COLLEGE OF MICRONESIA-FSM

FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

SEPTEMBER 30, 2006 AND 2005

COLLEGE OF MICRONESIA-FSM

TABLE OF CONTENTS
YEARS ENDED SEPTEMBER 30, 2006 AND 2005

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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, a component unit of the FSM National Government, as of September 30, 2006 and 2005, 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, 2006 and 2005, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 12 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the College's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 22, 2007, 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.

Deloitte & Touche LLP

May 22, 2007

The Management's Discussion and Analysis (MD & A) is supplementary information required by the new Government Accounting Standards Board 35 (GASB 35) on reporting model. The preparation of MD & A is the responsibility of the management of COM-FSM, and it is designed to help the readers in understanding the accompanying financial statements and the accompanying notes to the financial statements.

Institution Background

The College of Micronesia-FSM (COM-FSM) is a multi-campus institution and serves as the only higher education facility in the Federated States of Micronesia (FSM) which has a population of over 110,000. The COM-FSM has a network of six college campuses located on four different islands in the Western Pacific. The main campus (referred to as the National campus) is located in Palikir, Pohnpei. The other college sites are state campuses on Pohnpei (Kolonia Town), Kosrae, Yap and Chuuk. FSM Fisheries and Maritime Institute (FSM – FMI), the sixth campus, is located in Yap State.

COM – FSM is a public corporation of FSM established by Public Law 7 – 79 on September 25, 1992 and is considered a component unit of the FSM National Government. The governing body for the general management and control of COM – FSM is the five-member Board of Regents appointed by the FSM President with the advice and consent of the FSM Congress. The President of the College, appointed by the Board of Regents, has the full charge and control of the administration and business affairs of the College.

COM – FSM is accredited by the Accrediting Commission for Community and Junior Colleges of the Western Association of Schools and Colleges, an institutional accrediting body recognized by the Commission on Recognition of Post-secondary Accreditation and the U.S. Department of Education. Accreditation was awarded to the College in 1978 and reaffirmed in 1982, 1987, 1992, 1998 and June, 2005.

COM-FSM Mission

The mission statement of the College adopted by the Board of Regents in its September 2005 meeting reads:

> "Historically diverse, uniquely Micronesian, and globally connected, the College of Micronesia-FSM is a continuously improving and student centered institute of higher education. The college is committed to assisting in the development of the Federated States of Micronesia by providing academic, career and technical education opportunities for student learning.

The College's mission statement links to the FSM Strategic Development Plan (SDP) under the strategic goal "To allow FSM students to complete postsecondary education to assist in the economic development of the FSM".

Overview of Fiscal Year 2006

COM – FSM offered thirty-six degree and certificate programs: five Associate of Arts degrees, seven Associate of Science degrees, three Associate of Applied Science degrees, four Third-year Certificates of Achievement and seventeen other Certificates of Achievement. There were 5,627 students enrolled in degree and certificate programs across all campuses for fall 05, spring 06 and summer 06. National campus enrolled 2,063 students or 37%, Pohnpei campus enrolled 1,446 students or 26%, Chuuk campus enrolled 770 students or 14%, Kosrae campus enrolled 756 students or 13% and Yap campus enrolled 592 students or 11%. The total enrollment for fiscal year 2006 dropped by 9% or 553 students compared with fiscal year 2005 enrollment of 6,180. The significant reduction of enrollment was at Chuuk campus, from 1,479 students to 770 students or by 709 students. National and Pohnpei campuses also showed slight reductions of enrollment by 78 and 62 students, respectively. However, Kosrae and Yap campuses provided an increase in enrollment by 199 and 97 students, respectively.

The significant reduction of enrollment in Chuuk campus was caused by the implementation of a "teach out" from summer 2005 to summer 2006. Under the "teach out", the College allowed only continuing students to enroll while the College improved the facilities at Chuuk campus. No new students were admitted.

FSM National Government continues to provide financial support to the College. For fiscal year 2006, FSM National Government provided $3.8 Million to support the operating expenses of the College, $600K for full subsidy of the operations of Fisheries and Maritime Institute, $267K for Work Study and Supplemental Education Opportunity Grant programs, $300K for financial assistance to FSM students, $84K for the College's Board of Regents, and $1.5 Million for facility improvements. The total financial support from FSM for fiscal year 2006 was $6.551 Million or $1.353 Million higher in comparison with fiscal year 2005 of $5.198 Million.

The College continues to administer three U.S. Federal Student Aid Programs (Pell Grant, FSEOG and Work Study). The U.S. Federal Student Aid Programs awarded to students provided more than 90% of students' tuition and fees. In fiscal yea 2006, the Federal Pell Grant Program dropped by $1.163 Million, from $8.215 Million to $7.052 Million. The reduction of the Federal Pell Grant was due to reduced enrollment of students at the Chuuk campus.

The College continues to receive U.S. Federal grants from the U.S. Department of Education and the U.S. Department of the Interior.

Financial Statements Analysis

The College started implementing the new financial reporting standards for public colleges and universities in accordance with Government Accounting Standards Board (GASB) principles in fiscal year 2003. Since then, the funds are presented in consolidated financial statements as a whole, rather than on the fund basis used in the accounting model prior to fiscal year 2003. Adopting the GASB principles provide the new financial reporting of the following three basic financial statements:

1. Statement of Net Assets (SNA)

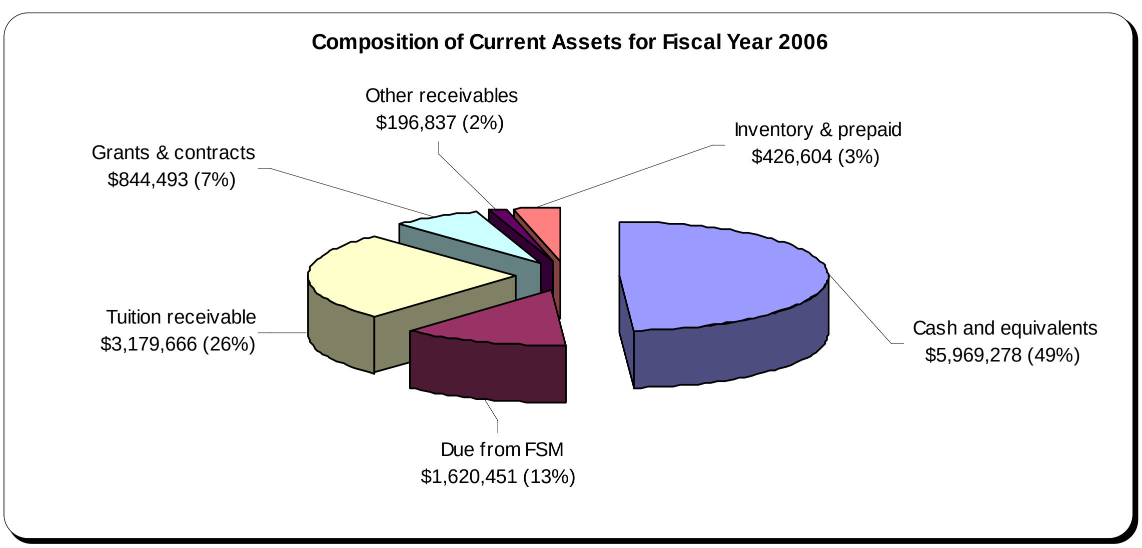
The SNA presents what the College owns (assets), owes (liabilities) and the net assets (the difference between total assets and total liabilities) at the end of the fiscal year. The "net assets" is one indicator of the current financial condition of the College, while the change in net assets is an indicator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

