

**UTRIK ATOLL LOCAL GOVERNMENT**

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**FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT**

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**YEAR ENDED SEPTEMBER 30, 2007**

# UTRIK ATOLL LOCAL GOVERNMENT

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## INDEPENDENT AUDITORS' REPORT

Mayor John Kaiko  
Utrik Atoll Local Government  
Republic of the Marshall Islands:

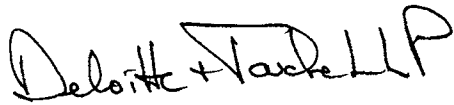
We have audited the accompanying financial statements of the governmental activities and each major fund of the Utrik Atoll Local Government (UALGOV) as of and for the year ended September 30, 2007, which collectively comprise UALGOV's basic financial statements as set forth in Section II of the foregoing table of contents. These financial statements are the responsibility of the management of UALGOV. Our responsibility is to express an opinion on the respective financial statements based on our audit.

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

In our opinion, such financial statements present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of UALGOV as of September 30, 2007, and the respective changes in financial position thereof for the year 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 7, as well as the Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund and notes thereto, as set forth in Section III of the foregoing table of contents, are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the management of UALGOV. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2008, on our consideration of the UALGOV's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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.

A handwritten signature in black ink that reads "Deloitte + Tatchell LLP". The signature is written in a cursive, slightly stylized font.

November 14, 2008

# UTRIK ATOLL LOCAL GOVERNMENT

## Management's Discussion and Analysis September 30, 2007

This Management Discussion and Analysis (MD&A) is submitted by Utrök Atoll Local Government (UALGOV) in compliance with Governmental Accounting Standards Board (GASB) and is intended to present an overview of the activities of the local government for the fiscal year ended September 30, 2007.

Fiscal Year 2007 outperformed all previous years since 2003. With incomes that are well above the projections, expenses that are equally managed well and lower total liabilities, FY2007 had been a fruitful year for UALGOV.

### UALGOV Funds and its Sources

1. Claims Trust Fund (CTF). This fund is awarded to UALGOV Local Distribution Authority (LDA) through the Nuclear Claims Tribunal for the purpose of compensating the exposed (directly affected by the radiation fall-out) people of Utrök Atoll. The corpus of this trust fund is not expendable. The income generated by the trust fund may be used for the distribution to people listed in the Utrök LDA; however, only 70% of such income is allowed to be disbursed as stated in the Claims Trust Fund Agreement.
2. Distribution Fund. This fund obtains funding from the income of the CTF. This disburses the payment for quarterly and land distribution to the LDA recipients.
3. General Fund. This fund sources its money from CTF. This is used for operating expenditures, which includes salaries, office rent, travels, session allowances, council meeting costs and other expenditures related to operations of the local government.

### Financial Highlights

1. UALGOV's net assets increased by \$486,500 or 2.9% over the course of this year's performance. CTF fund balance at the end of the year increased by \$541,000 or 3.3% as compared to last year's balance.
2. Total revenues dramatically increased by \$1.27 million or 98% while expenses for the year increased by \$31,567 or 1.5%.
3. Expenditures for the General Fund and Distribution Fund decreased by \$53,800 or 8.4% and \$80 or 0.01%, respectively.

### Financial Status

This analysis serves as an overview of UALGOV's basic financial statements. The Statement of Net Assets serves as a financial tool to measure the net worth of the local government. It shows the resources, liabilities and net assets. At the end of fiscal year 2007, total assets of \$17.4 million exceeded total liabilities of \$96,000.

#### Statement of Net Assets

	<u>2007</u>	<u>2006</u>
Cash and cash equivalents	\$ 198,944	\$ 172,032
Receivables, net	13,025	81,081
Investments	17,156,831	16,615,857
Capital assets, net	<u>106,059</u>	<u>115,107</u>
Total assets	17,474,859	16,984,077

## UTRIK ATOLL LOCAL GOVERNMENT

### Management's Discussion and Analysis September 30, 2007

Less current liabilities	<u>96,455</u>	<u>92,208</u>
Net assets	\$ <u>17,378,404</u>	\$ <u>16,891,869</u>
Net assets:		
Invested in capital assets	\$ 106,059	\$ 115,107
Restricted	17,156,831	16,615,857
Unrestricted	<u>115,514</u>	<u>160,905</u>
Total net assets	\$ <u>17,378,404</u>	\$ <u>16,891,869</u>

- Receivables decreased due mainly to collection of the DOI Fiscal Management Grant during the year. A receivable of \$9,755 was recorded for the year that pertains to the USDA Food Grant expenses paid by the local government. Ministry of Finance subsequently partly released the reimbursement in October 2008.
- CTF fair value increased by \$540,900 or 3.3% after deductions for investment management fees and drawdowns. This is the result of a good performance of the CTF portfolio that brought a net income of \$2.17 million before drawdowns.
- Capital assets comprise an airport terminal on Rongelap Atoll as well as certain motor vehicles. Additional information on UALGOV's capital assets can be found in note 4 to the financial statements.

