

PROTECTED AREAS NETWORK FUND
(A COMPONENT UNIT OF THE REPUBLIC OF PALAU)

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2015 AND 2014

INDEPENDENT AUDITORS' REPORT

Board of Directors
Protected Areas Network Fund:

Report on the Financial Statements

We have audited the accompanying financial statements of the Protected Areas Network Fund (PAN Fund), a component unit of the Republic of Palau, which comprise the statements of net position as of September 30, 2015 and 2014, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Protected Areas Network Fund as of September 30, 2015 and 2014, and the changes in its net position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. This supplementary information is the responsibility of PAN Fund's management. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 17, 2016 on our consideration of PAN Fund'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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering PAN Fund's internal control over financial reporting and compliance.

Deloitte & Touche LLC

June 17, 2016



Protected Areas Network Fund

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Management's Discussion and Analysis Year Ended September 30, 2015

This report presents a management's discussion and analysis of the Protected Areas Network Fund's (PAN Fund) financial performance during the fiscal year ended September 30, 2015, with selected comparative information for the fiscal years ended September 30, 2014 and 2013.

ORGANIZATION AND PURPOSE

Republic of Palau Public Law (RPPL) 6-39 (the PAN Act) established a national system of support from the National Government of Palau to the States for its conservation programs to preserve, conserve and manage its natural resources and ecological biodiversity. RPPL 7-42 was then enacted creating a national financial mechanism and PAN Fund. The purpose of PAN Fund is to serve as a financial trustee corporation for the "green fee" and for all monies received for the PAN, to support and finance PAN projects and programs thus administering, managing, fundraising, investing, monitoring and disbursing PAN monies for the financial sustainability of the PAN in Palau for conservation of ecological biodiversity and sustainable management and use of its natural resources. These enabling legislations were published under Title 24 PNC Chapter 34 - Protected Areas Network.

PAN Fund is a registered non-profit corporation governed by a nine-member Board of Directors appointed by the initial four-member incorporators; namely The Nature Conservancy (TNC), Conservation International (CI), the Ministry of Natural Resources, Environment and Tourism (MNRET) and the Ministry of Finance (MOF) with advice and consent of the Senate of the Olbiil Era Kelulau (OEK-Palau National Congress). The Board of Directors' major responsibilities include governance, fiduciary and grant-making. Subsequent appointments of directors, other than an ex-officio director and a director appointed in accordance with the Articles of Incorporation, must be in accordance with procedures and regulations prescribed by the Board of Directors. The mission of PAN Fund is to "efficiently and equitably provide funding to the Protected Areas Network, and its associated activities, through strategic actions and medium- to long-term financial support that will advance effective management and conservation of Palau's natural and cultural resources."

The types of funds administered, managed and invested by PAN Fund as the financial trustee corporation to the PAN include the environmental protection fee, donations, grants and income and other property derived from or attributable to the investment. The "green fee" or environmental impact fee allocation and distribution to the PAN Member States are prioritized based on annual work plans as per management plans to effectively implement each respective conservation program. The "green fee" is disbursed quarterly and is subject to verification of activities and program implementation. The "green fee" is utilized to finance, support and further the PAN's conservation programs and sustainable economic development in Palau. These constitute an economic subsidy to further the cause of conservation programs, including but not limited to, job creation, institutional capacity building (i.e., legislative infrastructure and enforcement programs) and capacity building to train and build the workforce for effective conservation management in areas of program management, public awareness and socialization, surveillance, enforcement and biological monitoring programs to achieve the Micronesia Challenge (MC) 30/20 goals by 2020.

OVERVIEW OF FINANCIAL STATEMENTS

Statements of Net Position:

	<u>2015</u>	<u>2014</u>	<u>2013</u>
Current assets	\$ 3,069,329	\$ 2,734,591	\$ 2,595,052
Fixed assets	<u>16,739</u>	<u>19,122</u>	<u>18,684</u>
Total assets	<u>3,086,068</u>	<u>2,753,713</u>	<u>2,613,736</u>
Current liabilities	<u>319,677</u>	<u>219,013</u>	<u>89,955</u>
Net position:			
Invested in capital assets	16,739	19,122	18,684
Restricted	<u>2,749,652</u>	<u>2,515,578</u>	<u>2,505,097</u>
Total net position	\$ <u>2,766,391</u>	\$ <u>2,534,700</u>	\$ <u>2,523,781</u>

Statements of Revenues, Expenses and Changes in Net Position:

