

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

**INDEPENDENT AUDITOR'S REPORT
AND
FINANCIAL STATEMENTS**

Years Ended September 30, 2010 and 2009

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

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SEPTEMBER 30, 2010 and 2009

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SAIPAN

Family Building, Suite 201
PMB 297 Box 10000
Saipan, MP 96950
Tel Nos. (670) 233-1837/0456
Fax No. (670) 233-8214

GUAM

Reflection Center, Suite 204
P.O. Box 12734
Tamuning, GU 96931
Tel Nos. (671) 472-2680/2687
Fax No. (671) 472-2686

PALAU

PIDC Apartment No. 11
P.O. Box 1266
Koror, PW 96940
Tel No. (680) 488-8615
Fax No. (680) 488-8616

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Palau District Housing Authority

I have audited the accompanying combined financial statements of Palau District Housing Authority (the Authority), a component unit of the Republic of Palau (ROP), as set forth in Section I of the foregoing Table of Contents, as of September 30, 2010 and 2009, and for the years then ended. These financial statements are the responsibility of the Authority's management. My responsibility is to express an opinion on these financial statements based on my audits. The prior year summarized comparative information has been derived from the Authority's 2009 financial statements and, in my report dated January 10, 2010, I expressed an unqualified opinion on those financial statements.

I conducted my 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 I plan and perform the audits 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 Authority's internal control over financial reporting. Accordingly, I do not express such an 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audits provide a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Palau District Housing Authority as of September 30, 2010 and 2009, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, I have also issued my report dated January 25, 2011 on my consideration of Palau District Housing Authority's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts, grants and other matters. The purpose of that report is to describe the scope of my 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 my audits.

The Management's Discussion and Analysis and Statistical Section on pages 3 through 14 and 46 through 49, respectively, are not a required part of the basic financial statements but are supplementary information required by the *Governmental Accounting Standards*. I have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, I did not audit the information and express no opinion on it.


Koror, Republic of Palau
January 25, 2011

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Management's Discussion and Analysis
September 30, 2010

As management of the Palau District Housing Authority (the Authority), a component unit of the Republic of Palau, we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal year ended September 30, 2010. We encourage readers to consider the information presented in conjunction with the Authority's financial statements, and accompanying notes to the financial statements on pages 15 through 41.

Financial Highlights

- The assets of the Authority exceeded its liabilities at September 30, 2010 by \$2,807,879 (net assets).
- The Authority's cash and cash equivalents at September 30, 2010 was \$971,330 representing a decrease of \$42,305 from September 30, 2009.
- The Authority had net operating revenues of \$169,703 and operating expenses of \$127,405 for the year ended September 30, 2010.
- The Authority's net assets (assets less liabilities) increased by \$197 from the previous year. Specifically, net assets were \$2.8 million in each year 2010 and 2009, and \$2.7 million in 2008. The increase in net assets is a result of revenues earned exceeding expenses incurred.

Overview of the Financial Statements

The Management Discussion and Analysis is intended to serve as an introduction to the Authority's basic financial statements. The Authority's basic financial statements are comprised of two components: 1) authority-wide financial statements; and 2) notes to the financial statements.

AUTHORITY-WIDE FINANCIAL STATEMENTS

The authority-wide financial statements are designed to provide readers with a broad overview of the Authority's finances, in a manner similar to a private-sector business.

The *Statement of Net Assets* presents information on all of the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Management's Discussion and Analysis
September 30, 2010

Overview of the Financial Statements, Continued

AUTHORITY-WIDE FINANCIAL STATEMENTS, Continued

The *Statement of Revenues, Expenses and Changes in Net Assets* presents information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this Statement for some items that will only result in cash flows in future fiscal periods (e.g., depreciation and earned but unused vacation leave).

The *Statement of Cash Flows* provides information about the Authority's cash receipts and cash payments during the reporting period. The Statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities.

The authority-wide financial statements report on the function of the Authority that is principally supported by intergovernmental revenues. The Authority's function is to develop and administer low-cost housing projects and to assist in correcting housing conditions endangering the health, safety, and welfare of the people residing in the Republic of Palau, which is funded primarily with grant revenue received from the U.S. Department of Housing and Urban Development.

The authority-wide financial statements can be found on pages 15 through 19 of this report.

NOTES TO THE FINANCIAL STATEMENTS

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the authority-wide financial statements. The notes to the financial statements can be found on pages 21 through 41 of this report.

PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

FUND FINANCIAL STATEMENTS

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is now on Major Funds rather than fund types. The Authority consists of exclusively Enterprise Funds. Enterprise funds utilize the full accrual basis of accounting. The Enterprise method of accounting is similar to accounting utilized by the private sector accounting.

Many of the funds maintained by the Authority are required by the U.S. Department of Housing and Urban Development. Others are segregated to enhance accountability and control.

Authority-Wide Financial Analysis

Fiscal year 2010 is the eighth year of implementation of Governmental Accounting Standards Board (GASB) Statement No. 34. The financial statement focuses on the Authority as a whole. The Authority's financial statements are designed to emulate corporate presentation models whereby all Authority activities are combined into one total. The focus of the Statement of Net Assets is designed to be similar to bottom line results for the Authority. This statement combines current financial resources (short-term spendable resources) with capital assets. The Statement of Revenues, Expenses, and Changes in Net Assets focuses on both the gross costs and the net costs of Authority activities which are supported mainly by appropriations from Palau National Congress (PNC) and by other revenues. This approach is intended to summarize and simplify the user's analysis of cost of Authority services to the public.

PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Authority-Wide Financial Analysis, Continued

Net Assets
As of September 30, 2010, 2009, and 2008

	2010	2009	2008
Assets			
Current assets:			
Cash and cash equivalents	\$ 971,330	\$ 929,025	\$ 973,467
Notes receivable, current portion	208,450	195,261	176,389
Accounts receivable	36,431	51,886	27,361
Due from grantor agency	30,375	30,375	-
Interest receivable	9,590	9,590	9,589
Due from other fund	55,000	45,000	45,000
Total current assets	1,311,176	1,261,137	1,231,806
Noncurrent assets:			
Notes receivable, net of current portion	1,631,538	1,605,668	1,555,558
Allowance for loan losses	(87,994)	(78,556)	(78,556)
Capital assets, net	23,552	39,555	22,424
Other assets	-	43,041	43,041
Total noncurrent assets	1,567,096	1,609,708	1,542,467
Total Assets	\$ 2,878,272	\$ 2,870,845	\$ 2,774,273

PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Authority-Wide Financial Analysis, Continued

Net assets			
As of September 30, 2010, 2009, 2008			
	2010	2009	2008
Liabilities			
Current Liabilities:			
Due to other fund	\$ 55,000	\$ 45,000	\$ 45,000
Accrued expenses	15,393	18,163	17,197
Total liabilities	70,393	63,163	62,197
Net Assets			
Invested in capital assets	23,552	39,555	22,424
Restricted	1,839,988	2,374,498	2,344,123
Unrestricted	944,339	393,629	345,529
Total net assets	2,807,879	2,807,682	2,712,076
Total Liabilities and Net Assets	\$ 2,878,272	\$ 2,870,845	\$ 2,774,273

This schedule is prepared from the Authority's Statement of Net Assets, which is presented on an accrual basis of accounting whereby liabilities and expenses are recorded when incurred, whether paid or not, and revenue is recorded when earned, whether received or not.

Total net assets as of FY 2010 remained at \$2.81 million as in FY 2009. There were (17) new loans approved in FY 2010 totaling \$254,907, of which, five approved loans aggregating \$150,000 are in various stages of construction.

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Management's Discussion and Analysis
September 30, 2010

Authority-Wide Financial Analysis, Continued

Noncurrent assets decreased from \$1.61 million in FY 2009 to \$1.57 million in FY 2010. The decrease is attributed to a decrease in capital assets and other assets. Of the total outstanding notes receivable, \$1,621,950 pertains to the Home Rehabilitation Loan Program as of September 30, 2010.

As noted earlier, net assets may serve over time as a useful indicator of an entity's financial position. In the case of the Authority, assets exceeded liabilities by \$2,807,879 as of September 30, 2010.

