162	243,012	11,455,107
	$ 10,767,144	$ 793,002	$ 243,012	$ 11,803,158

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF FSM NATIONAL GOVERNMENT)

Trust Funds
Statement of Changes in Fiduciary Net Assets
Year Ended December 31, 2009

	IDF	PDLF	YDLF	Total
Additions:				
Investment interest	$ 15,279	$ 12,275	$ 993	$ 28,547
Loan interest	144,072	4,447	4,898	153,417
Miscellaneous	2,069	59	435	2,563
Total additions	161,420	16,781	6,326	184,527
Deductions:				
Investment management fee	251,600	-	-	251,600
Loan receivable write-off	208,280	-	-	208,280
Transfers to FSMDB	-	10,534	3,200	13,734
Total deductions	459,880	10,534	3,200	473,614
Change in net assets	(298,460)	6,247	3,126	(289,087)
Net assets at beginning of year	10,784,393	719,915	239,886	11,744,194
Net assets at end of year	$ 10,485,933	$ 726,162	$ 243,012	$ 11,455,107

See accompanying notes to financial statements.

TRUST FUNDS ADMINISTERED BY THE
FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Notes to Financial Statements
December 31, 2009

(1) Purpose and Summary of Significant Accounting Policies

Purpose

The Investment Development Fund (IDF), the Pohnpei Development Loan Fund (PDLF), and the Yap Development Loan Fund (YDLF), are administered by the Federated States of Micronesia Development Bank (the Bank). The Bank utilizes the Funds to carry out its stated purpose of providing loans for the economic development of the FSM. The specific purpose of each fund is as follows:

IDF – IDF was created to finance projects which will (1) have their operations primarily located within the FSM; (2) improve the balance of payments position of the FSM; (3) increase the value of visible and invisible exports or result in import substitutions; (4) demonstrate positive economic returns; (5) contribute to the furtherance of close economic relations with the USA. The IDF is administered by the Bank in a Trust capacity.

The Pohnpei Development Loan Fund (PDLF) and the Yap Development Loan Fund (YDLF) are administered by the Bank in a Trust capacity. All loan decisions are made by executives of the respective state governments.

Fund Structure and Basis of Accounting

The accounts of the IDF, PDLF and YDLF are accounted for as fiduciary fund types as the amounts are to be reported on the respective entities' financial statements (the FSM National Government, Pohnpei State and Yap State, respectively).

Cash

For the purposes of the statement of fiduciary net assets, cash is defined as cash in bank checking and savings accounts, and commercial paper with original maturities of three months or less from the date of acquisition. Deposits maintained in time certificates of deposit with original maturity dates greater than three months are separately classified.

Investments

Investments and related investment earnings are recorded at fair value. 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 and is primarily determined based on quoted market values..

Loan and Allowance for Loan Losses

Loans under the trust funds are usually reported at gross unpaid principal balances, without an allowance for loan losses. The loans are reserved in net assets as restricted net assets. Loans are written off directly against income based on discussions with the owners of the managed funds. When the loans are recorded in the respective owner's financial statements, the owners of these funds will bear responsibility for establishing the related loan loss reserve.

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

TRUST FUNDS ADMINISTERED BY THE FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK (A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Notes to Financial Statements
December 31, 2009

(1) Purpose and 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 disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(2) Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

The deposit and investment policies of the Funds are governed by their enabling legislation. The Bank is required to engage one or more fund custodians to assume responsibility for the physical possession of the Funds' investments. Legally authorized investments are as follows:

(i) Government obligations - Obligations issued or guaranteed as to principal and interest by the National Government and/or State governments of the Federated States of Micronesia or by the Government of the United States, provided that the principal and interest on each obligation are payable in the currency of the United States.

(ii) Corporate obligations and mortgage-backed securities - Obligations of any public or private entity or corporation created or existing under the laws of the Federated States of Micronesia or of the United States or any state, territory or commonwealth thereof, or obligations of any other government or economic community which are payable in United States dollars, or other mortgage-backed securities provided that the obligation is an agency of the United States Government, the National Government of the Federated States of Micronesia, or is rated in one of the three highest categories by two nationally recognized rating agencies. No investment under this heading shall exceed ten percent of the market value of the Funds' investments or ten percent of the outstanding value of the issue at the time of purchase.