Comparative Statement of Net Assets at September 30, 2006 and 2005 is summarized below:

	FY 2006 (In 000's)	FY 2005 (In 000's)	Difference (In 000's)	FY 2004 (In 000's)
Assets:				
Current assets	$ 12,237	$ 12,589	$ (352)	$ 11,415
Noncurrent assets	15,047	15,191	(144)	15,327
Total assets	27,284	27,780	(496)	26,712
Liabilities:				
Current liabilities	4,568	4,892	(324)	4,044
Noncurrent liabilities	231	214	17	192
Total liabilities	4,799	5,106	(307)	4,236
Net assets	$ 22,485	$ 22,674	$ (189)	$ 22,506

The comparison of the statement of net assets for fiscal year 2006 with fiscal year 2005 presents a reduction in net assets by $189K.

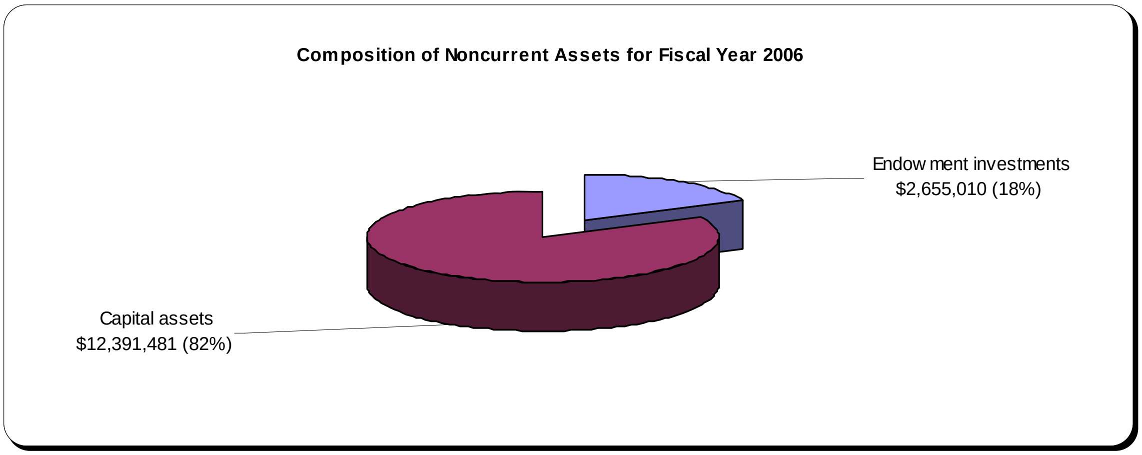
Current assets: The total current assets of $12.237 Million for fiscal year 2006 showed a reduction by 3% or $352K in comparison with fiscal year 2005 current assets of $12.589 Million. The composition of current assets for fiscal year 2006 is presented in the following pie graph:



The reduction by $352K in current assets is the net result of the following:

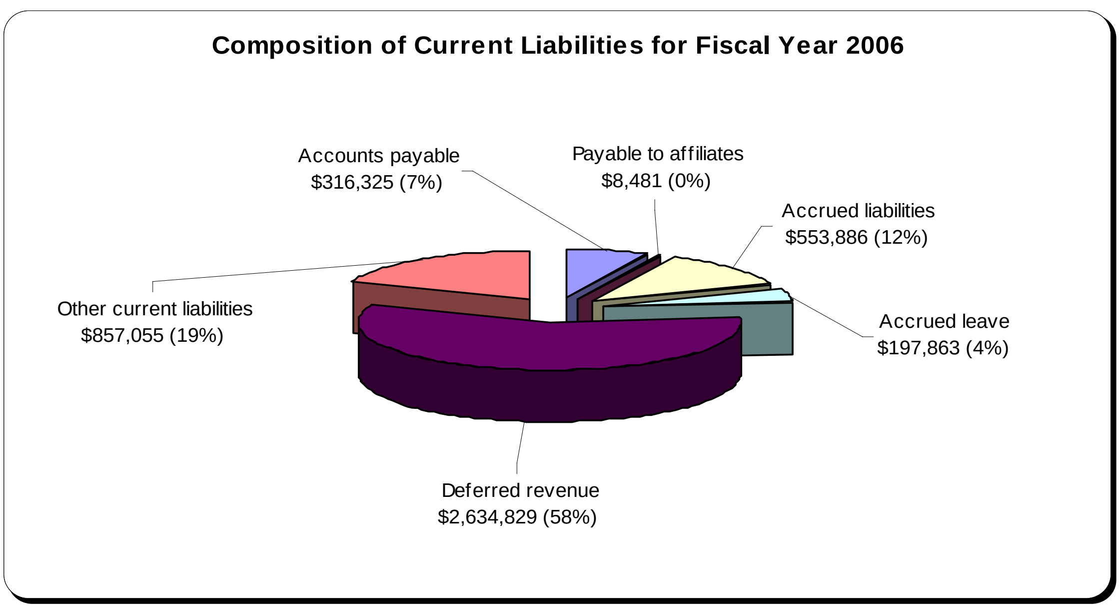
- Increases from tuition receivable by $993K, inventory and prepayments by $158K, grants and contract receivable by $108K, and other receivables by $50K; and
- Decreases in cash and equivalents by $933K and due from FSM by $728K. The reduction of cash and equivalents is primarily due to increase in tuition receivable and reduction in current liabilities.