By far the largest portion of the Authority's net assets (66%) reflects its restricted net assets. Restricted net assets pertain to grants received from U.S. Department of Housing and Urban Development (HUD), contributions received from the Trust Territory of the Pacific Islands and from the Republic of Palau.

With prudent fund management, the Authority was able to increase its surplus from \$967,198 in FY 2009 to a surplus of \$944,339 in FY 2010.

Statement of Revenues, Expenses, and Changes in Net Assets

**Operating Revenues for the Year Ended
September 30, 2010**

Operating revenues:		
Republic of Palau appropriations	\$	60,000
Interest on loans		88,600
Section 8 income		13,550
National treasury income		9,000
Other		<u>15,605</u>
Total operating revenues	\$	<u><u>186,755</u></u>

The above schedule indicates total revenues realized by the Authority in FY 2010 totaling \$186,755. The Olbiil Era Kelulau (Palau National Congress) contributed \$60,000 and \$9,000 through cost reimbursement grants during FY 2010. The Authority draws down monies from the grant awards for allowable program expenses, except for non-cash transactions, such as depreciation expense and changes in compensated absences. The Authority's intergovernmental revenues and charges for services were sufficient to cover all expenses incurred during the year.

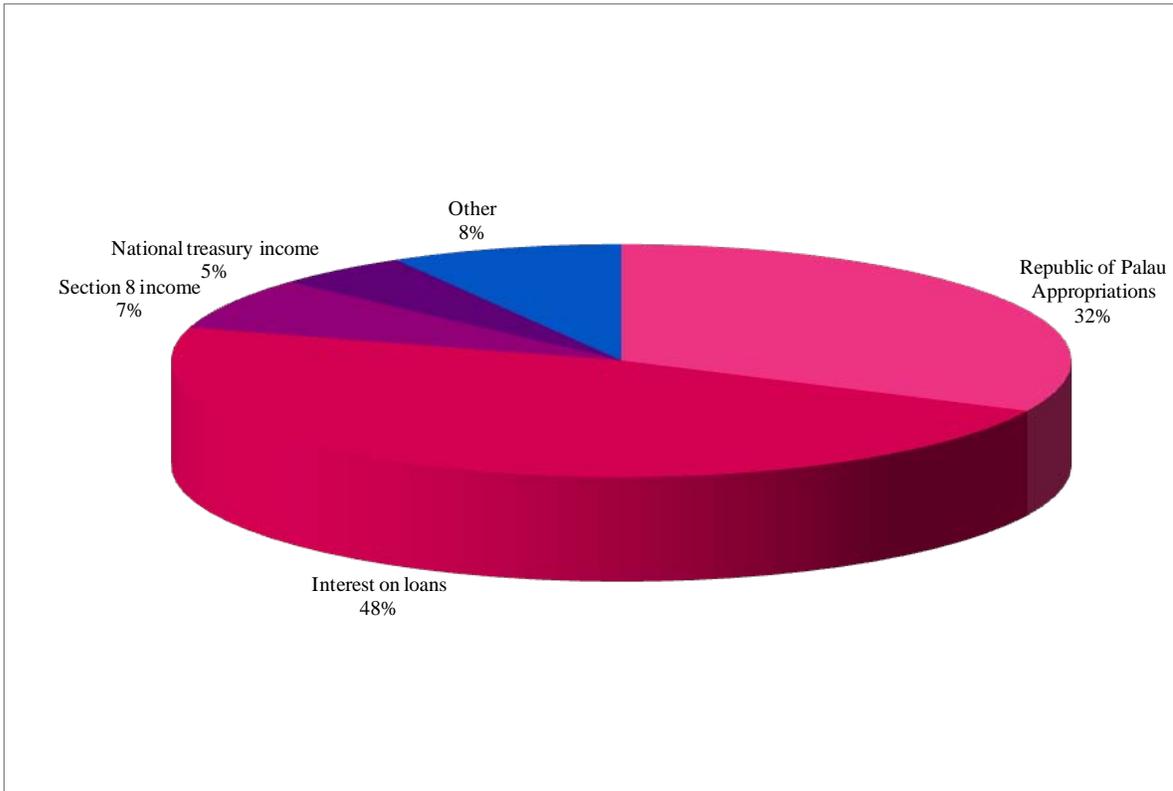
PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Authority-Wide Financial Analysis, Continued

The following chart exhibits the breakdown of revenues for Palau District Housing Authority in FY 2010.

Operating Revenues Breakdown



PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Authority-Wide Financial Analysis, Continued

**Operating Expenses for the Year Ended
September 30, 2010**

Operating expenses:

Salaries and wages	\$	65,458
Depreciation		14,549
Professional fees		12,000
Rent expense		11,320
Employee benefits		6,693
Travel		2,848
Communication		2,722
Repairs and maintenance		2,710
Miscellaneous		<u>9,105</u>
Total expenses	\$	<u>127,405</u>

The above schedule shows total operating expenses of \$127,405 in FY 2010.

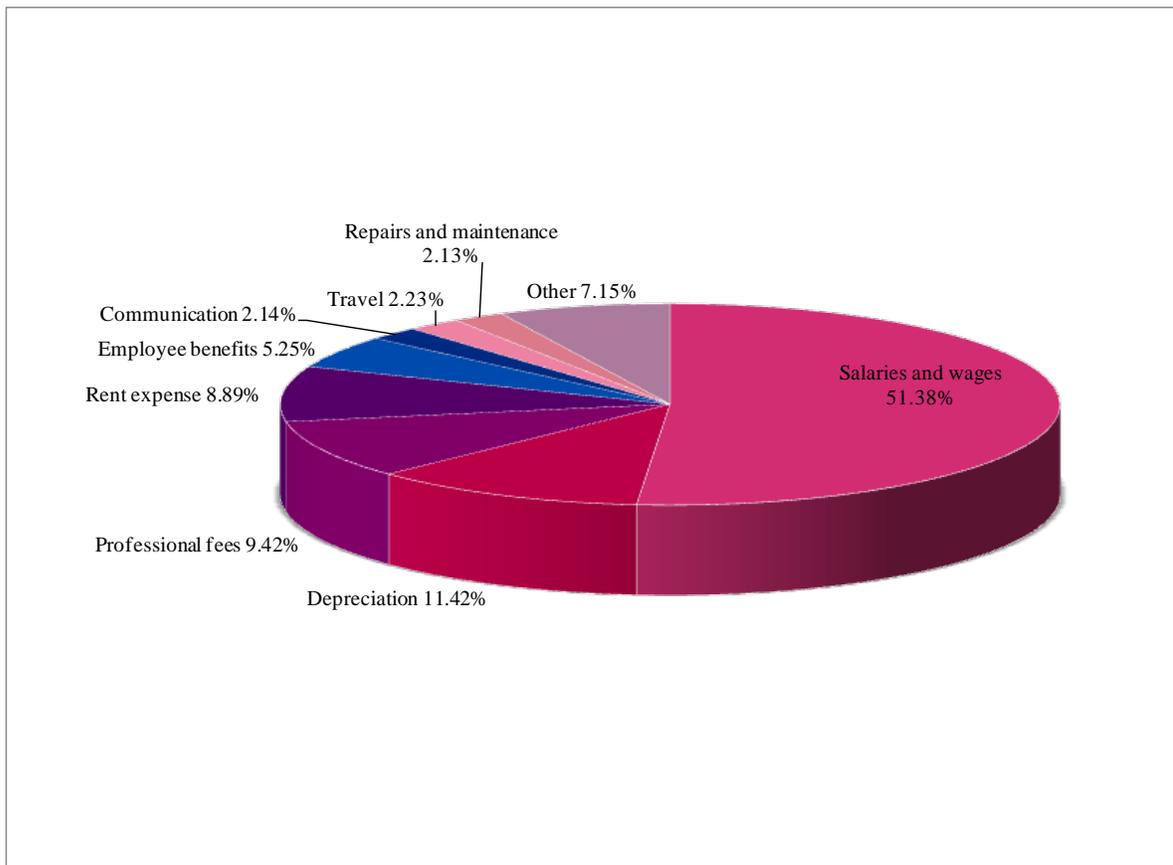
The largest expenditure in FY 2010 was for employee salaries and wages totaling \$65,458 covering four (4) full-time employees.

PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Authority-Wide Financial Analysis, Continued

Expense Breakdown
For Year Ended September 30, 2010



PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Authority-Wide Financial Analysis, Continued

CAPITAL ASSETS

As of September 30, 2010, the Authority's investment in capital assets for its business-type activities was \$23,552 (net of accumulated depreciation) as reflected in the following schedule:

Residential units	\$ 213,431
Furniture, fixtures and equipment	37,328
Vehicles	<u>45,979</u>
	296,738
Accumulated depreciation	<u>(273,186)</u>
Total	<u>\$ 23,552</u>

Additional information on the Authority's capital assets can be found in Notes 1 and 6 of the accompanying Notes to Combined Financial Statements.

BUDGETARY INFORMATION

Accounting principles used in developing data on a budgetary basis differ from those used in preparing financial statements in conformity with accounting principles generally accepted in the United States of America. Amounts included in the Statement of Revenues, Expenses and Changes in Net Assets – Budget and Actual which are presented on a non-GAAP budgetary basis reconcile to the increase in net assets on the accompanying Statement of Revenues, Expenses, and Changes in Net Assets.

Palau District Housing Authority has no authority to impose taxes to generate revenue. The Authority as an autonomous agency of the Republic of Palau receives annual appropriation from the legislative branch, the Olbiil Era Kelulau (Palau National Congress). The Palau National Congress legislative budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. An annual appropriated budget is adopted by the Legislature for Palau District Housing Authority through an Annual Appropriations Act.

PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Economic Factors and Next Year's Budget and Rates

The following factors were considered in preparing the Authority's budget for the 2010 fiscal year:

- An increase in the collections of loan payments. The increase will be due to additional loan disbursed.
- The number of loans to be disbursed will be similar to previous years.
- An increase in interest income primarily due to additional loan disbursements.
- Appropriation from the Palau National Government for administrative and operation expenditures.
- Rental revenue derived from leasing Section 8 rental housing units.
- Re-construct and re-build six new detached housing units.

Future Events that will Financially Impact the Authority

- The Authority will continue its housing programs, but will depend entirely on its limited revolving funds to fund and continue its programs.
- To continue partnership with National Development Bank of Palau (NDBP) in the Energy Efficiency Subsidy Program ("EESP"). Under this program, the NDBP home loan borrowers may be eligible for loan subsidies of \$3,000 to \$6,000 for incorporating energy efficiency measures into their newly constructed homes.
- The Section 8 public housing program land lease has been approved by Koror State and the lease agreement has been transmitted to Palau Housing Authority for final approval.
- The Palau Housing Authority plans to discontinue the Section 8 Rental Program and construct ten housing units on the leased property. Subdivision type project will be the first community development housing subdivision in the Republic of Palau which will include energy efficient features that can be used as a model for other State housing projects.

PALAU DISTRICT HOUSING AUTHORITY
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Management's Discussion and Analysis
September 30, 2010

Contacting the Authority's Financial Management

The Management Discussion and Analysis is intended to provide information concerning known facts and conditions affecting the Authority's operations. This financial report is designed to provide a general overview of the Authority's finances and demonstrate its ability to manage its resources.

For additional information concerning this report, please contact the Executive Director of the Palau District Housing Authority, PO Box 197, Koror, Republic of Palau, 96940, or call (680) 488-6207.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Combined Statements of Net Assets
September 30, 2010

(With comparative totals as of September 30, 2009)

	Major Enterprise Funds				Total 2010	Total 2009
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
ASSETS						
Current assets:						
Cash and cash equivalents (Notes 1, 2 and 3)	\$ 73,241	\$ 569,489	\$ 59,426	\$ 269,174	\$ 971,330	\$ 929,025
Notes receivable, current portion (Notes 1, 4 and 9)	-	178,705	24,303	5,442	208,450	195,261
Accounts receivable	33,677	2,754	-	-	36,431	51,886
Due from grantor agency	-	-	30,375	-	30,375	30,375
Interest receivable	-	7,791	1,799	-	9,590	9,590
Due from other fund (Note 5)	-	-	-	55,000	55,000	45,000
Total current assets	106,918	758,739	115,903	329,616	1,311,176	1,261,137
Noncurrent assets:						
Notes receivable, net of current portion (Notes 1, 4 and 9)	-	1,448,372	140,886	42,280	1,631,538	1,605,668
Allowance for loan losses (Notes 1 and 4)	-	(69,442)	(18,552)	-	(87,994)	(78,556)
Notes receivable, net	-	1,378,930	122,334	42,280	1,543,544	1,527,112
Capital assets, net (Notes 1 and 6)	22,847	-	-	705	23,552	39,555
Other assets	-	-	-	-	-	43,041
Total noncurrent assets	22,847	1,378,930	122,334	42,985	1,567,096	1,609,708
Total assets	\$ 129,765	\$ 2,137,669	\$ 238,237	\$ 372,601	\$ 2,878,272	\$ 2,870,845

See accompanying notes to the basic financial statements.

PALAU DISTRICT HOUSING AUTHORITY

(A Component Unit of the Republic of Palau)

Combined Statements of Net Assets, Continued

September 30, 2010

(With comparative totals as of September 30, 2009)

	Major Enterprise Funds				Total 2010	Total 2009
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
LIABILITIES						
Current Liabilities:						
Due to other fund (Note 5)	\$ -	\$ -	\$ 55,000	\$ -	\$ 55,000	\$ 45,000
Accrued expenses (Note 1)	204	295	-	14,894	15,393	18,163
Total liabilities	204	295	55,000	14,894	70,393	63,163
Commitments and Contingencies (Note 9)						
NET ASSETS (Note 1)						
Invested in capital assets	22,847	-	-	705	23,552	39,555
Restricted	-	1,627,077	165,189	47,722	1,839,988	1,800,929
Unrestricted	106,714	510,297	18,048	309,280	944,339	967,198
Total net assets	129,561	2,137,374	183,237	357,707	2,807,879	2,807,682
Total liabilities and net assets	\$ 129,765	\$ 2,137,669	\$ 238,237	\$ 372,601	\$ 2,878,272	\$ 2,870,845

See accompanying notes to the basic financial statements.

PALAU DISTRICT HOUSING AUTHORITY

(A Component Unit of the Republic of Palau)

Combined Statements of Revenues, Expenses and Changes in Net Assets
Year Ended September 30, 2010

(With comparative totals as of September 30, 2009)

	Major Enterprise Funds				Total 2010	Total 2009
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
Operating revenues:						
Republic of Palau appropriation	\$ -	\$ -	\$ -	\$ 60,000	\$ 60,000	\$ 66,645
Interest on loans	-	82,277	4,418	1,905	88,600	74,975
Section 8 income	13,550	-	-	-	13,550	16,200
National treasury income	-	4,500	-	4,500	9,000	9,000
Other	613	8,937	497	5,558	15,605	11,856
Total operating revenues	14,163	95,714	4,915	71,963	186,755	178,676
Provision for loan loss	-	-	(17,052)	-	(17,052)	-
Net operating revenues (loss)	14,163	95,714	(12,137)	71,963	169,703	178,676
Operating expenses:						
Salaries and wages	8,811	7,359	-	49,288	65,458	64,122
Depreciation	14,285	-	-	264	14,549	14,153
Professional fees	3,000	4,500	-	4,500	12,000	9,000
Rent expense	1,970	850	-	8,500	11,320	11,320
Employee benefits	904	730	-	5,059	6,693	6,549
Travel	325	256	-	2,267	2,848	2,559
Communication	1,393	157	-	1,172	2,722	5,312
Repairs and maintenance	2,432	-	-	278	2,710	2,610
Miscellaneous	3,272	1,320	47	4,466	9,105	14,424
Total operating expenses	36,392	15,172	47	75,794	127,405	130,049
Operating income (loss)	(22,229)	80,542	(12,184)	(3,831)	42,298	48,627
Non-operating revenue (expense):						
Interest income	324	367	19	230	940	16,604
Other expense (Note 12)	-	(43,041)	-	-	(43,041)	-
Total non-operating revenue (expense)	324	(42,674)	19	230	(42,101)	16,604
Change in net assets	(21,905)	37,868	(12,165)	(3,601)	197	65,231
Total net assets at beginning of year	151,466	2,099,506	195,402	361,308	2,807,682	2,712,076
Capital contribution	-	-	-	-	-	30,375
Total net assets at end of year	\$ 129,561	\$ 2,137,374	\$ 183,237	\$ 357,707	\$ 2,807,879	\$ 2,807,682

