FSM Development Bank

2022 Annual Report

Transforming Lives

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Contact Details:
FSM Development Bank
HQ Corporate Office
PO Box M
Kolonia, Pohnpei
Federated States of Micronesia (FM), 96941

(691)320-2840/5300

www.fsmdb.fm

LETTER TO THE SHAREHOLDERS:

Dear Shareholders,

We summarize below a general synopsis of the operations of the bank for the year ended December 31, 2022 and the financial statements for the periods ended December 2022 and December 2021.

It's difficult to find a single great headline describing the year 2022. We went into 2022 with great hopes that things in the banking sector were going to start improving. Because of prior year challenges caused by the pandemic, and the opening of the borders, coupled with FSM's own unique economic, social, and environmental challenges, we went into the year with much optimism for continuous growth. Towards the end of 2022, we felt that borrowers were still hesitant to borrow due to many factors. The world opened again and we were happy to once again be able to travel, meet with customers more freely, communicate face to face more with colleagues and counterparts, etc. However, in addition to FSM's internal challenges, our country was still affected by the limiting activities we have mentioned in years past. Under these sometimes-tough conditions, here we are, still able to operate. Indeed, we could say our 2022 performance is a testament to our strength and resiliency.

FSMDB ended the financial year in December 2022 with a net decrease in assets of $3.5 million, mainly due to mark to market losses in the U.S. financial investment market and a decrease in the book value of our Bank of FSM stocks. This was a tough year for the financial markets due to many influences within and outside of the US. Internally, FSMDB was able to generate sufficient revenue to cover all its expenses and yielded a small operating income of $23,870. Though we spent only 79% of our total budget, our revenue collections in terms of loan interest were below target, contributing to only reaching 71% of total projected revenues. Our total assets declined from $72 million in 2021 to $68 million due to above mentioned reductions in the US financial markets.

In terms of statistics regarding our lending/portfolio, FSMDB approved a total of 923 loans in 2022 totaling $22.5 million. Thirty-five loans amounting to $12 million were for business term loans, 22 for $3.4 million were for line of credits, 11 for $595,000 for residential loans, 751 in consumer loans for $5.4 million, and lastly 104 for $1 million in microloans, of which 39 of those loans were for women owned or women run small enterprises representing 34%. Total outstanding balance for our portfolio at the end of December 31, 2022 was at $45.2 million.

FSMDB has and continues to experience first-hand our ability to adapt to our own nation's challenges as well as global challenges. We continue to look for ways that enable sustainable economic development over the entire nation, stimulating economic growth and transforming the livelihoods of people in our country. We are hopeful for good changes that are forthcoming for the FSM…changes that involve new compact funding arrangements; and benefits from recently becoming accredited by the GCF (Green Climate Fund. We believe the FSM can benefit from access, though the bank, to environment friendly and climate resiliency & climate mitigation funding from GCF.

And lastly, we conclude by expressing our thanks to shareholders for their assistance, our employees who work hard to make our operations continue, our Board of Directors for their continued wisdom and guidance, but most especially our customers – the people we work hand-in-hand with to transform lives. FSMDB will continue to remain steadfast in our mandate to be a key contributor to the sustainable economic development of the FSM. We are pleased to be your institution you can continue to rely on – **to transform your lives.**

Sincerely,

Anna Mendiola	Sihna Lawrence
President/CEO	Chairwoman, Board of Directors

ABOUT THE BANK:

Establishment:

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 operations in 1980 with the establishment of lending in 1982. In 1994, the enabling law that created the Bank was amended to reorganize the structure of the Bank into a corporation. The bank's headquarters is located in the State of Pohnpei, the capital of the FSM. The Bank also has branch offices in the other three FSM states of Chuuk, Kosrae and Yap and an online presence at **www.fsmdb.fm**.

Initially, the primary function of the Bank was 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. The Bank in 2008 created its residential home loan program to help locals build or renovate homes. In 2019, this residential home loan program transitioned into an energy efficiency home loan program, from what originally was a 2015 grant to the Bank from the International Union for Conservation of Nature Resources (IUCN) with emphasis on energy efficiency, cost savings, and home comfort.

Consumer lending began in 2011 to help generate revenue, which has grown over the years. In 2021, through grant funding from the Asia Development Bank and in collaboration with the FSM Government, the bank introduced its Micro/Small loan program to budding entrepreneurs and existing small businesses.

The FSM Development Bank is a key player in the development of the private sector in the Federated States of Micronesia that enjoys the confidence of the national and state leaders, its customers, and stakeholders. The Bank has been growing organically for the past 17 years, maintaining its status as a viable lending institution.

Vision:

To be Micronesia's Premiere Development Finance Partner and Leading Catalyst for Transforming FSM Sustainable Development.

Mission:

To facilitate sustainable development of FSM through strategic partnership with our stakeholders, delivering financial products and services for the benefit of the people of FSM.

Core Values:

- ***Customer satisfaction*** – through the provision of professional customer service;
- ***Teamwork*** – through mutual respect, cooperation, loyalty, commitment, collaboration and dedication;
- ***Integrity***– through observing the highest standards of ethics, accountability, transparency and to treat all stakeholders equitably;
- ***Inclusiveness*** – through undertaking economic development that enhances the life of all the people of FSM whilst sensitive to the protection of the environment and respectful of our culture and heritage;
- ***Excellence*** – through achieving the highest level of performance by continuously improving our skills and business practices;
- ***Resilience*** – we remain positive and respond constructively to challenges;
- ***Diversity*** – through ensuring equal opportunity for all, no matter our differences.

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. All the FSM states are provided representation on the Bank's Board of Directors.

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	3,236,883	$32,368,830

BOARD OF DIRECTORS:

The Board of Directors 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 for the period under review were as follows:

Chairman – Sihna Lawrence (Pohnpei State), Vice Chairman – Peter Aten (Chuuk State)

Members: Kun Sigrah (Kosrae State), Vacant (Yap State)

Elina Akinaga (FSM Government), Sos John (FSM Government),

Anna Mendiola (CEO & Ex-Officio)

MANAGEMENT:

FSMDB is managed by a senior management team of corporate officers comprised of a President/Chief Executive Officer (CEO), Senior Vice President/Chief Operating Officer (COO), a Senior Vice President/Chief Credit Officer, and finally a Chief Financial Officer (CFO). Assisting the senior management team are a General Counsel, an Internal Auditor, and a team of managers. For the period under review, the Bank's corporate officers comprised of the following:

President/CEO:	***Anna H. Mendiola***
Senior Vice President/COO:	***Fabian S. Nimea***
Senior Vice President/CCO:	***Alik J. Alik***
Chief Financial Officer:	***Brandon J. Tara***

