COLLEGE OF MICRONESIA-FSM

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

FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

SEPTEMBER 30, 2012 AND 2011

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INDEPENDENT AUDITORS' REPORT

Board of Regents
College of Micronesia-FSM:

We have audited the accompanying statements of net assets of the College of Micronesia-FSM (the College), a component unit of the Federated States of Micronesia (FSM) National Government, as of September 30, 2012 and 2011, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the College's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such financial statements present fairly, in all material respects, the financial position of the College of Micronesia-FSM as of September 30, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 12, 2013, on our consideration of the College'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 and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 10 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.

Deloitte + Touche LLP

June 12, 2013

Financial Statements Analysis

The College implemented the financial reporting standards for public colleges and universities in accordance with Governmental Accounting Standards Board (GASB) principles in fiscal year 2003. The funds are presented in consolidated financial statements as a whole, rather than on the fund basis used prior to fiscal year 2003. The adoption of the GASB principles provides financial reporting of the following three basic financial statements:

1. Statement of Net Assets (SNA)

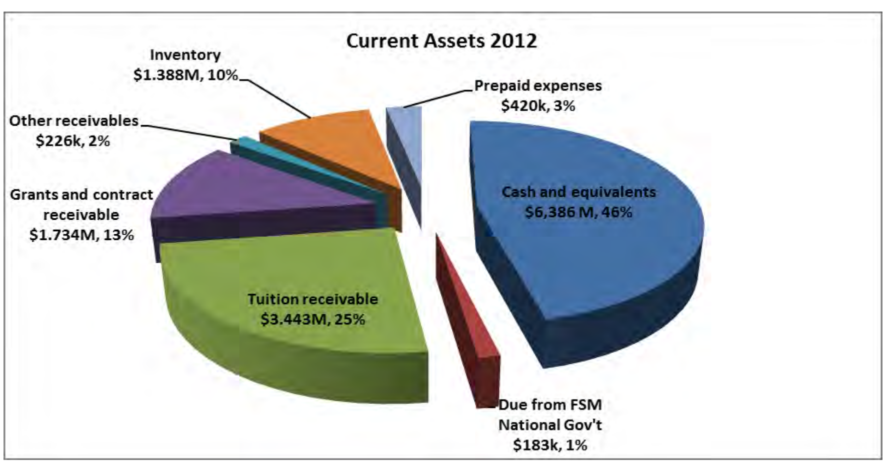
The SNA presents what the College owns (assets), owes (liabilities) and the net assets (the difference between total assets and total liabilities) at the end of the fiscal year. The net asset is one indicator of the current financial condition of the College, while the change in net assets is an indicator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

A Comparative Statement of Net Assets at September 30, 2012, 2011 and 2010 is summarized below:

	FY 2012 (In 000's)	FY 2011 (In 000's)	Difference (In 000's)	FY 2010 (In 000's)
Assets:				
Current assets	$ 13,780	$ 14,609	$ 829	$ 13,939
Noncurrent assets	13,566	13,107	(459)	13,563
Total assets	27,346	27,716	370	27,502
Liabilities:				
Current liabilities	4,289	4,555	(266)	4,420
Noncurrent liabilities	304	266	38	263
Total liabilities	4,593	4,821	(228)	4,683
Net assets	$ 22,753	$ 22,895	$ (142)	$ 22,819

The comparison of the statement of net assets for fiscal year 2012 with prior year indicates a slight decline in net assets by $142k.

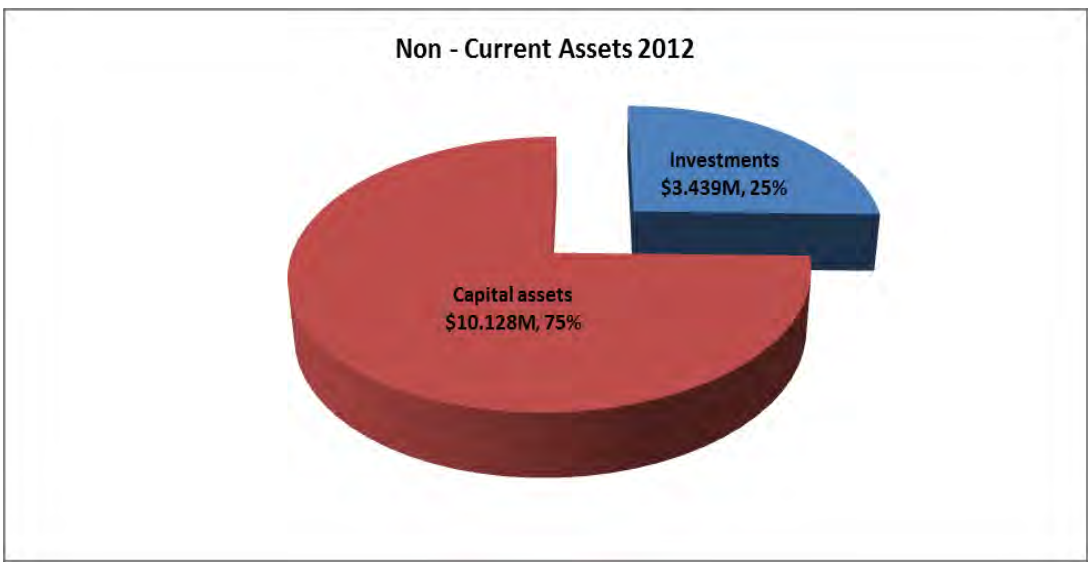
Current assets: The total current assets dropped by $829k, from $14.609 Million in fiscal year 2011 to $13.780 Million in current fiscal year 2012. Below is the composition of current assets for fiscal year 2012:



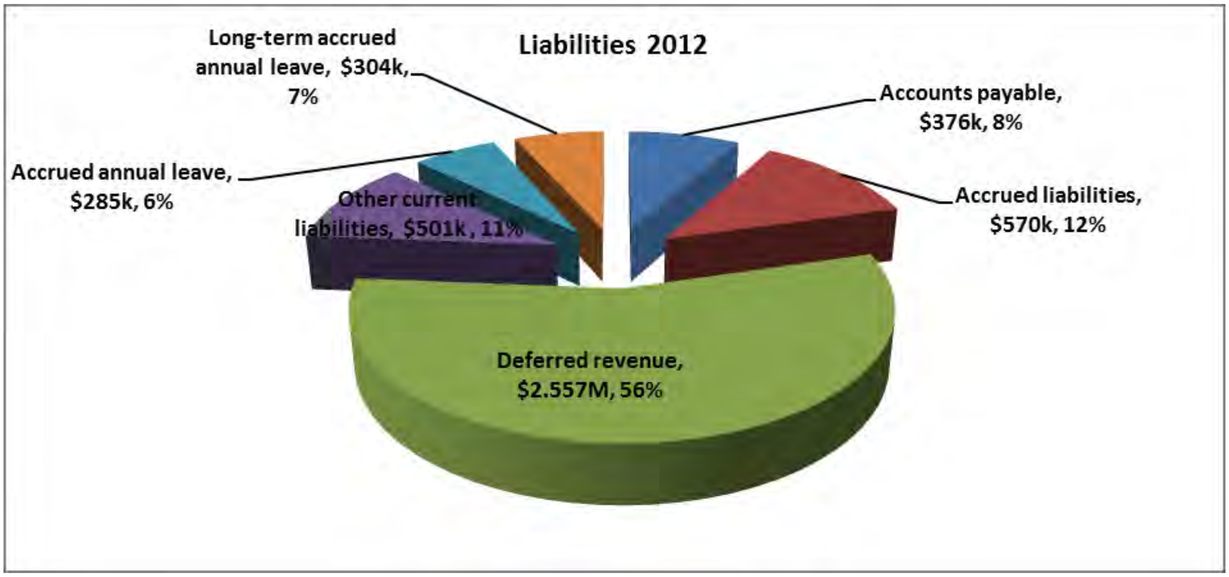
The net decrease by $829k in current assets consists of the following changes:

- Increase in inventory by $233k or 20%, from $1.155 Million to $1.388 Million;
- Increase in prepaid expenses by $132k or 46%, from $288k to $$420k;
- Increase in other receivables by $10k or 5%, from $216k to $226k;
- Decrease in cash and equivalents by $782k or 11%, from $7.168 Million to $6.386 Million;
- Decrease in grants and contract receivable by $243k or 12%, from $1.977 Million to $1.734 Million;
- Decrease in due from FSM National Government by $137k or 43%, from $320k to $183k;
- Decrease in tuition receivable by $42k or 1%, from $3.485 Million to $3.443 Million.

Noncurrent assets: The total noncurrent assets have increased by $459k from $13.107 Million in fiscal year 2011 to $13.566 Million in current fiscal year 2012. More than 99% of the increase or $457k is from investments. Below is the graph for the breakdown of noncurrent assets:



Liabilities: The liabilities dropped by $228k or 5%, from $4.821 Million to $4.593 Million. About 93% of the liabilities are current and 7% is non – current from long – term accrued annual leave. The details of the current liabilities and long – term liability are presented in the following graph:



The net decrease in liabilities consists of the following:

- Increase in accounts payable by $27k or 8%, from $349k to $376k;
- Increase in accrued annual leave by $15k or 6%, from $271k to $286k;
- Increase in deferred revenue by a $10k or less than 1%, from $2.547 Million to $2.557 Million;
- Decrease in other current liabilities by $274k or 35%, from $775k to $501k;
- Decrease in accrued liabilities by $43k or 7%, from $613k to $570k;
- Increase in non – current liability by $38k or 14%, from $266k to $304k.

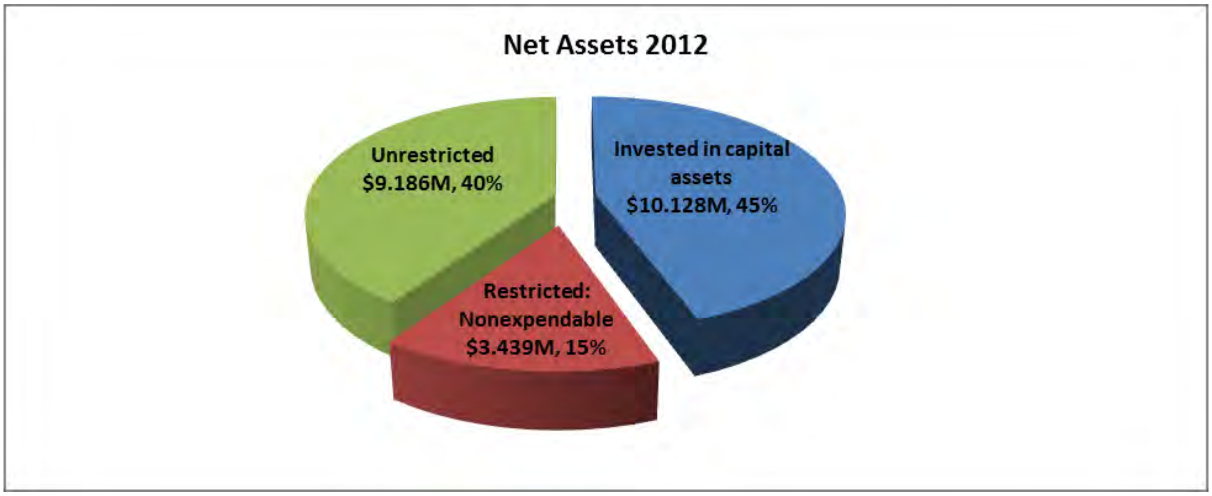
Net Assets: Net assets represent the residual interest in the College's assets after liabilities are deducted. The College's net assets for fiscal year 2011 are $22.895 Million which is slightly higher by $76k compared with $22.819 Million in fiscal year 2010. Below is the breakdown of the College's net assets categorized according to the reporting model of GASB:

	FY 2012 (In 000's)	FY 2011 (In 000's)	Difference (In 000's)	FY 2010 (In 000's)
Invested in capital assets	$ 10,128	$ 10,126	$ 2	$ 10,463
Restricted:				
Nonexpendable	3,439	2,982	457	3,100
Unrestricted	9,186	9,787	(601)	9,256
Total	$ 22,753	$ 22,895	$ (142)	$ 22,819

The net assets dropped by $142k consisting of the following changes:

1. The slight increase in capital assets by $2k or less than 1% represents the net amount from various improvement projects on facilities and procurement of equipment of $990k less the annual depreciation of $988k for the wear and tear of physical assets;
2. The increase in restricted assets by $457k or 15% represents the unrealized market gain and contributions for the endowment fund;
3. The decrease in unrestricted net assets by $601k or 6% represents the negative fund balance change after the non – cash item from the provision of bad debts. The net positive fund balance change before the non – cash item is $418k.