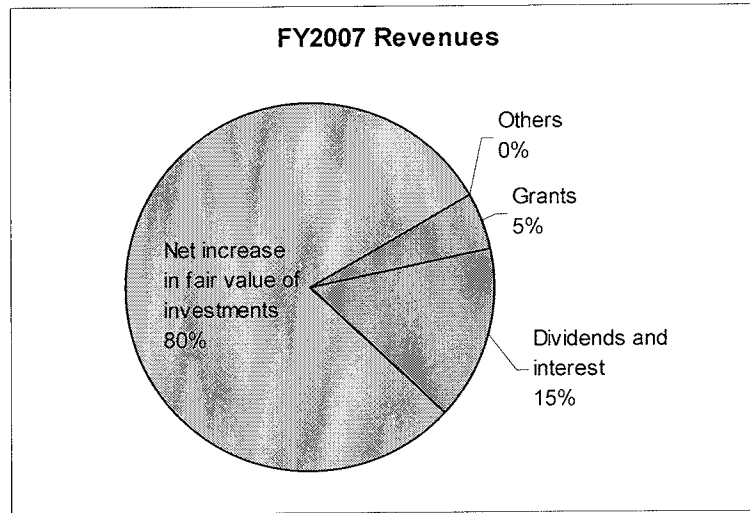
The Statement of Activities shows total revenues and total expenses during the fiscal year. Total revenues increased as well as total expenses as compared to last year.

#### Change in Net Assets

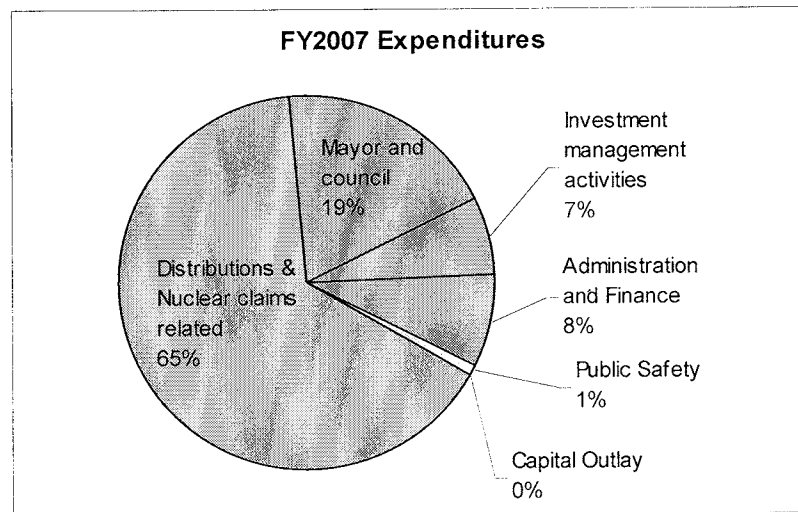
	<u>2007</u>	<u>2006</u>
Revenues:		
Grants	\$ 128,356	\$ 207,289
Dividends and interest	392,819	443,338
Net increase in the fair value of investments	2,057,347	649,121
Other	<u>1,601</u>	<u>5,613</u>
Total revenues	<u>2,580,123</u>	<u>1,305,361</u>
Less expenses:		
Distributions and Nuclear claims related	1,359,988	1,389,741
Mayor and council	410,190	326,882
Investment management activities	141,832	148,414
Administration and finance	166,892	182,417
Public safety	<u>14,686</u>	<u>14,567</u>
Total expenses	<u>2,093,588</u>	<u>2,062,021</u>
Change in net assets	486,535	(756,660)
Net assets at the beginning of year	<u>16,891,869</u>	<u>17,648,529</u>
Net assets at end of fiscal year	\$ <u>17,378,404</u>	\$ <u>16,891,869</u>

# UTRIK ATOLL LOCAL GOVERNMENT

## Management's Discussion and Analysis September 30, 2007



- Although the dividends and interest income decreased by \$50,000 or 11%, the net increase in fair value of investments of \$1.4 million or 216% was enough to bring up the investment balance at the end of the year.
- Grants for this year are:
  - \$117,524-from USDA Food Grant
  - \$4,515-from USDOJ Fiscal Management Grant
  - \$6,317-from USDOC for sale of NOAA boat



- The composition of the expenditures is basically the same as with last year.