Noncurrent assets: The total noncurrent assets dropped by $144K from $15.191 Million in fiscal year 2005 to $15.047 Million in fiscal year 2006. The breakdown of noncurrent assets is presented in the following pie graph:



Capital assets dropped by 3% or $432K compared with fiscal year 2005 of $12.823 Million. However, the market value of endowment investment increased by $288K from an unrealized gain of $238K and additional investment contribution of $50K for fiscal year 2006.

Current liabilities: The current liabilities dropped by $324K, from $4.892 Million in fiscal year 2005 to $4.568 Million in fiscal year 2006. The composition of current liabilities is also presented in the following pie graph:



In comparison with fiscal year 2005, deferred revenue and accounts payable provide a significant reduction in current liabilities by $488K and $76K, respectively. However, the other current liabilities indicate an increase by $283K.

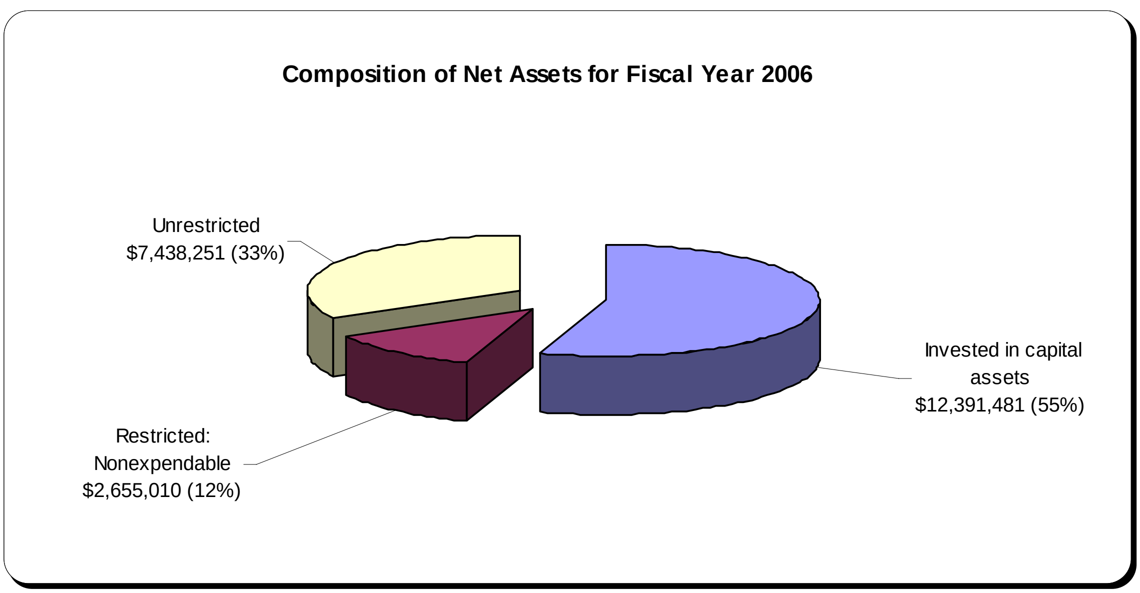
Please note that the reduction of current liabilities contributes to the reduction of cash and equivalents as discussed in the current assets section.

Noncurrent liabilities: The noncurrent liability of $231K represents the long-term portion of the accrued annual leave which showed an increase of $17K or 8% compared with the previous year.

Net Assets: Net assets present the residual interest in the College's assets after liabilities are deducted. The College's net asset for fiscal year 2006 is $22.485 Million. In comparison with that of fiscal year 2005 of $22.674 Million, the net assets dropped by $189K. Below is the breakdown of the College's net assets categorized according to the new reporting model of GASB:

	FY 2006 (In 000's)	FY 2005 (In 000's)	Difference (In 000's)	FY 2004 (In 000's)
Invested in capital assets	$ 12,392	$ 12,824	$ (432)	$ 13,157
Restricted:				
Nonexpendable	2,655	2,400	255	1,987
Unrestricted	7,438	7,450	(11)	7,362
Total	$ 22,485	$ 22,674	$ (189)	$ 22,506

Below is the pie graph for the breakdown of net assets for fiscal year 2006:



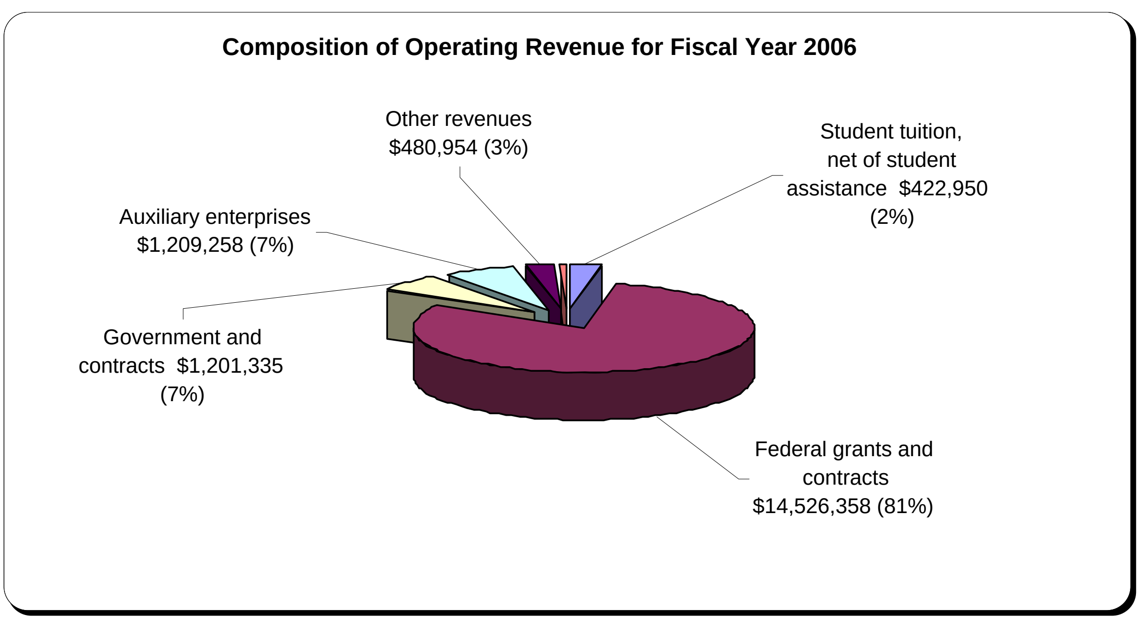
The investment in capital assets, net of accumulated depreciation dropped by $432K. The restricted - nonexpendable, representing the endowment investment which is required to be retained in perpetuity, showed an increase of $255K or 11% from the prior year. The unrestricted net assets, which represent all remaining assets that can be committed or designated by the COM-FSM Board of Regents to support specific academic programs, capital construction projects, and others dropped only by $11K compared with the prior year.

