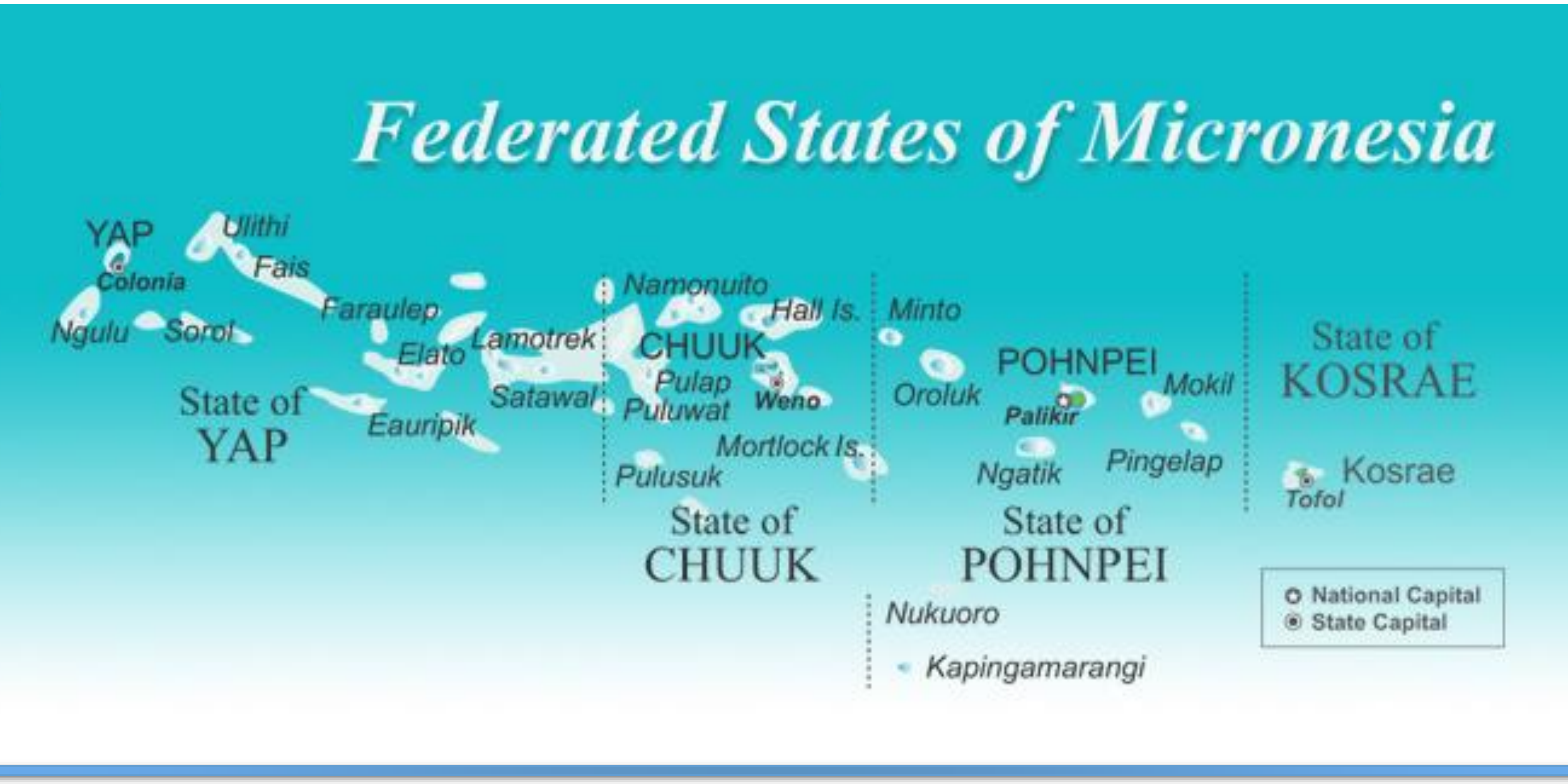
# 2014 ANNUAL REPORT

## FSM DEVELOPMENT BANK




Pohnpei


Chuuk

Kosrae

Yap

## TABLE OF CONTENTS

## LETTER TO THE SHAREHOLDERS

Dear Shareholders:

On behalf of the Board of Directors, we are pleased to submit the Annual Report for the year ending December 31, 2014 and the Audited Financial Statements of the FSM Development Bank (Bank) for the 12 months period ending December 31, 2014 and 2013.

The bank ended the year 2014 with a surplus increasing its total assets by $1.7 million. The bank generated $2.2 million in loan interest income and covered its operating expenses in full. Total revenue was about $3.5 million against expense of $1.8 million. Expenses decreased by 3% compared to last year. Total assets increased by 9% from $46.5 million to $50.5 million. Capital also increased by 4.8% from $45.8 million to $47.9 million. Return on equity was 3.5% and return on asset was 3.3%.

The bank booked a total amount of $10.3 million in new loans for 449 borrowers. Overall, lending has increased compared to last year by 30% and 4% in terms of number and in value, respectively. 91% of total loan approval accounted for projects located in Pohnpei and Chuuk. Business term loans represents little over 50% of total approval. About 32% of total approval ($3.3 million) was approved for women as primary borrowers.

The bank continues to finance its lending operations mainly from its loan collections with minimal borrowings from overseas sources. The bank continues to grow its loan portfolio by 7% from $24.4 million to $26.1 million. The loan portfolio growth has plateaued for the past four years after reaching a high of $28.4 million in 2009.

As part of the Bank reform efforts, we established the bank's Development & Finance Training Institute in April, 2014. Its primary objectives include, among others, to provide training supports for the bank clients, employees, officers, other stakeholders. The bank also created a new position for Senior Vice President & Business Development Officer whose primary duty is to work closely with both existing and prospective clients of the bank in developing business proposals.

Looking ahead, we will maintain our focus and efforts towards projects with developmental impacts. The agriculture, fisheries and tourism sectors are priority sectors with emphasis on export oriented projects and import substitution in the Agriculture and Fisheries sectors. With the continued stagnant economy, we anticipate similar results in 2015. We hope to continue a favorable trend in lending to the priority sectors.

We wish to acknowledge and extend our sincere gratitude and appreciation for your continued support and confidence in the bank. We extend the same to our esteemed colleagues, members of the Board of Directors for their unwavering commitments and valuable insights that they have contributed to advance the bank throughout the years. We wish to also recognize the valuable efforts of every staff members for their hard work and firm commitments to put our words into actions. And finally, we thank our customers for their continued loyalty and confidence in 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 opportunity to other aspiring entrepreneurs. As always, we shall remain "your partners in business".

Sincerely,

Anna Mendiola, President/CEO

John Sohl, Chairman of the Board

## 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. It was established in 1979 by Public Law 1-37. The bank opened operation 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 into a corporation.

The primary function of the bank is to provide financing to commercial businesses mainly in the FSM. Over the years, the bank has added more 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. In 2011, the bank added a consumer lending revolving fund mainly to help generate revenue.

The bank headquarters is located in the State of Pohnpei, the capital of the FSM. The bank also has branch offices in the other three (3) FSM states of Chuuk, Kosrae and Yap.

### VISION:
We make the best investment decisions to achieve the national vision of a vibrant private-sector led economy throughout the Federated States of Micronesia.

### MISSION:
Our investments assist new and existing businesses to grow prosperously, creating jobs and producing economic vitality throughout our Nation.

In the pursuit of our mission we value:

- Customer satisfaction from professional customer service.
- Teamwork, collaboration and dedication to our mission.
- Patient capital, commitment to long term investment.
- Fairness in all our dealings.
- Economic development that enhances the lives of FSM's citizens while sensitive to the protection of our precious environment and respectful of our cultural values and heritage.

### SHAREHOLDERS
The FSM National Government is the principal shareholder of the bank. It owns 98.8% of the outstanding shares. The States of Chuuk and Kosrae each own 0.9% 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.

| Shareholders | No. of Shares | Amount |
|---|---|---|
| FSM National Government | 3,197,883 | $31,978,830 |
| State of Kosrae | 9,000 | $90,000 |
| State of Chuuk | 30,000 | $300,000 |
| Total Shares Outstanding | 3,236,883 | $32,368,830 |

## 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, 2014 were as follows:

John Sohl, Chairman (Pohnpei State Government)

Mr. Sohl was appointed to the Board in 2004 to represent the State of Pohnpei and elected as the Chairman of the Board in 2011.

Currently, Mr. Sohl is the President and Chief Executive Officer of the FSM Telecommunication Corporation (FSMTC) since April of 2010. He was previously the Executive Vice-President & Chief Operating Officer since 1988. He also worked for eight years at the FSM National government and seven years with the Pohnpei Agriculture and Trade School. He completed his studies at the University of Guam in 1973.

Hilary Tacheliol, Vice Chairman (Yap State Government)

Mr. Tacheliol has served on the Board since 1991 making him the longest serving member.

Among others, he holds prominent positions such as first Lt. Governor of his home state of Yap from 1978 to 1987, Director of the Department of Youth and Civic Affairs and Director of the Department of Administrative Services. Retired from office, he serves his people as the Chief of Mogmog of Ulithi atoll and also as the Paramount Chief of all outer islands in Yap State.

Mr. Tacheliol holds a Bachelor's degree in Political Science with a minor in Secondary Education. He completed his education from University of Guam and Xavier High School in Chuuk in 1968 and 1963, respectively.

Sisinio Willy, Director (Chuuk State Government)

Mr. Willy was appointed to the Board in 2006 to represent Chuuk State Government.

Currently, he is the Officer-in-Charge for the Office of Overseas Development Assistance, Chuuk State Government. He was the Chief of Budget for Chuuk State Government when appointed to the Board in 2006. In addition, he held other high level positions ranging from General Manager, Chuuk Public Utilities Corporation, Budget Officer for Chuuk State Government, Special Assistant to Director of Education and Special Assistant to Governor of Chuuk State. He holds a Bachelor's degree in Economics from Carrol College, Montana USA.

Juliet Jimmy, Director (FSM National Government)

Juliet currently serves as the Assistant Secretary for Treasury, Department of Finance at the FSM National Government. Prior to joining the FSM National Government, Juliet worked for the Pohnpei State Department of Finance. Recently, Juliet provided the needed leadership in managing a difficult conversion to a new national Financial Management System.

Juliet attended the Community College of Micronesia and Australian National University, where she focused her degrees on accounting.