### General Fund Budget Analysis

For fiscal year 2007, the General Fund has a deficiency of revenues and other financing sources under expenditures of \$45,403. See details below:

## UTRIK ATOLL LOCAL GOVERNMENT

Management's Discussion and Analysis  
September 30, 2007

### Budget and Actual-General Fund

	<u>Budget</u>	<u>Actual</u>	<u>Variance</u>
<b>Expenditures:</b>			
Salaries, wages and benefits	\$ 118,000	\$ 124,274	\$ (6,274)
Honorarium and sitting fees	104,550	135,882	(31,332)
Travel and stipends	102,000	58,715	43,285
Food program	-	118,077	(118,077)
Professional services	66,000	61,973	4,027
Contractual services	30,000	26,035	3,965
Contributions	5,000	1,020	3,980
Representation	2,000	144	1,856
Rental	21,000	20,005	995
Communications	8,200	10,675	(2,475)
Materials and supplies	9,350	4,870	4,480
Motor Vehicle	-	1,000	(1,000)
Equipment	-	3,438	(3,438)
Developmental Project	96,000	-	96,000
Miscellaneous	<u>53,950</u>	<u>16,612</u>	<u>37,338</u>
Total expenditures	<u>616,050</u>	<u>582,720</u>	<u>33,330</u>
<b>Less revenues:</b>			
Transfer in	432,050	407,360	(24,690)
Grants	169,000	128,356	(40,644)
Grant-in-aid	15,000	-	(15,000)
Other revenues	<u>-</u>	<u>1,601</u>	<u>1,601</u>
Total revenues	<u>616,050</u>	<u>537,317</u>	<u>(78,733)</u>
Deficiency of revenues under expenditures	-	(45,403)	(45,403)
Unreserved fund balance at beginning of year	<u>249,906</u>	<u>249,906</u>	<u>-</u>
Unreserved fund balance at end of year	\$ <u>249,906</u>	\$ <u>204,503</u>	\$ <u>(45,403)</u>

- Salaries account has a negative variance of \$6,274 primarily due to the hiring of an office clerk/radio operator in October 2006.
- Honorarium and sitting fees has a negative variance of \$31,000 mainly due to the payment during the year of FY2008 Session allowances of the council members amounting to \$32,000.
- A \$43,285 saving in travel and stipends is brought about by fewer international and domestic travels than budgeted for. Travel during the year was mainly to Washington D.C for the senate hearing and to New York for the investment committee meeting.
- A \$96,000 positive variance in Developmental projects is due to non utilization of this budget during the year. Projects were postponed for the next fiscal year.
- On December 2006, UALGOV received \$59,375 from Venture Pacific Marine Inc. for the sale proceeds of the Utrök boat. The McArthur Research Vessel was previously donated by the National Oceanic and Atmospheric Administration (NOAA) to UALGOV. However, due to excessively expensive renovation and operation costs that had to be shouldered by UALGOV, the management opted to sell the same with the approval of NOAA.

## **UTRIK ATOLL LOCAL GOVERNMENT**

Management's Discussion and Analysis  
September 30, 2007

### **NEXT YEAR'S BUDGET**

Next year's budget is basically the same but decreased by \$37,000 due to council's decision to cut down on expenditures and save on drawdowns from UCTF. The large cut was effected on contractual, stipends, food stuff and contingent/miscellaneous expenditures accounts. The distribution payments for quarterly and land compensations are the same as the previous years.

As of the preparation of this report, the U.S. Financial Market was heavily hit by the Housing Mortgage crisis. U.S. equity markets fell steeply following the depressing developments on the banking and insurance industry. The financial impact of these happenings to CTF was a gross loss of \$1.5M (from October 1, 2007 to September 30, 2008). With this, the return for FY2008 fell short of the usual 8% projected annual income of CTF.

### **CONTACTING UALGOV's MANAGEMENT**

This financial report is designed to provide our constituents, donors and customers with a general overview of UALGOV's finances and to demonstrate transparency and accountability for the money it is entrusted to manage. If you have any questions about this report or need additional information, contact the Mayor at P.O. Box 1499, Majuro, Marshall Islands, MH 96960, telephone number (692) 625-3749.

# UTRIK ATOLL LOCAL GOVERNMENT

## Statement of Net Assets September 30, 2007

### ASSETS

#### Current assets:

Cash and cash equivalents	\$ 198,944
Receivables, net	<u>13,025</u>
Total current assets	<u>211,969</u>

#### Noncurrent assets:

##### Restricted assets:

Investments	17,156,831
Capital assets, net of accumulated depreciation	<u>106,059</u>

Total noncurrent assets 17,262,890

Total assets \$ 17,474,859

### LIABILITIES

#### Current liabilities:

Accounts payable	\$ 7,122
Distribution payable	18,219
Deferred income	59,375
Other liabilities and accruals	<u>11,739</u>

Total liabilities 96,455

#### Contingencies

### NET ASSETS

Invested in capital assets	106,059
Restricted for:	
Nonexpendable	17,156,831
Unrestricted	<u>115,514</u>
Total net assets	<u>17,378,404</u>
Total liabilities and net assets	<u>\$ 17,474,859</u>

See accompanying notes to basic financial statements.