2. Summary 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 revenue and expenses and the corresponding net operating results, as well as non-operating revenues and expenses for the College. Below is the comparative summary of SRECNA for the College for fiscal years ended September 30, 2006 and 2005:

	FY 2006 (In 000's)	FY 2005 (In 000's)	Difference (In 000's)	FY 2004 (In 000's)
Operating revenues	$ 17,840	$ 17,220	$ 621	$ 16,904
Operating expenses	18,268	17,745	523	18,008
Operating loss	(427)	(525)	98	(1,104)
Nonoperating revenue	238	693	(454)	1,063
Net increase(decrease) in net assets	(189)	168	(356)	(41)
Net assets at beginning of year	22,674	22,506	167	22,547
Net assets at end of year	$ 22,485	$ 22,674	$ (189)	$ 22,506

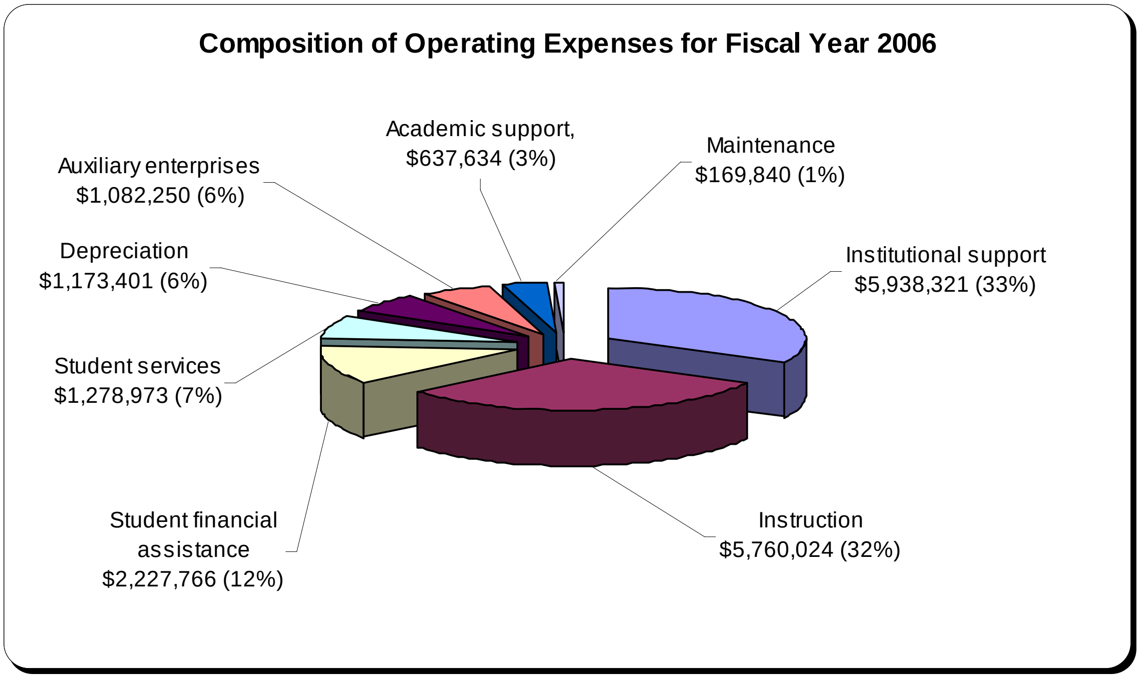
Operating revenues: The operating revenue for fiscal year 2006 is $17.841 Million with the following breakdown as presented in the pie graph:



The operating revenue has increased by $621K compared with fiscal year 2005 of $17.220 Million. The increase in operating revenues is the net result of the following:

- Increases from government and contracts by $862K, sales from auxiliary enterprises by $199K, other revenues by $267K and reduction of bad debts by $277K; and
- Decreases in Federal grants and contracts by $914K and student tuition by $70K. The reduction of Federal grants and student tuition is due to the implementation of the "teach out" at Chuuk campus.

Operating expenses: The operating expenses for fiscal year 2006 is $18.268 Million. Below is the breakdown of operating expenses presented in pie graph:



The total operating expenses for fiscal year 2006 indicate an increase by $523K compared with fiscal year 2005. The increase in operating expenses is primarily due to expenditures of projects funded from fund balance such as construction of buildings at Chuuk campus amounting to $534K.

Nonoperating revenues: The nonoperating revenue for fiscal year 2006 is $238K. In comparison with fiscal year 2005 of $693K, it dropped by 66% or $455K.

Net decrease in net assets: The College's financial performance for fiscal year 2006 showed a net decrease in net assets of $189K. As presented in a previous analysis, the decrease in net assets is due to low enrollment at the Chuuk campus as a result of the "teach out" implemented from summer 2005 to summer 2006.

3. Summary 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 Summary Statement of Cash Flows indicates a balance in cash and equivalents of $5.970 Million at end of fiscal year 2006. The fiscal year end balance reflects a decrease of 13% or $932K in cash and equivalents compared with the balance at beginning of year of $6.902 Million.

Below is the summary Statement of Cash Flows:

	FY 2006 (In 000's)	FY 2005 (In 000's)	Difference (In 000's)	FY 2004 (In 000's)
Used in operating activities	$ 97	$ 2,588	$ (2,491)	$ 83
Provided by (used in) noncapital financing activities	-	(156)	156	790
Used in capital and related financing activities	(741)	(838)	97	(492)
Used in investing activities	(288)	(100)	(188)	-
Net change in cash and equivalents	(932)	1,494	(2,426)	381
Cash and cash equivalents at beg. of year	6,902	5,408	1,494	5,027
Cash and cash equivalents at end of year	$ 5,970	$ 6,902	$ (932)	$ 5,408

The decrease in cash and equivalents is primarily from the net decrease of cash flow in operating activities by $2.491 Million.

The net cash flows in operating activities for fiscal year 2006 of $97K consist of cash inflows from student tuition and fees of $768K, grants and contracts of $16.348 Million, auxiliary services of $1.159 Million and other revenues of $481K. The cash outflows are payments to employees for salaries and benefits of $6.935 Million, and payments to suppliers and others of $11.724 Million.