Operating revenues	\$ -	\$ -	\$ -
Operating expenses	<u>1,821,436</u>	<u>1,898,207</u>	<u>1,232,842</u>
Operating loss	(1,821,436)	(1,898,207)	(1,232,842)
Nonoperating revenues	<u>2,053,127</u>	<u>1,909,126</u>	<u>1,710,254</u>
Change in net position	231,691	10,919	477,412
Net position at beginning of year	<u>2,534,700</u>	<u>2,523,781</u>	<u>2,046,369</u>
Net position at end of year	\$ <u>2,766,391</u>	\$ <u>2,534,700</u>	\$ <u>2,523,781</u>

Statements of Cash Flows:

Cash flows from operating activities	\$ (1,677,933)	\$ (1,803,276)	\$ (1,143,473)
Cash flows from noncapital financing activities	2,013,651	2,416,798	3,111,759
Cash flows from capital financing activities	<u>(3,059)</u>	<u>(5,116)</u>	<u>(10,456)</u>
Net increase in cash	332,659	608,406	1,957,830
Cash at beginning of year	<u>2,732,240</u>	<u>2,123,834</u>	<u>166,004</u>
Cash at end of year	\$ <u>3,064,899</u>	\$ <u>2,732,240</u>	\$ <u>2,123,834</u>

FINANCIAL HIGHLIGHTS

PAN Fund's fixed assets decreased by 12% from \$19,122 in fiscal year 2014 to \$16,739 in fiscal year 2015 and increased by 2% from \$18,684 in fiscal year 2013 to \$19,122 in fiscal year 2014. See note 3 for more detailed information on PAN Fund's fixed assets and changes therein.

Total net position increased by 9% from \$2,534,700 in fiscal year 2014 to \$2,766,391 in fiscal year 2015 and by 0.4% from \$2,523,781 in fiscal year 2013 to \$2,534,700 in fiscal year 2014. The increase was largely due to increases in green fee collections.

Total liabilities increased by 46% from \$219,013 in fiscal year 2014 to \$319,677 in fiscal year 2015 and by 143% from \$89,955 in fiscal year 2013 to \$219,013 in fiscal year 2014. The increase in liabilities factors in the \$98,177 payable to Palau's endowment account with MCT, the \$215,139 miscellaneous payable, mainly for PAN States, and the \$6,361 in accrued expenses for payroll and taxes.

FINANCIAL HIGHLIGHTS, CONTINUED

Total operating expenses decreased by 4% from \$1,898,207 in fiscal year 2014 to \$1,821,436 in fiscal year 2015 and increased by 54% from \$1,232,842 in fiscal year 2013 to \$1,898,207 in fiscal year 2014. The 4% decrease in total operating expenses for fiscal year 2015 was contributed largely to delays in reporting which subsequently delayed disbursements to PAN Sites/States and the PAN office, which resulted in an increase in accounts payable at the end of the fiscal year. Other contributing factors were reductions in competitive grant expenses and the lack of emergency disbursements in fiscal year 2015.

Green fee revenues increased by 7% from \$1,882,024 in fiscal year 2014 to \$2,007,500 in fiscal year 2015; thus, reaching the \$2,000,000 authorization/appropriation cap required by RPPL 9-46 and by 10% from \$1,706,923 in fiscal year 2013 to \$1,882,024 in fiscal year 2014. Following the allocation policy, PAN Fund restricted \$2,000,000 which will be allocated specifically for the fiscal year 2016 operations budget.

Net cash increased by 12% from \$2,732,240 in fiscal year 2014 to \$3,064,899 in fiscal year 2015 and by 29% from \$2,123,834 in fiscal year 2013 to \$2,732,240 in fiscal year 2014. The net cash at the end of the year is inclusive of ROP's cash transfer in of \$1,968,024; green fee revenue of \$1,960,524 (\$2,000,000 less \$39,476 due to ROP) and \$7,500 for audit expense reimbursement. The cash balance at the end of the year is also inclusive of encumbered funds allocated for fiscal year 2015 pending disbursements and subject to acceptable quarterly reports.

ECONOMIC OUTLOOK

Currently, PAN Fund relies heavily on environmental fees as the main source of revenue to finance its operations. Based on trending data provided by the Palau Visitors Authority (PVA), the number of visitors increased by 32% in 2015 (164,931 compared to 125,338 in 2014) and by 31% in 2014 (125,338 compared to 95,387 in 2013). PVA is projecting 147,289 in visitor arrivals in 2016, which is an 11% reduction compared to the 164,931 visitors in 2015. PAN Fund remains optimistic that it will be able to collect the maximum amount of \$2,000,000 in fiscal year 2016.