## UTRIK ATOLL LOCAL GOVERNMENT

Statement of Activities  
Year Ended September 30, 2007

<u>Functions/Programs</u>	Program Revenues			<u>Net (Expenses) Revenues</u>
	<u>Expenses</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>	
Governmental activities:				
Mayor and council	\$ 410,190	\$ 123,841	\$ -	\$ (286,349)
Administration and finance	166,892	4,515	-	(162,377)
Public safety	14,686	-	-	(14,686)
Nuclear claims related	1,359,988	-	-	(1,359,988)
Investment management activities	141,832	-	-	(141,832)
	\$ 2,093,588	\$ 128,356	\$ -	(1,965,232)
General revenues:				
Investment earnings				2,450,166
Other				1,601
Total general revenues				2,451,767
Change in net assets				486,535
Net assets at beginning of the year				16,891,869
Net assets at end of the year				\$ 17,378,404

See accompanying notes to basic financial statements.

**UTRIK ATOLL LOCAL GOVERNMENT**

Balance Sheet  
Governmental Funds  
September 30, 2007

<u>ASSETS</u>	<u>General</u>	<u>Special Revenue Local Distribution Authority</u>	<u>Permanent Claims Trust</u>	<u>Total</u>
Cash and cash equivalents	\$ 194,853	\$ 4,091	\$ -	\$ 198,944
Receivables, net	11,025	2,000	-	13,025
Due from other funds	74,993	-	-	74,993
Restricted assets:				
Investments	-	-	17,156,831	17,156,831
	<u>\$ 280,871</u>	<u>\$ 6,091</u>	<u>\$ 17,156,831</u>	<u>\$ 17,443,793</u>
 <u>LIABILITIES AND FUND BALANCES</u>				
Liabilities:				
Accounts payable	\$ 5,807	\$ 1,315	\$ -	\$ 7,122
Distribution payable	-	18,219	-	18,219
Deferred revenue	59,375	-	-	59,375
Other liabilities and accruals	11,186	553	-	11,739
Due to other funds	-	74,993	-	74,993
Total liabilities	<u>76,368</u>	<u>95,080</u>	<u>-</u>	<u>171,448</u>
Fund balances (deficit):				
Reserved for:				
Claims	-	-	17,156,831	17,156,831
Unreserved (deficit)	<u>204,503</u>	<u>(88,989)</u>	<u>-</u>	<u>115,514</u>
Total fund balances (deficit)	<u>204,503</u>	<u>(88,989)</u>	<u>17,156,831</u>	<u>17,272,345</u>
Total liabilities and fund balances	<u>\$ 280,871</u>	<u>\$ 6,091</u>	<u>\$ 17,156,831</u>	
 Amounts reported for governmental activities in the statement of net assets are different because:				
Capital assets used in governmental activities are financial resources and, therefore, are not not reported in the funds				<u>106,059</u>
Net assets of governmental activities				<u>\$ 17,378,404</u>

See accompanying notes to basic financial statements.

## UTRIK ATOLL LOCAL GOVERNMENT

Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit)  
 Governmental Funds  
 Year Ended September 30, 2007

	General	Special Revenue Local Distribution Authority	Permanent Claims Trust	Total
<b>Revenues:</b>				
Net increase in the fair value of investments	\$ -	\$ -	\$ 2,057,347	\$ 2,057,347
Dividends and interest	-	-	392,819	392,819
Federal grants	128,356	-	-	128,356
Other	1,601	-	-	1,601
Total revenues	129,957	-	2,450,166	2,580,123
<b>Expenditures:</b>				
<b>Current:</b>				
Mayor and council	400,142	-	-	400,142
Administration and finance	166,892	-	-	166,892
Public safety	14,686	-	-	14,686
Nuclear claims related	-	1,219,988	140,000	1,359,988
Investment management	-	-	141,832	141,832
Capital outlay	1,000	-	-	1,000
Total expenditures	582,720	1,219,988	281,832	2,084,540
Excess (deficiency) of revenues over (under) expenditures	(452,763)	(1,219,988)	2,168,334	495,583
<b>Other financing sources (uses):</b>				
Operating transfers in	407,360	1,220,000	-	1,627,360
Operating transfers out	-	-	(1,627,360)	(1,627,360)
Total other financing sources (uses), net	407,360	1,220,000	(1,627,360)	-
Net change in fund balances (deficit)	(45,403)	12	540,974	495,583
Fund balances (deficit) at beginning of year	249,906	(89,001)	16,615,857	16,776,762
Fund balances (deficit) at end of year	\$ 204,503	\$ (88,989)	\$ 17,156,831	\$ 17,272,345

See accompanying notes to basic financial statements.