See accompanying notes to the basic financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Combined Statements of Cash Flows
September 30, 2010

(With comparative totals as of September 30, 2009)

	Major Enterprise Funds				Total 2010	Total 2009
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
Cash flows from operating activities:						
Receipts from customers, net	\$ 12,516	\$ 74,061	\$ (10,276)	\$ 8,154	\$ 84,455	\$ 245,624
Receipts from ROP appropriation	-	-	-	81,082	81,082	75,645
Payments to suppliers	(12,392)	(7,083)	(48)	(31,183)	(50,706)	(310,735)
Payments to employees	(11,222)	(7,793)	-	(55,905)	(74,920)	(70,671)
Net cash provided by (used in) operating activities	(11,098)	59,185	(10,324)	2,148	39,911	(60,137)
Cash flows from financing activities:						
Capital contribution	-	-	-	-	-	30,375
Net cash provided by financing activities	-	-	-	-	-	30,375
Cash flows from investing activities:						
Interest and dividends	324	367	19	230	940	16,604
Acquisition of capital assets	-	-	-	-	-	(31,284)
Other adjustments	1,380	-	-	74	1,454	-
Net cash provided by (used in) investing activities	1,704	367	19	304	2,394	(14,680)
Net increase (decrease) in cash and cash equivalents	(9,394)	59,552	(10,305)	2,452	42,305	(44,442)
Cash and cash equivalents at beginning of year	82,635	509,937	69,731	266,722	929,025	973,467
Cash and cash equivalents at end of year	\$ 73,241	\$ 569,489	\$ 59,426	\$ 269,174	\$ 971,330	\$ 929,025

See accompanying notes to the basic financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Combined Statements of Cash Flows, Continued
September 30, 2010

(With comparative totals as of September 30, 2009)

	Major Enterprise Funds				Total 2010	Total 2009
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:						
Operating income (loss)	\$ (22,229)	\$ 80,542	\$ (12,184)	\$ (3,831)	\$ 42,298	\$ 48,627
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities						
Depreciation	14,285	-	-	264	14,549	14,153
Provision for loan loss	-	-	17,052	-	17,052	-
(Increase) decrease in assets:						
Accounts receivable	(1,647)	(1,980)	2,500	16,582	15,455	(24,525)
Due from grantor agency	-	-	-	-	-	(30,375)
Notes receivable	-	(19,672)	(27,692)	691	(46,673)	(68,983)
Due from other funds	-	-	-	(10,000)	(10,000)	-
Increase (decrease) in liabilities:						
Accrued expenses	(1,507)	295	-	(1,558)	(2,770)	966
Due to other funds	-	-	10,000	-	10,000	-
 Net cash provided by (used in) operating activities	 <u>\$ (11,098)</u>	 <u>\$ 59,185</u>	 <u>\$ (10,324)</u>	 <u>\$ 2,148</u>	 <u>\$ 39,911</u>	 <u>\$ (60,137)</u>

See accompanying notes to the basic financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL
For the Year Ended September 30, 2010

	Budgeted Amounts		Actual Amounts	(Unfavorable) Variance
	Original	Final		
Operating revenues	\$ 152,661	\$ 152,661	\$ 186,755	\$ 34,094
Provision for loan losses	-	-	(17,052)	(17,052)
Net operating revenues	<u>152,661</u>	<u>152,661</u>	<u>169,703</u>	<u>17,042</u>
Operating expenses:				
Salaries and wages	65,250	65,250	65,458	(208)
Depreciation	-	-	14,549	(14,549)
Professional fees	6,500	6,500	12,000	(5,500)
Rent	11,080	11,080	11,320	(240)
Employee benefits	7,250	7,250	6,693	557
Travel	5,200	5,200	2,848	2,352
Communication	4,100	4,100	2,722	1,378
Repairs and maintenance	34,877	34,877	2,710	32,167
Miscellaneous	18,404	18,404	9,105	9,299
Total operating expenses	<u>152,661</u>	<u>152,661</u>	<u>127,405</u>	<u>25,256</u>
Operating income	-	-	42,298	42,298
Non-operating revenues (expense)				
Investment income earned	-	-	940	940
Impaired asset	-	-	(43,041)	(43,041)
Total non-operating expense, net	-	-	(42,101)	(42,101)
Increase in net assets	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 197</u>	<u>\$ 197</u>

See accompanying notes to the basic financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies

The Palau District Housing Authority (the Authority), a component unit of the Republic of Palau, was established by Public Law 4-5-5 (June 20, 1970) of the Palau District Legislature (of the Trust Territory of the Pacific Islands). Its purpose is to develop and administer low cost housing and urban renewal projects and to assist in correcting housing conditions endangering the health, safety, and welfare of the people. The Authority was reorganized by Trust Territory Public Law 5-37 (April 5, 1973). Upon emergence of the Republic of Palau Constitutional Government (January 1, 1981), the Authority was transferred to the Republic. The Authority is a public corporation administered by a five-member Board of Directors appointed by the President of the Republic of Palau with the advice and consent of the Olbiil Era Kelulau (OEK – Palau National Congress).

The Authority's primary operations are comprised of a number of housing and grant programs as follows:

Major Enterprise Funds

Section 8 Housing Assistance Program

The program provides temporary housing for rental to assist low-income families who lack sufficient income to obtain safe, decent, and sanitary housing. The program was originally funded through the U.S. Department of Housing and Urban Development (HUD), until it phased-out in December 2004. However, the program has been able to sustain itself and continue to provide this service.

Home Rehabilitation Loan Program

The Home Rehabilitation Loan Program provides long-term financing to low income and moderate income families to rehabilitate existing dwellings or construct new single-family housing units. This Program is made possible through the initial funding from the U.S. Department of Housing and Urban Development (HUD). The maximum amount that can be borrowed for a new single family dwelling is \$35,000 at 4.5% interest per annum with a 25 year term. The maximum loan amount to rehabilitate an existing dwelling is \$5,000 with a 10 year term at 3% interest rate per annum, and \$10,000 with a 15 year term at 4.5% interest rate per annum.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Major Enterprise Funds, Continued

Low-Cost Housing Program

The U.S. Department of Housing and Urban Development (HUD) was the primary source of funds for the Loan Fund Housing Program. The program initially provided funding for loans to low-income families for up to \$12,000, payable over a period of 30 years, at an interest rate of 3 percent per annum to rehabilitate/construct family homes.

Currently, under this loan program and with the initial funding from HUD and U.S. Department of Agriculture (USDA), the Home Improvement and Repair Assistance Program was established specifically to provide low cost and long-term loans to low income and very low-income senior citizens, 60 years old and over, to rehabilitate their homes. Under this program, the borrower can obtain a maximum loan of \$5,000 with interest rate of 3 percent per annum payable over a 10-year period.

Non-Major Enterprise Funds

The following funds were determined to be non-major enterprise funds for the year ended September 30, 2010:

Emergency Housing Revolving Loan Program

The Emergency Housing Revolving Loan Program was established as an emergency loan program for citizens of the Republic of Palau for whose homes were destroyed by natural disaster or fire. The Program was funded by a \$500,000 appropriation from the Republic of Palau. Pursuant to Republic of Palau Public Law 6-26, §4, the Program was initially established to provide loans to private homeowners whose homes were destroyed or made uninhabitable because of damage done by storm Utor. Loans are available from a minimum of \$500 to a maximum amount of \$30,000, with repayment terms ranging from 3-to 30 years at an interest rate of 3 percent per annum. During the fiscal year ending September 30, 2002, the Authority remitted \$250,000 of the initial funding back to the Republic of Palau National Government.