*****

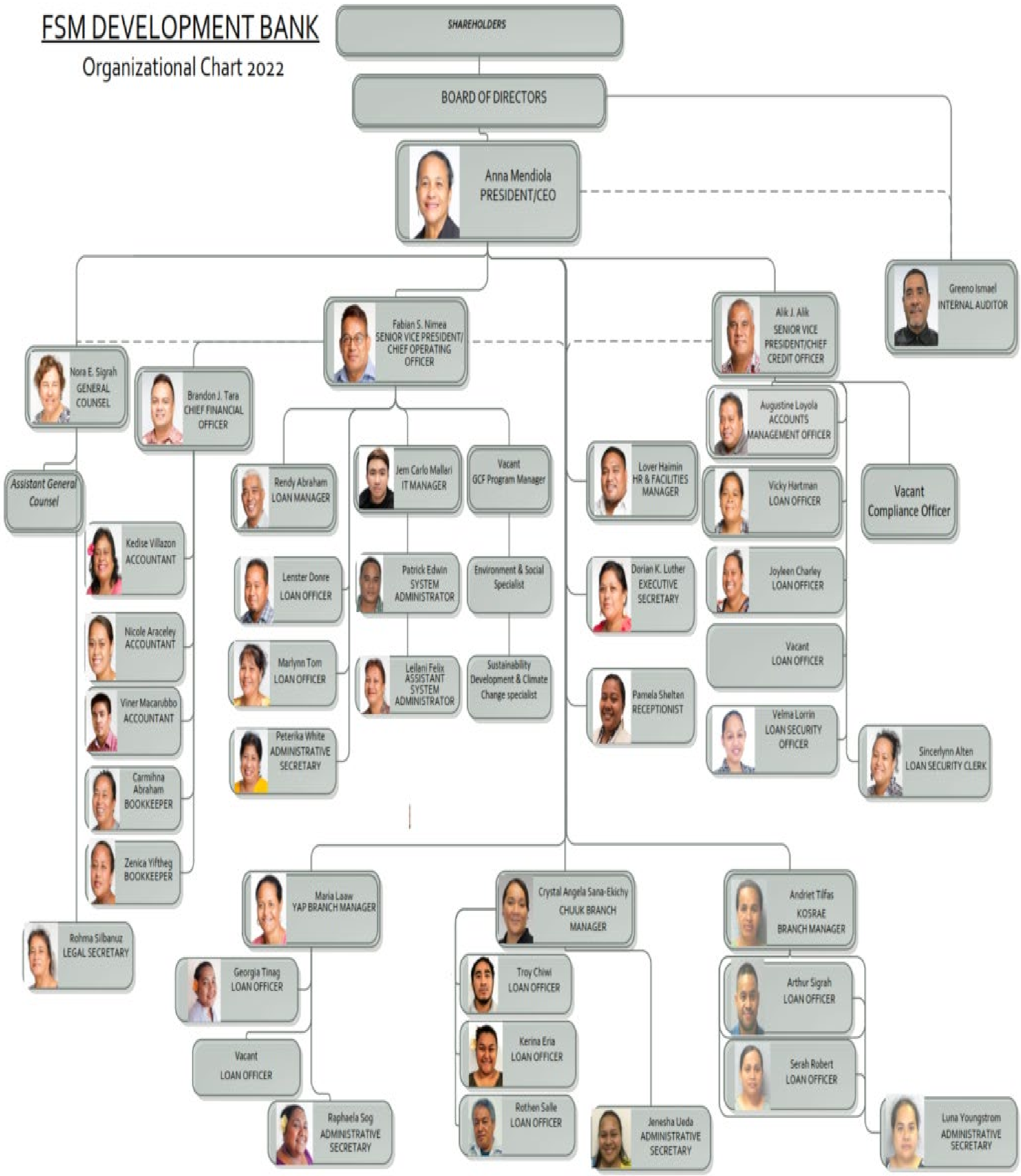
General Counsel, Nora Sigrah, Esq.

Internal Auditor, Greeno Ismael

Appreciation to former staff:

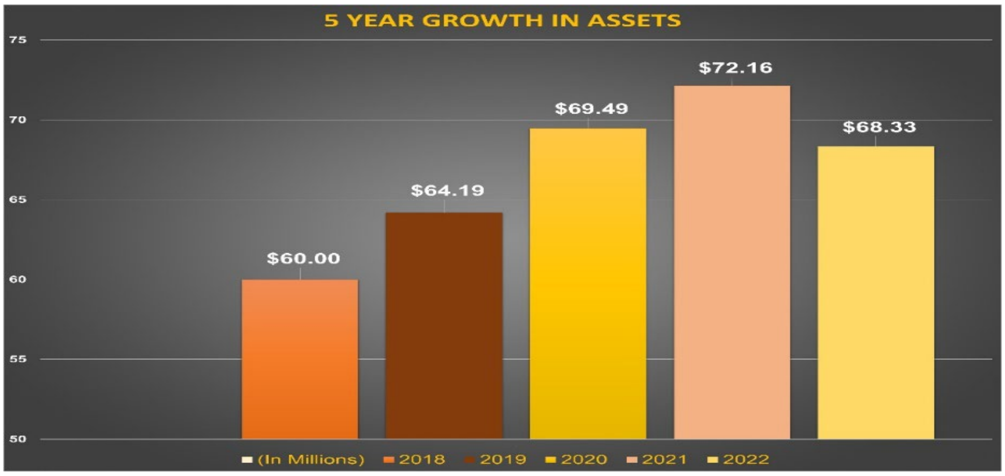
We would like to acknowledge former Human Resources & Facilities Manager Lover Haimin, Senior Loan Officer Mary Lou Yatilman, and Branch Manager Kathy Gisog who left the Bank in 2022 to pursue other endeavors, and we wish them well! Former Yap State Board member Maria Laaw joined the bank as manager for the Yap branch.

Organizational Chart:



MANAGEMENT REPORT:

FSMDB's goals are to grow its assets by strategically ensuring that more than enough revenues are generated to cover operating expenses and surplus earnings are retained to increase assets. To ensure future growth and sustainability, within the last five years, the Bank grew its assets from $60 MM beginning in 2018 to over $72 million in 2021. In 2022, the decline in net assets amounting to $(3.5) MM was mainly due to mark to market losses in the U.S. financial investment market and a decrease in the book value of our Bank of FSM stocks, reducing the $72 million in 2021 to $68 million in 2022. Despite this shortcoming, out net operating income was positive $23K, which means, we were able to cover all of our operating expenses with the revenues we generated for the year. Consequently, the losses in investments in 2022 caused the decline in ROA and ROE. But the Bank has been able to streamline expenses, especially during these challenging times, to maintain financial stability.



LENDING UPDATES:

923 new loans were approved in 2022 totaling $22.48 million. Out of that total, $12.04 went to commercial loans, $3.4 million to lines of credit, $595K for residential loans, and $5.43 million for consumer loans. As a whole, 73% represented commercial/business loans and 27% represented consumer loans. The breakdown of sectors is presented below.

Compared to 2021 when customers were weary to borrow due to the limited movements and somewhat closed borders, plus constraints due to the ban on the recruitment of skilled workers from the Philippines, the year 2022 saw more customers returning to the bank for business following the opening of our borders, the improvements/changes in international shipping schedules, many more constructions projects, and other movements in the economy.

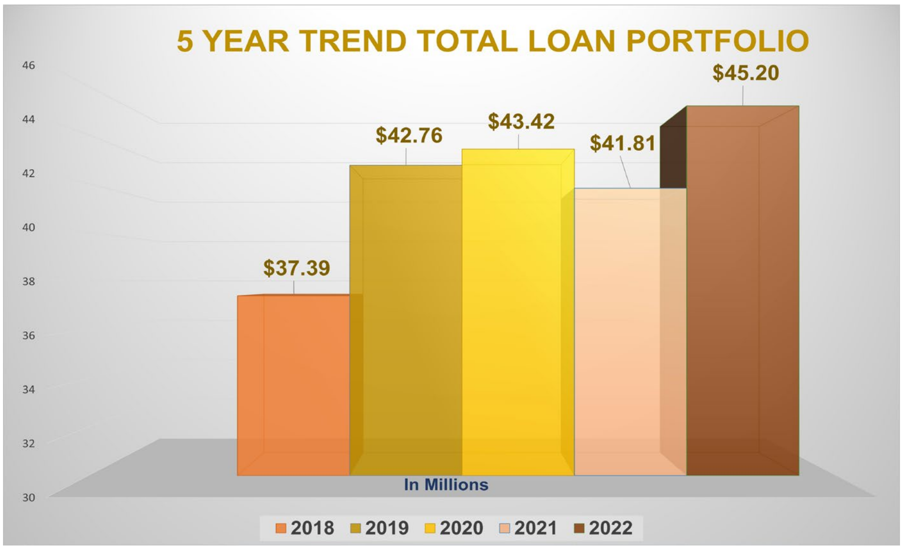
Bank loans provide the opportunity to create jobs, generate income, produce uses of local resources, reduce imports and increase exports, and provide other essential services. The Bank has been growing organically for the past 17 years, maintaining its status as a viable lending institution.