**UTRIK ATOLL LOCAL GOVERNMENT**

Reconciliation of the Statement of Revenues, Expenditures,  
and Changes in Fund Balances (Deficit) of Governmental Funds  
to the Statement of Activities  
Year Ended September 30, 2007

Net change in fund balances (deficit) - total governmental funds from page 11	\$ 495,583
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation expense exceeded capital outlays in the current period.	<u>(9,048)</u>
Change in net assets of governmental activities as presented on page 9	<u>\$ 486,535</u>

See accompanying notes to basic financial statements.

# UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

## (1) Organization

The Utrik Atoll Local Government (UALGOV) was established pursuant to Public Law 1981-2, the Local Government Act of the Republic of the Marshall Islands and operates under the Constitution of the Utrik Atoll Local Government. UALGOV is governed by an elected mayor and a thirty two-member council.

## (2) Summary of Significant Accounting Policies

The accompanying financial statements of UALGOV have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as applied to government units. The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of UALGOV's accounting policies are described below.

### A. Government-Wide Financial Statements

The Statement of Net Assets and the Statement of Activities report financial information on all of the non-fiduciary activities of UALGOV. UALGOV's activities are defined as governmental activities, which are supported by intergovernmental revenues and other non-exchange revenues.

The Statement of Net Assets presents all of UALGOV's non-fiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt that are attributed to the acquisition, construction or improvement of those assets.
- Restricted net assets – nonexpendable consists of permanent funds in which donors or other outside sources have stipulated 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 the principal.
- Restricted net assets – expendable consists of resources in which UALGOV is legally or contractually obligated to spend resources in accordance with restrictions either externally imposed by creditors, grantors, contributors, and the like, or imposed by law.
- Unrestricted net assets consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, (for example, internally restricted), to indicate that management does not consider them to be available for general operations.

The Statement of Activities demonstrates the degree to which the direct expenses of given functions or segments are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function or segment. Program revenues include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items not meeting the definition of program revenues are, instead, reported as general revenue.

# UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

## (2) Summary of Significant Accounting Policies, Continued

### B. Fund Financial Statements

The fund financial statements present a balance sheet and a statement of revenues, expenditures, and changes in fund balances for UALGOV's major funds. Major individual governmental funds are reported as separate columns in the fund financial statements pursuant to GASB reporting standards.

UALGOV reports its financial position and results of operations in funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures/expenses. Transactions between funds within a fund type, if any, have not been eliminated.

### C. Measurement Focus and Basis of Accounting

The government-wide financial statements are reported using the economic resources management focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements account for the general governmental activities of UALGOV and are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as they become susceptible to accrual; generally when they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, UALGOV considers revenues to be available if they are collected within 90 days of the end of the current fiscal period.

Miscellaneous revenues from other financing sources are recognized when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available. 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. Expenditures generally are recorded in the period in which the related fund liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Amounts reported as program revenue include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as general revenues rather than as program revenues. General revenue is derived from taxation, investment income and other fees that are not allocated to specific programs.

# UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

## (2) Summary of Significant Accounting Policies, Continued

### C. Measurement Focus and Basis of Accounting, Continued

UALGOV reports the following governmental fund types:

#### i. General Fund

This fund is the primary operating fund of UALGOV. It is used to account for all governmental transactions, except those required to be accounted for in another fund.

#### ii. Special Revenue Fund

This fund accounts for specific revenue resources that have been aggregated according to enabling legislation to support specific governmental activities.

The special revenue fund of UALGOV (the Local Authority Distribution Fund) accounts for funds received under the Utrik Claims Trust Fund. These funds are distributed by UALGOV to the people of Utrik based on an approved distribution scheme.

#### iii. Permanent Fund

This fund accounts for resources that are legally restricted to the extent that only earnings, and not principal, may be used to support programs for the benefit of the government.

UALGOV's permanent fund (the Claims Trust Fund) accounts for funds received under Article II, Section 4, of the agreement between the Government of the United States and the Government of the Republic of the Marshall Islands for the implementation of Section 177 of the Compact of Free Association (the Compact). In accordance with Article II, Section 8, of the Compact, UALGOV executed the Utrik Claims Trust Agreement and established the Claims Trust Fund. Pursuant to Section 4.2 of the trust agreement, after the final payment was received on October, 2001, the Claim Trust Fund was required to distribute annually to the people of Utrik between 15% and 70% of its net income. In addition, pursuant to Section 5.1 of the trust agreement, UALGOV may also invade up to 3% of the corpus of the Claims Trust Fund. Such invasion may occur in the event of an unforeseen natural disaster or other similar circumstance, as determined by the sole discretion of UALGOV Council, in order to prevent hardship to the people of Utrik. An invasion of the corpus shall not occur more frequently than once every three years.