The graph for the breakdown of net assets for fiscal year 2012 is illustrated below:

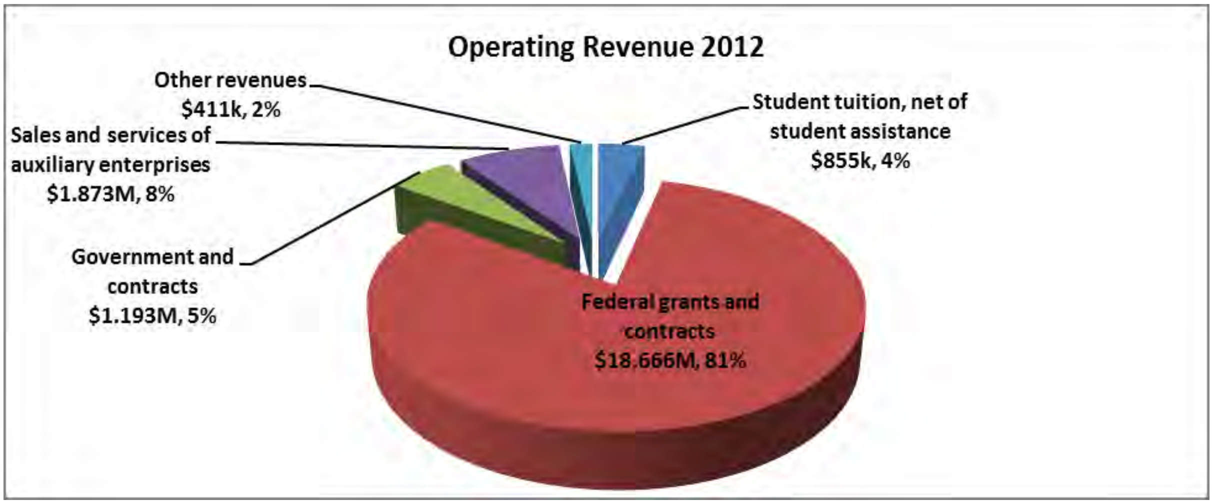


2. Statement of Revenues, Expenses and Changes in Net Assets (SRECNA)

The SRECNA provides information on the College's financial performance for the current fiscal year in terms of revenues and expenses. It presents the operating revenues and expenses and the corresponding net operating results, as well as non-operating revenues and expenses and net change in net assets. Below is the comparative summary of SRECNA for fiscal years ended September 30, 2012, 2011 and 2010:

	FY 2012 (In 000's)	FY 2011 (In 000's)	Difference (In 000's)	FY 2010 (In 000's)
Operating revenues	$ 22,998	$ 23,016	$ (18)	$ 25,137
Operating expenses	23,549	22,728	(821)	23,635
Operating income (loss)	(551)	288	(839)	1,502
Nonoperating revenue	409	(212)	621	226
Change in net assets	(142)	76	(218)	1,728
Net assets at beginning of year	22,895	22,819	76	21,091
Net assets at end of year	$ 22,753	$ 22,895	$ (142)	$ 22,819

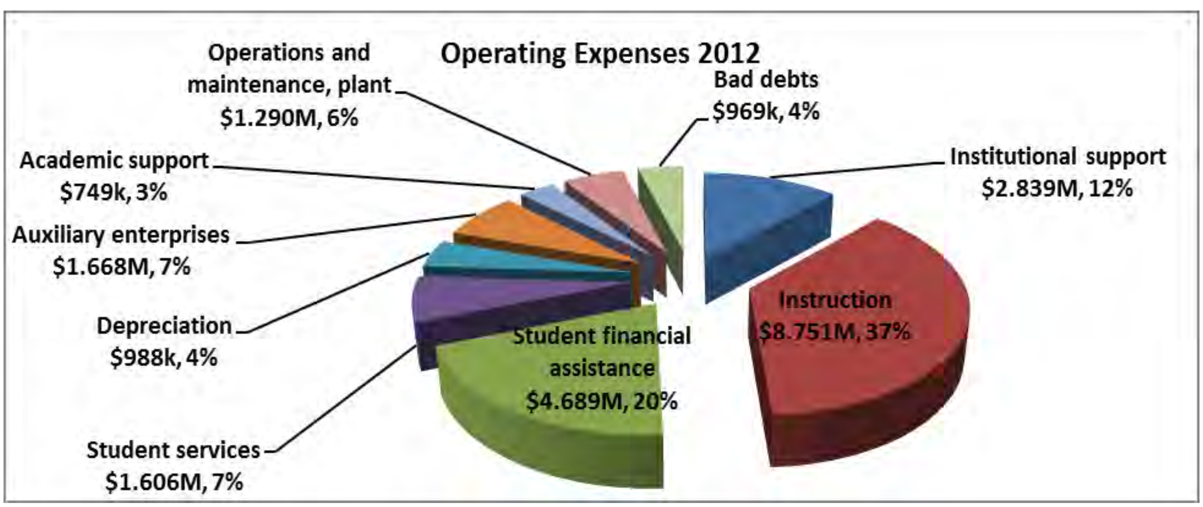
Operating revenues: The composition of the operating revenue amounting to $22.998 Million for fiscal year 2012 is presented in the following graph:



The gross operating revenue for fiscal year 2012 is basically at the same level with last year 2011. Below are the details of the changes for each classification of operating revenue:

- Increase in other revenues by $249k or 153%, from $162k to $411k;
- Increase in sales and services of auxiliary enterprises by $74k or 4%, from $1.799 Million to $1.873 Million;
- Increase in government and contracts by $44k or 4%, from $1.149 Million to $1.193 Million;
- Decrease in federal grants and contracts by $242k or 1%, from $18.908 Million to $18.666 Million; and
- Decrease in student tuition by $143k or 14%, from $998k to $855k.

Operating expenses: The College's operating expenses for fiscal year 2012 of $23.549 Million is presented in the following graph:



The total operating expenses indicated a net increase by $821k consisting of the net decrease from cash items of $33k, and total increase from non – cash items from depreciation and provision for bad debts of $854k. The details of the increases and decreases for cash items are as follows:

- Increase in operations and maintenance by $189k or 17%, from $1.101 Million to $1.290 Million;
- Increase in student services by $104k or 7%, from $1.502 Million to $1.606 Million;
- Increase in student financial assistance by $84k or 2%, from $4.605 Million to $4.689 Million;
- Increase in academic support by $47k or 7%, from $702k to $749k;
- Decrease in institutional support by $361k or -11%, from $3.200 Million to $2.839 Million;
- Decrease in instruction by 59k or -1%, from $8.810 Million to $8.751 Million.

For non – cash items, the changes are as follows:

- Increase in the provision of bad debts by $808k or 501%, from $161k to $969k;
- Increase in depreciation by $46k or 5%, from $942k to $988k.