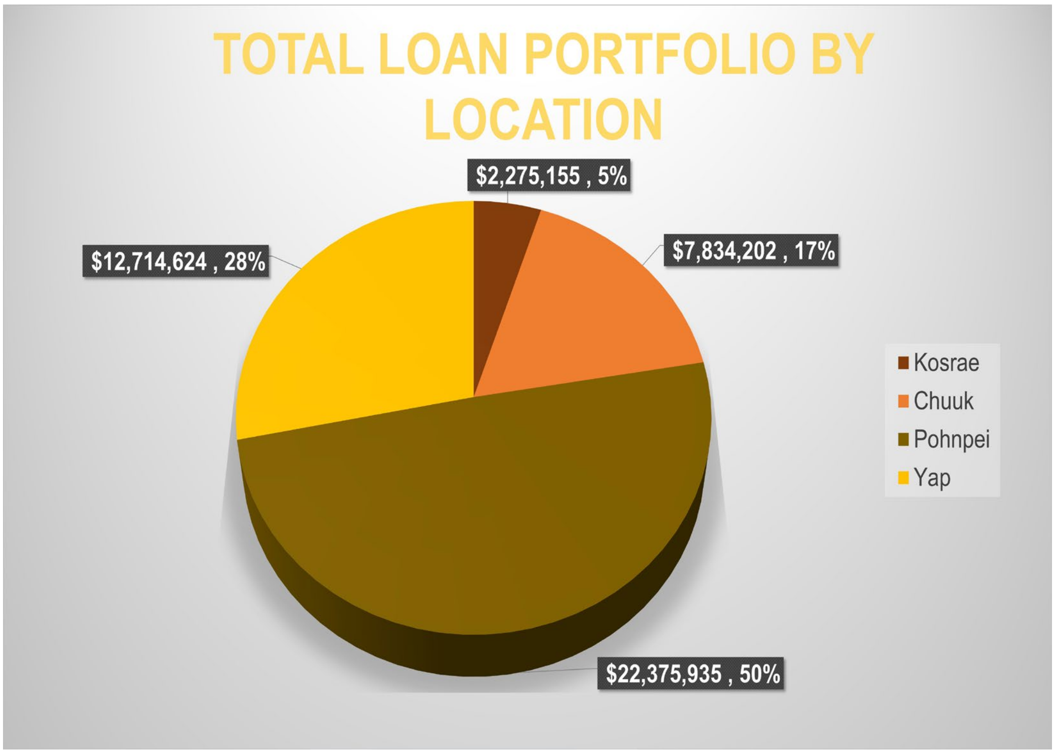
2022 Loan Approvals	Stats	Amount	%
Agri/Forestry/Fishing	6	$ 6,059,228	27%
Services	12	964,257	4%
Manufacturing	1	10,000	0%
Real Estate	7	2,545,522	11%
Wholesale/Retail	23	2,828,867	13%
Tourism	0	-	0%
Transportation	5	127,974	1%
Construction/Mining	3	2,901,810	13%
Consumer & Home Loans	762	6,028,772	27%
Micro/Small Enterprises	104	1,010,068	4%
TOTAL	923	$ 22,476,498	100%

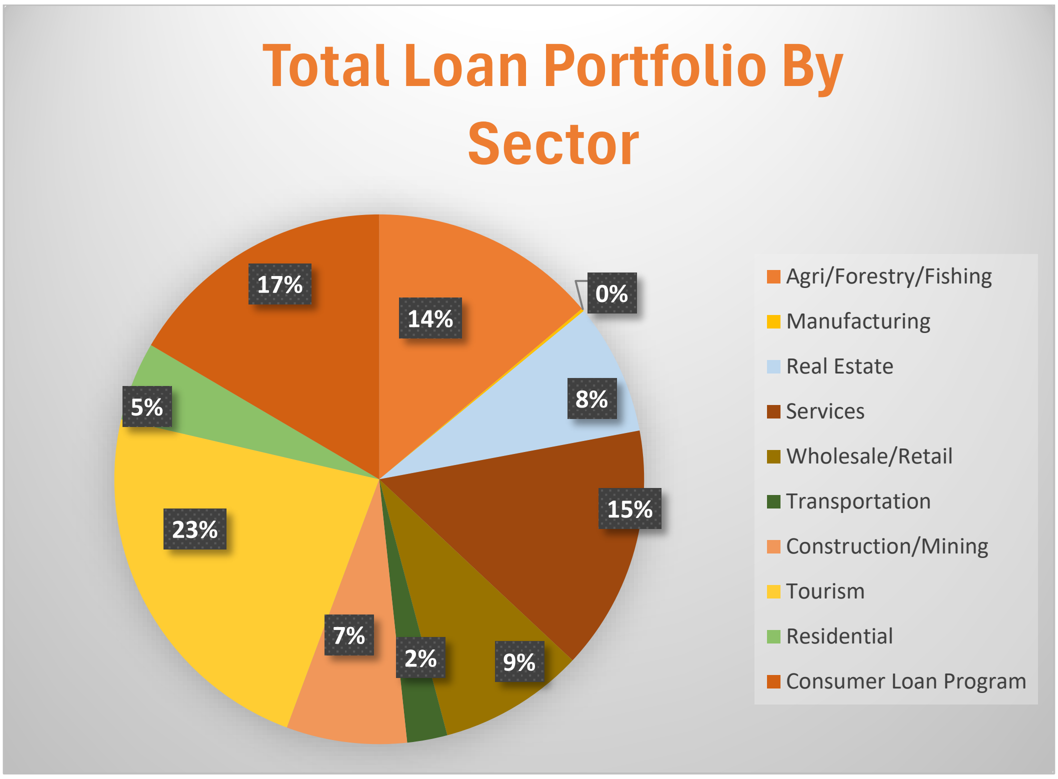
2022 Micro/Small Loans	Stats	Amount	%
Agri/Forestry/Fishing	35	$ 350,665.00	35%
Tourism	27	252,073	25%
Services	3	12,527	1%
Real Estate	1	30,000	3%
Wholesale/Retail	35	284,783	28%
Transportation	3	80,020	8%
TOTAL	104	$ 1,010,068	100%

Micro/Small Loans: 34% approved to women run or women owned businesses

Total Outstanding Loan Portfolio as of December 31, 2022			
		In Millions	
Sector	Stats	Amount	%
Agri/Forestry/Fishing	87	$ 6.26	14%
Manufacturing	31	0.08	0%
Real Estate	25	3.62	8%
Services	99	6.75	15%
Wholesale/Retail	221	4.01	9%
Transportation	36	1.11	2%
Construction/Mining	11	3.33	7%
Tourism	12	10.38	23%
Residential	62	2.18	5%
Consumer Loan Program	1,378	7.48	17%
TOTAL		$ 45.20	100%




TOTAL LOAN PORTFOLIO BY LOCATION
$2,275,155 , 5%
$7,834,202 , 17%
$12,714,624 , 28%
$22,375,935 , 50%
Kosrae
Chuuk
Pohnpei
Yap


Total Loan Portfolio By Sector
17%
14%
0%
8%
5%
15%
23%
7%
2%
9%
Agri/Forestry/Fishing
Manufacturing
Real Estate
Services
Wholesale/Retail
Transportation
Construction/Mining
Tourism
Residential
Consumer Loan Program

Project Photos: Gas Station, Hotel, Local produce & fish vendors, Catering & Takeout, Laundromat, Retail Store

RESIDENTIAL LOANS:

Our Home Loan program aims to help FSM consumers construct new homes, renovate or improve existing homes with emphasis on energy efficiency, costs savings and comfort. The year 2022 saw 11 approved residential loans: 6 of them new constructions and 5 of them home renovations. At the conclusion of 2022, FSMDB had assisted over 92 families in the FSM build or renovate comfortable homes, which represents a loan portfolio of $2.18 million.