### D. Cash and Cash Equivalents

Cash and cash equivalents include cash held in demand accounts.

### E. Investments

Investments are carried at fair value. Fair value is the amount at which an investment could be exchanged in a current transaction between willing parties.

**UTRIK ATOLL LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2007

(2) Summary of Significant Accounting Policies, Continued

F. Receivables

Receivables consist of amounts advanced to individuals, on an unsecured basis, substantially all of whom are situated in the Republic of the Marshall Islands. Receivables are stated net of allowances for uncollectable accounts.

Receivables as of September 30, 2007, for the primary government's individual major governmental funds, including applicable allowance for uncollectible accounts, are as follows:

	<u>General</u>	<u>Local Distribution Authority</u>	<u>Total</u>
Receivables:			
Federal grants receivable	\$ 9,755	\$ -	\$ 9,755
Loan receivable	4,309	-	\$ 4,309
Other	<u>16,523</u>	<u>2,000</u>	<u>18,523</u>
Gross receivable	30,587	2,000	32,587
Less allowance for uncollectible account	<u>(19,562)</u>	-	<u>(19,562)</u>
	<u>\$ 11,025</u>	<u>\$ 2,000</u>	<u>\$ 13,025</u>

G. Interfund Receivables/Payables

During the course of its operations, UALGOV records transactions between individual funds for goods provided or services rendered. Receivables and payables resulting from transactions between funds are classified as "due from other funds" or "due to other funds" on the governmental funds balance sheet.

Interfund receivables and payables have been eliminated from the statement of net assets.

H. Restricted Assets

Certain assets of UALGOV are classified as restricted assets because their use is completely restricted by trust agreements or enabling legislation. Specifically, investments of \$17,156,831 recorded in the Claims Trust Fund are restricted in that they are not available to be used in current operations.

I. Capital Assets

Capital assets, which include property, plant and equipment and infrastructure assets (e.g. pads, docks, airports, water catchments, and other similar items), whether purchased or constructed, are recorded at historical cost. UALGOV capitalizes all capital assets that exceed \$5,000 and have a useful life greater than one year. Depreciation is provided over the estimated useful lives of the assets through use of the straight-line method. The estimated useful lives of these assets are as follows:

Airport terminal	25 years
Motor vehicles	3 years

# UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

## (2) Summary of Significant Accounting Policies, Continued

### J. Interfund/Intrafund Transactions

As a general rule, the effect of interfund activity has been eliminated in the government-wide statements. Exceptions to this rule are: 1) activities between funds reported as governmental activities and funds reported as business-type activities and 2) activities between funds that are reported in different functional categories in either the governmental or business-type activities column. Elimination of these activities would distort the direct costs and program revenues for the functions concerned.

### K. Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the general purpose financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

### L. Compensated Absences

UALGOV recognizes expenditures for annual leave and sick leave when leave is actually taken. Accordingly, unused annual leave and sick leave are not included as an obligation within the governmental funds balance sheet. The estimated accumulated amounts of unused annual and sick leave at September 30, 2007 are presently not determinable.

### M. New Accounting Standards

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, 2006. Management does not believe that the implementation of this statement will have a material effect on the financial statements of UALGOV.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other post employment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of UALGOV.

In September 2006, GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues*. GASB Statement No. 48 establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing. The statement also includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. The provisions of this statement are effective for periods beginning after December 15, 2006. Management does not believe that the implementation of this statement will have a material effect on the financial statements of UALGOV.

## UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

### (2) Summary of Significant Accounting Policies, Continued

#### M. New Accounting Standards, Continued

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB Statement No. 49 provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of UALGOV.

In May 2007, GASB issued Statement No. 50, *Pension Disclosures an amendment of GASB Statements No. 25 and 27*. GASB Statement No. 50 more closely aligns the financial reporting requirements for pensions with those for other post-employment benefits. The provisions of this statement are effective for periods beginning after June 15, 2007. Management does not believe the implementation of this statement will have a material effect on the financial statements of UALGOV.

In June 2007, GASB issued statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. GASB Statement No. 51 addresses whether and when intangible assets should be considered capital assets for financial reporting purposes. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of UALGOV.

### (3) Deposits and Investments

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

UALGOV does not have formal deposit and investment policies. Investments in the Claims Trust Fund are governed by a trust agreement.

#### A. Deposits

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

- Category 1 Deposits that are federally insured or collateralized with securities held by UALGOV or its agent in UALGOV'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 UALGOV'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 UALGOV's name and non-collateralized deposits.

# UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

## (3) Deposits and Investments, Continued

### A. Deposits, Continued

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, UALGOV'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. UALGOV does not have a deposit policy for custodial credit risk.