The amount of environmental fees per year is dependent on the number of visitors. The number of visitors is dependent on many factors. A simple change in aviation strategy to include more charter flights can contribute to a significant increase in the number of visitors, while a change in purchasing power can skew visitor arrivals. PAN Fund is mindful of these factors and its implications on the main source of revenue for the PAN. PAN Fund has taken steps to mitigate risks associated with the environmental fee by adopting budget allocation strategies whereby the budget for the subsequent year is based on realized environmental fee revenues from the current year. Furthermore, mechanisms in place for PAN Fund to mitigate risks and buffer economic downturns and environmental impacts attributed to climate change (i.e., typhoons, tsunamis, rising sea levels, drought, etc.), include a sustainable finance plan that incorporates allocation of emergency funds, legal reserves and endowment accounts. Going forward, it will be necessary for PAN Fund to diversify its investment to further reduce risks while ensuring sustainable financing to support the PAN.

ECONOMIC OUTLOOK, CONTINUED

The continuous promotion and branding of “Pristine Palau” by the PVA combined with the international interest and support for Palau’s shark sanctuary and the initiative for a marine sanctuary, continues to provide a positive outlook for the tourism industry and the generation of environmental fee revenue for PAN Fund. The continued commitment by leadership for environment and conservation causes will facilitate the collaboration and supportive linkages from the international and regional communities to the national community with the national network of protected areas on ecological biodiversity and natural resource conservation management programs in Palau. Furthermore, the international community’s support and momentum generated by the MC and the United Nations Convention on Biological Diversity, as well as the fiscal and technical support from donor communities such as The David & Lucile Packard Foundation, The Nature Conservancy, Conservation International, the Global Environment Fund, the International Union for Conservation of Nature and other supporting partners and patrons offer opportunities for PAN Fund to further diversify its revenue stream.

CONCLUDING SUMMARY

The Management’s Discussion and Analysis for the year ended September 30, 2014 is set forth in PAN Fund’s report on the audit of financial statements, which is dated April 30, 2015. That Discussion and Analysis explains the major factors impacting the 2014 financial statements and can be viewed at the Office of the Public Auditor’s website at www.palauopa.org.

Moving forward, PAN Fund needs to continuously evolve with the application of adaptive management and improve existing management policies and practices in sync with the PAN. Improvement to policies and practices will enhance reporting and the disbursement flow to and from recipients of PAN funds and the capacity for PAN Fund to further diversify its investment and in the process, minimize risk for PAN funds, while enabling the sustainable financing mechanism for the PAN.

CONTACTING PAN FUND’S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of PAN Fund’s finances and to demonstrate PAN Fund’s accountability for the money it receives. If you have questions about this report, or need additional information, please contact the Protected Areas Network Fund, P.O. Box 6094, Koror, Republic of Palau 96940, via the following: Phone: (680) 488-FUND (3863) | Fax: (680) 488-1314 | Email: info@palaupanfund.org.

PROTECTED AREAS NETWORK FUND

Statements of Net Position
September 30, 2015 and 2014

	<u>2015</u>	<u>2014</u>
<u>ASSETS</u>		
Current assets:		
Cash	\$ 3,064,899	\$ 2,732,240
Prepaid expenses	<u>4,430</u>	<u>2,351</u>
Total current assets	3,069,329	2,734,591
Fixed assets, net	<u>16,739</u>	<u>19,122</u>
	<u>\$ 3,086,068</u>	<u>\$ 2,753,713</u>
<u>LIABILITIES AND NET POSITION</u>		
Current liabilities:		
Accounts payable	\$ 215,139	\$ 80,099
Accrued expenses	6,361	2,688
Due to Republic of Palau	-	39,476
Due to Micronesia Conservation Trust	<u>98,177</u>	<u>96,750</u>
Total liabilities	<u>319,677</u>	<u>219,013</u>
Commitment		
Net position:		
Invested in capital assets	16,739	19,122
Restricted	<u>2,749,652</u>	<u>2,515,578</u>
Total net position	<u>2,766,391</u>	<u>2,534,700</u>
	<u>\$ 3,086,068</u>	<u>\$ 2,753,713</u>

See accompanying notes to financial statements.