Thank you for relying on FSMDB to *transform your lives.*

This annual report is printed in gloss paper using local resources, and distributed to our shareholders, board of directors, partner organizations, and the FSM leadership in limited published copies as well as uploaded on our website, consistent with our commitment to reduce our carbon footprint. Please visit our website at www.fsmdb.fm for more information.

Financial Statements, Required Supplementary Information, and Supplementary Information

Federated States of Micronesia Development Bank

(A Component Unit of the Federated States of Micronesia National Government)

Year ended December 31, 2022
with Report of Independent Auditors

Building a better working world

Federated States of Micronesia Development Bank
(A Component Unit of The Federated States of Micronesia National Government)

Year Ended December 31, 2022

Contents

Ernst & Young LLP
231 Ypao Road
Suite 201 Ernst & Young Building
Tamuning, Guam 96913

Tel: +1 671 649 3700
Fax: +1 671 649 3920
ey.com

Report of Independent Auditors

Board of Directors
Federated States of Micronesia Development Bank:

Report on the Audit of the Financial Statements

Opinions

We have audited the financial statements of the business-type activities and fiduciary activities of Federated States of Micronesia (FSM) Development Bank (the Bank), a component unit of the FSM National Government, as of and for the year ended December 31, 2022, and the related notes to the financial statements, which collectively comprise the Bank's basic financial statements as listed in the table of contents.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and fiduciary activities of the Federated States of Micronesia Development Bank as of December 31, 2022, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinions

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States *(Government Auditing Standards)*. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Bank and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Bank's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we

- Exercise professional judgment and maintain professional skepticism throughout the audit.

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.

- Obtain an understanding of internal control relevant to the audit 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 Bank's internal control. Accordingly, no such opinion is expressed.

- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.

- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Bank's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 6 be presented to supplement the financial statements. Such information is the responsibility of management and, 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 GAAS, 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.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Bank's basic financial statements. The Schedule of European Investment Bank December 2018 and August 2010 Finance Contract Ratios, As Amended March 2021 on page 34 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The 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 GAAS. In our opinion, the Schedule of European Investment Bank December 2018 and August 2010 Finance Contract Ratios, As Amended March 2021 is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2023, 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 solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Bank's 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.

Ernst + Young LLP

October 31, 2023

The following is a discussion and analysis of the Federated States of Micronesia Development Bank's (FSMDB or the Bank) financial performance for the fiscal year ended December 31, 2022.

It's difficult to find a single great headline describing the year 2022. We went into 2022 with great hopes that things in the banking sector were going to start improving. Because of prior year challenges caused by the pandemic, and the opening of the borders, coupled with FSM's own unique economic, social, and environmental challenges, we went into the year with much optimism for continuous growth. Towards the end of 2022, we felt that borrowers were still hesitant to borrow due to many factors. The world opened again and we were happy to once again be able to travel, meet with customers more freely, communicate face to face more with colleagues and counterparts, etc. However, in addition to FSM's internal challenges, our country was still affected by the limiting activities we have mentioned in years past. Under these sometimes-tough conditions, here we are, still able to operate. Indeed, we could say our 2022 performance is a testament to our strength and resiliency.

FSMDB ended the financial year in December 2022 with a net decrease in assets of $3.5 million, mainly due to mark to market losses in the U.S. financial investment market and a decrease in the book value of our Bank of FSM stocks. This was a tough year for the financial markets due to many influences within and outside of the US. Internally, FSMDB was able to generate sufficient revenue to cover all its expenses and yielded a small operating income of $23,870. Though we spent only 79% of our total expected budget, our revenue collections in terms of loan interest were below target by 35%, contributing to only reaching 71% of total projected revenues. Our total assets declined from $72 million in 2021 to $68 million due to the reduction in the Bank's investments.

Summary Statements of Net Position

	2022	2021
Assets	$68,332,009	$72,161,441
Liabilities:		
Liabilities	3,298,473	3,585,425
Net Position:		
Net investment in capital assets	1,318,800	1,428,805
Unrestricted	63,714,736	67,147,211
Total net position	65,033,536	68,576,016
Total liabilities and net position	$68,332,009	$72,161,441

Our long-term debt to the European Investment Bank (EIB) bank at the end of 2022 decreased to $3 million down from an original total of $4.3 million. Borrowed funds represents only 4% of total assets. For additional information concerning the Bank's debt, please refer to note 8 in the financial statements.

Regarding the bank's lending/portfolio, in 2022, FSMDB approved a total of $22.4 million in new loans. In this figure, $15.4 million for business loans, $595,000 for residential loans, $5.4 million for consumer loans, and lastly $1 million for microloans. Total outstanding balance for our portfolio at the end of December 31, 2022 was at $45.6 million.

Summary Statements of Revenues, Expenses and Changes in Net Position

	2022	2021
Operating revenues	$ 3,117,469	$ 3,194,395
Provision for loan losses	(1,000,000)	(3,083,405)
Operating expenses	(2,093,599)	(1,806,242)
Earnings (loss) from operations	23,870	(1,695,252)
Non-operating (expense) revenues, net	(3,566,350)	4,859,478
Change in net position	(3,542,480)	3,164,226
Net position at beginning of year	68,576,016	65,411,790
Total assets	$65,033,563	$68,576,016

The two trust funds, the Investment Development Fund (IDF) and Yap Development Loan Fund (YDLF) that are under the bank's management have been inactive for the past year with no new loans approved. The total assets for each of these funds at the end of 2022 were $2,047,336 and $278,633 respectively.

Economic Outlook

Looking ahead in the near future, FSMDB continues to experience first-hand how our ability to adapt to our own nation's challenges as well as global challenges. We continue to look for ways that enable sustainable economic development over the entire nation, stimulating economic growth and transforming the livelihoods of people in our country.

With the final stages of the compact negotiations and the new expected financial provisions in the Compact kicking in, the Bank intends to work with all of its stakeholders, including the government, to confront any future challenges, whatever they may be. As a partner, the Bank anticipates to be more proactive in developing ideas into viable business proposals and providing entrepreneurial training to help improve the management of successful businesses in the FSM. Lastly, the bank is hopeful to become accredited to the Green Climate Fund (GCF) to access for the benefit of the country environment-friendly and climate mitigation/climate resiliency funding.

Moving forward, despite many challenges, the bank remains committed to working with our government leaderships and with the private sector community as in prior years, to continue to advocate for a better business environment that would encourage more investment which then leads to job creation for our people and revenue source for the governments.

Contacting Financial Management

The Management's Discussion and Analysis report is intended to provide information concerning known facts and conditions affecting the Bank's operations. This financial report is designed to provide a general overview of the Bank's finances and to demonstrate the Bank's accountability for the funds it receives and expends.