Transitional/Emergency Shelter Program

This Program provides short-term temporary housing to individuals or families who become victims of domestic violence or abuse and whose homes are destroyed due to fire or natural disaster. The Program was originally funded through the HUD.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Local Funds

Local funds consist of appropriations from Republic of Palau for general operations of the Authority.

Measurement Focus, Basis of Accounting, and Basis of Presentation

During 2003, the Authority implemented GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis – for State and Local Government*, GASB Statement No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus*, GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, and GASB Interpretation No. 6 *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

GASB Statement No. 34 creates new basic financial statements for reporting on the Authority's financial activities. The new financial statements now include government-wide financial statements prepared on an accrual basis of accounting and fund accounting which present information for individual major funds rather than by fund type. Requirements in order to comply also include adopting depreciation on capital assets and classifying assets and liabilities as current and non-current.

GASB Statement No. 37 clarifies certain provisions of GASB Statement No. 34, including the required content of the Management Discussion and Analysis, the classification of program revenues and the criteria for determining major funds. GASB Statement No. 38 modifies, establishes and rescinds certain financial statement note disclosures. GASB Interpretation No. 6 clarifies the application of standards for modified accrual recognition of certain liabilities and expenditures in areas where differences have arisen, or potentially could arise, in interpretation and practice.

The accounts of the Authority are organized and operated on the basis of funds and grant programs. A fund is an independent fiscal year and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions. The minimum number of funds is maintained consistent with legal and managerial requirements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

The Authority has elected to use proprietary fund types as its principal reporting. Proprietary funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Authority's proprietary funds are enterprise funds used to account for those operations that are financed and operated in a manner similar to private business or where the Authority has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability.

The general purpose financial statements of the Palau District Housing Authority have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. Government Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Palau District Housing Authority has implemented GASB No. 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Authority's audited financial statements for the year ended September 30, 2009, from which the summarized information was derived.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Recent Pronouncements

In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This Statement establishes accounting and financial reporting standards for many different types of assets that may be considered intangible assets, including easements, water rights, timber rights, patents, trademarks, and computer software. This Statement is effective for periods beginning after June 30, 2010. This Statement did not have an impact on the financial statements of the Authority.

In March 2008, GASB issued Technical Bulletin No. 2008-1, *Determining the Annual Required Contribution Adjustment for Postemployment Benefit*, which clarifies the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and Statement No. 45, *Accounting and Financial Reporting by Employers of Postemployment Benefits Other Than Pensions*, for calculating the annual required contribution (ARC) adjustment. The provisions of this Statement are effective for periods beginning after December 15, 2008. This Statement did not have an impact on the financial statements of the Authority.

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This Statement is intended to improve how State and Local governments report information about derivative instruments – financial arrangements used by governments to manage specific risks or make investments in their financial statements. The provisions of this Statement are effective for periods beginning after June 15, 2009. This statement did not have an impact on the financial statements of the Authority.

In February 2009, GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. This Statement is to enhance the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The provisions of this Statement are effective for periods beginning after June 15, 2010. The implementation of this Statement did not have a material effect on the accompanying financial statements of the Authority.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Recent Pronouncements, Continued

In March 2009, GASB issued Statement No 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This Statement is to improve financial reporting by contributing to the GASB efforts to codify all generally accepted accounting principles (GAAP) for State and Local Governments so that they derive from a single source. This Statement is effective upon issuance. The Authority does not believe that the implementation of this Statement will have a material effect on its financial statements.

In March 2009, GASB issued Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*. This Statement incorporates accounting and financial reporting guidance previously only contained in the American Institute of Certified Public Accountants (AICPA) auditing literature into the GASB's accounting and financial reporting literature for State and Local governments, and addresses three issues from the AICPA's literature – related party transactions, going concern considerations and subsequent events. This Statement is effective upon issuance. The implementation of this Statement did not have a material effect on the accompanying financial statements of the Authority.

In December 2009, the GASB issued Statement No. 58, *Accounting and Financial Reporting for Chapter 9 Bankruptcies*, which provides accounting and financial reporting guidance for governments that have petitioned for protection from creditors by filing for bankruptcy under Chapter 9 of the United States Bankruptcy Code. This Statement is effective beginning after June 15, 2010 with retroactive application for all periods presented during which a government was in bankruptcy. The effect of the implementation of this Statement on the financial statements of the Authority has not been determined.

In June 2010, GASB issued Statement No. 59, *Financial Instruments Omnibus*. The Statement updates and improves existing standards regarding financial reporting of certain financial instruments and external pools. The Statement is effective for financial statements prepared by state and local governments for periods beginning after June 15, 2010, with earlier application encouraged. The implementation of this Statement did not have a material effect on the accompanying financial statements of the Authority.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Recent Pronouncements, Continued

In November 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*—an amendment of GASB Statements No. 14 and No. 34. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. The requirements of Statement No. 14, *The Financial Reporting Entity*, and the related financial reporting requirements of Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*, were amended to better meet user needs and to address reporting entity issues that have arisen since the issuance of those Statements. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2012. Earlier application is encouraged. Management has not evaluated the effect that the implementation of this Statement will have on the financial statements of the Authority.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The objective of this Statement is to incorporate into GASB’s authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict or contradict GASB pronouncements:

1. Financial Accounting Standards Board (FASB) Statements and Interpretations;
2. Accounting Principles Board Opinions; and
3. Accounting Research Bulletins of the American Institute of Certified Public Accountants’ (AICPA) Committee on Accounting Procedure.

Hereinafter, these pronouncements collectively are referred to as the *FASB and AICPA Pronouncements*. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2011. Earlier application is encouraged. The provisions of this Statement generally are required to be applied retroactively for all periods presented.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Budgets

Budgets are prepared on an annual basis for each major operating program and are used as a management tool throughout the accounting cycle. Budgets, however are not legally adopted or legally required for financial statement presentation.

The Authority's governing body, the Board of Directors, adopts budgets on a program or fund level basis. These budgets are submitted by the Authority's Executive Director, and approved by resolutions of the Board of Directors. The Authority's Board of Directors may authorize revisions to the budget based on the availability of financial resources. Formal budget revisions are authorized in the same manner as original budget submissions

Annual budgets are adopted for all Enterprise Funds. Throughout the fiscal year, the Authority monitors and evaluates expenditures rates and patterns. However, timely notice is not given to executive management regarding forthcoming changes in objectives or other conditions that may cause significant variations from approved budget-defined plans.

Management's Use of Estimates

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

Fair Value of Financial Instruments

The Authority adopted Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, in fiscal year 2009 and there was no material impact to the financial statements. SFAS No. 157 applies to all assets and liabilities that are being measured and reported on a fair value basis and requires new disclosure that establishes a framework for measuring fair value under accounting principles generally accepted in the United States of America (GAAP), and expands disclosures about fair value measurements. At September 30, 2010, the Authority has no financial assets and liabilities required to be measured at a fair value on a recurring basis.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Cash and Cash Equivalents

For the purposes of the Statement of Net Assets and Statement of Cash Flows, the Authority considers cash and cash equivalents to be cash on hand, cash in checking and savings accounts, and time certificates of deposit of less than ninety-day maturities. All of the Authority's cash and cash equivalents are with a federally insured bank, \$250,000 of which is subject to coverage by federal insurance as of September 30, 2010 and 2009, respectively, with the remaining balance exceeding insurable limits. The Authority does not require collateralization of its bank accounts and, therefore, amounts in excess of insurable limits are uncollateralized. Deposits in excess of federal depository insurance are considered uncollateralized by GASB Statement No. 40. Custodial credit risk for deposits is the risk that in the event of a bank failure, the government's deposits may not be returned to it. All of the Authority's deposits are insured by the Federal Deposit Insurance Corporation (FDIC) at September 30, 2010 and 2009.