Lipar George, Director (Kosrae State Government)

Mr. George was appointed in 2013 to represent Kosrae State Government. Currently, Lipar is the Administrator for the Office of Budget, Statistics and Overseas Development Assistance, Kosrae State Government Department of Administration and Finance. Previously, Lipar was the Chief of Staff for the Office of the Governor of Kosrae State. He was also elected as a representative to the Kosrae State Legislature from 2007-2009 and a Legislative Aide for the committee on Resources and Development.

Mr. Lipar received a Bachelor's Degree in Philosophy from the University of Hawaii-Hilo in 1993.

Anna Mendiola, Ex-Officio (President/CEO)

Anna Mendiola has been the President and Chief Executive Officer of the FSM Development Bank since March 2001. Prior to her appointment, she had served in the position as Chief Financial Officer for one year. In addition, Ms. Mendiola held various high level positions with the FSM National and Pohnpei State Government ranging from Accountant to Director. She also worked for Asia Development Bank (ADB) as the Assistant to the Executive Director for two years.

She holds a Master's degree in Business Administration from California Coast University and a Bachelor's degree in Economics and Business Administration from Eastern Oregon University.

## MANAGEMENT

On a daily basis, the bank is managed by a senior management team comprised of a President/Chief Executive Officer (CEO), Senior Vice President/Chief Operating Officer (COO), Senior Vice President/Business Development Officer and Chief Financial Officer (CFO). Assisting the senior management is a Legal Counsel and Internal Auditor/Compliance Officer. As of December 31, 2014, the composition of the management team was as follows:


Anna Mendiola, President/CEO


Alik J. Alik, SVP/COO


Fabian S. Nimea, SVP/BDO


Sihna Lawrence, CFO


Nora Sigrah, Legal Counsel


Greeno Ismael, Internal Auditor/CO

The bank's headquarters is located in Pohnpei with three branch offices each in the other three states of Chuuk, Kosrae and Yap. There were about 37 employees in 2014.