Management's Discussion and Analysis for the year ended December 31, 2021 is set forth in the Bank's report on the audit of financial statements, which is dated November 9, 2022. That Discussion and Analysis explains the major factors impacting the 2021 financial statements and can be viewed at the Bank's website at www.fsmdb.fm or Office of the Public Auditor's website at www.fsmopa.fm.

For additional information about this report, please contact Ms. Anna Mendiola, President/Chief Executive Officer, P.O. Box M, Pohnpei, FM 96941 or visit the website at www.fsmdb.fm.

Statement of Net Position

December 31, 2022

Assets	
Cash and cash equivalents	$ 5,810,211
Time certificates of deposit	2,981,450
Investments	13,703,962
Interest and other receivables	329,233
Loans receivable, net of allowance for loan losses	38,580,333
Equity investment	5,605,440
Prepaid expenses	2,580
Depreciable capital assets, net	1,318,800
Total assets	$68,332,009
Liabilities and Net Position	
Liabilities:	
Accounts payable	$ 93,624
Long-term debt	3,003,816
Credit life payable	21,466
Payable to trust funds	46,732
Unearned grant revenues	132,835
Total liabilities	3,298,473
Commitments and contingencies	
Net position:	
Net investment in capital assets	1,318,800
Unrestricted	63,714,736
Total net position	65,033,536
Total liabilities and net position	$68,332,009

See accompanying notes.

Federated States of Micronesia Development Bank
(A Component Unit of The Federated States of Micronesia National Government)

Statement of Revenues, Expenses, and Changes in Net Position

Year ended December 31, 2022

Operating revenues:	
Interest income on loans	$ 2,657,025
Loan fees	279,544
Rental	29,700
Interest income on time certificates of deposit	4,836
Miscellaneous	146,364
Total operating revenues	3,117,469
Provisions for loan losses	1,000,000
Net operating revenues	2,117,469
Operating expenses:	
Interest expense	79,391
General and administrative expenses:	
Personnel services	1,318,562
Depreciation	165,960
Contractual services	86,222
Rent	85,020
Retirement plan contributions	74,522
Utilities	55,462
Communication	47,859
Branch automation	32,346
Travel	30,854
Supplies	28,900
Equipment	20,367
Community development	11,030
Staff relations	10,341
Fuel, oil and petroleum	10,160
Repair and maintenance	8,538
Insurance	6,876
Miscellaneous	21,189
Total general and administrative expenses	2,014,208
Earnings from operations	23,870
Nonoperating expenses: Investment losses, net	(3,566,350)
Change in net position	(3,542,480)
Net position at beginning of year	68,576,016
Net position at end of year	$65,033,536

See accompanying notes.

Statement of Fiduciary Net Position

December 31, 2022

	Investment Development Fund (IDF)	Yap Development Loan Fund (YDLF)	Total
Assets			
Cash and cash equivalents	$ ---	$127,412	$ 127,412
Time certificates of deposit	1,969,455	151,221	2,120,676
Receivable from FSMDB	72,950	---	72,950
Interest and other receivables	4,931	---	4,931
Total assets	$2,047,336	$278,633	$2,325,969
Liabilities and Net Position			
Liabilities:			
Payable to FSMDB	$ 6,111	$ 20,107	$ 26,218
Unrestricted net position	2,041,225	258,526	2,299,751
Total liabilities and net position	$2,047,336	$278,633	$2,325,969

See accompanying notes.

Statement of Fiduciary Revenues, Expenses and Changes in Fiduciary Net Position

Year Ended December 31, 2022

	Investment Development Fund (IDF)	Yap Development Loan Fund (YDLF)	Total
Additions:			
Investment interest	$ 154	$ 689	$ 843
Miscellaneous	920	---	920
Change in net position	1,074	689	1,763
Net position at beginning of year	2,040,151	257,837	2,297,988
Net position at beginning of year	$2,041,225	$258,526	$2,299,751

See accompanying notes.

Federated States of Micronesia Development Bank

(A Component Unit of The Federated States of Micronesia National Government)

Statement of Cash Flows

Year ended December 31, 2022

Cash flows from operating activities:	
Cash received from customers	$ 3,102,140
Cash paid to suppliers for goods and services	(462,305)
Cash paid to employees for services	(1,318,562)
Net cash provided by operating activities	1,321,273
Cash flows from noncapital financing activities:	
Principal repayment of long-term debt	(334,014)
Net transfers in from trust funds	2,143
Interest paid	(104,433)
Net cash used in noncapital financing activities	(436,304)
Cash flows from capital and related financing activities:	
Acquisition of capital assets	(55,955)
Cash flows from investing activities:	
Loan origination and principal disbursements, net	(5,294,483)
Increase in time certificates of deposit	(2,976,614)
Purchases of investments, net	(171,524)
Dividends received	245,251
Net cash used in investing activities	(8,197,370)
Net change in cash and cash equivalents	(7,368,356)
Cash and cash equivalents at beginning of year	13,178,567
Cash and cash equivalents at end of year	$ 5,810,211
Reconciliation of earnings from operations to net cash provided by operating activities:	
Earnings from operations	$ 23,870
Adjustments to reconcile earnings from operations to net cash provided by operating activities:	
Provision of loan losses	1,000,000
Depreciation	165,960
Others	74,554
(Increase) decrease in assets:	
Interest and other receivables	(10,493)
Prepaid expenses	(2,580)
Increase (decrease) in liabilities:	
Accounts payable	51,641
Credit life payable	7,146
Unearned grant revenues	11,175
Net cash provided by operating activities	$ 1,321,273

See accompanying notes.

1. Organization and Summary of Significant Accounting Policies

Organization

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 FSM. 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, 2022, the Bank has issued 3,236,883 shares to the FSM National Government (98.80%), Chuuk State (0.92%) and Kosrae State (0.28%). 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.

Primary Government Financial Statements

The primary government financial statements consist of the statement of net position, statement of revenues, expenses, and changes in net position and statement of cash flows. Fiduciary activities are not included in the primary government financial statements.

Fiduciary Fund Financial Statements

Separate financial statements are provided for fiduciary funds. Fiduciary financial statements include assets, liabilities and activities of the Investment Development Fund (IDF) and the Yap Development Loan Fund (YDLF), for which the Bank has been legally designated to control but the Bank itself is not a beneficiary.

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; and (5) contribute to the furtherance of close economic relations with the United States.

YDLF is administered by the Bank in a Trust capacity. All loan decisions are made by executives of the respective state governments.

1. Organization and Summary of Significant Accounting Policies, continued

Fund Structure and Basis of Accounting

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 primary government financial statements of the Bank are not obligations of the FSM National Government unless specifically authorized by the FSM National Government. To date, no such authorizations have been made.

The 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 accounting policies of the primary government financial statement and fiduciary fund financial statements conform to accounting principles generally accepted in the United Statements of America (GAAP), as applicable to governmental entities, specifically proprietary funds. The Bank utilizes the flow of economic resources measurement focus. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, requires assets and liabilities of enterprise funds be presented in a classified format to distinguish between current and long-term assets and liabilities. The Bank is a government-owned bank. Banks do not present a classified statement of net position because current assets are not matched with current liabilities. The statements of net position of the Bank present assets and liabilities in order of their relative liquidity, rather than in a classified format.

Accounting 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.

1. Organization and Summary of Significant Accounting Policies, continued

Cash and Cash Equivalents

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

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

Investments

Investments and related investment earnings are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the date as of which the fair value of an asset or liability is determined.

An equity investment in the common stock of Bank of the FSM (investee) is stated at the net asset value (NAV). The NAV is used as a practical expedient to estimate fair value. The NAV is determined based on the total shareholders' equities reported by the investee.

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 and recorded as reduction or addition to operating revenues.

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.

1. Organization and Summary of Significant Accounting Policies, continued

Capital Assets

Capital 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 capital 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.

Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (deduction of net position) until then. As of December 31, 2022, the Bank has no items that qualify for reporting in this category.

Deferred Inflows of Resources

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (additions to net position) until then. As of December 31, 2022, the Bank has no items that qualify for reporting in this category.

Unearned Grant Revenues

Unearned grant revenues represent amounts received from grant and contract sponsors that have not yet been earned.

Compensated Absences

Earned but unused annual leave is paid to employees upon termination of their employment. Accordingly, vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. It is the policy of the Bank to record the cost of sick leave when leave is actually taken and an expense is actually incurred. Accordingly, no liability is recorded for non-vesting accumulating rights to receive sick pay benefits, which approximated $179,000 at December 31, 2022.

1. Organization and Summary of Significant Accounting Policies, continued

Taxes

The Bank exists and operates solely for the benefit of the public and shall be exempted from any State or Municipal taxes or assessments on any of its property, operations or activities. The Authority shall be liable for employees' contributions to the National Social Security System or other employees' benefits of the State or FSM National Governments, if any, in such manner as provided by law.

Net position

Net position represents the residual interest in the Bank's assets and deferred outflows of resources after liabilities and deferred inflows of resources are deducted and consist of two sections:

> 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.
>
> 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.

Operating and Non-operating Revenues and Expenses

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, which is lending. Operating expenses include the cost to provide services, including cost of funds, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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.

1. Organization and Summary of Significant Accounting Policies, continued

Recently Adopted Accounting Pronouncements

In June 2017, GASB issued Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and as inflows of resources or outflows of resources recognized based on the payment provisions of the contract. The adoption of GASB Statement No. 87 during the year ended December 31, 2022 did not result in a material effect on the accompanying financial statements.

In May 2019, GASB issued Statement No. 91, *Conduit Debt Obligations*. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. The adoption of GASB Statement No. 91 during the year ended December 31, 2022 did not have an effect on the accompanying financial statements.

In January 2020, GASB issued Statement No. 92, *Omnibus 2020*. The requirements of this Statement will enhance comparability in the application of accounting and financial reporting requirements and will improve the consistency of authoritative literature. More comparable reporting will improve the usefulness of information for users of state and local government financial statements. This Statement addresses a variety of topics and includes specific provisions about leases; reporting of intra-entity transfers of assets between a primary government employer and a component unit defined benefit pension plan or defined benefit other postemployment benefit (OPEB) plan; applicability of Statement no. 73 and 84 for postemployment benefits, measurement of liabilities (and assets, if any) related to asset retirement obligations (AROs) in a government acquisition; reporting by public entity risk pools for amounts that are recoverable from reinsurers or excess insurers; reference to nonrecurring fair value measurements of assets or liabilities in authoritative literature and terminology used to refer to derivative instruments. The adoption of GASB Statement No. 92 during the year ended December 31, 2022 did not have an effect on the accompanying financial statements.

1. Organization and Summary of Significant Accounting Policies, continued

Recently Adopted Accounting Pronouncements, continued

In June 2020, GASB issued Statement No. 97, *Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans – an amendment of GASB Statements No. 14 and No. 84, and a supersession of GASB Statement No. 32*. The primary objectives of this Statement are to (a) increase consistency and comparability related to the reporting of fiduciary component units in circumstances in which a potential component unit does not have a governing board and the primary government performs the duties that a governing board typically would perform; (b) mitigate costs associated with the reporting of certain defined contribution pension plans, defined contribution OPEB plans, and employee benefit plans other than pension plans or OPEB plans as fiduciary component units in fiduciary fund financial statements; and (c) enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans. The adoption of GASB Statement No. 97 during the year ended December 31, 2022 did not have an effect on the accompanying financial statements.

In October 2021, GASB issued Statement No. 98, *The Annual Comprehensive Financial Report*. This Statement establishes the term annual comprehensive financial report and its acronym ACFR. That new term and acronym replace instances of comprehensive annual financial report and its acronym in generally accepted accounting principles for state and local governments. Management does not believe that this Statement, upon implementation, will have a material effect on the financial statements. The adoption of GASB Statement No. 98 during the year ended December 31, 2022 did not have an effect on the accompanying financial statements.

In April 2022, GASB issued Statement No. 99, *Omnibus 2022*, which provides clarification guidance on several of its recent statements that addresses different accounting and financial reporting issues identified during implementation of the new standards and during the GASB's review of recent pronouncements. GASB Statement No. 99:

- Amends guidance in GASB Statement No. 24, *Accounting and Financial Reporting for Certain Grants and Other Financial Assistance*, requiring that the accounting and financial reporting of Supplemental Nutrition Assistance Program (SNAP) transactions should follow the provisions of GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions, as amended.

- Requires disclosures related to nonmonetary transactions, in the notes to financial statements, of the measurement attribute(s) applied to the assets transferred rather than the basis of accounting for those assets.

1. Organization and Summary of Significant Accounting Policies, continued

Recently Adopted Accounting Pronouncements, continued

- Provides guidance on accounting for pledges of future revenues when resources are not received by the pledging government. The guidance addresses the process of blending a component unit created to issue debt on behalf of a primary government when that component unit is required to be presented as a blended component unit.

- Provides clarification of provisions in GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, as amended,* related to the focus of the government-wide financial statements.

- Provides terminology updates related to certain provisions of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, and terminology used in GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments.*

- GASB Statement No. 93, *Replacement of Interbank Offered Rates*, which amended GASB Statement No. 53 to address transition away from the London Interbank Offered Rate (LIBOR). GASB Statement No. 99 extends the period during which the LIBOR is considered an appropriate benchmark interest rate to when LIBOR ceases to be determined using methodology in place as of December 31, 2021.

These provisions of GASB Statement No. 99 were effective upon issuance and implementation did not have a material effect on the accompanying financial statements.

Upcoming Accounting Pronouncements

In March 2020, GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The primary objective of this Statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements. This Statement also provides guidance for accounting and financial reporting for availability payment arrangements. Management does not believe that this statement, upon implementation, will have a material effect on the financial statements. GASB Statement No. 94 will be effective for fiscal year ending December 31, 2023.

In May 2020, GASB issued Statement No. 96, *Subscription-Based Information Technology Arrangements*. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset—an intangible asset—and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA. To the extent relevant, the standards for SBITAs are based on the standards established in Statement No. 87, *Leases*, as amended. GASB Statement No. 96 will be effective for fiscal year ending December 31, 2023.

1. Organization and Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In April 2022, GASB issued Statement No. 99, *Omnibus 2022*, which include guidance that are effective for future periods:

- Modifies guidance in GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, to bring all guarantees under the same financial reporting requirements and disclosures effective for fiscal year ending December 31, 2024.

- Provides guidance on classification and reporting of derivative instruments within the scope of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, effective for fiscal year ending December 31, 2024.

- Provides clarification of provisions in GASB Statement No. 87 related to the determination of the lease term, classification of a lease as a short-term lease, recognition and measurement of a lease liability and a lease asset, and identification of lease incentives effective for fiscal year ending December 31, 2023.

- Provides clarification of provisions in GASB Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*, related to (a) the determination of the public-private and public-public partnership (PPP) term and (b) recognition and measurement of installment payments and the transfer of the underlying PPP asset. Effective for fiscal year ending December 31, 2023.

- Provides clarification of provisions in GASB Statement No. 96, *Subscription-Based Information Technology Arrangements*, related to the subscription-based information technology arrangement (SBITA) term, classification of a SBITA as a short-term SBITA, and recognition and measurement of a subscription liability. Effective for fiscal year ending December 31, 2023.