As of September 30, 2007, the carrying amount of the UALGOV's total cash and cash equivalents was \$198,944 and the corresponding bank balance was \$221,579. Of the bank balance amount, \$173,117 is maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2007, bank deposits in the amount of \$100,000 were FDIC insured. UALGOV does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

### B. Investments

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

- Category 1      Investments that are insured or registered, or securities held by UALGOV or its agent in UALGOV'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 UALGOV'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 UALGOV'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.

**UTRIK ATOLL LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2007

**(3) Deposits and Investments, Continued**

**B. Investments, Continued**

Permanent Fund:

As of September 30, 2007, investments at fair values are as follows:

Claims Trust Fund:		
Cash management	\$	1,051,867
Future managed assets		1,550,203
Domestic equities		10,686,501
U.S. Government notes and bonds		2,990,335
Corporate notes and bonds		716,938
Exchange traded equity funds		<u>160,987</u>
	<b>\$</b>	<b><u>17,156,831</u></b>

The Claims Trust Fund investments are held and administered by a trustee agreement. Based on negotiated trust and custody contracts, all of these investments were held in the name of UALGOV by their custodial financial institutions at September 30, 2007.

As of September 30, 2007 investments in debt securities were as follows:

	S & P Rating	<u>Investment Maturities (In years)</u>				Total
		<u>Less than 1</u>	<u>1 to 5</u>	<u>6 to 10</u>	<u>Greater than 10</u>	
U.S. Treasury Obligations	AAA	\$ -	\$ 1,870,046	\$ 538,954	\$ -	\$ 2,409,000
U.S. Government agencies	AA-	-	320,345	-	-	320,345
U.S. Government agencies	AAA	-	260,991	-	-	260,991
Corporate bonds	A	-	165,583	-	-	165,583
Corporate bonds	AA+	-	111,252	-	-	111,252
Corporate bonds	AAA	-	82,790	-	-	82,790
Corporate bonds	AA-	-	74,446	-	-	74,446
Corporate bonds	A-	-	150,180	-	-	150,180
Corporate bonds	A+	-	-	74,484	-	74,484
Corporate bonds	BBB-	-	-	<u>58,202</u>	-	<u>58,202</u>
		<u>\$ -</u>	<u>\$ 3,035,633</u>	<u>\$ 671,640</u>	<u>\$ -</u>	<u>\$ 3,707,273</u>

UALGOV does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

## UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

### (4) Capital Assets

Capital asset activities during the year ended September 30, 2007, are as follows:

	<u>Balance October 1, 2006</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance September 30, 2007</u>
Airport terminal	\$ 90,310	\$ -	\$ -	\$ 90,310
Motor vehicles	77,145	18,000	(36,550)	58,595
Less accumulated depreciation	<u>(52,348)</u>	<u>(15,327)</u>	<u>24,829</u>	<u>(42,846)</u>
	<u>\$ 115,107</u>	<u>\$ 2,673</u>	<u>\$ (11,721)</u>	<u>\$ 106,059</u>

Depreciation expense of \$11,715 was charged to Mayor and Council and \$3,612 was charged to Administration and Finance.

### (5) Transfers In/Out

Operating transfers in/out for all fund types, for the year ended September 30, 2007, are as follows:

<u>Source</u>	<u>Recipient</u>	<u>Transfer Out</u>	<u>Transfer In</u>
Claims Trust Fund	General Fund	\$ 407,360	\$ 407,360
Claims Trust Fund	Local Distribution Authority Fund	<u>1,220,000</u>	<u>1,220,000</u>
		<u>\$ 1,627,360</u>	<u>\$ 1,627,360</u>

### (6) Contingencies

#### Settlement Agreement

On May 9, 1997, UALGOV entered into a Settlement Agreement with the Bank of New York, the former trustee for the Utrik Claims Trust Fund. During fiscal year 1996, the Bank transferred \$390,000 of funds to the Utrik Local Distribution Authority (LDA) Fund, which should have been transferred to the Utrik Claims Trust Fund. These funds were subsequently loaned out or were otherwise disbursed by the LDA. Under the terms of the Settlement Agreement, the Bank agreed to reimburse the Utrik Claims Trust Fund the money erroneously transferred and UALGOV agreed to repay \$180,000 to the Bank plus any additional amounts that are subsequently identified and collected. As of September 30, 2007, UALGOV repaid \$180,000 under this agreement. Repayment of the remaining \$210,000 is contingent upon future collection of amounts previously loaned or disbursed by the LDA. UALGOV elected to not record the receivable for the loans amount and the related liability in the accompanying financial statements.

#### Section 177 Compact Funding

UALGOV received its final compensatory payment under the terms of the Compact on October 22, 2001. Management believes that investment income is sufficient to cover future cost of operations and distributions of the General Fund and the Local Distribution Authority Fund, respectively. However, in the event of a decline in future investment income, UALGOV will need to obtain revenue from other sources to be able to support its cost of operations and distributions.