Rendy Abraham, Loan Analyst


Augustine Loyola, Loan Analyst


Lover Haimin, HR & Facilities Manager


Gabriel Ramoloilug, System Administrator


Lenster Donre, Loan Officer


Galverson Eliou, Loan Officer


Vicky T. Hartman, Loan Officer


Joyleen Charley, Loan Officer


Charito B. Soriano, Accountant


Kedise R. Villazon, Accountant


Nicole Araceley, Accountant


Marlynn S. Tom, Loan Security Officer


Leilany Felix, Assistant System Administrator


Carmina Abraham, Bookkeeper


Zenica Yiftheg, Bookkeeper


Dorian K. Phillip, Executive Secretary


Rohma B. Silbanuz, Legal Secretary


Peterika White, Administrative Secretar

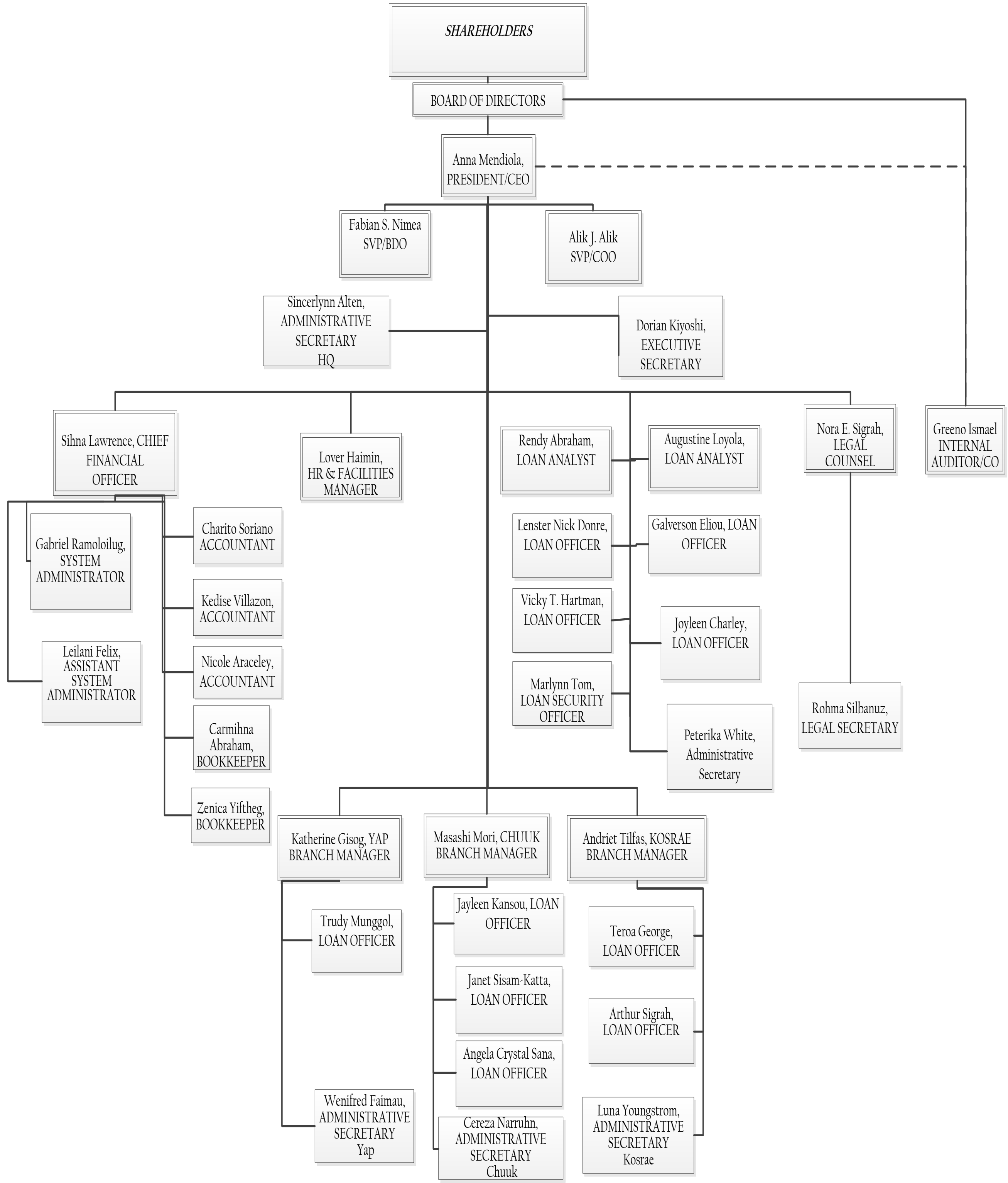

Sincerlynn Alten, Admin Secretary

**Chuuk Branch Office**


**Kosrae Branch Office**

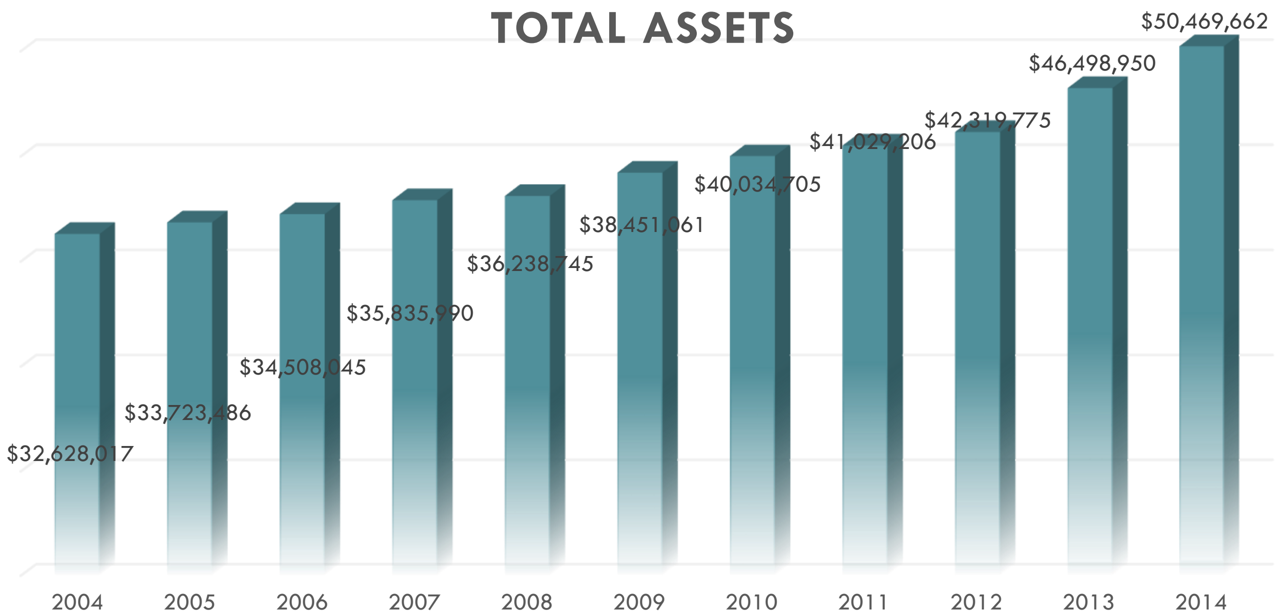

**Yap Branch Office**

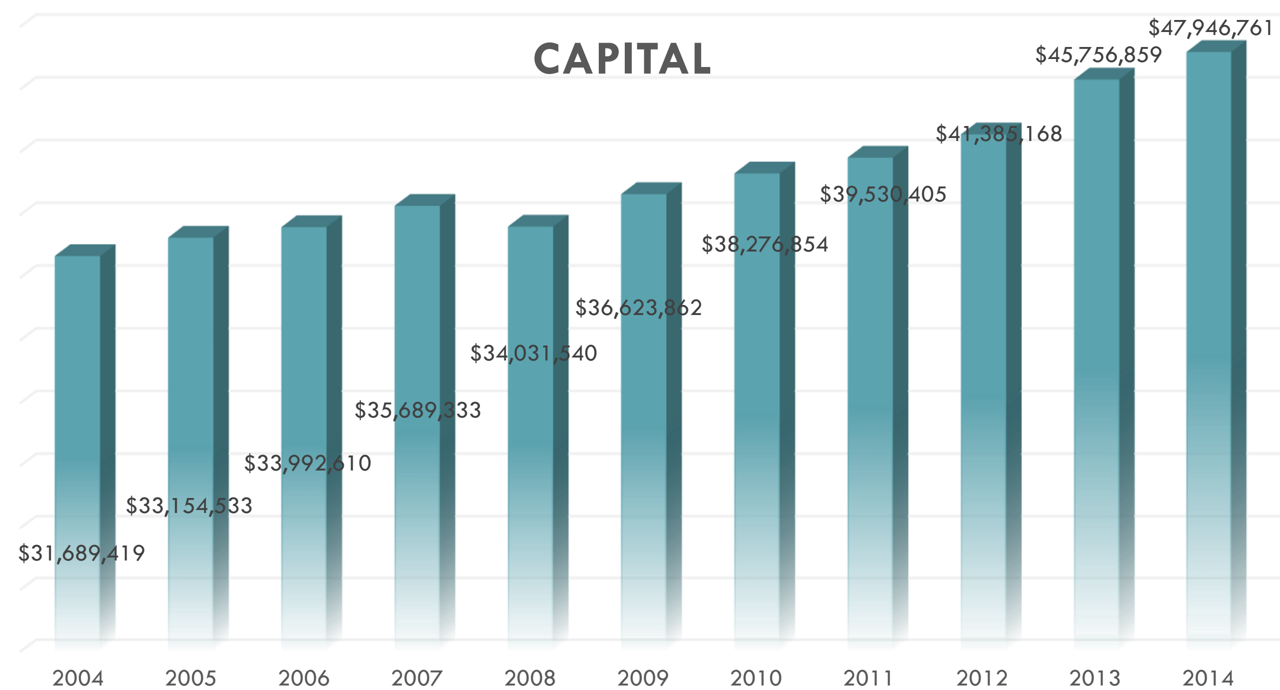
## ORGANIZATIONAL CHART

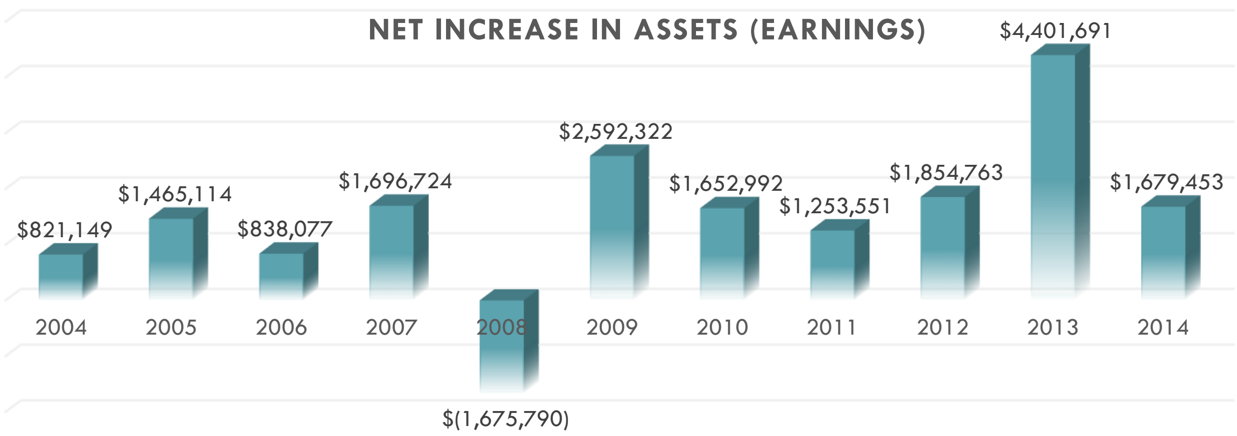


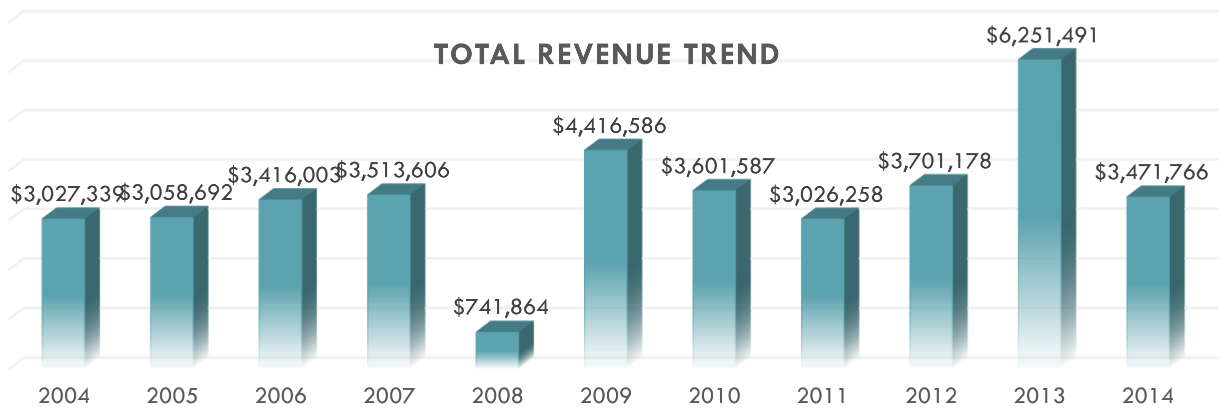
## MANAGEMENT REPORT

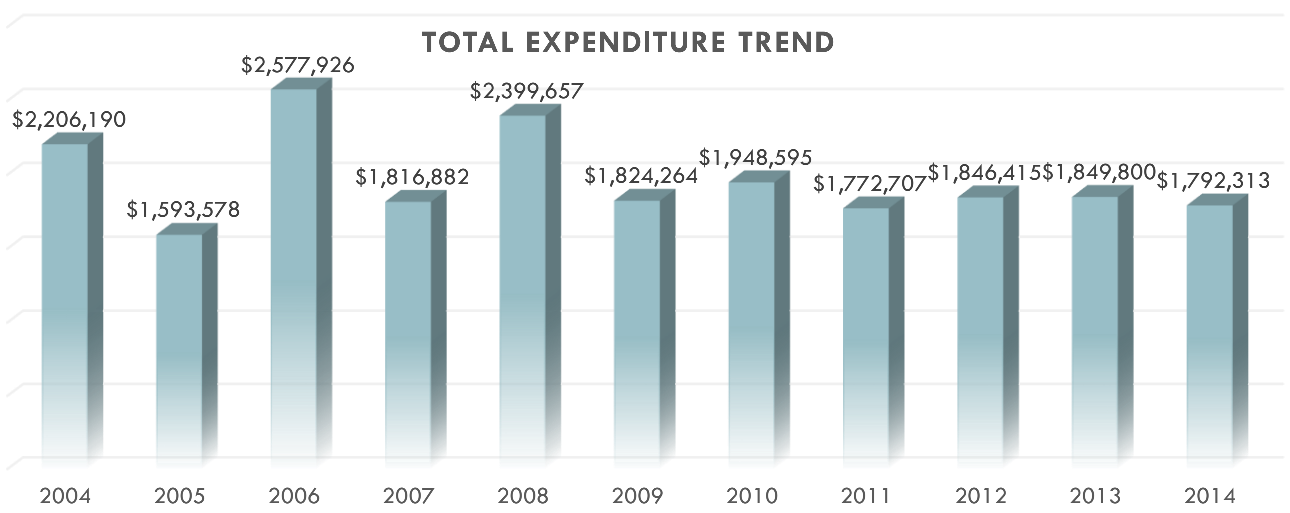
Looking at performance based on the bank's 10-year strategic plan (2005-2014), the charts below show favorable trends of performance. Both assets and capital increased annually by 4% and by more than 50% over the decade. Although revenue and expenses fluctuate over time overall performance improved since 2008. In 2014, the bank has a net increase in assets of $1.7 million (earnings).




NET INCREASE IN ASSETS (EARNINGS)
$821,149
$1,465,114
$838,077
$1,696,724
$(1,675,790)
$2,592,322
$1,652,992
$1,253,551
$1,854,763
$4,401,691
$1,679,453
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014


TOTAL REVENUE TREND
$3,027,339
$3,058,692
$3,416,003
$3,513,606
$741,864
$4,416,586
$3,601,587
$3,026,258
$3,701,178
$6,251,491
$3,471,766
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014


TOTAL EXPENDITURE TREND
$2,206,190
$1,593,578
$2,577,926
$1,816,882
$2,399,657
$1,824,264
$1,948,595
$1,772,707
$1,846,415
$1,849,800
$1,792,313
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014

## LENDING UPDATES

The graph below shows the bank loan approval for the past years based on the bank's strategic plan from 2005-2014. Although the trend shows a fluctuation in total loan approval over the past ten years, the bank managed to increase its overall loan approval amount by an average of 13% annually. In 2014, we approved and booked 449 new loans for a total of $10.3 million. The charts and pie graphs below further show the details and distribution of the loans in the various economic sectors.