Management's Discussion and Analysis for the year ended September 30, 2005 is set forth in the College's report on the audit of financial statements, which is dated June 14, 2006. That Discussion and Analysis explains the major factors impacting the 2005 financial statements and can be obtained via the Office of the Public Auditor's website at www.fsmpublicauditor.fm.

Budget Information

The College undertakes a yearly budget process as an integral part of financial planning that is linked with the Strategic Plan. The budget process includes the formulation and approval of budget guidelines, preparation of revenue and expenditure budgets by campus directors and budget heads in consultation with the faculty and staffs. The budgets are reviewed by Vice-Presidents, Finance and Planning Council Committees and Cabinet. The College's budgets are approved by the Board of Regents. The operating budget for Compact's Education Sector Grant (ESG), FSM – FMI budget, Board of Regents budget, Infrastructure Development Project (IDP) budget and Supplemental Education Grant (SEG) budget are transmitted to the FSM National Government's Executive Budget Review Committee.

For fiscal year 2006, the FSM National Government appropriated a total of $6.555 Million, consisting of:

- $3.8 Million to support the operations of the college;
- $600K for the full subsidy of the operations of FSM – FMI;
- $1.5 Million for IDP; and
- $570K for SEG.

The total budget for the operations of the College for fiscal year 2006 was $9.884 Million wherein the $3.8 Million was funded from FSM National Government through the Education Sector Grant of Compact II.

Capital Assets and Long-term Debt Activity

At September 30, 2006, the College's net investment in capital assets is $12.391 Million, net of accumulated depreciation. Depreciation for the current year totaled to $1.173 Million, and capital additions for furniture and equipment, vehicles and library books totaled to $741K.

The long-term debt of the College consists of accrued annual leave. The Personnel Policy and Procedure Manual of the College provides accumulation of annual leave balance in the employees' records. As of September 30, 2006, only 180 hours of the accumulated annual leave shall be paid to the employee upon resignation/termination of employment, thus the value of only 180 hours was recorded as a current liability. However, during the December 2006 board meeting, the Board of Regents adopted a directive increasing the accumulated annual leave to be paid by the College upon employee's resignation/termination of employment by 60 hours, from 180 to 240.

The College did not incur any long-term debt in fiscal year 2006.

Economic Outlook

The economic position of the College is dependent on tuition fees generated from students who primarily received financial assistance from U.S. Federal Student Aid programs and on the annual subsidy from FSM National Government. The authority for the U.S. Department of Education to award Student Financial Aid grants to the College resides in U.S. Public Law 99 – 239. If this award authority is not extended or renewed by the U.S. Congress, the result could be a significant reduction in the amount of funds available for student financial aid and, in turn, a significant reduction in tuition revenue for the College. It should be noted that the U.S. Department of Education, Federal Student Aid approved the Program Participation Agreement for the College through June 30, 2008.

In June 2005, the College's accreditation was reaffirmed until June 2010 by the Accrediting Commission for Community and Junior Colleges (ACCJC) of the Western Association of Schools and Colleges (WASC). The reaffirmation of accreditation allows the College to continue to receive and administer US Pell Grant funding for the College's eligible students, and other competitive grants. In fiscal year 2006, the College received and administered $9.39 Million from the U.S. Department of Education consisting of $7.052 Million for Federal Pell Grant Program, $185K for Supplemental Education Opportunity Grant (SEOG), $146K for Federal Work Study (WS), and $2.007 Million from TRIO and other competitive programs.

About 65% of the College's operating cost is funded through tuition and fees, and more than 90% of students pay tuition and fees through the financial assistance from U.S. Federal Student Aid's Pell Grant, SEOG and WS programs. These programs are available to citizens of the FSM under the terms of Compact II. Concerted efforts are being made by the College to ensure that the U.S. Federal Government includes the College of Micronesia-FSM in the re-authorization of the Higher Education Act (HEA) that is currently under discussion in the U.S. Congress. The current HEA expires on June 30, 2007. The Association of American Community Colleges, of which the College is a member, proposed that any regionally U.S. accredited institution be eligible for U.S. Federal Student Aid.

The College receives an annual subsidy from the FSM National Government under the Education Sector Grant of Compact II. The continued funding support from the Education Sector Grant of Compact II of at least $3.8 Million annually, about 30% - 35% of the operating cost of the College, will allow the administration to plan for the future of the College.

In order to tap alternative sources of funding and reduce reliance by the College on financial assistance from the U.S. and FSM governments in the long-run, a new Office of "Development and Community Relations" was created and a director was hired in August 2006. The office is currently developing alumni databases in order to track and cultivate alumni for giving. The office is also preparing a development strategy which will include proposals targeted at corporate donors, foundations, and governments. This is an effort aimed at the long-term financial stability of the College through the College's endowment fund.

In order to meet rising costs and still provide adequate services, the College is developing a recruitment and retention plan. This will help to increase enrollment and to retain students once they have enrolled. A grant writer position is also planned to further develop new sources of grant funding to support the operations of the college.

Finally, with the upcoming military build up in neighboring Guam, the College is positioning itself to take advantage of Guam's economic boom - $10 Billion over the next ten years, not considering the multiplier effect. Partnerships with employers and employer associations, with the governments of FSM, Guam, and the U.S., and with other agencies are expected to provide significant financial benefits to the College.

COLLEGE OF MICRONESIA-FSM

Statements of Net Assets
September 30, 2006 and 2005

ASSETS		2006		2005
Current assets:				
Cash and cash equivalents	$	5,969,278	$	6,902,109
Due from FSM National Government, net		1,620,451		2,348,417
Tuition receivable, net		3,179,666		2,186,992
Grants and contracts receivable - U.S. Government (net of allowance for doubtful accounts of $93,890 for 2006 and 2005)		844,493		736,639
Other receivables (net of allowance for doubtful accounts of $69,576 and $77,807 for 2006 and 2005, respectively)		196,837		146,676
Inventory		233,795		233,975
Prepaid expenses		192,809		34,632
Total current assets		12,237,329		12,589,440
Noncurrent assets:				
Investments		2,655,010		2,366,568
Capital assets, net of accumulated depreciation		12,391,481		12,823,907
Total noncurrent assets		15,046,491		15,190,475
Total assets	$	27,283,820	$	27,779,915
LIABILITIES AND NET ASSETS				
Current liabilities:				
Accounts payable	$	316,325	$	392,033
Payable to affiliates		8,481		11,686
Accrued liabilities		553,886		591,403
Accrued annual leave		197,863		199,397
Deferred revenue		2,634,829		3,123,439
Other current liabilities		857,055		573,970
Total current liabilities		4,568,439		4,891,928
Noncurrent liabilities:				
Long-term portion of accrued annual leave		230,639		214,446
Total liabilities		4,799,078		5,106,374
Contingencies				
Net assets:				
Invested in capital assets		12,391,481		12,823,907
Restricted:				
Nonexpendable		2,655,010		2,399,955
Unrestricted		7,438,251		7,449,679
Total net assets		22,484,742		22,673,541
Total liabilities and net assets	$	27,283,820	$	27,779,915

See accompanying notes to financial statements.