- Modifies accounting and reporting guidance in GASB Statement No. 53 related to termination of hedge. Guidance is effective for fiscal year ending December 31, 2023.

1. Organization and Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In June 2022, GASB issued Statement No. 100, *Accounting Changes and Error Corrections – An Amendment of GASB Statement No. 62*. The primary objective of this Statement is to enhance accounting and financial reporting requirements for accounting changes and error corrections to provide more understandable, reliable, relevant, consistent, and comparable information for making decisions or assessing accountability. The requirements of this Statement will improve the clarity of the accounting and financial reporting requirements for accounting changes and error corrections, which will result in greater consistency in application in practice. In turn, more understandable, reliable, relevant, consistent, and comparable information will be provided to financial statement users for making decisions or assessing accountability. In addition, the display and note disclosure requirements will result in more consistent, decision useful, understandable, and comprehensive information for users about accounting changes and error corrections. GASB Statement No. 101 will be effective for fiscal year ending December 31, 2023.

In June 2022, GASB issued Statement No. 101, *Compensated Absences*. The objective of this Statement is to better meet the information needs of financial statement users by updating the recognition and measurement guidance for compensated absences. That objective is achieved by aligning the recognition and measurement guidance under a unified model and by amending certain previously required disclosures. The unified recognition and measurement model in this Statement will result in a liability for compensated absences that more appropriately reflects when a government incurs an obligation. In addition, the model can be applied consistently to any type of compensated absence and will eliminate potential comparability issues between governments that offer different types of leave. The model also will result in a more robust estimate of the amount of compensated absences that a government will pay or settle, which will enhance the relevance and reliability of information about the liability for compensated absences. GASB Statement No. 101 will be effective for fiscal year ending December 31, 2024.

The Bank is currently evaluating the effects the above upcoming accounting pronouncements might have on its financial statements

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:

(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.

2. Deposits and Investments, continued

(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.

2. Deposits and Investments, continued

A. Deposits, continued

As of December 31, 2022, the carrying amount of the Bank's total cash and cash equivalents and time certificates of deposit, including fiduciary funds, was $11,039,749, and the corresponding bank balances were $11,735,396, which were all maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2022, bank deposits in the amounts of $4,281,614, are subject to the FDIC insurance limit. 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, 2022.

B. Investments

As of December 31, 2022, investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	$ 4,786,707
Equity securities:	
Domestic equities	7,463,082
Shares in a mutual fund	1,454,173
	$13,703,962

As of December 31, 2022, investments in domestic fixed income securities are as follows:

		Investment maturities (in Years)				
	Moody's Credit Rating	Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Government securities:						
U.S. Treasury Notes	Aaa	$ ---	$852,263	$ 550,155	$ ---	$1,402,418
U.S. Government agencies:						
Fannie Mae Pool	Not rated	---	---	---	1,619,909	1,619,909
Freddie Mac Group	Not rated	---	---	---	1,136,013	1,136,013
Corporate bonds	A1	---	91,725	166,193	---	257,918
Corporate bonds	A2	---	---	256,564	---	256,564
Corporate bonds	A3	---	---	113,885	---	113,885
		$ ---	$943,988	$1,086,797	$2,755,922	$4,786,707

2. Deposits and Investments, continued

B. Investments, continued

The Bank categorizes its fair value measurements within the fair value hierarchy established by GASB Statement No. 72. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The Bank has the following recurring fair value measurements as of December 31, 2022:

	December 31, 2022	Fair Value Measurements Using Level 1	Level 2	Level 3
Fixed income:				
U.S. Treasury obligations	$ 1,402,418	$ ---	$1,402,418	$ ---
U.S. Government agencies	2,755,921	---	2,755,921	---
Corporate notes	628,367	---	628,367	---
Total fixed income	4,786,707	---	4,786,707	---
Equity securities:				
U.S. equities	7,463,082	7,463,082	---	---
Mutual fund shares	1,454,173	1,454,173	---	---
Total investments at fair value	$13,703,962	$ 8,917,255	$4,786,707	$ ---

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, 2022.

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, 2022, the Bank's investment in securities of U.S Treasury Notes and agency obligations of the Fannie Mae Pool and Freddie Mac Group constituted 10%, 12% and 8%, 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 December 31, 2022, the equity investment in Bank of the FSM represents 225,001 common shares and approximately 24% ownership interest. Total shareholders' equity reported by Bank of the FSM approximated $5,605,440 at December 31, 2022.

4. Loans Receivable

A summary of loans receivable at December 31, 2022 follows:

Unpaid principal balance	$45,568,130
Allowance for loan losses	(6,987,798)
	$38,580,333

At December 31, 2022, estimated total principal collections and loan maturities in 2023 approximated $12,034,000.

Movements in the allowance for loan losses during the year ended December 31, 2022, are as follow:

Balance at beginning of year	$ 7,521,719
Provision for loan losses	1,000,000
Loans charged off	(2,347,365)
Loan recoveries from previously charged off loans	813,444
Balance at end of year	$ 6,987,798

At December 31, 2022, $2.73 million of the allowance is related to one Yap loan, which was fully provided due to management's assessment of remote collectability.

In an effort to constructively work with borrowers affected by the COVID-19 pandemic, the Bank initiated temporary programs beginning in February 2020 to allow for loan repayment deferrals for eligible borrowers. At December 31, 2022, twenty-seven loans with total outstanding balances of $11.8 million, were under the deferral program, which ended June 30, 2022. In December 2020, the FSM National Government enacted Public Law No. 21-211 (the Act) towards providing financial assistance to the private sector to mitigate the impact of the COVID-19 pandemic. In accordance with the Act, the Bank received $220,411 for interest payments for eligible loans during the year ended December 31, 2022.

In August and September 2023, the Bank received an insurance settlement for a sunken ship for a borrower totaling $4,470,806, which was applied to the outstanding loan with an outstanding loan of $5.6 million as of December 31, 2022.

5. Capital Assets

A summary of capital assets as of December 31, 2022, is as follows:

	Beginning January 1, 2022	Additions/ Transfers	Deletions/ Transfers	Ending December 31, 2022
Land	$ 7,889	$ ---	$ ---	$ 7,889
Building	1,674,348	---	---	1,674,348
Computers and software	676,045	140,628	---	816,673
Vehicles	246,934	3,327	---	250,261
Office furniture, fixtures and equipment	15,658	---	---	15,658
	2,620,874	143,955		2,764,829
Less accumulated depreciation	(1,280,069)	(165,960)		(1,446,029)
	1,340,805	(22,005)		1,318,800
Software installation in progress	88,000	---	(88,000)	---
Capital assets, net	$1,428,805	$(22,005)	$(88,000)	$1,318,800

6. Related Party Transactions

As of December 31, 2022, the Bank has direct loans with outstanding balances of $358,952, to Bank employee and family members and project loans extended to three component units of FSM governments totaling $7,409,317. 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.

During the year ended December 31, 2022, the Bank recognized interest income of $220,411, which was granted by the FSM National Government (see Note 4).

During the year ended December 31, 2021, the Bank received a $3,000,000 grant from the FSM National Government for the FSM Health Expenditure and Livelihood Support Program which is supported by the Asian Development Bank Group. The grant is for the Bank to launch its micro and small business loans for the program for a total of $2,500,000. The loans are interest-free for the first two years for loans approved as of September 30, 2021 with subsequent loans bearing an interest of 3%. At December 31, 2022, total loans disbursed and outstanding balances under the loan program approximated $2,250,000 and $1,986,000, respectively.