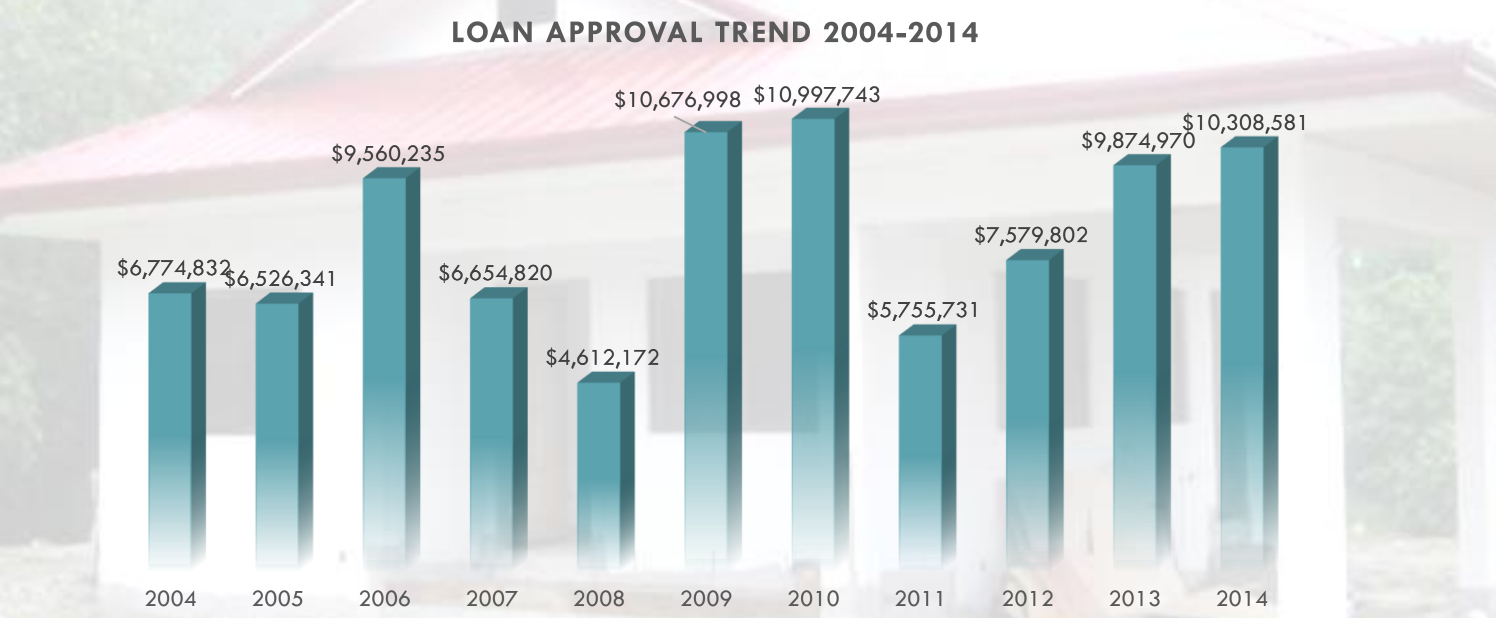
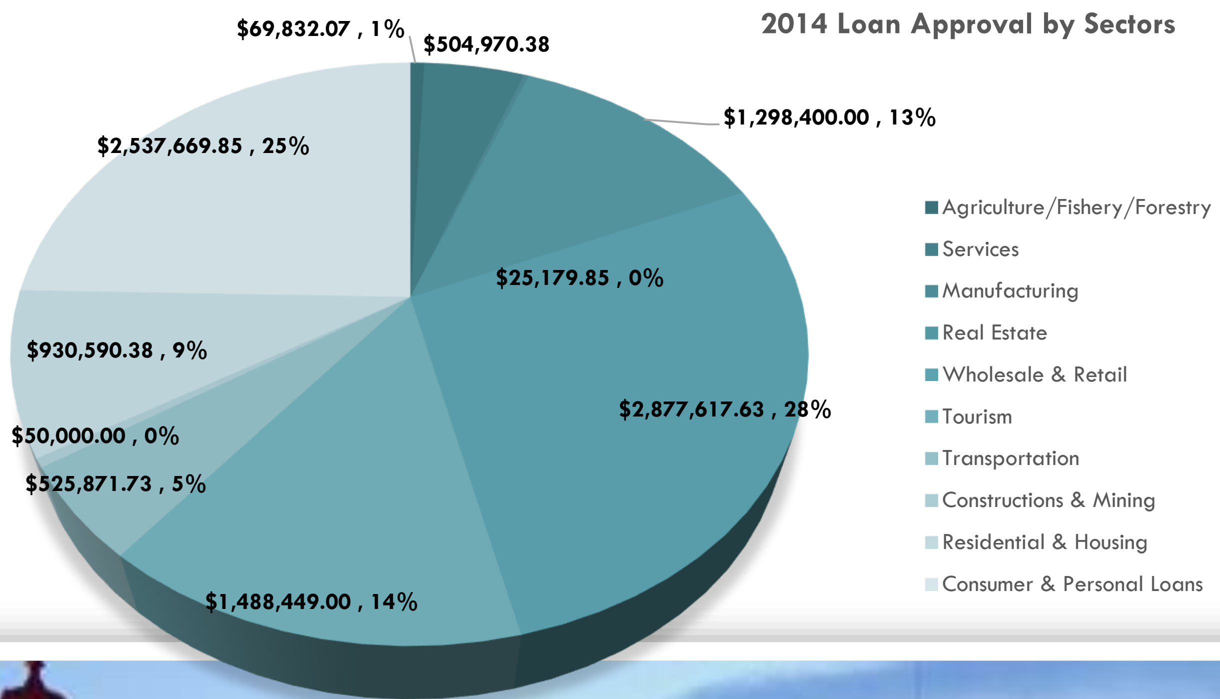


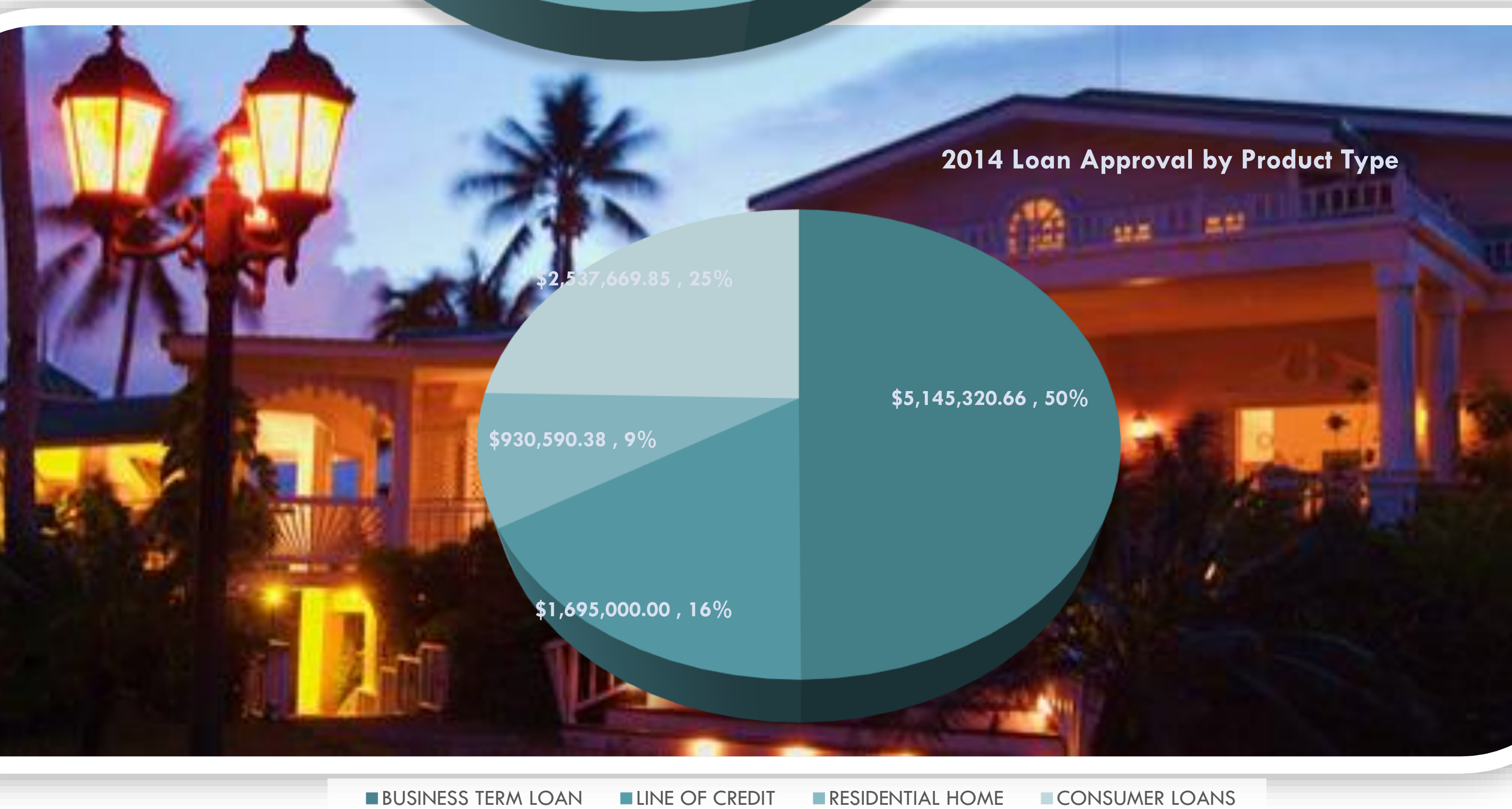

Table 1. 2014 Loans Approved by Sectors

| *LOAN SECTORS* | *No.* | *Amount* | *% (amount)* |
|---|---|---|---|
| *Agriculture/Fishery/Forestry* | 12 | $69,832.07 | 1% |
| *Services* | 18 | $504,970.38 | 5% |
| *Manufacturing* | 13 | $25,179.85 | 0% |
| *Real Estate* | 3 | $1,298,400.00 | 13% |
| *Wholesale & Retail* | 39 | $2,877,617.63 | 28% |
| *Tourism* | 5 | $1,488,449.00 | 14% |
| *Transportation* | 6 | $525,871.73 | 5% |
| *Constructions & Mining* | 1 | $50,000.00 | 0% |
| *Residential & Housing* | 14 | $930,590.38 | 9% |
| *Consumer & Personal Loans* | 338 | $2,537,669.85 | 25% |
| | **449** | **$10,308,580.89** | 100% |

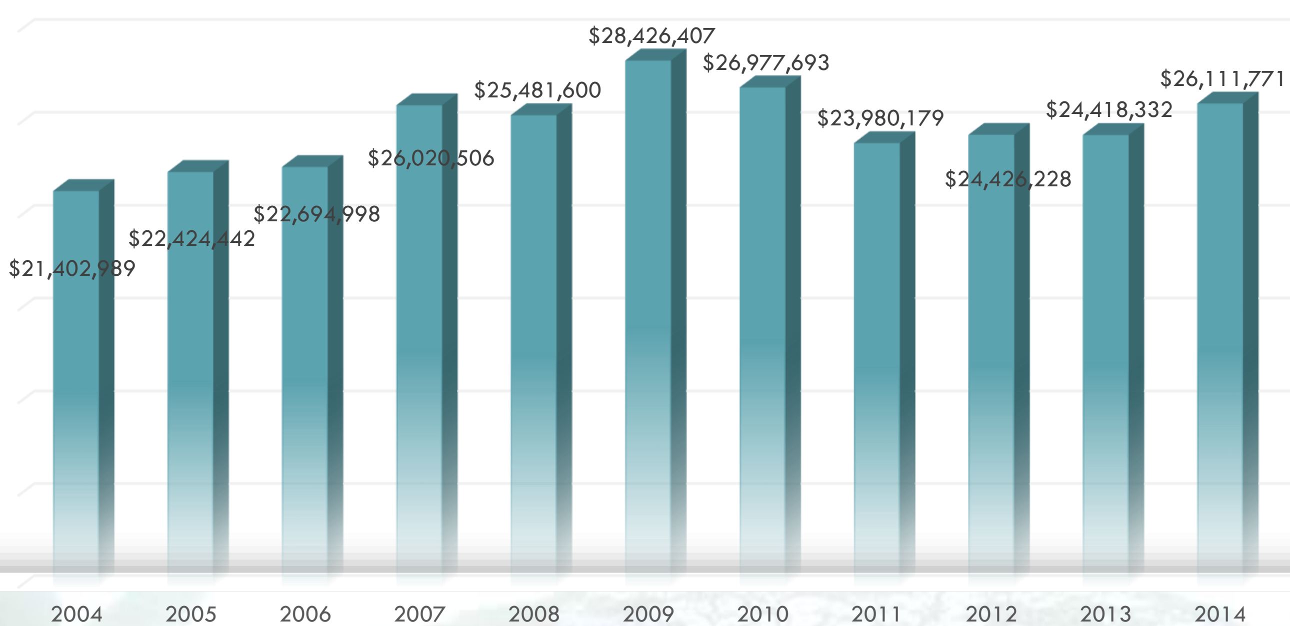
Of the total of $10.3 million, about $1.6 million (15%) was approved for Tourism, Agriculture and fisheries projects for all the FSM states.