(iii) Preferred and common stocks - Shares of preferred or common stocks of any corporation created or existing under the laws of the Federated States of Micronesia or under the laws of the United States or any state, territory or commonwealth thereof provided that the purchase of such shares shall be considered reasonable and prudent by the Funds' investment advisor at the time of purchase, that not more than five percent of the market value of its investments shall be invested in the stock of any one corporation, and that not more than ten percent of the market value of its investments shall be invested in any one industry group.

TRUST FUNDS ADMINISTERED BY THE FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK (A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Notes to Financial Statements
December 31, 2009

(2) Deposits and Investments, Continued

(iv) Insurance company obligations - Contracts and agreements supplemental thereto providing for participation in one or more accounts of a life insurance company authorized to do business in the Federated States of Micronesia or in any state, territory or commonwealth of the United States provided that the total market value of these investments at no time shall exceed ten percent of all investments.

A. Deposits

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1 — Deposits that are federally insured or collateralized with securities held by the Funds or its agent in the Funds' name;

Category 2 — Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the Funds' name; or

Category 3 — Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in the Funds' name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Funds' deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Funds do not have a deposit policy for custodial credit risk.

As of December 31, 2009, the carrying amount of the Funds' total cash and time certificates of deposit was $2,314,143 and the corresponding bank balances approximated the same amount. All of the bank balances are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2009, bank deposits in the amount of $500,000 were FDIC insured. The Funds do not require collateralization of their cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk. Management's confidence in the financial strength of their banking institutions was the basis of the decision to not require collateralization. No losses as a result of this practice were incurred for the year ended December 31, 2009.

**TRUST FUNDS ADMINISTERED BY THE
FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)**

Notes to Financial Statements
December 31, 2009

(2) Deposits and Investments, Continued

B. Investments

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

Category 1 Investments that are insured or registered, or securities held by the Funds or its agent in the Funds' name;

Category 2 Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in the Funds' name; or

Category 3 Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the Funds' name.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

As of December 31, 2009, investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	$ 1,949,285
Other investments:	
Money market funds	529,380
	$ 2,478,665

As of December 31, 2009, the Funds' fixed income securities had the following maturities:

	Less Than 1 Year	1 to 5 Years	6 to 10 Years	Greater 10 Years	Fair Value
U.S. Government agency obligations	$1,949,285	$ -	$ -	$ -	$1,949,285

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

The Funds' exposure to credit risk at December 31, 2009, was as follows:

Moody's Rating	Total	Domestic	International
AAA	$ 1,949,285	$ 1,949,285	$ -
Total credit risk debt securities	$ 1,949,285	$ 1,949,285	$ -

**TRUST FUNDS ADMINISTERED BY THE
FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)**

Notes to Financial Statements
December 31, 2009

(2) Deposits and Investments, Continued

B. Investments, Continued

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Funds will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Funds' investments are held and administered by trustees. Accordingly, these investments are exposed to custodial credit risk. Based on negotiated trust and custody contracts, all of these investments were held in the Funds' name by the Funds' custodial financial institutions at December 31, 2009.

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 Bank. As of December 31, 2009, the Funds' investment in agency obligations of Federal Home Loan Mortgage Corporation and Federal Home Loan Bank constituted 58% and 20%, respectively, of its total investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The Funds do not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

(3) Loans Receivable

The following is a schedule of loans receivable as of December 31, 2009:

	Loan Balance	Allowance	Net
State Development Funds (Pohnpei and Yap)	$ 96,954	$ -	$ 96,954
IDF	6,874,033	19,500	6,854,533
	$ 6,970,987	$ 19,500	$ 6,951,487

Management is of the opinion that since these are trust funds, they are unable to provide against these balances, and therefore these loans have been presented as restricted net assets.

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

The Board of Directors
Federated States of Micronesia Development Bank:

We have audited the financial statements of the Federated States of Micronesia Development Bank (the Bank), as of and for the year ended December 31, 2009, and have issued our report thereon dated June 30, 2010. 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 the Bank'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 the Bank's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Bank's internal control over financial reporting.

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 Bank's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Bank's financial statements that is more than inconsequential will not be prevented or detected by the Bank's internal control.

A *material weakness* is a significant deficiency, or 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 Bank's internal control.

Our consideration of 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 internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

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

This report is intended for the information of the Board of Directors and management of Federated States of Micronesia Development Bank, the Office of the National Public Auditor, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

Deloitte & Touche LLP

June 30, 2010

"Your partner in Business"