7. Unearned Grant Revenues

During the year ended December 31, 2015, the Bank was awarded a $250,000 Home Energy Loan Program grant from the International Union for Conservation of Nature Resources (IUCN). $232,000 of the grant is to be awarded to the qualified borrowers for new loans to construct homes that demonstrate features and measures designed to conserve energy, reduce consumption of fossil fuels and enhance energy efficiency as principal reduction of loans, while the remaining $18,000 will be used by the Bank for renovations to improve energy efficiency. As of December 31, 2022, unearned grant revenue was $132,835. A grant extension was received during the year ended December 31, 2018.

8. Long-Term Debt

Direct Borrowings:

Long-term debt consists of the following at December 31, 2022:

Unsecured loans payable to European Investment Bank (EIB) under an August 2010 master finance contract of EUR 4 million:

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 principal 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.	$ 108,093
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 principal 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.	257,502
Unsecured loans payable to European Investment Bank (EIB) under a December 2018 master finance contract of USD 4 million:	
Drawn on March 9, 2020; original amount of $3,193,637, bearing interest fixed at 2,774%, and payable through semi-annual interest payment beginning on September 9, 2020 and principal installments of $138,854 beginning on March 9, 2021 through maturity on March 9, 2032.	2,638,221
	$3,003,816

8. Long-Term Debt, continued

Direct Borrowings, Continued:

Under the 2010 and 2018 Agreements, including Amendments dated March 2021, the EIB (or the "Lender") loans contain (1) a provision that in an event of default, the timing of repayment of outstanding amounts may become immediately due if: the capital to total assets ratio is not above 20%; nonperforming loans to total loans ratio exceeds certain ratios (effective 35% at December 31, 2022); provision for loan losses to nonperforming loans ratio is less than certain ratios (effective 80% at December 31, 2022), and (2) a provision that the Bank shall repay the loan or any part thereof, together with accrued interest and other accrued sums immediately, forthwith upon demand by the Lender if:

a. the Bank fails on due date to repay any part of the loan, to pay interest thereon or to make any other payment to the Lender;
b. if any information or document given to the Lender by the Bank or on its behalf is or proves to be incorrect, incomplete or misleading in any material respect;
c. the Bank is unable to pay its debts, or makes or seeks to make a composition with its creditors;
d. an order is made or an effective resolution is passed for the winding up of the Bank, or the Bank takes steps towards a substantial reduction in its capital, is declared insolvent or ceases or resolves to cease to carry on the whole or any substantial part of its business or activities;
e. an encumbrancer takes possession of, or a receiver, liquidator, administrator, administrative receiver or similar officer is appointed, whether by a court of competent jurisdiction or by any competent administrative authority or by any person, any part of the business or assets; if any distress, execution, sequestration, or other process is levied or enforced upon the property of the Bank and is not discharged or stayed within 14 days; or if any event occurs which is likely to jeopardize the servicing of the loan or adversely affect any security therefore;
f. if any other financial indebtedness is either not paid when due, or following any default in relation thereto, is capable of being declared due and payable prior to its scheduled maturity;
g. If the Bank is liable, by reason of any default, to be required to effect immediate prepayment of any loan granted to it by the Lender from the resources of the Bank or of the European Community;
h. If a material adverse change occurs, as compared to the Bank's condition at the time of the loan agreement;
i. If it is or becomes unlawful for the Bank to perform any of its obligation under the loan agreement.

At December 31, 2022, the Bank is not in compliance with the ratios of non-performing loans to total loans and the allowance for loan losses to non-performing loans requirements, including the March 2021 amendments. Management is working on obtaining a waiver from the Lender.

8. Long-Term Debt, continued

Direct Borrowings, Continued:

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

Year Ending December 31,	Principal	Interest	Total
2023	$ 394,140	$ 86,509	$ 480,649
2024	399,463	73,483	472,946
2025	405,709	60,214	465,923
2026	277,708	48,148	325,856
2027	277,708	40,444	318,152
Thereafter	1,249,088	86,666	1,335,754
	$3,003,816	$395,464	$3,399,280

Long-term debt changes during the year ended December 31, 2022 are as follows:

	Balance January 1,	Additions	Reductions	Balance December 31,	Due Within One Year
Loans payable	$3,337,830	$ ---	$(334,014)	$3,003,816	$394,140

9. 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 Administration. The Plan is a contributory plan in which the Bank matches 100% of the participants' contributions up to a maximum of 10% of the participant's annual salary, if the participant contributes 3% or more of 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, 2022 were $78,920. Total Plan assets as of December 31, 2022 were $1,496,980. Management is of the opinion that the Plan does not represent an asset or a liability of the Bank.

10. 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, 2022.

Loan Commitments

Undrawn balances on lines of credit and loan commitments for loans approved but undisbursed approximated $6,339,000 at December 31, 2022, of which $3,410,000 represent undisbursed funds on three loans.

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.

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 three operating leases for its State operating locations. These leases expire at varying dates through May 2031. Several of these leases provide options to renew upon expiration, based on renegotiated rates. Future minimum annual lease payments payable under the noncancellable leases are as follows:

Year ending December 31,	
2023	$ 53,220
2024	53,220
2025	49,770
2026	42,920
2027	45,420
Thereafter	94,300
	$338,850

10. Commitments and Contingencies, continued

Lease Commitments, continued

The Bank leases portions of its headquarters building under three separate agreements expiring through September 2025. Future minimum annual lease income under the noncancellable leases are as follows:

Year ending December 31,	
2023	$ 27,500
2024	20,700
2025	15,500
	$ 63,700

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

Total recorded lease expense and income under the aforementioned agreements amounted to $85,020 and $29,700, respectively, for the year ended December 31, 2022.

11. Risks and Uncertainties

On March 11, 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic and recommended containment and mitigation measures worldwide. In response, governments all over the world implemented actions which impacted the macroeconomic environment, increased economic uncertainty and reduced economic activities. The Bank's business and earnings are closely tied to the economies of the FSM. The impacts of travel restrictions and limited business orders have resulted in immediate adverse impact to some of the Bank's customers. During the year ended December 2020, the Bank granted temporary principal and interest payment relief for certain loans and received funds from the FSM National Government for interest payments (see Note 4). The Bank has further extended the loan deferral program during the year ended December 2021through June 30, 2022. The length of time such conditions will continue to exist as well as the significance of the impact to the Bank's ultimate realization of these underlying loans in accordance with their contractual terms is presently not determinable.

Supplementary Information

Federated States of Micronesia Development Bank
(A Component Unit of The Federated States of Micronesia National Government)

Schedule of European Investment Bank December 2018 and 2010 Finance Contract Ratios, As Amended March 2021

December 31, 2022

1) Ratio of Capital (paid in capital plus reserves) to total assets should be above 20%:

Total net position	$65,033,536
Total assets	$68,322,009
	95%

2) Ratio of non-performing loans, as defined, to total loans do not exceed 35%:

Total non-performing loan	$25,259,694
Total loans	$45,568,130
	55%

3) Ratio of allowance for loan losses to non-performing loans shall not be less than 80%:

Allowance for loan losses	$ 6,987,798
Total non-performing loans	$25,259,694
	28%

See accompanying notes.

Building a better
working world

Ernst & Young LLP
231 Ypao Road
Suite 201 Ernst & Young Building
Tamuning, Guam 96913

Tel: +1 671 649 3700
Fax: +1 671 649 3920
ey.com

Independent Auditor's Report On Internal Control Over Financial Reporting And On Compliance And Other Matters Based On An Audit Of Consolidated 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, 2022, 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 October 31, 2023.

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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify a certain deficiency in internal control, described in the accompanying Schedule of Findings and Responses, that we consider to be a significant deficiency as item 2022-001.

Report on 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*.

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.

Ernst + Young LLP

October 31, 2023