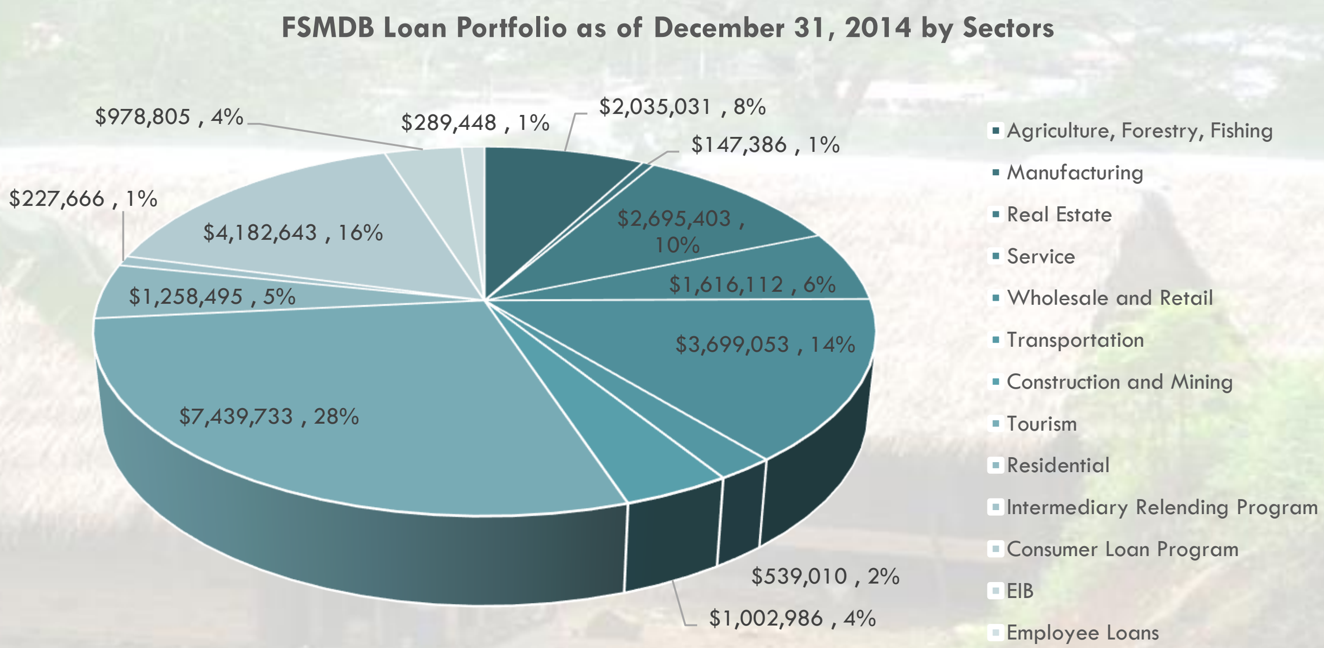
The pie charts below show additional information relating to amount and type of loans as approved for 2014.



Overall collection efforts on delinquent accounts have been consistent for the last three years. The charts show the trends in gross loan outstanding over the past ten years.



## SECTOR DEVELOPMENTS

Agriculture, Fisheries and Tourism remain the priority sectors for the bank. However, during the year, the bank actually approved over $1.6 million in new loans to fund various small scale farms, fishing and tourism related projects across the FSM states.

## SOURCES FUNDS

The bank mainly relies on loan repayment and overseas borrowing to fund its lending activities. About $1.4 million was drawn down from funds under the European Investment Bank (EIB) Loan during the year. Although the bank received $1.million in contribution from the FSM National Government in 2013, there was none in 2014.

## ADMINISTERED FUNDS

The bank manages two non-propriety type funds: the Investment Development Fund (IDF) and the Yap Development Loan Fund (YDLF). In 2014, the bank ceased to administer the Pohnpei Development Loan Fund (PDLF) and all assets and net equity were transferred to the Pohnpei State government. The detail and the current status of these funds can be found in the financial section of the report.

## DEVELOPMENT & FINANCE TRAINING INSTITUTE

In April of 2014, the Board of Directors approved the establishment of the Development & Finance Training Institute (DFI) as part of the bank's reform efforts in response to the recommendations made by States and National Leaders during the Investment Symposium in 2013. The DFI has conducted three separate week-long training sessions featuring courses such as Decision Making for Executives, Trainers Training, Competitive Business Strategy for Entrepreneurs and Small Business, Risk Management and Financial Accounting for Non-accountants to its employees, clients or customers and government executives.

*Photos: Participants in Decision Making & Trainers Training February 2015 (above), and Competitive Business Strategy for Entrepreneurs in October 2014 (below).*

In addition, the bank has also created and filled a position of business development services to work closely with prospective clients of the bank and to enhance business success.

The bank continues to offer scholarships to students pursing graduate degrees in Accounting, Business, Finance, Banking, Economics and other related fields.

The Bank also received students during the summer through internship under a program called HELP funded and coordinated by the Pacific Islander Student Center at the University of Hawaii in Hilo. HELP stands for Highly Engaged Learning Positions (HELP) program and among others, its main objectives include providing internship opportunities for students to work during the summer and gain experiences in the field of studies they pursue and at the same time fulfill a need in the Pacific Island communities.

## PERSONNEL UPDATES

New Hires, Promotions & Departures

During the year, the bank has hired new staff members and promoted one. We would like to welcome and congratulate all the new staff members and the one being promoted as follows:

Zenica Yiftheg, Bookkeeper
Nicole Araceley, Accountant
Joyleen Charley, Loan Officer (HQ)
Charito B. Soriano, Accountant
Alik J. Alik, SVP/Chief Operating Officer
Fabian S. Nimea, SVP/Business Development Officer
Greeno Ismael, promoted to Internal Auditor/Compliance Officer

ACKNOWLEDGMENT

We would like to take this opportunity to extend our appreciation and thanks to Mr. Gillian Doone who served on the Board representing the National Government. Also, we extend our sincere appreciation and thanks to the following former staff members of the bank:

Dahlia Phillip, Loan Clerk
Lleonor Hulguin, Accountant
Ignacio Stephen, SVP/COO
Micheal Henry, Internal Auditor/Compliance Officer

## FINANCIAL REPORT

Federated States of Micronesia Development Bank

(A component Unit of the FSM National Government)

Financial Statements and Independent Audit Reports

Years Ended December 31, 2014 and 2013.

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

Board of Directors
Federated States of Micronesia Development Bank:

## Report on the Financial Statements

We have audited the accompanying financial statements of the Federated States of Micronesia Development Bank (the Bank), which comprise the statements of net position as of December 31, 2014 and 2013, and the related statements of revenues, expenses and changes in net position and of 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.

### *Auditor's 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 Federated States of Micronesia Development Bank as of December 31, 2014 and 2013, and the results of its operations 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 4 to 6 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. 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 audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Bank's basic financial statements. The supplemental schedule of net position - Intermediary Relending Program and schedule of revenues, expenses and changes in net position - Intermediary Relending Program on pages 24 and 25, respectively, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The supplemental schedule of net position - Intermediary Relending Program and schedule of revenues, expenses and changes in net position - Intermediary Relending Program are the responsibility of management and were derived from and relate 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 standards generally accepted in the United States of America. In our opinion, the supplemental schedule of net position - Intermediary Relending Program and schedule of revenues, expenses and changes in net position - Intermediary Relending Program are 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 April 7, 2015, on our consideration of the Bank'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 financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Bank's internal control over financial reporting and compliance.

Deloitte & Touche LLP

April 7, 2015

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

Statements of Net Position
December 31, 2014 and 2013

| | 2014 | 2013 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 5,478,528 | $ 6,408,568 |
| Time certificates of deposit | 1,993,326 | 1,410,562 |
| Accounts receivable | 37,091 | 43,414 |
| Receivable from trust funds | 79,888 | 204,108 |
| Prepaid expenses | 9,319 | 667 |
| Interest and other receivables | 206,163 | 210,967 |
| Current portion of loans receivable | 6,083,000 | 5,809,000 |
| Total current assets | 13,887,315 | 14,087,286 |
| Noncurrent assets: | | |
| Depreciable assets, net | 1,581,749 | 1,694,055 |
| Fixed assets in progress | 75,757 | - |
| Investments | 15,778,622 | 15,197,400 |
| Equity investment, at cost | 1,912,188 | 1,162,188 |
| Loans receivable, net of current portion and allowance for loan losses | 16,212,240 | 14,358,021 |
| Total noncurrent assets | 35,560,556 | 32,411,664 |
| Total assets | $ 49,447,871 | $ 46,498,950 |
| LIABILITIES AND NET POSITION | | |
| Current liabilities: | | |
| Current portion of long-term debt | $ 138,363 | $ 15,294 |
| Accounts payable | 84,857 | 143,034 |
| Accrued interest payable | 13,325 | - |
| Credit life payable | 61,897 | 52,479 |
| Payable to trust funds | - | 66,715 |
| Total current liabilities | 298,442 | 277,522 |
| Noncurrent liabilities: | | |
| Long-term debt, net of current portion | 1,683,117 | 434,569 |
| Total liabilities | 1,981,559 | 712,091 |
| Commitments and contingencies | | |
| Net position: | | |
| Net investment in capital assets | 1,657,506 | 1,694,055 |
| Unrestricted | 45,808,806 | 44,092,804 |
| Total net position | 47,466,312 | 45,786,859 |
| Total liabilities and net position | $ 49,447,871 | $ 46,498,950 |