Lending Policy

The Authority extends loans to qualifying residents of the Republic of Palau for rehabilitating existing dwellings or for constructing approved low-cost housing. The loans have terms from five to thirty years at an interest rate of 3% and 4.5%. Loans are restricted to a maximum ninety percent (90%) debt (aggregate of all debts associated with the property) to the appraised value of the property ratio or ninety percent (90%) of the estimated replacement cost, whichever is lower. The loans are collateralized by the property being rehabilitated.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Loans and Allowance for Loan Losses

Loans are stated at the amount of unpaid principal, reduced by an allowance for loan losses. Interest on loans is calculated by using the simple interest method on daily balances of the principal amount outstanding. The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collection of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans that may be uncollectible, based on evaluation of the collectability of loans and prior loan loss experience. The evaluation takes into consideration such factors as specific problem loans and current economic conditions that may affect the borrowers' ability to pay. The Authority recognizes bad debts using the allowance method and is only written-off after approval by management and subsequent reporting to the Board of Directors.

Capital Assets

All capital assets with a value greater than \$500 and a useful life over one year are capitalized.

The cost of repairs and maintenance is charged to operations as incurred and improvements are capitalized. Depreciation of capital assets is computed using the straight-line method over the estimated useful lives of the assets. Assets are depreciated using the following depreciation guidelines:

<u>Category</u>	<u>Useful Life – Years</u>
Residential units	28
Furniture, fixtures and equipment	5
Vehicles	5

Upon retirement or other disposition of capital assets recorded, the cost and related accumulated depreciation are removed from the respective program's or fund's accounts and any gain or loss is included in the respective program's or fund's current operations.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Compensated Absences

Compensated absences are those absences for which employees will be paid, such as vacation and sick leave. Employees are credited 104, 156 or 208 hours per fiscal year, based on their lengths of service. The accumulation of vacation and sick credits is limited to 360 at fiscal year-end and is convertible to pay upon termination of employment. The Authority recognizes as a liability all vested vacation and sick leave benefits accrued by its employees. When the employees use vacation and sick leave benefits, the liability account is reduced accordingly. At September 30, 2010 and 2009, compensated absences payable to employees were \$13,782 and \$14,104, respectively, and are recorded as a component of accrued expenses in the accompanying Combined Statement of Net Assets. At September 30, 2010 and 2009, all compensated absences are current.

Income Tax

Based on 34 PNC 7006, the Authority is exempt from all national and state non-payroll taxes or fees.

Net Assets

The Authority's net assets are classified as follows:

Invested in capital assets - This represents the Authority's total investment in capital assets, net of accumulated depreciation.

Restricted net assets – This includes grants from HUD, USDA, and contributions received from the Trust Territory of the Pacific Islands for the establishment of the Home Rehabilitation Revolving Loan Program and the Low-Cost Housing Revolving Loan program, respectively. It also includes contributions received from the Republic of Palau National Government for the establishment of Emergency Loan Program.

Unrestricted net assets – This includes resources derived from government appropriations. These resources are used for transactions relating to the general operations of the Authority and may be used at the discretion of the governing board to meet current expenses for any purpose.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Classification of Revenues

The Authority has classified its revenues as either operating or non-operating according to the following criteria:

Operating Revenues – Operating revenues include activities that have the characteristics of exchange transactions, such as federal, state and local grants and contracts and federal appropriations.

Non-operating Revenues – Non-operating revenues include activities that have the characteristics of nonexchange transactions, such as interest income, and other revenue sources that are defined as non-operating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting*.

Advertising

For the fiscal years ending September 30, 2010 and 2009, the Authority incurred advertising costs totaling \$1,285 and \$1,153, respectively. These costs primarily relate to construction bids and related procurement solicitation costs.

(2) Cash and cash equivalents

Cash and cash equivalents at September 30, 2010 and 2009 consist of the following:

	<u>2010</u>	<u>2009</u>
Cash	\$ 521,330	\$ 479,025
Time certificates of deposit	<u>450,000</u>	<u>450,000</u>
	<u>\$ 971,330</u>	<u>\$ 929,025</u>

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(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. This statement also requires disclosure of formal policies related to deposit and investment risks.

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 the Authority or its agent in the Authority'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 Authority'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 Authority's name and noncollateralized 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 Authority's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Authority has an investment and deposit policy for custodial credit risk. For deposits, a general depository agreement pursuant to HUD regulations, must be executed by the Authority and the depository. The depository bank must be a bank or financial institution whose deposits are insured by FDIC, Federal Savings and Loan Insurance Corporation or the National Credit Union Administration and all deposits must be fully collateralized by U.S. securities.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(3) Deposits and investments, Continued

For credit risk in the case of deposits, there is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. As of September 30, 2010 and 2009, the carrying amount of the Authority's total cash and cash equivalents was \$971,330 and \$929,025, respectively with a corresponding bank balance of \$975,464 and \$932,455 respectively which is insured by the FDIC. From these deposits, \$975,464 and \$932,455 at September 30, 2010 and 2009, respectively was subject to coverage by FDIC. The Authority does not require collateralization of bank accounts, and therefore, amounts in excess of insurable limits are uncollateralized and are subject to custodial credit risk.

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

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits 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 risk in GASB Statement No. 3.

As of September 30, 2010 and 2009, the Authority did not have investments subject to GASB Statement No. 40.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(4) Notes Receivable

A summary of notes receivable at September 30, 2010 and 2009 consists of the following:

	<u>2010</u>	<u>2009</u>
Home Rehabilitation loans	\$ 1,627,077	\$ 1,609,518
Emergency Loan Revolving Fund loans	47,722	53,913
Low-Cost Housing loans	<u>165,189</u>	<u>137,498</u>
	1,839,988	1,800,929
Less current portion	<u>(208,450)</u>	<u>(195,261)</u>
Long-term notes receivable, net of current portion	1,631,538	1,605,668
Less allowance for loan losses	<u>(87,994)</u>	<u>(78,556)</u>
Long-term notes receivable, net of allowance for loan losses	<u>\$ 1,543,544</u>	<u>\$ 1,527,112</u>

A summary of the activity in the allowance for loan losses is as follows:

	<u>2010</u>	<u>2009</u>
Balance at beginning of year	\$ 78,556	\$ 78,556
Additions to provision for loan loss	17,052	-
Loans charged-off	-	-
Recoveries of loans charged-off	<u>(7,614)</u>	<u>-</u>
Balance at end of year	<u>\$ 87,994</u>	<u>\$ 78,556</u>

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(5) Interfunds

The Authority maintains interfund receivable and payable accounts for all housing projects and funds that it administers and reports interfund transfers between many of its funds. The outstanding balances between funds result mainly from time lags between the date that (1) interfund goods and services are provided or reimbursable expenditures occur; (2) transactions are recorded in the accounting system; and (3) payments between funds are made. The amounts payable to the revolving fund are expected to be collected in the subsequent year. The composition of the inter-fund receivable and payable balances as of September 30, 2010 is as follows:

	Due from Other Funds	Due to other Funds	Net Receivable (Payable)
Major Enterprise Funds			
Low-Cost Housing Programs	\$ -	\$ 55,000	\$ (55,000)
Non-Major Enterprise Funds	55,000	-	55,000
	\$ 55,000	\$ 55,000	\$ -

(6) Capital Assets

A schedule of changes in capital assets for the fiscal years ended September 30, 2010 and 2009 is shown below:

Capital assets activity for the fiscal year ended September 30, 2010:

	Balance 09/30/09	Additions	Disposal/ Adjustment	Balance 09/30/10
Residential units	\$ 213,431	\$ -	\$ -	\$ 213,431
Furniture, fixtures, and equipment	38,782	-	(1,454)	37,328
Vehicles	45,979	-	-	45,979
	298,192	-	(1,454)	296,738
Accumulated depreciation	(258,637)	(14,549)	-	(273,186)
	\$ 39,555	\$ (14,549)	\$ (1,454)	\$ 23,552

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(6) Capital Assets, Continued

Capital assets activity for the fiscal year ended September 30, 2009:

	Balance 09/30/08	Additions	Disposal	Balance 09/30/09
Residential units	\$ 213,431	\$ -	\$ -	\$ 213,431
Furniture, fixtures, and equipment	43,134	6,300	(10,652)	38,782
Vehicles	27,795	24,984	(6,800)	45,979
	284,360	31,284	(17,452)	298,192
Accumulated depreciation	(261,936)	(14,153)	17,452	(258,637)
	<u>\$ 22,424</u>	<u>\$ 17,131</u>	<u>\$ -</u>	<u>\$ 39,555</u>

Depreciation expense for the years ended September 30, 2010 and 2009 was \$14,549 and \$14,153, respectively.