PROTECTED AREAS NETWORK FUND

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Operating revenues	\$ -	\$ -
Operating expenses:		
PAN site/states	1,169,122	1,311,115
PAN Institutional System	198,541	203,435
Micronesia Conservation Trust contribution	98,177	96,750
Salaries and wages	85,814	65,765
PAN technical assistance	63,741	-
Grants	41,819	25,000
Employee benefits	26,524	17,176
Professional development	26,047	11,636
Competitive grant expense	23,486	37,219
Travel and conferences	13,955	1,444
Rent	13,645	12,600
Outreach/awareness meetings	11,507	20,953
Communications	8,349	8,002
Audit	7,500	7,500
Depreciation	5,442	4,678
Professional fees	5,389	14,968
Utilities	4,117	2,848
Repairs and maintenance	1,621	2,230
Advertisements	666	2,424
Emergency disbursement	-	31,210
Other	15,974	21,254
	<u>1,821,436</u>	<u>1,898,207</u>
Total operating expenses		
	<u>(1,821,436)</u>	<u>(1,898,207)</u>
Operating loss		
Nonoperating revenues:		
Transfer in from Republic of Palau	2,007,500	1,882,024
Grant revenue	43,400	25,000
Other income	2,227	2,102
	<u>2,053,127</u>	<u>1,909,126</u>
Total nonoperating revenues		
Change in net position	231,691	10,919
Net position at beginning of year	<u>2,534,700</u>	<u>2,523,781</u>
Net position at end of year	<u>\$ 2,766,391</u>	<u>\$ 2,534,700</u>

See accompanying notes to financial statements.

PROTECTED AREAS NETWORK FUND

Statements of Cash Flows
Years Ended September 30, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Cash flows from operating activities:		
Micronesia Conservation Trust contribution	\$ (96,750)	\$ (84,596)
Cash payments to PAN sites/States and institutional system	(1,160,094)	(1,514,550)
Cash payments to suppliers for goods and services	(314,801)	(123,877)
Cash payments to employees for services	<u>(106,288)</u>	<u>(80,253)</u>
Net cash used for operating activities	<u>(1,677,933)</u>	<u>(1,803,276)</u>
Cash flows from noncapital financing activities:		
Transfer in from Republic of Palau	1,968,024	2,389,696
Grant revenue	43,400	25,000
Other income	<u>2,227</u>	<u>2,102</u>
Net cash provided by noncapital financing activities	<u>2,013,651</u>	<u>2,416,798</u>
Cash flows from capital financing activities:		
Fixed asset acquisitions	<u>(3,059)</u>	<u>(5,116)</u>
Net cash used for capital financing activities	<u>(3,059)</u>	<u>(5,116)</u>
Net increase in cash	332,659	608,406
Cash at beginning of year	<u>2,732,240</u>	<u>2,123,834</u>
Cash at end of year	<u>\$ 3,064,899</u>	<u>\$ 2,732,240</u>
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (1,821,436)	\$ (1,898,207)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	5,442	4,678
(Increase) decrease in assets:		
Prepaid expenses	(2,079)	671
Increase (decrease) in liabilities:		
Accounts payable	135,040	80,099
Accrued expenses	3,673	(2,671)
Due to Micronesia Conservation Trust	<u>1,427</u>	<u>12,154</u>
Net cash used for operating activities	<u>\$ (1,677,933)</u>	<u>\$ (1,803,276)</u>
Supplemental disclosure of noncash transactions:		
Due to Republic of Palau offset against transfer in (note 1)		
Noncash transfer in from Republic of Palau	\$ 39,476	\$ -
Noncash decrease in due to Republic of Palau	<u>(39,476)</u>	<u>-</u>
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2015 and 2014

(1) Organization

The Protected Areas Network Fund (PAN Fund), a component unit of the Republic of Palau (ROP), was formed on May 2, 2008, under the provisions of the Republic of Palau Public Law (RPPL) No. 7-42 for the purpose of administering and managing all funds received for the financial sustainability of the Protected Areas Network (the PAN) in Palau and for other related purposes. Portions of RPPL 7-42 were revised by RPPL 8-9 and RPPL 8-18. The Law created a registered non-profit corporation under the ROP corporate registry managed by a Board of Directors, consisting of seven voting members and the ROP Minister of Finance and the ROP Minister of Resources and Development, appointed in accordance with PAN Fund's Articles of Incorporation and approved by no less than two thirds of the Senate of the Olbiil Era Kelulau (ROP National Congress). PAN Fund's non-profit corporate charter was issued on November 2, 2010 by ROP and operations formally launched on March 24, 2012 upon receiving tourist and visitor environmental protection and arrival fee (Green Fee) monies from the ROP Ministry of Finance (MOF).