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 Position
Years Ended December 31, 2014 and 2013

| | 2014 | 2013 |
|---|---|---|
| Operating revenues: | | |
| Interest income on loans | $ 2,194,498 | $ 2,187,963 |
| Interest income on time certificates of deposit | 13,005 | 20,197 |
| Loan fees | 174,990 | 105,321 |
| Rental | 50,907 | 40,277 |
| Miscellaneous | 112,545 | 74,293 |
| Total operating revenues | 2,545,945 | 2,428,051 |
| (Provision for) reversal of loan losses | (72,962) | 446,769 |
| Net operating revenues | 2,472,983 | 2,874,820 |
| Operating expenses: | | |
| Interest expense | 34,350 | 23,847 |
| General and administrative expenses: | | |
| Personnel services | 901,661 | 929,939 |
| Rent | 137,084 | 128,820 |
| Depreciation | 131,210 | 128,940 |
| Travel | 114,090 | 96,176 |
| Contractual services | 104,604 | 81,452 |
| Utilities | 56,217 | 63,771 |
| Communication | 40,224 | 42,904 |
| Retirement plan contributions | 39,484 | 44,524 |
| Training | 32,601 | 52,395 |
| Supplies | 32,519 | 31,923 |
| Equipment | 31,638 | 25,886 |
| Branch automation | 20,862 | 22,743 |
| Community development | 20,647 | 8,667 |
| Staff relations | 9,400 | 12,056 |
| Fuel, oil and petroleum | 9,018 | 10,814 |
| Insurance | 7,004 | 7,159 |
| Repair and maintenance | 5,626 | 7,192 |
| Printing | 5,188 | 5,069 |
| Miscellaneous | 58,886 | 125,523 |
| Total general and administrative expenses | 1,757,963 | 1,825,953 |
| Earnings from operations | 680,670 | 1,025,020 |
| Nonoperating revenues: | | |
| IDF reimbursement | 250,000 | 250,000 |
| Investment earnings, net | 740,127 | 2,095,025 |
| Gain on sale of assets | 8,656 | 31,646 |
| FSMNG contributions | - | 1,000,000 |
| Total nonoperating revenues, net | 998,783 | 3,376,671 |
| Change in net position | 1,679,453 | 4,401,691 |
| Net position at beginning of year | 45,786,859 | 41,385,168 |
| Net position at end of year | $ 47,466,312 | $ 45,786,859 |

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, 2014 and 2013

| | 2014 | 2013 |
|---|---|---|
| Cash flows from operating activities: | | |
| Cash received from customers | $ 2,544,067 | $ 2,451,651 |
| Cash paid to suppliers for goods and services | (782,503) | (696,247) |
| Cash paid to employees for services | (901,661) | (929,939) |
| Interest received on time certificates of deposit | 13,005 | 20,197 |
| Interest paid | (21,025) | (38,935) |
| Net cash provided by operating activities | 851,883 | 806,727 |
| Cash flows from noncapital financing activities: | | |
| Proceeds from long-term debt | 1,406,526 | 139,108 |
| Principal repayment of long-term debt | (34,909) | (400,000) |
| Net transfers in from trust funds | 307,505 | 508,385 |
| FSMNG contributions | - | 1,000,000 |
| Net cash provided by noncapital financing activities | 1,679,122 | 1,247,493 |
| Cash flows from capital and related financing activities: | | |
| Proceeds from sale of fixed assets | 8,656 | 31,646 |
| Acquisition of fixed assets | (94,661) | (413,660) |
| Net cash used for capital and related financing activities | (86,005) | (382,014) |
| Cash flows from investing activities: | | |
| Loan origination and principal collections, net | (2,201,181) | 65,307 |
| Additions to time certificates of deposit, net | (582,764) | 1,440,480 |
| Additions to investments, net | (6,405) | (1,290,797) |
| Additions to equity investment | (750,000) | - |
| Interest income on savings accounts | 1,060 | 998 |
| Dividends received | 164,250 | 129,000 |
| Net cash (used for) provided by investing activities | (3,375,040) | 344,988 |
| Net change in cash and cash equivalents | (930,040) | 2,017,194 |
| Cash and cash equivalents at beginning of year | 6,408,568 | 4,391,374 |
| Cash and cash equivalents at end of year | $ 5,478,528 | $ 6,408,568 |

Statements of Cash Flows, Continued
Years Ended December 31, 2014 and 2013

| | 2014 | 2013 |
|---|---|---|
| Reconciliation of earnings from operations to net cash provided by operating activities: | | |
| Earnings from operations | $ 680,670 | $ 1,025,020 |
| Adjustment to reconcile earnings from operations to net cash provided by operating activities: | | |
| Provision for (reversal of) loan losses | 72,962 | (446,769) |
| Depreciation | 131,210 | 128,940 |
| (Increase) decrease in assets: | | |
| Accounts receivable | 6,323 | 6,829 |
| Interest and other receivables | 4,804 | 36,968 |
| Prepaid expenses | (8,652) | 3,980 |
| Increase (decrease) in liabilities: | | |
| Accounts payable | (58,177) | 48,680 |
| Accrued interest payable | 13,325 | (15,088) |
| Credit life payable | 9,418 | 18,167 |
| Net cash provided by operating activities | $ 851,883 | $ 806,727 |

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, 2014 and 2013

(1) Summary of Significant Accounting Policies

Reporting Entities

The Federated States of Micronesia (FSM) Development Bank (the Bank) was created in 1979 by Public Law 1-37 of the First Congress of the Federated States of Micronesia. The 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 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, 2010, the Bank has issued 2,997,883 shares to the FSM National Government (98.7%), Kosrae State (0.3%) and Chuuk State (1.0%). These shares do not convey ownership and have been made in accordance with the aforementioned law but these shares have no financial impact on the accompanying financial statements.

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 United States.

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.

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.

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).

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

Notes to Financial Statements
December 31, 2014 and 2013

(1) Summary of Significant Accounting Policies, Continued

Fund Structure and Basis of Accounting, Continued

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 (GAAP) 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.

The Statement of Net Position presents all of the Bank's non-fiduciary assets, deferred outflows of resources, liabilities and deferred inflows of resources, with the difference reported as net position. Net position is classified for accounting and reporting purposes into the following four 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 as well as deferred outflows of resources and deferred inflows of resources that are attributable to those assets or related debt.
- Restricted - restricted assets reduced by liabilities and deferred inflows of resources related to those assets that are subject to externally imposed stipulations.
- Unrestricted - the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

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 include 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 position 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

Investment securities 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.

An equity investment in the common stock of Bank of the FSM is stated at cost as there is no active market for this investment.

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

Notes to Financial Statements
December 31, 2014 and 2013

(1) Summary of Significant Accounting Policies, Continued

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 their useful lives. Assets with a purchase value less than $5,000 are expensed fully in the year of purchase.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Bank enters 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 GAAP 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.

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

Notes to Financial Statements
December 31, 2014 and 2013

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended December 31, 2014, the Bank implemented the following pronouncements:

- 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. 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 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 has not yet determined the effect of implementation of this statement on the financial statements of the Bank.

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 has not yet determined the effect of implementation of this statement on the financial statements of the Bank.

(2) Deposits and Investments

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, 2014 and 2013

(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:

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, 2014 and 2013, the carrying amount of the Bank's total cash and cash equivalents and time certificates of deposit was $7,471,854 and $7,819,130, respectively, and the corresponding bank balances were $7,610,727 and $9,138,875, respectively, which were all maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2014 and 2013, bank deposits in the amounts 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, 2014 and 2013.

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

Notes to Financial Statements
December 31, 2014 and 2013

(2) Deposits and Investments, Continued

B. Investments

As of December 31, 2014 and 2013, investments at fair value are as follows:

| | 2014 | 2013 |
|---|---|---|
| Fixed income securities: | | |
| Domestic fixed income | $ 4,987,915 | $ 4,640,931 |
| Other investments: | | |
| Domestic equities | 8,387,491 | 7,985,153 |
| Money market funds | 1,375,093 | 2,571,316 |
| Shares in a mutual fund (Templeton Global BD FD ADV TGBAX) | 1,028,123 | - |
| | $ 15,778,622 | $ 15,197,400 |

As of December 31, 2014, investments in domestic fixed income are as follows:

| | Amount | Maturity | Moody's Rating |
|---|---|---|---|
| U.S. Government Securities | | | |
| U.S. Treasury Bond | $ 514,041 | 08/15/2021 | AAA |
| U.S. Treasury Note | 421,541 | 11/15/2021 | AAA |
| U.S. Treasury Note | 335,838 | 02/15/2022 | AAA |
| U.S. Treasury Note | 594,745 | 05/15/2022 | AAA |
| | 1,866,165 | | |
| U.S. Government Agency Securities | | | |
| Federal Home Loan Mortgage Corporation (FHLMC) note | 214,818 | 02/09/2015 | AA2 |
| Federal Home Loan Bank (FHLB) note | 257,302 | 06/13/2016 | A2 |
| FHLB note | 341,057 | 03/27/2017 | AAA |
| FHLB note | 522,241 | 04/28/2017 | AAA |
| Federal National Mortgage Associateion (FNMA) note | 343,751 | 09/20/2017 | AAA |
| FNMA note | 91,720 | 09/26/2017 | AAA |
| FHLMC note | 338,547 | 12/14/2018 | AAA |
| FHLMC mortgage-backed securities | 116,861 | 10/01/2023 | not rated |
| FNMA mortgage-backed securities | 244,339 | 09/01/2027 | not rated |
| | 2,470,636 | | |
| Corporate Bonds: | | | |
| Aflac, Inc. (CUSIP 001055AC6) | 56,237 | 05/15/2019 | A3 |
| Morgan Stanley (CUSIP 61747WAF6) | 57,398 | 01/25/2021 | BAA2 |
| Goldman Sachs Group, Inc. (CUSIP 38141GGQ1) | 39,503 | 07/27/2021 | BAA1 |
| General Electric Capital Corp (CUSIP 36962G5J9) | 50,721 | 10/17/2021 | A1 |
| Bank of America Corp (CUSIP 06051GEM7) | 46,338 | 01/24/2022 | BAA2 |
| PNC Funding Corp (CUSIP 693476BN2) | 41,137 | 03/08/2022 | A3 |
| Citigroup Inc. (CUSIP 172967GK1) | 72,426 | 07/30/2022 | BAA3 |
| Wells Fargo & Company (CUSIP 94974BFJ4) | 70,944 | 02/13/2023 | A3 |
| Metlife Inc (CUSIP 59156RBB3) | 54,520 | 09/15/2023 | A3 |
| IBM Corp (CUSIP 459200HU8) | 83,346 | 02/12/2024 | AA3 |
| Apple Inc (CUSIP 037833AS9) | 78,544 | 05/06/2024 | AAA |
| | 651,114 | | |
| | $ 4,987,915 | | |