Nonoperating revenues: The College endowment fund performance for the current fiscal year showed an unrealized market gain by $409k.

Change in net assets: The result of the College's financial performance for fiscal year 2012 is a net decrease in net assets by $142k. However, the results of operations provided a positive fund balance change in net assets by $418k before the provision for bad debts.

3. Statement of Cash Flows (SCF)

The SCF presents information about changes in the College' cash position using the direct method of reporting sources and uses of cash. The direct method reports all major cash inflows and outflows at gross amounts, differentiating these activities into cash flows arising from operating activities, noncapital financing, capital and related financing, and investing.

The SCF indicates a balance in cash and equivalents of $6.386 Million at end of fiscal year 2012. The fiscal year - end balance is lower by $781k or 11% compared with fiscal year 2011 balance of $7.167 Million.

Below is the summary Statement of Cash Flows:

	FY 2012 (In 000's)	FY 2011 (In 000's)	Difference (In 000's)	FY 2010 (In 000's)
Provided by operating activities	$ 256	$ 217	$ 39	$ 1,141
Used in capital and related financing activities	(990)	(605)	(385)	(434)
Used in investing activities	(47)	(93)	46	-
Net decrease in cash and equivalents	(781)	(481)	(300)	707
Cash and cash equivalents at beginning of year	7,167	7,648	(481)	6,941
Cash and cash equivalents at end of year	$ 6,386	$ 7,167	$ (781)	$ 7,648

The net reduction in cash and equivalents was from the operating loss for the current fiscal year.

Budget Information

The budgets are developed by departments, campuses and offices, and are approved by the Board. The budgets of the College include the following:

1. $10.139 Million – for the administration and management of the College wherein the sources of revenue are from tuition and fees of $7.339 Million, and $3.800 Million from the appropriation from FSM National Government from the Education Sector Grant of the Compact of Free Association II.
2. $655k – for the administration and management of the FSM – FMI at Yap State and 100% funded by FSM National Government.
3. $684k – for work study, supplemental education opportunity grant and teacher corps programs funded by Compact of Free Association II through FSM National Government.
4. $75k – for the operations of the Board of Regents of the College funded by FSM National Government.
5. $289k – for the operating expenditures of auxiliary enterprises funded from service charges.

Capital Assets and Long-term Debt Activity

At September 30, 2012, the College's net investment in capital assets is $10.128 Million, with gross amount of $27.227 Million for depreciable and non – depreciable assets, less accumulated depreciation of $17.099 Million. Depreciation for the current year totaled to $988k, and capital additions for furniture, equipment and vehicles totaled to $990k.

The College's long-term obligation is $304k representing the long – term portion of the accrued annual leave. The College provides accumulation of annual leave balance, wherein accumulated leave of not exceeding 240 hours shall be paid to the employee upon resignation/termination of employment. The college has no other long-term debt as of the end of fiscal year 2012.

Management's Discussion and Analysis for the year ended September 30, 2011, is set forth in the College's report on the audit of the financial statements, which is dated June 29, 2012, and that Discussion and Analysis explains the major factors impacting 2011 and 2010. To learn more about the College or to clarify matters in the Management's Discussion and Analysis, please contact Mr. Joseph M. Daisy, President or Danilo V. Dumantay, Comptroller at email addresses jdaisy@comfsm.fm or comptroller@comfsm.fm, respectively, or please write us at P.O. Box 159, Kolonia, Pohnpei, FSM 96941.

Economic Outlook

The College's sources of revenue are tuition and other fees from students receiving financial assistance from U.S. Federal Student Aid programs, and from the annual subsidy from FSM National Government. The subsidy is under the Education Sector Grant of the Compact of Free Association (ESG) between the Government of the United States of America and the Government of the FSM (Compact of Free Association II).

The U.S. Federal Student Aid programs are from the U.S. Department of Education under the U.S. Public Law 99 – 239. The U.S. Department of Education, Federal Student Aid renewed the Program Participation Agreement for the College through March 31, 2014. In school year 2011 – 2012, about 91% of the students at the college received financial assistance from U.S. Federal Student Aid programs. The college's projection of the percentage of students receiving financial assistance from U.S. Federal Student Aid programs will remain at the range of 85% to 95% in the next couple of years

The College is accredited by the Accrediting Commission for Community and Junior Colleges (ACCJC) of the Western Association of Schools and Colleges (WASC). On July 02, 2012, the college continued to be on "probation" status. The college submitted a combined Midterm and Follow-up report on March 15, 2013 proceeded by an ACCJC team visit on April 23 – 25, 2013. The college also submitted a Supplemental Report last month and appeared before the Commission on June, 2013 hearing at San Francisco, California. On July, 2013, the Commission will issue an "Action Letter" regarding the accreditation status of the college in the next six year. Currently, the college remains accredited and continues to receive and administer U.S. Federal Student Aid programs for eligible students.

The College is expected to receive continued support of funding assistance in succeeding years from the FSM National Government through the ESG and FSM local revenue. The level of support from ESG was reduced by $700k in fiscal year 2013, and will be reduced by $700k for each year for the next three years up to fiscal year 2016. Accordingly, the funding support from ESG was reduced from $3.800 Million to $3.100 Million in fiscal year 2013. For the next three years, the ESG level of $3.800 Million will be reduced by $1.400 Million in fiscal year 2014, by $2.100 Million in fiscal year 2015 and by $2.800 Million in fiscal year 2016 and beyond. The FSM Government provided its commitment to absorb the funding decrements from ESG fund through the local revenue of the FSM. On May 30th Congress Resolution, the FSM Congress provided the funding assistance of $1.400 Million to cover the decrement from ESG for fiscal year 2014.

The College Five – Year Financial Plan (5YFP) provided a structured tuition fee increases for three consecutive fiscal years from 2014 to 2016. On January, 2013 board meeting, the board approved the fiscal year 2014 budget that provides additional revenues from tuition fee increase by $10 per credit, from $105 to $115, and facility fee of $50 to $150 per student effective fall 2013. For the next fiscal years 2015 and 2016, the tuition fee will likewise increase by an additional $10 per credit for each fiscal year.

The College has completed its Integrated Educational Master Plan which has taken into consideration program prioritization and cost savings measures. The college's Five-Year Integrated Educational Master Plan is linked to its Five-Year Financial Plan. These plans have given the college a clear picture of its financial outlook for the next five years.