COLLEGE OF MICRONESIA-FSM

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2006 and 2005

	2006	2005
Operating revenues:		
Student tuition and fees	$ 5,688,827	$ 6,448,429
Less: Scholarship discounts and allowances	(5,265,877)	(6,102,373)
	422,950	346,056
Federal grants and contracts	14,526,358	15,310,023
Government grants and contracts	1,201,335	339,530
Sales and services of auxiliary enterprises	1,209,258	1,010,305
Other revenues	480,954	214,245
Total operating revenues	17,840,855	17,220,159
Operating expenses:		
Institutional support	5,938,321	5,684,704
Instruction	5,760,024	4,951,602
Student financial assistance	2,227,766	2,565,971
Student services	1,278,973	1,084,834
Depreciation	1,173,401	1,171,117
Auxiliary enterprises	1,082,250	1,028,934
Academic support	637,634	863,756
Operations and maintenance, plant	169,840	394,443
Total operating expenses	18,268,209	17,745,361
Operating loss	(427,354)	(525,202)
Nonoperating revenues:		
FSM National Government appropriations:		
Operations	-	375,296
Net investment income	238,555	317,746
Net nonoperating revenues	238,555	693,042
Net change in net assets	(188,799)	167,840
Net assets:		
Net assets at beginning of year	22,673,541	22,505,701
Net assets at end of year	$ 22,484,742	$ 22,673,541

See accompanying notes to financial statements.

COLLEGE OF MICRONESIA-FSM

Statements of Cash Flows
Years Ended September 30, 2006 and 2005

	2006	2005
Cash flows from operating activities:		
Student tuition and fees, net	$ 767,949	$ 1,618,299
Grants and contracts	16,347,805	16,094,105
Auxiliary services	1,159,097	1,250,240
Other receipts	480,954	214,245
Payments to employees for salaries and benefits	(6,935,170)	(7,121,901)
Payments to suppliers and others	(11,723,936)	(9,466,919)
Net cash provided by operating activities	96,699	2,588,069
Cash flows from noncapital financing activities:		
FSM National Government appropriations, grants and contracts	-	(155,984)
Net cash used in noncapital financing activities	-	(155,984)
Cash flows from capital and related financing activities:		
Purchases of capital assets	(740,975)	(838,011)
Net cash used in capital and related financing activities	(740,975)	(838,011)
Cash flows from investing activities:		
Investment income	238,555	317,746
Purchase of investments	(527,110)	(417,746)
Net cash used in investing activities	(288,555)	(100,000)
Net change in cash and cash equivalents	(932,831)	1,494,074
Cash and cash equivalents at beginning of year	6,902,109	5,408,035
Cash and cash equivalents at end of year	$ 5,969,278	$ 6,902,109
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	$ (427,354)	$ (525,202)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	1,173,401	1,171,117
Bad debts	109,869	386,949
Change in assets and liabilities:		
Tuition receivable	(863,875)	285,878
Grants and contracts receivable	620,112	314,112
Other receivables	(50,161)	239,935
Inventories	180	(135,974)
Prepaid expenses	(158,177)	(18,382)
Accounts payable	(75,708)	(65,078)
Payable to affiliates	(3,205)	(291,042)
Accrued liabilities	(22,858)	408,126
Deferred revenue	(488,610)	729,856
Other liabilities	283,085	87,774
Net cash provided by operating activities	$ 96,699	$ 2,588,069

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 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

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. Time certificates of deposit with initial maturities in excess of three months are classified as investments.

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

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

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

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

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the 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, 2006 and 2005, COM-FSM has recorded cash balances of $5,969,278 and $6,902,109, respectively, with corresponding bank balances of $6,429,091 and $7,252,952, respectively. Of these amounts, $200,000 in each year is insured by the Federal Deposit Insurance Corporation (FDIC). 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, 2006 and 2005.

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, are net of an allowance for uncollectible accounts as of September 30, 2006, are as follows:

	National Campus	State Campuses	Totals
Accounts receivable, gross	$ 3,770,006	$ 2,588,647	$ 6,358,653
Allowance for uncollectible accounts	(1,526,010)	(1,652,977)	(3,178,987)
Accounts receivable, net	$ 2,243,996	$ 935,670	$ 3,179,666

Accounts receivable tuition and fees and accounts receivable employees net of an allowance for uncollectible accounts as of September 30, 2005, are as follows:

	National Campus	State Campuses	Totals
Accounts receivable, gross	$ 3,175,608	$ 2,080,502	$ 5,256,110
Allowance for uncollectible accounts	(1,417,662)	(1,651,456)	(3,069,118)
Accounts receivable, net	$ 1,757,946	$ 429,046	$ 2,186,992

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.

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, 2006 and 2005, are recorded as prepaid expenses. Prepaid expenses represent prepayments for laboratory 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 been recorded neither as in-kind contributions nor expenses.

G. Deferred Revenue. Deferred revenues include amounts received for tuition and fees and certain auxiliary activities 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.

(3) Summary of Significant Accounting Policies, Continued

H. Accrued Leave. COM-FSM recognizes as a liability all vested leave benefits accrued by its employees at the time such leave is earned.

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 2006 and 2005 is as follows:

Balance, Oct. 1, 2005	Addition	Reduction	Balance, Sept. 30, 2006	Current
$413,843	$256,448	$(241,789)	$428,502	$197,863

Balance, Oct. 1, 2004	Addition	Reduction	Balance, Sept. 30, 2005	Current
$375,413	$233,724	$(195,294)	$413,843	$199,397

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. COM-FSM has classified its revenues as either operating or nonoperating according to the following criteria:

Operating Revenues – Operating revenues 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 Revenues – Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues 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 FSM National Government appropriations and investment income.

(3) Summary of Significant Accounting Policies, Continued

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. Reclassifications. Certain reclassifications have been made to the 2005 financial statements in order to conform with the 2006 presentation.