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

Notes to Financial Statements
December 31, 2014 and 2013

(2) Deposits and Investments, Continued

B. Investments, Continued

As of December 31, 2013, investments in domestic fixed income are as follows:

| | Amount | Maturity | Moody's Rating |
|---|---|---|---|
| U.S. Government Securities | | | |
| U.S. Treasury Note | $ 201,750 | 05/31/2014 | AAA |
| U.S. Treasury Note | 256,368 | 08/15/2014 | AAA |
| U.S. Treasury Note | 234,545 | 02/15/2015 | AAA |
| U.S. Treasury Note | 206,038 | 04/30/2015 | AAA |
| U.S. Treasury Note | 190,134 | 02/15/2016 | AAA |
| U.S. Treasury Note | 325,306 | 01/31/2017 | AAA |
| U.S. Treasury Note | 194,852 | 11/15/2017 | AAA |
| U.S. Treasury Note | 192,883 | 05/15/2018 | AAA |
| U.S. Treasury Note | 243,808 | 01/31/2019 | AAA |
| U.S. Treasury Note | 213,126 | 05/15/2019 | AAA |
| U.S. Treasury Note | 108,844 | 02/15/2020 | AAA |
| U.S. Treasury Note | 343,531 | 02/15/2022 | AAA |
| | 2,711,185 | | |
| U.S. Government Agency Securities | | | |
| FNMA note | 139,717 | 10/15/2014 | AAA |
| FHLMC note | 308,772 | 02/09/2015 | AAA |
| FHLMC note | 202,617 | 09/10/2015 | AAA |
| FHLMC note | 291,832 | 11/17/2015 | AAA |
| FHLMC note | 284,380 | 08/25/2016 | AAA |
| FNMA note | 235,603 | 09/15/2016 | AAA |
| FNMA note | 253,008 | 01/30/2017 | AAA |
| FNMA note | 213,817 | 02/13/2017 | AAA |
| | 1,929,746 | | |
| | $ 4,640,931 | | |

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

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 institution at December 31, 2014 and 2013.

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

Notes to Financial Statements
December 31, 2014 and 2013

(2) Deposits and Investments, Continued

B. Investments, Continued

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, 2014, the Bank's investment in U.S. Treasury Notes and agency obligations of the FHLB constituted 12% and 7%, respectively, of its total investments. As of December 31, 2013, the Bank's investment in U.S. Treasury Notes and agency obligations of the FHLMC and FNMA constituted 18%, 7% and 6%, 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

At December 31, 2014 and 2013, the equity investment in Bank of the FSM, carried at cost, represents 225,000 and 150,000 common shares, respectively, and approximately 24.1% and 16.1%, respectively 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, 2014 and 2013 follows:

| | 2014 | 2013 |
|---|---|---|
| Unpaid principal balance | $ 26,124,133 | $ 24,415,555 |
| Allowance for loan losses | (3,828,893) | (4,248,534) |
| | $ 22,295,240 | $ 20,167,021 |

Movements in the allowance for loan losses during the years ended December 31, 2014 and 2013, are as follows:

| | 2014 | 2013 |
|---|---|---|
| Balance at beginning of year | $ 4,248,534 | $ 4,626,865 |
| Provision for (reversal of) loan losses | 72,962 | (446,769) |
| Loans charged off | (1,548,067) | (981,744) |
| Loan recoveries from previously charged off loans | 1,055,464 | 1,050,182 |
| Balance at end of year | $ 3,828,893 | $ 4,248,534 |

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

Notes to Financial Statements
December 31, 2014 and 2013

(5) Fixed Assets

A summary of fixed assets as of December 31, 2014 and 2013, is as follows:

| | Beginning January 1, 2014 | Additions/ Transfers | Deletions/ Transfers | Ending December 31, 2014 |
|---|---|---|---|---|
| Building | $ 1,674,348 | $ - | $ - | $ 1,674,348 |
| Computers and software | 466,199 | 18,904 | - | 485,103 |
| Vehicles | 170,651 | - | (26,079) | 144,572 |
| Office furniture, fixtures and equipment | 39,733 | - | - | 39,733 |
| | 2,350,931 | 18,904 | (26,079) | 2,343,756 |
| Less accumulated depreciation | (656,876) | (131,210) | 26,079 | (762,007) |
| | 1,694,055 | (112,306) | - | 1,581,749 |
| Projects in progress | - | 75,757 | - | 75,757 |
| Fixed assets, net | $ 1,694,055 | $ (36,549) | $ - | $ 1,657,506 |

| | Beginning January 1, 2013 | Additions/ Transfers | Deletions/ Transfers | Ending December 31, 2013 |
|---|---|---|---|---|
| Building | $ 1,413,988 | $ 260,360 | $ - | $ 1,674,348 |
| Computers and software | 411,613 | 54,586 | - | 466,199 |
| Vehicles | 151,565 | 90,750 | (71,664) | 170,651 |
| Office furniture, fixtures and equipment | 31,769 | 7,964 | - | 39,733 |
| | 2,008,935 | 413,660 | (71,664) | 2,350,931 |
| Less accumulated depreciation | (599,600) | (128,940) | 71,664 | (656,876) |
| Fixed assets, net | $ 1,409,335 | $ 284,720 | $ - | $ 1,694,055 |

(6) Related Party Transactions

As of December 31, 2014 and 2013, the Bank has direct loans with outstanding balances of $289,127 and $128,388, respectively, to employees of the Bank and project loans extended to businesses owned by or affiliated with employees of $497,004 and $295,216, 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) 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, 2014 and 2013, the account has a balance of $156,693 and $178,576, respectively.

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

Notes to Financial Statements
December 31, 2014 and 2013

(8) Long-Term Debt

Long-term debt consists of the following at December 31, 2014 and 2013:

| | 2014 | 2013 |
|---|---|---|
| Payable on an Intermediary Relending Program (IRP) loan by the U.S. Department of Agriculture, granted in December, 2009 for $466,254. The loan bears interest fixed at 1% per annum, requires interest only payments for the first three years and semi-annual principal and interest installments of $19,793 beginning on December 8, 2013 through December 8, 2039. | $ 414,954 | $ 449,863 |
| Loans payable to European Investment Bank under a August 2010 master finance contract of EUR 4 million: | | |
| Drawn on August 20, 2014; original amount of $275,000 (equivalent EUR 205,500), bearing interest fixed at 3.705%, and payable through semi-annual principle and interest installments of $24,778 on January 15, 2015 and equal installments of $25,772 beginning on July 15, 2015 through maturity on July 15, 2020. | 275,000 | - |
| Drawn on August 20, 2014; original amount of $334,550 (equivalent EUR 250,000), bearing interest fixed at 4.520%, and payable through semi-annual principle and interest installments of $17,997 on January 15, 2015 and equal installments of $19,467 beginning on July 15, 2015 through maturity on July 15, 2025 | 334,550 | - |
| Drawn on August 20, 2014; original amount of $796,976 (equivalent EUR 595,558), bearing interest fixed at 4.520%, and payable through semi-annual principle and interest installments of $42,873 on January 15, 2015 and equal installments of $46,375 beginning on July 15, 2015 through maturity on July 15, 2025 | 796,976 | - |
| Total long-term debt | 1,821,480 | 449,863 |
| Less current portion | (138,363) | (15,294) |
| Long-term debt, net of current portion | $ 1,683,117 | $ 434,569 |

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

| Year Ending December 31, | Principal | Interest | Total |
|---|---|---|---|
| 2015 | $ 138,363 | $ 58,692 | $ 197,055 |
| 2016 | 144,249 | 58,771 | 203,020 |
| 2017 | 149,919 | 53,102 | 203,021 |
| 2018 | 155,827 | 47,193 | 203,020 |
| 2019 | 161,988 | 41,032 | 203,020 |
| 2020-2024 | 691,843 | 117,084 | 808,927 |
| 2025-2029 | 216,148 | 15,182 | 231,330 |
| 2030-2034 | 92,643 | 6,322 | 98,965 |
| 2035-2039 | 70,500 | 1,667 | 72,167 |
| | $ 1,821,480 | $ 399,045 | $ 2,220,525 |

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

Notes to Financial Statements
December 31, 2014 and 2013

(8) Long-Term Debt, Continued

Long-term debt changes during the years ended December 31, 2014 and 2013 are as follows:

| | Balance January 1, | Additions | Reductions | Balance December 31, | Due Within One Year |
|---|---|---|---|---|---|
| 2014: | | | | | |
| Loan payable | $ 449,863 | $ 1,406,526 | $ (34,909) | $ 1,821,480 | $ 138,363 |

| | Balance January 1, | Additions | Reductions | Balance December 31, | Due Within One Year |
|---|---|---|---|---|---|
| 2013: | | | | | |
| Loan payable | $ 710,755 | $ 139,108 | $ (400,000) | $ 449,863 | $ 15,294 |

(9) Nonoperating Revenue

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, 2014 and 2013. Additionally, the Bank received $1,000,000 in contributions from FSMNG in 2013.

(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 Chief Financial Officer is the designated Plan Administrator. Matching contributions to the Plan during the years ended December 31, 2014 and 2013 were $39,484 and $44,524 respectively. Total Plan assets as of December 31, 2014 and 2013 were $700,999 and $676,487, respectively. Management is of the opinion that the Plan does not represent an asset or a liability of the Bank.

(11) 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, 2014 and 2013.

Loan Commitments

Undrawn balances on lines of credit and loan commitments for loans approved but undisbursed approximated $2,284,000 at December 31, 2014.

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.

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

Notes to Financial Statements
December 31, 2014 and 2013

(11) Commitments and Contingencies, Continued

Insurance

The Bank carries insurance to cover its potential risks from vehicle usage. The 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 during the past three years.