The College implemented a reorganizational structure with a new compensation model. The new structure and compensation model is expected to address the challenges of the college. The administration is in the process of reviewing the reporting system of the new structure. The college continues to review and assess the new structure for improvement and efficiency.

The College's endowment fund started in 1997, has the goal of growing in size to provide the long-term financial stability of the College. The board and administration started soliciting assistance from businesses, private individuals and governments to generate the annual fund raising target of the endowment fund. Fundraising efforts through college alumni, annual founding day activities, on campuses student fundraising events contribute to the growth of the endowment fund. The college organized the COM-FSM Foundation along with a new Board of Directors to serve as a fundraising vehicle for the college to secure its future long term funding. This new initiative is expected to boost the fund raising activities for the endowment fund.

COLLEGE OF MICRONESIA-FSM
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Net Assets
September 30, 2012 and 2011

ASSETS	2012	2011
Current assets:		
Cash and cash equivalents	$ 6,385,567	$ 7,167,689
Due from FSM National Government	182,993	319,799
Tuition receivable, net	3,443,380	3,485,235
Grants and contracts receivable, net	1,734,449	1,977,107
Other receivables, net	225,801	216,069
Inventory	1,388,192	1,155,571
Prepaid expenses	419,568	287,649
Total current assets	13,779,950	14,609,119
Noncurrent assets:		
Investments	3,438,961	2,981,912
Capital assets:		
Nondepreciable capital assets	1,455,685	1,455,685
Capital assets, net of accumulated depreciation	8,672,024	8,670,002
Total noncurrent assets	13,566,670	13,107,599
Total assets	$ 27,346,620	$ 27,716,718
LIABILITIES AND NET ASSETS		
Current liabilities:		
Accounts payable	$ 375,893	$ 349,360
Accrued liabilities	570,005	613,280
Accrued annual leave, current portion	285,580	270,503
Deferred revenue	2,556,902	2,547,086
Other current liabilities	501,090	775,194
Total current liabilities	4,289,470	4,555,423
Noncurrent liabilities:		
Long-term portion of accrued annual leave	303,820	266,184
Total liabilities	4,593,290	4,821,607
Commitments and contingencies		
Net assets:		
Invested in capital assets	10,127,709	10,125,687
Restricted:		
Nonexpendable	3,438,961	2,981,912
Unrestricted	9,186,660	9,787,512
Total net assets	22,753,330	22,895,111
Total liabilities and net assets	$ 27,346,620	$ 27,716,718

See accompanying notes to financial statements.

COLLEGE OF MICRONESIA-FSM
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2012 and 2011

	2012	2011
Operating revenues:		
Student tuition and fees	$ 8,224,997	$ 8,169,566
Less: Scholarship discounts and allowances	(7,370,291)	(7,171,774)
	854,706	997,792
Federal grants and contracts	18,666,048	18,907,617
Government grants and contracts	1,192,803	1,148,951
Sales and services of auxiliary enterprises	1,873,502	1,798,834
Other revenues	411,542	162,495
Total operating revenues	22,998,601	23,015,689
Less bad debts	(969,320)	(161,196)
Net operating revenues	22,029,281	22,854,493
Operating expenses:		
Institutional support	2,838,993	3,199,944
Instruction	8,751,543	8,810,218
Student financial assistance	4,688,553	4,604,912
Student services	1,605,684	1,501,833
Depreciation	988,117	942,211
Auxiliary enterprises	1,667,815	1,704,703
Academic support	749,454	702,074
Operations and maintenance, plant	1,290,002	1,100,696
Total operating expenses	22,580,161	22,566,591
Operating (loss) income	(550,880)	287,902
Nonoperating revenues (expenses):		
Net investment income (loss)	409,099	(211,516)
Change in net assets	(141,781)	76,386
Net assets:		
Net assets at beginning of year	22,895,111	22,818,725
Net assets at end of year	$ 22,753,330	$ 22,895,111

See accompanying notes to financial statements.

COLLEGE OF MICRONESIA-FSM
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Cash Flows
Years Ended September 30, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Grants and contracts	$ 20,188,604	$ 20,227,605
Auxiliary services	1,873,502	1,798,834
Other receipts	401,810	38,146
Payments to employees for salaries and benefits	(8,282,247)	(8,116,767)
Payments to suppliers and others	(13,925,702)	(13,730,523)
Net cash provided by operating activities	255,967	217,295
Cash flows from capital and related financing activities:		
Purchases of capital assets	(990,139)	(605,017)
Cash flows from investing activities:		
Purchase of investments	(47,950)	(93,157)
Net change in cash and cash equivalents	(782,122)	(480,879)
Cash and cash equivalents at beginning of year	7,167,689	7,648,568
Cash and cash equivalents at end of year	$ 6,385,567	$ 7,167,689
Reconciliation of operating (loss) income to net cash provided by operating activities:		
Operating (loss) income	$ (550,880)	$ 287,902
Adjustments to reconcile operating (loss) income to net cash provided by operating activities:		
Depreciation	988,117	942,211
Bad debts	969,320	161,196
Due from FSM	136,806	488,747
Tuition receivable	(904,417)	(1,224,496)
Grants and contracts receivable	242,658	34,643
Other receivables	(9,732)	(124,349)
Inventories	(255,669)	(531,089)
Prepaid expenses	(131,919)	44,268
Accounts payable	26,534	107,519
Accrued liabilities	9,438	83,251
Deferred revenue	9,815	(125,650)
Other current liabilities	(274,104)	73,142
Net cash provided by operating activities	$ 255,967	$ 217,295

See accompanying notes to financial statements.

(1) Organization

The College of Micronesia-FSM (COM-FSM or the College), formerly Community College of Micronesia or CCM, was one of the three component campuses of the College of Micronesia (COM) prior to April 1, 1993. The COM was established on March 29, 1977, by the treaty among the governments of the Republic of the Marshall Islands, the Federated States of Micronesia (FSM), and the Republic of Palau. The treaty ended on March 31, 1993, and the COM was restructured to render autonomy to each of the three nations.

CCM and the centers for continuing education (CE) in Pohnpei, Chuuk, Yap and Kosrae were merged to form COM-FSM, a FSM public corporation established by Public Law 7-79 on September 25, 1992, under the general management and control of a seven-member Board of Regents, appointed by the FSM President with the advice and consent of the FSM Congress. This law was subsequently amended to reduce the number of Board members to five. The term of all board members is 3 years and limited to 2 consecutive terms. However, a member may serve beyond the expiration date of his/her term until a successor has been appointed. The purpose of COM-FSM is to serve the varied post-secondary and adult educational needs of the FSM.