## UTRIK ATOLL LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2007

### (7) Risk Management

UALGOV is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. UALGOV has elected to purchase commercial automobile insurance from independent third parties for the risks of loss to which it is exposed to with respect to the use of motor vehicles. Settled claims have not exceeded this commercial coverage in any of the past three years. For other risks of loss to which it is exposed, UALGOV has elected not to purchase commercial insurance. Instead, UALGOV management believes it is more economical to manage its risks internally. In the event of claim settlements and judgments, UALGOV reports all of its risk management activities in its General Fund.

Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. No material losses have resulted from UALGOV's risk management activities.

UTRIK ATOLL LOCAL GOVERNMENT  
REQUIRED SUPPLEMENTARY INFORMATION  
- BUDGETARY REPORTING  
YEAR ENDED SEPTEMBER 30, 2007

## UTRIK ATOLL LOCAL GOVERNMENT

### Schedule of Revenues, Expenditures and Changes in Fund Balance (Deficit) - Budget and Actual - General Fund Year Ended September 30, 2007

	Budgeted Amounts		Actual	Variance with
	Original	Final		Final Budget - Positive (Negative)
<b>Revenues:</b>				
Grant-in-aid	\$ 15,000	\$ 15,000	\$ -	\$ (15,000)
Federal and other grants	169,000	169,000	128,356	(40,644)
Other	-	-	1,601	1,601
<b>Total revenues</b>	<u>184,000</u>	<u>184,000</u>	<u>129,957</u>	<u>(54,043)</u>
<b>Expenditures:</b>				
Salaries, wages and benefits	118,000	118,000	124,274	(6,274)
Honorarium and sitting fees	104,550	104,550	135,882	(31,332)
Travel and stipends	102,000	102,000	58,715	43,285
Food program	-	-	118,077	(118,077)
Professional services	66,000	66,000	61,973	4,027
Contractual services	30,000	30,000	26,035	3,965
Contributions	5,000	5,000	1,020	3,980
Representation	2,000	2,000	144	1,856
Rental	21,000	21,000	20,005	995
Communications	8,200	8,200	10,675	(2,475)
Materials and supplies	9,350	9,350	4,870	4,480
Motor vehicle	-	-	1,000	(1,000)
Equipment	-	-	3,438	(3,438)
Development project	96,000	96,000	-	96,000
Miscellaneous	53,950	53,950	16,612	37,338
<b>Total expenditures</b>	<u>616,050</u>	<u>616,050</u>	<u>582,720</u>	<u>33,330</u>
<b>Deficiency of revenues under expenditures</b>	<u>(432,050)</u>	<u>(432,050)</u>	<u>(452,763)</u>	<u>(20,713)</u>
<b>Other financing sources:</b>				
Operating transfers in	432,050	432,050	407,360	(24,690)
<b>Deficiency of revenues and other financing sources under expenditures</b>	-	-	(45,403)	(45,403)
Unreserved fund balance at the beginning of year	249,906	249,906	249,906	-
<b>Unreserved fund balance at end of year</b>	<u>\$ 249,906</u>	<u>\$ 249,906</u>	<u>\$ 204,503</u>	<u>\$ (45,403)</u>

See Accompanying Independent Auditors' Report.

## UTRIK ATOLL LOCAL GOVERNMENT

### Notes to Required Supplementary Information - Budgetary Reporting September 30, 2007

#### Budgetary Information

The UALGOV constitution provides for the Executive Committee to introduce into the Council the proposed budget for the Fiscal Year effective October 1. The budget includes estimates of the proposed expenditures for all the funds and the sources of funds. The Executive members of the UALGOV Council review and recommend changes to the proposed budget during the budget deliberation prior to presentation to the Council. UALGOV council meeting holds public hearing/s during which the council presents to the constituents the proposed budget for the coming fiscal year. After all of the feedbacks are heard, the council en banc amends if necessary, and then approves the budget through an ordinance duly enacted by the Local Government Council.

Formal budget integration is employed as a management control device during the year for all funds. The Executive Council has the authority to reprogram budgeted estimates in accordance with the UALGOV Constitution. All annual appropriations lapse at fiscal year end unless otherwise specified in the Ordinance. Supplemental appropriations may occur throughout the year. Unexpended encumbrances at each fiscal year end are carried forward until they are expended or canceled without further ordinance for the matter.

Accounting principles used in developing data on a budgetary basis differ from those used in preparing the financial statements in conformity with GAAP. Amounts included on the Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund (which are presented on a non-GAAP budgetary basis) are reconciled to unreserved deficit of the Governmental Fund Balance Sheet within the other changes in unreserved deficit section of that statement.

Encumbrance accounting has not been utilized by the General Fund.