P. New Accounting Standards. During the year ended September 30, 2006, COM-FSM implemented the following pronouncements:

- GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which establishes standards for impairment of capital assets when its service utility has declined significantly and unexpectedly.

- GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section, an amendment to NCGA Statement 1,* which improves the understandability and usefulness of statistical section information and adds information from the new financial reporting model for state and local governments required by GASB Statement No. 34.

- GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation (an amendment to GASB Statement No. 34)*, which requires that limitations on the use of net assets imposed by enabling legislation be reported as restricted net assets.

- GASB Statement No. 47, *Accounting for Termination of Benefits*, which establishes guidance for state and local governmental employers on accounting and financial reporting for termination of benefits.

- GASB Technical Bulletin No. 2004-2, *Recognition of Pension and Other Postemployment Benefits Expenditures/Expense and Liabilities by Cost-Sharing Employers*, which clarifies the requirements of GASB Statement Nos. 27 and 45 for recognition of pension and other postemployment benefit expenditures/expense and liabilities by cost-sharing employers.

(3) Summary of Significant Accounting Policies, Continued

P. New Accounting Standards, Continued

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

In September 2006, GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*. GASB Statement No. 48 establishes uniform financial reporting for these types of revenues. The provisions of this Statement are effective for periods beginning after December 15, 2006. In April 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. GASB Statement No. 43 establishes uniform financial reporting for other postemployment benefit plans by state and local governments. The provisions of this Statement are effective for periods beginning after December 15, 2007. Additionally, in June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Post Employment Benefits Other than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition and display of other postemployment benefit expenses and related liabilities, note disclosures, and, if applicable, required supplementary information in the reports of the state and local employers. The provisions of this Statement are effective for periods beginning after December 15, 2006.

Management does not believe that the implementation of these Statements will have a material effect 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.

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 on 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.

(4) Investments, Continued

The composition of investments as of September 30, 2006 and 2005, by funding source, is as follows:

	2006	2005
Donor		
FSM Telecommunications Corporation (FSMTC)	$ 165,000	$ 165,000
U.S. Department of Education and local match (Challenge)	2,490,010	2,201,568
	$ 2,655,010	$ 2,366,568

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.

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

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

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

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

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

As of September 30, 2006 and 2005, investments at fair value are as follows:

	2006	2005
Fixed income securities:		
Domestic fixed income	$ 582,443	$ 636,465
International fixed income	13,800	6,147
	596,243	642,612
Other investments:		
Common equities	2,006,517	1,658,900
Money funds	52,250	65,056
	2,058,767	1,723,956
	$ 2,655,010	$ 2,366,568

(4) Investments, Continued

As of September 30, 2006, 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
International bond	$ 13,800	$ -	$ 7,000	$ 6,800	$ -
Corporate bond	103,721	-	5,411	86,486	11,824
Government bond	478,722	15,874	244,185	152,965	65,698
	$ 596,243	$ 15,874	$ 256,596	$ 246,251	$ 77,522

As of September 30, 2005, 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
International bond	$ 6,147	$ -	$ -	$ -	$ 6,147
Corporate bond	104,472	-	11,086	63,285	30,101
Government bond	531,993	16,868	344,063	98,270	72,792
	$ 642,612	$ 16,868	$ 355,149	$ 161,555	$ 109,040

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, 2006, was as follows:

Moody's Rating	Total	Domestic	International
AAA/AAA	$ 487,620	$ 487,620	$ -
AA3/A +	11,402	11,402	-
A1/A	5,303	5,303	-
A1/AA-	6,947	6,947	-
A2/A	11,646	11,646	-
A3/A-	13,800	-	13,800
A3/A	6,907	6,907	-
BAA1/BBB +	6,768	6,768	-
BAA2/BBB	24,628	24,628	-
BAA2/BBB-	7,084	7,084	-
BAA2/BBB+	7,459	7,459	-
BAA3/BBB	6,679	6,679	-
Total credit risk debt securities	$ 596,243	$ 582,443	$ 13,800

(4) Investments, Continued

The College's exposure to credit risk at September 30, 2005, was as follows:

Moody's Rating	Total	Domestic	International
AAA/AAA	$ 541,068	$ 541,068	$ -
AAA1/AA-	5,029	5,029	-
AA3/A +	11,644	11,644	-
A1/A	10,312	10,312	-
A2/A	11,922	11,922	-
A2/A+	6,091	6,091	-
A3/BBB	2,172	2,172	-
BAA1/BBB +	5,858	5,858	-
BAA2/BBB	12,299	12,299	-
BAA2/BBB-	6,001	6,001	-
BAA2/BBB+	12,003	12,003	-
BAA3/BBB	12,156	6,009	6,147
BAA3/BBB-	6,057	6,057	-
Total credit risk debt securities	$ 642,612	$ 636,465	$ 6,147

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, 2006 and 2005.

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, 2006. As of September 30, 2005, the College's investment in agency obligations of Federal National Mortgage Association constituted 17% 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 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, College Work-Study and Supplemental Educational Opportunity Grants, Talent Search Program, Upward Bound Program, and Strengthening Institution Program. In addition, COM-FSM also administers Land Grant Programs on behalf of COM Land Grant College. The grants and contracts receivable – U.S. Government are comprised of the following uncollected grants as of September 30, 2006 and 2005:

	2006	2005
Due from U.S. Department of Education	$ 461,961	$ 600,864
Due from COM-Land Grant, net	382,532	135,775
	$ 844,493	$ 736,639

(6) Capital Assets

Capital assets at September 30, 2006 and 2005 consist of the following:

	Balance October 1, 2005	Additions	Retirements	Balance September 30, 2006
Non-depreciable assets:				
Land	$ 1,455,685	$ -	$ -	$ 1,455,685
Depreciable assets:				
Building	13,661,263	-	-	13,661,263
Furniture and equipment	6,145,138	561,018	-	6,706,156
Vehicles/boats	667,863	56,320	-	724,183
Library books	582,184	123,637	-	705,821
	21,056,448	740,975	-	21,797,423
Less accumulated depreciation	(9,688,226)	(1,173,401)	-	(10,861,627)
	11,368,222	(432,426)	-	10,935,796
Net investment in capital assets	$ 12,823,907	$ (432,426)	$ -	$ 12,391,481

	Balance October 1, 2004	Additions	Retirements	Balance September 30, 2005
Non-depreciable assets:				
Land	$ 1,455,685	$ -	$ -	$ 1,455,685
Depreciable assets:				
Building	13,661,263	-	-	13,661,263
Furniture and equipment	5,488,476	656,662	-	6,145,138
Vehicles/boats	580,243	87,620	-	667,863
Library books	488,455	93,729	-	582,184
	20,218,437	838,011	-	21,056,448
Less accumulated depreciation	(8,517,109)	(1,171,117)	-	(9,688,226)
	11,701,328	(333,106)	-	11,368,222
Net investment in capital assets	$ 13,157,013	$ (333,106)	$ -	$ 12,823,907

(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, 2006 and 2005, receivables from the FSM National Government amounted to $1,620,451 and $2,424,805, respectively, net of an allowance for doubtful accounts of $0 and $76,388, respectively.