COM-FSM is considered a component unit of the FSM National Government for the following reasons: (1) the governing body, the Board of Regents, is appointed by the FSM President with the advice and consent of FSM Congress, and (2) COM-FSM has the potential to impose financial burdens on the FSM National Government.

(2) Basis of Presentation

A. Financial Statement Presentation. In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. This was followed in November 1999 by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*. The financial statement presentation required by GASB No. 34 and No. 35 provides a comprehensive, entity-wide perspective of the COM-FSM assets, liabilities, net assets, revenues, expenses, changes in net assets, and cash flows, and replaces the fund-group perspective previously required.

Other GASB Statements are required to be implemented in conjunction with GASB Statements No. 34 and No. 35. Therefore, the FSM National Government and COM-FSM have also implemented Statement No. 36, *Recipient Reporting for Certain Shared Nonexchange Revenues*, Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*; *Omnibus,* and Statement No. 38, *Certain Financial Statement Note Disclosures*.

B. Basis of Accounting. For financial statement purposes, COM-FSM is considered a special-purpose government engaged only in business-type activities. Accordingly, COM-FSM's financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-college transactions have been eliminated. COM-FSM reports as a business-type activity, as defined by GASB Statement No. 35. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods and services.

(2) Basis of Presentation, Continued

B. Basis of Accounting, Continued

COM-FSM has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. COM-FSM has elected to not apply FASB pronouncements issued after the applicable date.

(3) Summary of Significant Accounting Policies

A. Cash and Cash Equivalents. Cash and cash equivalents are defined as cash on hand, cash in bank and time certificates of deposit with initial maturities of three months or less.

Custodial credit risk is the risk that in the event of a bank failure, the College'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 College does not have a deposit policy for custodial credit risk.

At September 30, 2012 and 2011, COM-FSM has recorded cash balances of $6,385,567 and $7,167,689, respectively, with corresponding bank balances of $6,766,927 and $7,704,042, respectively. Of these amounts, $2,040,528 in 2012 and $2,738,421 in 2011 are insured by the Federal Deposit Insurance Corporation (FDIC) and $250,000 in each year is subject to coverage by the Securities Investor Protection Corporation. The remaining balances are not insured or collateralized by securities held by a trustee in the name of the financial institution. Management elected not to require insurance or collateralization on the remaining balances based on confidence in the financial health of the banking institutions. No losses as a result of this practice were incurred during the years ended September 30, 2012 and 2011.

B. Investments. COM-FSM accounts for its investments at fair value in accordance with GASB Statement No. 31, *Accounting for Financial Reporting for Certain Investments and for External Investment Pools*. Unrealized gains and losses on the carrying value of investments are reported as a component of net investment income in the Statement of Revenues, Expenses and Changes in Net Assets.

(3) Summary of Significant Accounting Policies, Continued

C. Accounts Receivable. Accounts receivable tuition and fees and accounts receivable employees, net of an allowance for uncollectible accounts as of September 30, 2012, follows:

	National Campus	State Campuses	Totals
Accounts receivable, gross	$ 3,782,906	$ 1,662,010	$ 5,444,916
Allowance for uncollectible accounts	(1,321,593)	(679,943)	(2,001,536)
Accounts receivable, net	$ 2,461,313	$ 982,067	$ 3,443,380

Accounts receivable tuition and fees and accounts receivable employees net of an allowance for uncollectible accounts as of September 30, 2011, follows:

	National Campus	State Campuses	Totals
Accounts receivable, gross	$ 2,696,237	$ 1,844,262	$ 4,540,499
Allowance for uncollectible accounts	(561,947)	(493,317)	(1,055,264)
Accounts receivable, net	$ 2,134,290	$ 1,350,945	$ 3,485,235

The allowance for uncollectible accounts is established through a provision charged to expense. Accounts are charged against the allowance when management believes that the collection of the balance is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing balances that may be uncollectible, based on evaluations of collectibility and prior loss experience.

Other receivables are net of an allowance for doubtful accounts of $153,778 as of September 30, 2012 and 2011.

D. Inventory. Inventory is stated at the lower of cost (first-in, first-out) or market (net realizable value).

E. Prepaid Expenses. Payments made to vendors for goods and services that will benefit periods beyond September 30, 2012 and 2011, are recorded as prepaid expenses. Prepaid expenses represent prepayments for office supplies, textbooks and computers.

F. Capital Assets and Depreciation. All buildings and equipment transferred to COM-FSM were recorded at management's estimate of fair market value at the date of transfer. Subsequent additions have been recorded at cost and/or realizable value, as estimated and provided by COM-FSM. Depreciation is calculated using the straight-line method over estimated useful lives of three to thirty years. COM-FSM has adopted a capitalization policy of $500. Purchases less than this threshold are expensed.

Certain real property and buildings being used by COM-FSM were contributed to COM-FSM by the FSM National Government. No user fee or allowance has been computed or charged to COM-FSM by the FSM National Government. Therefore, such costs have not been recorded as in-kind contributions or expenses.

(3) Summary of Significant Accounting Policies, Continued

G. Deferred Revenue. Deferred revenues include amounts received for tuition and fees and certain grants prior to the end of the fiscal year but relate to the subsequent accounting period. Deferred revenues also include amounts received from grant and contract sponsors that have not yet been earned.

H. Compensated Absences. COM-FSM recognizes as a liability all vested vacation leave benefits accrued by its employees at the time such leave is earned. It is the policy of COM-FSM to record the cost of sick leave when leave is actually taken and an expense is actually incurred. Accordingly, no liability is recorded for nonvesting accumulating rights to receive sick pay benefits.

I. Noncurrent Liabilities. Noncurrent liabilities include estimated amounts for accrued compensated absences that will not be paid within the next fiscal year.

The change in accrued compensated absences during fiscal years 2012 and 2011 is as follows:

Balance, Oct. 1, 2011	Addition	Reduction	Balance, Sept. 30, 2012	Current
$ 536,687	$ 262,488	$ (209,775)	$ 589,400	$ 285,580

Balance, Oct. 1, 2010	Addition	Reduction	Balance, Sept. 30, 2011	Current
$ 544,166	$ 292,858	$ (300,337)	$ 536,687	$ 270,503

J. Net Assets. COM-FSM net assets are classified as follows:

Invested in Capital Assets – This represents COM-FSM's total investment in capital assets, net of outstanding debt obligations related to those capital assets.

Restricted Net Assets – Nonexpendable – Nonexpendable restricted net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal.