Lease Commitments

The Bank has four operating leases for each of its State operating locations. These leases expire in varying dates through February 2018. Several of these leases provide options to renew upon expiration, based on renegotiated rates. In 2013, the Bank moved its Pohnpei branch and the headquarters office (the "HQ building") to the building which was acquired in a loan settlement during 2011. In July 2013, the Bank entered into a sub-lease agreement for the former location, for which the lease expires in April 2015. Future minimum annual lease payments payable, net of sub-lease income, under the noncancellable lease agreements are as follows:

| Year ending December 31, | Expense | Income | Net |
|---|---|---|---|
| 2015 | $ 57,990 | $ 8,000 | $ 49,990 |
| 2016 | 16,100 | - | 16,100 |
| 2017 | 15,000 | - | 15,000 |
| 2018 | 1,250 | - | 1,250 |
| | $ 90,340 | $ 8,000 | $ 82,340 |

The Bank leases portions of the HQ building under three separate agreements expiring from May 2015 to November 2020. Future minimum annual lease income receivable under the noncancellable lease agreements are as follows:

| Year ending December 31, | |
|---|---|
| 2015 | $ 17,600 |
| 2016 | 9,000 |
| 2017 | 9,000 |
| 2018 | 9,000 |
| 2019 | 9,000 |
| 2020 | 7,900 |
| | $ 61,500 |

Additionally, the Bank provides housing benefits for certain contract employees with payment included as part of rent expense. The lease agreements are between the respective landlords and the employees.

Total recorded lease expense and income under the aforementioned agreements amounted to $137,084 and $50,907, respectively, for the year ended December 31, 2014 and $128,820 and $40,277, respectively, for the year ended December 31, 2013.

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

Notes to Financial Statements
December 31, 2014 and 2013

(12) Subsequent Events

In March 2015, Typhoon Maysak ravaged Chuuk and Yap causing severe damages. The ultimate impact on the Bank's branch offices and borrowers' ability for loan repayments is presently indeterminable.

Management has evaluated subsequent events through April 7, 2015, which is the date that the financial statements are available to be issued. Except for the above, there were no other material subsequent events that would require recognition or disclosure in the financial statements for the year ended December 31, 2014.

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

Schedule of Net Position - Intermediary Relending Program
December 31, 2014

| | | |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ | 809,878 |
| Interest and other receivables | | 168 |
| Loans receivable, net | | 211,745 |
| Total assets | $ | 1,021,791 |
| **LIABILITIES AND NET POSITION** | | |
| Current liabilities: | | |
| Due to FSMDB, net | $ | 126,215 |
| Credit life payable | | 173 |
| Total current liabilities | | 126,388 |
| Noncurrent liabilities: | | |
| Long-term debt | | 414,954 |
| Total liabilities | | 541,342 |
| Net position: | | |
| Unrestricted | | 480,449 |
| Total net position | | 480,449 |
| Total liabilities and net position | $ | 1,021,791 |

See accompanying Independent Auditors' Report.

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

Schedule of Revenues, Expenses and Change in Net Position -
Intermediary Relending Program
Year Ended December 31, 2014

| | |
|---|---|
| Operating revenues: | |
| Interest income on loans | $ 24,391 |
| Miscellaneous | 3,099 |
| Total operating revenues | 27,490 |
| Operating expenses: | |
| Provision for loan losses | 16,400 |
| Interest expense | 4,677 |
| Total operating expenses | 21,077 |
| Income from operations | 6,413 |
| Non-operating revenues: | |
| Interest income on savings account | 1,060 |
| Change in net position | 7,473 |
| Net position at beginning of year | 472,976 |
| Net position at end of year | $ 480,449 |

See accompanying Independent Auditors' Report.

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

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**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT**

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**DECEMBER 31, 2014**

Deloitte.

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## INDEPENDENT AUDITORS' REPORT

Board of Directors
Federated States of Micronesia Development Bank:

**Report on the Financial Statements**

We have audited the accompanying financial statements of the Investment Development Fund, the Pohnpei Development Loan Fund, and the Yap Development Loan Fund (the Funds), administered by the Federated States of Micronesia Development Bank (the Bank), which comprise the respective statement of fiduciary net position as of December 31, 2014, and the related statement of changes in fiduciary net position for the year 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.

***Auditor's Responsibility***

Our responsibility is to express opinions 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 opinions.

***Opinions***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Investment Development Fund, the Pohnpei Development Loan Fund, and the Yap Development Loan Fund as of December 31, 2014, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Other Matters***

As discussed in Note 1 to the financial statements, the financial statements referred to above present only the respective financial position of the Investment Development Fund, the Pohnpei Development Loan Fund, and the Yap Development Loan Fund and are not intended to present fairly the financial position and results of operations of the Federated States of Micronesia Development Bank in conformity with accounting principles generally accepted in the United States of America.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated April 7, 2015, on our consideration of the Bank'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 financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Bank's internal control over financial reporting and compliance.

Deloitte & Touche LLP

April 7, 2015

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

Trust Funds
Statement of Fiduciary Net Position
December 31, 2014

| | IDF | PDLF | YDLF | Total |
|---|---|---|---|---|
| ASSETS | | | | |
| Cash and cash equivalents | $ 1,444,624 | $ - | $ 116,378 | $ 1,561,002 |
| Time certificates of deposit | - | - | 147,833 | 147,833 |
| Interest and other receivables | 4,990 | - | 623 | 5,613 |
| Loans receivable, net | 386,511 | - | 18,506 | 405,017 |
| Total receivables | 391,501 | - | 19,129 | 410,630 |
| | $ 1,836,125 | $ - | $ 283,340 | $ 2,119,465 |
| LIABILITIES AND NET POSITION | | | | |
| Liabilities: | | | | |
| Payable to FSMDB | $ 50,601 | $ - | $ 29,287 | $ 79,888 |
| Commitments | | | | |
| Net position: | | | | |
| Restricted | 386,511 | - | 18,506 | 405,017 |
| Unrestricted | 1,399,013 | - | 235,547 | 1,634,560 |
| Total net position | 1,785,524 | - | 254,053 | 2,039,577 |
| | $ 1,836,125 | $ - | $ 283,340 | $ 2,119,465 |

See accompanying notes to financial statements.

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

Trust Funds
Statement of Changes in Fiduciary Net Position
Year Ended December 31, 2014

| | IDF | PDLF | YDLF | Total |
|---|---|---|---|---|
| Additions: | | | | |
| Loan interest | $ 29,668 | $ - | $ 754 | $ 30,422 |
| Investment interest | 7,325 | - | 828 | 8,153 |
| Miscellaneous | - | 1,951 | 9 | 1,960 |
| Total additions | 36,993 | 1,951 | 1,591 | 40,535 |
| Deductions: | | | | |
| Recovery of loan losses | (37,867) | - | - | (37,867) |
| Investment management fee | 250,000 | - | - | 250,000 |
| Miscellaneous | 782 | - | - | 782 |
| Total deductions | 212,915 | - | - | 212,915 |
| Change in net position | (175,922) | 1,951 | 1,591 | (172,380) |
| Net position at beginning of year | 1,961,446 | 735,580 | 252,462 | 2,949,488 |
| Distributions | - | (737,531) | - | (737,531) |
| Net position at end of year | $ 1,785,524 | $ - | $ 254,053 | $ 2,039,577 |

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, 2014

(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 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 United States. The IDF is administered by the Bank in a Trust capacity on behalf of the FSM National Government and its four States.

PDLF and YDLF are administered by the Bank in a Trust capacity. All loan decisions are made by executives of the respective state governments as these funds represent local appropriations designated to be loaned for development purposes. During the year ended December 31, 2014, all assets and net equity of PDLF were returned to the Pohnpei State Government.

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 and Time Certificates of Deposit

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

Loans and Allowance for Loan Losses

Loans receivable are stated at unpaid principal balance less the allowance for loan losses and are reserved in net position as restricted net position.

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.

**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, 2014

(1) Purpose and Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended December 31, 2014, the Funds implemented the following pronouncements:

- 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. 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 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 has not yet determined the effect of implementation of this statement on the financial statements of the Funds.

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 has not yet determined the effect of implementation of this statement on the financial statements of the Funds.

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.

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, 2014

(2) Deposits

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.

(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.

Custodial credit risk is the risk that in the event of a bank failure, the Funds' deposits may not be returned to them. 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.

**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, 2014

(2) Deposits, Continued

As of December 31, 2014, the carrying amount and corresponding bank balances of the Funds' total cash and time certificates of deposit was $1,708,835. All of the bank balances are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. However, none of the balances were covered as the FSMDB have already exceeded the insurable limit per depositor. For purposes of FDIC insurance termination, funds held in trust are not differentiable with regular accounts held by FSMDB. 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, 2014.

(3) Loans Receivable

The following is a schedule of loans receivable as of December 31, 2014:

| | Loan Balance | Allowance | Net |
|---|---|---|---|
| YDLF | $ 18,506 | $ - | $ 18,506 |
| IDF | 5,479,396 | 5,092,885 | 386,511 |
| | $ 5,497,902 | $ 5,092,885 | $ 405,017 |

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

(4) Subsequent Events

In March 2015, Typhoon Maysak ravaged Chuuk and Yap causing severe damages. The ultimate impact on the Bank's branch offices and borrowers' ability for loan repayments is presently indeterminable.

Management has evaluated subsequent events through April 7, 2015, which is the date that the financial statements are available to be issued. Except for the above, there were no other material subsequent events that would require recognition or disclosure in the financial statements for the year ended December 31, 2014.

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# 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*

The Board of Directors
Federated States of Micronesia Development Bank:

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 Development Bank (the Bank), which comprise the statement of net position as of December 31, 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 April 7, 2015.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Bank'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 Bank's internal control. Accordingly, we do not express an opinion on the effectiveness of the Bank'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 any 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 Bank'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Bank in a separate letter dated April 7, 2015.

**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

April 7, 2015

Deloitte.

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# 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*

The Board of Directors
Federated States of Micronesia Development Bank:

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 Investment Development Fund, the Pohnpei Development Loan Fund, and the Yap Development Loan Fund, administered by the Federated States of Micronesia Development Bank (the Bank), which comprise the respective statement of fiduciary net position as of December 31, 2014, and the related statement of change in fiduciary net position for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 7, 2015.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Bank'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. Accordingly, we do not express an opinion on the effectiveness of the Bank'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 any 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 respective financial statements of the Investment Development Fund, the Pohnpei Development Loan Fund, and the Yap Development Loan Fund are free from material misstatement, we performed tests of their compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Bank in a separate letter dated April 7, 2015.

**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

April 7, 2015