Payable to affiliates is comprised of the following at September 30, 2006 and 2005:

	2006	2005
FSM National Government	$ 460	$ 3,050
FSM Telecommunications Corporation	8,021	8,636
	$ 8,481	$ 11,686

(8) Contingencies

COM-FSM purchases commercial insurance to cover its potential risks from fire and property damage on some of its building and contents. COM-FSM is substantially self-insured for all other risks. In the event of a catastrophe, COM-FSM may be self-insured to a material extent. Settlements have not exceeded insurance coverage in the past three years.

COM-FSM is party to various legal proceedings. Legal counsel is of the opinion that the probable outcome of these proceedings is not predictable but will have no material impact on the accompanying financial statements.

During fiscal years ended September 30, 2006 and 2005, immaterial unreconciled differences exist between the College's and COM Land Grant's financial records. The College is resolving this matter with its counterpart and such reconciliation is not expected to have a material impact on the accompanying financial statements.

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

Board of Regents
College of Micronesia-FSM:

We have audited the financial statements of the College of Micronesia-FSM as of and for the year ended September 30, 2006, and have issued our report thereon dated May 22, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered College of Micronesia-FSM's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

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

We noted certain matters that we reported to management of the College of Micronesia-FSM's in a separate letter dated May 22, 2007.

This report is intended solely for the information and use of the College of Micronesia-FSM, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

Deloitte & Touche LLP

May 22, 2007

Deloitte.

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND INTERNAL CONTROL OVER COMPLIANCE APPLICABLE TO EACH MAJOR FEDERAL AWARD PROGRAM AND ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Board of Regents
College of Micronesia-FSM:

Compliance

We have audited the compliance of College of Micronesia-FSM with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2006. College of Micronesia-FSM's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (page 32). Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of College of Micronesia-FSM's management. Our responsibility is to express an opinion on College of Micronesia-FSM's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about College of Micronesia-FSM's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the College of Micronesia-FSM's compliance with those requirements.

In our opinion, the College of Micronesia-FSM complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended September 30, 2006.

Internal Control Over Compliance

The management of the College of Micronesia-FSM is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the College of Micronesia-FSM's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of the College of Micronesia-FSM, as of and for the year ended September 30, 2006, and have issued our report thereon dated May 22, 2007. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of the management of the College of Micronesia-FSM. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects when considered in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the College of Micronesia-FSM, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.

Deloitte & Touche LLP

May 22, 2007

COLLEGE OF MICRONESIA-FSM

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2006

Grantor/Program Title	CFDA Number	Expenditures
U.S. Department of Education:		
Federal Pell Grant Program	84.063	$ 7,052,524
Federal Supplemental Education Opportunity Grant	84.007	185,500
Federal Work-Study Program	84.033	145,750
TRIO: Upward Bound	84.047	1,069,815
TRIO: Talent Search	84.044	244,997
TRIO: Student Support Services	84.042	215,672
Bilingual Education: Professional Development	84.195	390,037
Gaining Early Awareness and Readiness for Undergraduate Programs	84.334	86,590
Total U.S. Department of Education		$ 9,390,885
U.S. Department of the Interior:		
Compact of Free Association II, Amended	15.875	$ 3,800,000
Compact of Free Association II, Amended(SEG)	15.875	453,733
Operation and Maintenance Technical Assistance	15.875	141,876
Total U.S. Department of the Interior		$ 4,395,609
Total Federal Awards		$ 13,786,494

Notes: The above grants are received in a direct capacity from the U.S. Department of Education and the U.S. Department of the Interior, with the exception of the Compact of Free Association, as amended, which is received in a subrecipient capacity through the FSM National Government. The Schedule of Expenditures of Federal Awards is prepared on the accrual basis of accounting.

Reconciliation to financial statements:

Total federal awards expenditures:	$ 13,786,494
Depreciation	1,173,401
Non-federal awards	3,308,314
Total expenditures per financial statements	$ 18,268,209

Part I - Summary of Auditors' Results

1. The Independent Auditors' Report on the financial statements expressed an unqualified opinion.
2. No reportable conditions in internal control over financial reporting were identified.
3. No instances of noncompliance considered material to the financial statements were disclosed by the audit.
4. No reportable conditions in internal control over compliance with requirements applicable to major federal awards programs were identified.
5. The Independent Auditors' Report on compliance with requirements applicable to major federal award programs expressed an unqualified opinion.
6. The audit disclosed no findings required to be reported by OMB Circular A-133.
7. COM-FSM's major programs were:

CFDA Number	Name of Federal Program or Cluster
U.S. Department of Education:	
	Federal Student Aid Cluster:
84.063	Federal Pell Grant Program
84.033	Federal Work-Study Program
84.007	Federal Supplemental Opportunity Grant
	TRIO Cluster:
84.047	TRIO: Upward Bound
84.044	TRIO: Talent Search
84.042	TRIO: Student Support Services
15.875	Economic, Social and Political Development of the Territories: Compact of Free Association II, Amended

8. A threshold of $413,595 was used to distinguish between Type A and Type B programs, as those terms are defined in OMB Circular A-133.
9. COM-FSM did qualify as a low-risk auditee as that term is defined in OMB Circular A-133.

Part II – Federal Award Findings and Questioned Cost Section

No matters are reportable.

Part III - Financial Statement Findings Section

No matters are reportable.

COLLEGE OF MICRONESIA-FSM

Schedule of Unresolved Prior Year Questioned Costs
Year Ended September 30, 2006

The following is a summary of unresolved federal questioned costs for the College of Micronesia-FSM:

	Questioned Costs Set Forth in the Audit Report 2005	Questioned Costs Resolved	Questioned Costs at September 30, 2006
Unresolved Questioned Costs FY05	$ -	$ -	$ -
Costs questioned during the year ended September 30, 2006	-	-	-
Total questioned costs outstanding as of September 30, 2006			$ -