Unrestricted Net Assets –Unrestricted net assets represent resources derived from student tuition and fees, governmental appropriations and contracts, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the COM-FSM, and may be used at the discretion of the governing board to meet current expenses for any purpose. These resources are to also be used for auxiliary enterprises, which are substantially self-supporting activities that provide services for student, faculty and staff.

K. Classification of Revenues and Expenses. COM-FSM has classified its revenues and expenses as either operating or nonoperating according to the following criteria:

(3) Summary of Significant Accounting Policies, Continued

K. Classification of Revenues and Expenses, Continued

Operating – Operating revenues and expenses include activities that have the characteristics of exchange transactions, such as (1) student tuition and fees, net of scholarship discounts and allowances, (2) sales and services of auxiliary enterprises, and (3) most federal, state and local grants and contracts and federal appropriations.

Nonoperating – Nonoperating revenues and expenses include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other sources and uses that are defined as nonoperating revenues and expenses by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement No. 34, such as investment income.

L. Scholarship Discounts and Allowances. Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the Statement of Revenues, Expenses and Changes in Net Assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by COM-FSM, and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants, and other federal, state or nongovernmental programs, are recorded as either operating or nonoperating revenues in COM-FSM's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, COM-FSM has recorded a scholarship discount and allowance.

M. Risk Management. COM-FSM purchases insurance to cover its risk of losses due to fire, lightning, and other risks normal to operating an institution of higher learning. Refer also to note 8.

N. Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

O. New Accounting Standards.

During fiscal year 2012, the College implemented the following pronouncements:

- GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which amends Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and addresses issues related to the frequency and timing of measurements for actuarial valuations first used to report funded status information in OPEB plan financial statements. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.

(3) Summary of Significant Accounting Policies, Continued

O. New Accounting Standards, Continued

- GASB Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions* (an amendment of GASB Statement No. 53), which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements,* which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the College.

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus,* which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity,* and No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments,* to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the College.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain FASB and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the College.

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management has not yet determined the effect of implementation of this statement on the financial statements of the College.

(3) Summary of Significant Accounting Policies, Continued

O. New Accounting Standards, Continued

In April 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of the College.

In April 2012, GASB issued Statement No. 66, *Technical Corrections - 2012*, which enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of the College.

In June 2012, GASB issued Statement No. 67, *Financial Reporting for Pension Plans,* which revises existing guidance for the financial reports of most pension plans, and 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 67 are effective for financial statements for periods beginning after June 15, 2013. 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 these statements on the financial statements of the College.

(4) Investments

In January 1994, COM-FSM received an endowment contribution in the amount of $150,000 from FSM Telecommunications Corporation. The principal is to be maintained inviolate and in perpetuity.

In November 1995, notification was received from the U.S. Department Education that COM-FSM had been selected for a grant under the Endowment Challenge Grant Program authorized by Title III of the Higher Education Act of 1965, as amended. Non-government funds raised for this endowment fund were matched by the U.S. Department of Education on a two-to-one basis.

The Secretary of Education awarded an amount to COM-FSM equal to two times the amount of the funds raised. The College of Micronesia-FSM raised $250,000 and the U.S. Department of Education awarded $500,000, bringing the total of this endowment fund to $750,000. The Endowment Challenge grant covers a period of twenty years.

The College has engaged in specific fund raising for the purpose of increasing net assets invested with the above Endowment funds. Therefore, the College is of the opinion that such investments and related investments income are appropriately classified as non expendable restricted net assets.

(4) Investments, Continued

In December 1997, COM-FSM adopted an investment policy, which guides current investment decisions. This policy is to be reviewed after 10 years. The policy provides that investment earnings may not be obligated until the principal has aggregated to a market value of $20 million. During the Board of Regents meeting in March 2005, an updated investment policy recommended by the Investment Consultant and reviewed by the Administration was approved by the Board. The investments are classified as restricted nonexpendable net assets in the accompanying Statement of Net Assets.

The composition of investments as of September 30, 2012 and 2011, by funding source, is as follows:

	2012	2011
Donor		
FSM Telecommunications Corporation (FSMTC)	$ 165,000	$ 165,000
U.S. Department of Education and local match (Challenge)	3,273,961	2,816,912
	$ 3,438,961	$ 2,981,912

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

As of September 30, 2012 and 2011, investments at fair value are as follows:

	2012	2011
Fixed income securities:		
Domestic fixed income	$ 829,454	$ 735,548
International fixed income	-	28,162
	829,454	763,710
Other investments:		
Common equities	2,470,806	2,072,279
Money market funds	138,701	145,923
	2,609,507	2,218,202
	$ 3,438,961	$ 2,981,912

As of September 30, 2012, the College's fixed income securities had the following maturities:

		Investment Maturities (in years)			
Investment Type	Fair Value	Less than 1	1-5	5-10	more than 10
Corporate bond	$ 273,324	$ 38,725	$ 52,831	$ 86,922	$ 94,846
Government bond	556,130	-	342,800	108,308	105,022
	$ 829,454	$ 38,725	$ 395,631	$ 195,230	$ 199,868

(4) Investments, Continued

As of September 30, 2011, the College's fixed income securities had the following maturities:

		Investment Maturities (in years)			
Investment Type	Fair Value	Less than 1	1-5	5-10	more than 10
Mortgage and asset backed	$ 281	$ -	$ -	$ -	$ 281
International bond	28,162	9,208	-	18,954	-
Corporate bond	258,026	-	101,556	84,540	71,930
Government bond	477,241	141,528	117,313	139,919	78,481
	$ 763,710	$ 150,736	$ 218,869	$ 243,413	$ 150,692

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

The College's exposure to credit risk at September 30, 2012, was as follows:

Moody's Rating	Domestic	International	Total
AAA/AAA	$ 498,804	$ -	$ 498,804
AA1/AA	11,642	-	11,642
AA2/AA+	7,425	-	7,425
AA2/AA	11,461	-	11,461
AA2/AA-	9,435	-	9,435
AA3/AA	20,509	-	20,509
A1/A+	30,840	-	30,840
A2/AA-	10,414	-	10,414
A2/A	17,105	-	17,105
A2/A-	10,918	-	10,918
A2/A+	8,629	-	8,629
A3/A-	10,675	-	10,675
BAA1/A-	8,303	-	8,303
BAA1/BBB+	51,486	-	51,486
BAA2/A-	8,268	-	8,268
BAA2/BBB	27,456	-	27,456
BAA2/BBB+	3,071	-	3,071
BAA3/BBB-	11,026	-	11,026
BA2/BBB	9,925	-	9,925
Not Rated	62,062	-	62,062
Total credit risk debt securities	$ 829,454	$ -	$ 829,454