The residential units are constructed on properties leased from the Trust Territory Government, which properties were transferred to Palau Public Land Authority in accordance with U.S. Department of the Interior Secretarial Order No. 2969. The properties were subsequently transferred to the Koror Municipal Public Lands Authority through quitclaim deeds dated May 14, 1980 and February 16, 1983. On October 6, 2009, the lease from the Koror Municipal Public Lands Authority was renewed for fifty years.

(7) Employees Retirement Plan

The Authority contributes to the Palau Civil Service Pension Trust Fund (the Fund), a defined benefit, cost-sharing, multi-employer pension plan established and administered by the Republic of Palau. The Fund issues a stand-alone financial report which is available at its office site.

The Fund provides retirement, security and other benefits to employees, and their spouses and dependents, of the Republic of Palau State Governments and Republic of Palau agencies, funds and public corporations, which are paid monthly and are two percent (2%) of each member's average monthly salary. Normal benefits are the credited total service up to a maximum of thirty years total service. Generally, benefits vest after three years of credited service. Members, who retire at or after age 60, or with 30 years of vesting service, are entitled to retirement benefits.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(7) Employees Retirement Plan, Continued

Republic of Palau Public Law 2-26 is the authority under which benefit provisions and contributions rates are established. Member contribution rates are established by Republic of Palau Public Law 2-26 at six percent (6%) of total payroll and are matched dollar for dollar by the employer. The Authority contributed \$3,816, \$3,752 and \$3,666 for fiscal years 2010, 2009, and 2008, respectively.

Under the provisions of the Republic of Palau Public Law 2-26, the Fund's Board of Trustees adopted a Trust Fund Operation which has the force and effect of law, and which sets forth the procedures for the administration and coverage of the Plan. Amendments to the Plan are subject to the requirements of Title 6 of the Palau National Code.

The Fund utilizes the actuarial cost method termed "level aggregate cost method" with actuarial assumptions used to compute the pension benefit obligation. The following is the statement of actuarial assumptions as of October 1, 2009 applicable to the plan year ending September 30, 2009 of the ROP Civil Service Pension Plan:

Actuarial Cost Method: Normal costs are calculated under the level aggregate method.
Investment Income : 8.5% per year
Expenses: : \$300,000 each year
Salary Increase: : 3% per year
Mortality : 1984 Unisex Pension Mortality Table
Disabled Mortality : PBGC Mortality Table for Disabled Persons Receiving
Social Security
Retirement Age : Earlier of age 60 or 30 Years of Total Service

The pension benefit obligation, which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefits, adjusted for the affects of projected salary increases and any step-rate benefits, estimated to be payable in the future as a result of employment service to date. The measure is intended to assist users to evaluate the Fund's funding status on a going-concern basis, and evaluate progress made in accumulating adequate assets to pay benefits when due.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(7) Employees Retirement Plan, Continued

Based on the actuarial valuation of the Fund as of October 1, 2009 issued in August 2010, the actuarial valuation determined the unfunded pension benefit obligation as follows:

Present value of accrued benefits as of October 1, 2009:

Active participants	\$ 56,060,970
Inactive participants with vested deferred benefits	1,779,610
Participants in pay status	<u>47,666,805</u>
Total pension benefit obligation	105,507,385
Market value of assets	<u>41,254,319</u>
Unfunded benefit obligation	<u>\$ 64,253,066</u>
Funded Ratio as of 10/1/2009 (ratio of assets to liabilities)	<u>39.1%</u>

(8) Risk Management

The Authority 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. The Authority has elected to be self-insured for the risks of loss to which it is exposed.

(9) Commitments and Contingencies

Litigation

The Authority is subject to various claims and other legal actions in the normal course of business. The Authority consults its legal counsel and the Office of the Attorney General of the Republic of Palau whenever there is a potential or asserted claim, and relies on the advice of counsel for direction and for establishing reserves for potential unfavorable outcomes.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(9) Commitments and Contingencies, Continued

The Authority has initiated several foreclosure actions now pending in the Trial Division of the Supreme Court of Palau (the Court) against five (5) borrowers who defaulted on rehabilitation loans whose principal and interest balance approximate \$44,625 as of September 30, 2010. The Authority intends to take the following courses of action with respect to these matters: (1) renegotiate the loan; (2) pursue the claim in Court to recover the amount through judgments for monetary awards; or (3) pursue the claim in court to recover the amount through judgments for foreclosure on mortgaged properties.

Commitments

The Authority entered a lease agreement with Koror State Government for a period of fifty years (50) years expiring on October 2059. The Authority constructed seven low-cost housing units on the property that was funded by the U.S. Department Housing Urban Development under the Section 8 Housing Federal grant program. Also, the Authority's operations are conducted from premises under a lease agreement expiring on December 4, 2010.

Future lease payments are as follows:

Years ended September 30, 2011	\$ 2,224
2012	524
2013	524
2014	524
2015	524
2016-2020	2,622
2021-2025	2,622
2026-2030	2,622
2031-2035	2,622
2036-2040	2,622
2041-2045	2,622
2046-2050	2,621
2051-2055	2,621
2056-2059	<u>2,621</u>
	<u>\$ 27,915</u>

At September 30, 2010 and 2009, rent expense was \$11,320 in each year, respectively.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2010 and 2009

(10) National Government Contributions

For the years ended September 30, 2010 and 2009, the Republic of Palau appropriated and contributed the following to the Authority:

	<u>2010</u>	<u>2009</u>
For operational costs of employees	\$ 60,000	\$ 66,645
Cost reimbursement	<u>9,000</u>	<u>9,000</u>
	<u>\$ 69,000</u>	<u>\$ 75,645</u>

(11) Economic Dependency

The PHA receives a substantial amount of its support from private sector and government donors. A significant reduction in the level of this support, if this were to occur, may have an adverse effect on the Authority's programs and activities. As of September 30, 2010 and 2009, the Authority received 58% and 49%, respectively, of its support from the private sector, and 42% and 51%, respectively, from government donors.

(12) Other expense

At September 30, 2010, the Authority has determined to write-off the amount of \$43,041 capitalized expenditures recorded as other assets in prior years. The amount written-off was reported in the non-operating expense in the accompanying Combined Statements of Revenues, Expenses and Changes in Net Assets.

(13) Reclassifications

Certain reclassifications have been made to the prior year's financial statements to conform to the current year presentation. These reclassifications had no effect on previously reported results of operations or retained earnings.

(14) Subsequent Events

The Authority has evaluated subsequent events from September 30, 2010 through January 25, 2011, the date the financial statements were available to be issued. The Authority did not note any subsequent events requiring disclosure or adjustment to the accompanying financial statements.

**PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)**

**INDEPENDENT AUDITOR'S REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE**

Year Ended September 30, 2010

SAIPAN

Family Building, Suite 201
PMB 297 Box 10000
Saipan, MP 96950
Tel Nos. (670) 233-1837/0456
Fax No. (670) 233-8214

GUAM

Reflection Center, Suite 204
P.O. Box 12734
Tamuning, GU 96931
Tel Nos. (671) 472-2680/2687
Fax No. (671) 472-2686

PALAU

PIDC Apartment No. 11
P.O. Box 1266
Koror, PW 96940
Tel No. (680) 488-8615
Fax No. (680) 488-8616

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT
AUDITING STANDARDS**

To the Board of Directors
Palau District Housing Authority

I have audited the financial statements of Palau District Housing Authority (the Authority) as of and for the year ended September 30, 2010, and have issued my report thereon dated January 25, 2011. I conducted my 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 the audit, I considered the Authority's internal control over financial reporting as a basis for designing my auditing procedures for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, I do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

My consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. I did not identify any deficiencies in internal control over financial reporting that I consider to be a material weakness, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, I 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 my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

I noted certain matters that I reported to the management of the Authority in a separate letter dated January 25, 2011.

This report is intended solely for the information of the Board of Directors and management of the Palau District Housing Authority, the Office of the Public Auditor of Palau, federal awarding agencies, pass-through entities and the cognizant audit and other federal agencies and is not intended to be, and should not be used by anyone other than the specified users. However, this report is also a matter of public record.


Koror, Republic of Palau
January 25, 2011

SAIPAN

Family Building, Suite 201
PMB 297 Box 10000
Saipan, MP 96950
Tel Nos. (670) 233-1837/0456
Fax No. (670) 233-8214

GUAM

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P.O. Box 12734
Tamuning, GU 96931
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Tel No. (680) 488-8615
Fax No. (680) 488-8616

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE
WITH SPECIFIC REQUIREMENTS APPLICABLE TO
AFFIRMATIVE FAIR HOUSING AND NON-DISCRIMINATION**

To the Board of Directors
Palau District Housing Authority:

I have audited the basic financial statements of Palau District Housing Authority (the Authority), a component unit of the Republic of Palau, as of and for the year ended September 30, 2010 and have issued my report thereon dated January 25, 2011.

I have applied procedures to test the Authority's compliance with the Affirmative Fair Housing and Non-Discrimination requirements applicable to its HUD assisted programs, for the year ended September 30, 2010.

My procedures were limited to the applicable compliance requirements described in the *Consolidated Audit Guide for Audits of HUD Programs* issued by the U.S. Department of Housing and Urban Development, Office of Inspector General. My procedures were substantially less in scope than an audit, the objective of which would be the expression of an opinion on the Authority's compliance with the Affirmative Fair Housing and Non-Discrimination requirements. Accordingly, I do not express such an opinion.

The results of my tests disclosed no instances of noncompliance with the Affirmative Fair Housing and Non-Discrimination requirements under the Guide.

This report is intended solely for the information of the Board of Directors and management of the Palau District Housing Authority, the Office of the Public Auditor of Palau, federal awarding agencies, pass-through entities and the cognizant audit and other federal agencies and is not intended to be, and should not be used by anyone other than the specified users. However, this report is also a matter of public record.


Koror, Republic of Palau
January 25, 2011

SAIPAN

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PMB 297 Box 10000
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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH SPECIFIC
REQUIREMENTS APPLICABLE TO NON-MAJOR HUD PROGRAM
TRANSACTIONS**

To the Board of Directors
Palau District Housing Authority:

I have audited the financial statements of Palau District Housing Authority (the Authority) as of and for the year ended, and have issued our report thereon dated January 25, 2011.

In connection with that audit and with my consideration of the Authority's internal control used to administer HUD programs, as required by the *Consolidated Audit Guide for Audits of HUD Programs* (the "Guide") issued by the U.S. Department of Housing and Urban Development, Office of the Inspector General, we selected certain transactions applicable to certain non-major HUD-assisted programs for the year ended September 30, 2010.

As required by the Guide, we performed auditing procedures to test compliance with the requirements governing (Activities Allowable or Unallowed, Eligibility, Cash Management, Davis-Bacon Act, Procurement, Suspension and Debarment, Subrecipient Monitoring and Special Tests and Provisions) that are applicable to those transactions. My procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the Authority's compliance with these requirements. Accordingly, I do not express such an opinion.

The results of my tests disclosed no instances of noncompliance that are required to be reported herein under the Guide.

This report is intended solely for the information of the Board of Directors and management of the Palau District Housing Authority, the Department of Housing and Urban Development and the Office of the Public Accountability – Palau and is not intended to be, and should not be, used by anyone other than those specified parties. However, this report is also a matter of public record.


Hagåtña, Guam
January 25, 2011

**PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)**

STATISTICAL SECTION

Year Ended September 30, 2010

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

NET ASSETS
Last Six Fiscal Years Ending September 30

	2010	2009	2008	2007	2006	2005
Invested in capital assets	\$ 23,552	\$ 39,555	\$ 22,424	\$ 28,175	\$ 35,481	\$ 48,713
Restricted	1,839,988	2,374,498	2,344,123	2,312,086	2,312,086	2,312,086
Unrestricted	944,339	393,629	345,529	278,135	195,475	138,455
Total Net Assets	\$ 2,807,879	\$ 2,807,682	\$ 2,712,076	\$ 2,618,396	\$ 2,543,042	\$ 2,499,254

Source: Annual reports on audited financial statements for the past six fiscal years.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

CHANGES IN NET ASSETS
Last Six Fiscal Years Ending September 30

	2010	2009	2008	2007	2006	2005
Operating revenues						
Republic of Palau appropriation	\$ 60,000	\$ 66,645	\$ 67,000	\$ 67,000	\$ 67,000	\$ 67,000
Interest on loans	88,600	74,975	63,740	61,479	45,341	38,266
Section 8 income	13,550	16,200	16,400	15,300	13,812	11,928
National treasury income	9,000	9,000	8,500	8,500	8,000	8,000
Other operating revenues	15,605	11,856	6,387	16,469	7,581	7,546
Federal contributions	-	-	-	4,050	-	19,516
Provision for bad debts	(17,052)	-	-	-	-	-
Total operating revenues, net	169,703	178,676	162,027	172,798	141,734	152,256
Operating expenses						
Salaries and wages	65,458	64,122	63,552	59,907	54,929	50,437
Depreciation	14,549	14,153	8,265	9,606	10,198	20,870
Professional fees	12,000	9,000	9,000	9,380	8,500	10,723
Rent expense	11,320	11,320	11,890	11,320	10,200	9,350
Employee benefits	6,693	6,549	6,373	5,748	5,309	4,962
Communication	2,722	5,312	3,446	2,925	2,919	2,883
Repairs and maintenance	2,710	2,610	2,699	2,666	3,888	2,228
Travel	2,848	2,559	2,887	7,823	9,040	2,930
Other operating expenses	9,105	14,424	11,490	12,928	12,208	9,701
Total operating expenses	127,405	130,049	119,602	122,303	117,191	114,084
Operating income	42,298	48,627	42,425	50,495	24,543	38,172
Non-operating revenues (expenses)						
Investment income earned	940	16,604	19,218	24,859	22,279	12,903
Other expense	(43,041)	-	-	-	-	-
Total non-operating revenues	(42,101)	16,604	19,218	24,859	22,279	12,903
Change in net assets	\$ 197	\$ 65,231	\$ 61,643	\$ 75,354	\$ 46,822	\$ 51,075

Source: Annual reports on audited financial statements for the past six fiscal years.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

REVENUES BY SOURCE
Last Six Fiscal Years Ending September 30

Function	2010	2009	2008	2007	2006	2005
ROP Appropriations	\$ 60,000	\$ 66,645	\$ 67,000	\$ 67,000	\$ 67,000	\$ 67,000
Interest on loans	88,600	74,975	63,740	61,479	45,341	38,266
Section 8 income	13,550	16,200	16,400	15,300	13,812	11,928
National treasury income	9,000	9,000	8,500	8,500	8,000	8,000
Other operating revenues	15,605	11,856	6,387	16,469	7,581	7,546
Federal contributions	-	-	-	-	-	19,516
Total Revenues	\$ 186,755	\$ 178,676	\$ 162,027	\$ 168,748	\$ 141,734	\$ 152,256

Source: Annual reports on audited financial statements for the past six fiscal years.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

SCHEDULE OF EXPENSES

Last Six Fiscal Years Ending September 30

Function	2010	2009	2008	2007	2006	2005
Salaries and wages	\$ 65,458	\$ 64,122	\$ 63,552	\$ 59,907	\$ 54,929	\$ 50,437
Depreciation	14,549	14,153	8,265	9,606	10,198	20,870
Professional fees	12,000	9,000	9,000	9,380	8,500	10,723
Rent expense	11,320	11,320	11,890	11,320	10,200	9,350
Employee benefits	6,693	6,549	6,373	5,748	5,309	4,962
Travel	2,848	2,559	2,887	7,823	9,040	2,930
Communication	2,722	5,312	3,446	2,925	2,919	2,883
Repairs and maintenance	2,710	2,610	2,699	2,666	3,888	2,228
Other operating expenses	9,105	14,424	11,490	12,928	12,208	9,701
Total Expenses	\$ 127,405	\$ 130,049	\$ 119,602	\$ 122,303	\$ 117,191	\$ 114,084

Source: Annual reports on audited financial statements for the past six fiscal years.