(4) Investments, Continued

The College's exposure to credit risk at September 30, 2011, was as follows:

Moody's Rating	Domestic	International	Total
AAA/AAA	$ 477,241	$ -	$ 477,241
AA1/AA	11,051	-	11,051
AA2/AA+	16,892	-	16,892
AA2/AA	10,675	-	10,675
AA2/AA-	9,194	-	9,194
AA3/A+	9,272	-	9,272
AA3/AA	18,491	-	18,491
A1/A+	10,488	-	10,488
A1/A	9,744	-	9,744
A2/AA-	8,292	-	8,292
A2/A	27,975	-	27,975
A2/A-	10,471	-	10,471
A3/A	8,134	-	8,134
A3/A-	19,385	9,208	28,593
A3/BBB+	-	9,136	9,136
BAA1/A-	-	9,818	9,818
BAA1/BBB+	30,380	-	30,380
BAA2/A-	7,984	-	7,984
BAA2/BBB	17,186	-	17,186
BAA2/BBB-	3,141	-	3,141
BAA3/BBB-	19,090	-	19,090
BA2/BBB	10,181	-	10,181
Not Rated	281	-	281
Total credit risk debt securities	$ 735,548	$ 28,162	$ 763,710

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the College will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The College's investments are held and administered by trustees. Based on negotiated trust and custody contracts, all of these investments were held in the College's name by the College's custodial financial institutions at September 30, 2012 and 2011.

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 College. There was no concentration of credit risk for investments as of September 30, 2012 and 2011.

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

(5) Due from Grantor Agencies

COM-FSM administers student financial aid (SFA) for the U.S. Department of Education. SFA funds related to Pell Grants, Talent Search Program, Upward Bound Program, and Student Support Services (TRIO program), Gaining Early Awareness and Readiness for Undergraduate Programs (GEAR UP). COM-FSM also administers Land Grant Programs on behalf of COM Land Grant College. The net grants and contracts receivable – U.S. Government (net of respective allowances of $21,090 in both 2012 and in 2011) comprised the following uncollected grants as of September 30, 2012 and 2011:

	2012	2011
Due from U.S. Department of Education	$ 1,021,185	$ 956,109
Due from COM-Land Grant, net	296,163	441,266
Due from University of Guam	355,793	404,457
Due from other grantor agencies, net	61,308	175,275
	$ 1,734,449	$ 1,977,107

(6) Capital Assets

Capital assets at September 30, 2012 and 2011 consist of the following:

	Balance October 1, 2011	Additions	Retirements	Balance September 30, 2012
Depreciable assets:				
Buildings	$ 14,209,215	$ 495,444	$ -	$ 14,704,659
Furniture and equipment	8,670,537	421,781	-	9,092,318
Vehicles/boats	1,195,446	72,914	-	1,268,360
Library books	706,402	-	-	706,402
	24,781,600	990,139	-	25,771,739
Less accumulated depreciation	(16,111,598)	(988,117)	-	(17,099,715)
	8,670,002	2,022	-	8,672,024
Non-depreciable assets:				
Land	1,455,685	-	-	1,455,685
Net investment in capital assets	$ 10,125,687	$ 2,022	$ -	$ 10,127,709

	Balance October 1, 2010	Additions	Retirements	Balance September 30, 2011
Depreciable assets:				
Buildings	$ 14,209,215	$ -	$ -	$ 14,209,215
Furniture and equipment	8,175,219	495,318	-	8,670,537
Vehicles/boats	1,085,747	109,699	-	1,195,446
Library books	706,402	-	-	706,402
	24,176,583	605,017	-	24,781,600
Less accumulated depreciation	(15,169,387)	(942,211)	-	(16,111,598)
	9,007,196	(337,194)	-	8,670,002
Non-depreciable assets:				
Land	1,455,685	-	-	1,455,685
Net investment in capital assets	$ 10,462,881	$ (337,194)	$ -	$ 10,125,687

(7) Related Party Transactions

COM-FSM receives annual appropriations from the FSM National Government for its operational needs, student financial assistance and other programs. At September 30, 2012 and 2011, receivables from the FSM National Government amounted to $182,993 and $319,799, respectively.

(8) Contingencies

Insurance

COM-FSM purchases commercial insurance to cover its potential risks from fire and property damage on some of its buildings and contents ($19,164,373 of coverage) and vehicles (up to $300,000 of coverage per vehicle per accident). Additionally, COM-FSM purchases fidelity insurance coverage for selected employees (total coverage of $97,500) and workmen's compensation insurance (coverage of up to $100,000 per employee). COM-FSM also purchases student personal insurance ($5,000 per student). There have been no settlements in excess of insurance coverage during the past three years.

Accreditation

The College is accredited by the Accrediting Commission for Community and Junior Colleges (ACCJC) of the Western Association of Schools and Colleges (WASC). On June 30, 2011, the College was placed on "probation" for four recommendations, and as a consequence was required to submit a follow-up report on March, 15, 2012 succeeded by an ACCJC team visit on April 23-25, 2012. The College has further submitted a supplemental report and will appear before the Commission at their June 6-9, 2012 hearings. An action letter was issued on July 2, 2012 which continued the College's probation status and was required to submit a follow-up report and mid-term report on March 15, 2013. Despite the current probation status, the College remains accredited and continues to receive and administer U.S. Federal Student Aid programs for eligible students.

Litigation

COM-FSM is periodically a defendant in legal actions inherent to the nature of its operations. COM-FSM management is of the opinion that resolution of any matters existing as of September 30, 2012 and 2011 will not have a material effect on the accompanying financial statements.

(9) Retirement Plan

The College has a retirement plan, administered by a private corporation. All employees with at least one year of service are eligible for the plan. Employee contributions can be made up to 100% of earnings with a 50% match by the College up to 3% of employee compensation. The College's President, Vice - President for Administrative Services and Comptroller are the designated plan administrators. During the years ended September 30, 2012, 2011 and 2010, the College incurred an expense of $112,474, $105,320 and $101,194, respectively, for matching contributions. For the years ended September 30, 2012, 2011 and 2010, plan assets were $2,572,211, $2,072,488 and $1,943,134, respectively.

(10) Lease

The College leases land in the State of Chuuk, where the Chuuk Campus is located. The future minimum lease payments are as follows:

Year Ending September 30,	Total
2013	$ 76,863
2014	78,650
2015	78,650
2016	78,650
2017	78,650
2018-2022	430,609
2023	21,629
	$ 843,701