RPPL 7-42 authorized MOF to implement Green Fees to be used for the purpose of the operation of the PAN and to be deposited into an account at the National Treasury. The ROP Minister of Finance shall subsequently transfer the funds collected to the PAN Fund. RPPL 9-15, passed into law on August 29, 2013 and effective for fiscal year 2014, reduced amounts transferred to the PAN Fund to 50% of Green Fees collected or \$2,000,000, whichever is less. During the years ended September 30, 2015 and 2014, MOF remitted \$2,000,000 and \$1,874,524, respectively, for this purpose, which PAN Fund recorded as transfers in from ROP Green Fees. PAN Fund recorded Green Fees payable of \$-0- and \$39,476 as of September 30, 2015 and 2014, respectively. The fiscal year 2014 Green Fee payable balance of \$39,476 was offset against current year Green Fees and was recorded as transfer in from ROP. PAN Fund recorded \$7,500 as other transfers in from ROP for audit expense reimbursement for the years ended September 30, 2015 and 2014. The payables and transfers with ROP constitute all of PAN Fund's related party transactions, except for the grant described in note 4.

Funds administered, managed and invested by PAN Fund as the financial trustee corporation of the PAN shall include:

- Green Fees from ROP are to be used for general operations of the PAN. PAN Fund shall place five percent (5%) received from Green Fees and any unallocated funds remaining at the end of each fiscal year in the Micronesia Conservation Trust (MCT) Endowment, net investment revenues from which are available for PAN Fund's exclusive use at a later time, pursuant to guidelines of MCT. PAN Fund recorded MCT contributions of \$98,177 and \$96,750 for the years ended September 30, 2015 and 2014, respectively. PAN Fund considers its ensuing year budget to be an allocation of funds and therefore has not recorded a liability to MCT for any unallocated funds at September 30, 2015 and 2014;
- Donations, grants and other aid given to PAN Fund; and
- Income and other property derived from or attributed to the investment or application of property.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2015 and 2014

(1) Organization, Continued

PAN Fund shall disburse all funding for:

- The implementation of PAN protected areas management, sustainable development and work plans for PAN sites based on performance, impact/outcome and appropriate management costs for the continuing sustainable operation of the PAN Fund. During the years ended September 30, 2015 and 2014, PAN Fund provided funding to PAN sites/states for mobilization and implementation of PAN work plan in the amounts of \$1,169,122 and \$1,311,115, respectively, and is recorded as PAN sites/states expense in the accompanying statements of revenue, expenses and changes in net position. Additionally, PAN Fund provided technical assistance for PAN sites/states special projects in the amounts of \$63,741 and \$-0- for the years ended September 30, 2015 and 2014, respectively.
- The undertaking of necessary research and educational activities substantially related to carrying out the provisions of RPPL No. 7-42;
- The performance of any other functions that is necessary in order to carry out the purposes of RPPL No. 7-42 including the operation of the PAN Office. The PAN Office operates under the ROP Ministry of Natural Resources, Environment and Tourism. During the years ended September 30, 2015 and 2014, PAN Fund provided funding for activities specified in an annual work plan of PAN Office in the amounts of \$193,541 and \$143,435, respectively. Additionally, PAN Fund entered into agreements of support for PAN Office of \$65,000 for fisheries management of Ngarchelong and Kayangel PAN States. Funding of \$5,000 and \$60,000 for the years ended September 30, 2015 and 2014, respectively, is recorded as PAN Institutional System expense in the accompanying Statements of Revenues, Expenses and Changes in Net Position; and
- Emergency funding to help PAN sites address exceptional needs arising from natural disasters or accidents. During the years ended September 30, 2015 and 2014, PAN Fund provided funding for the repair, assistance and relief efforts for PAN sites affected by Typhoon Haiyan in the amounts of \$-0- and \$31,210, respectively. Funding is recorded as emergency disbursement in the accompanying Statements of Revenues, Expenses and Changes in Net Position.

PAN Fund's financial statements are incorporated into the financial statements of ROP as a component unit.

(2) Summary of Significant Accounting Policies

The accounting policies of PAN Fund conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds. PAN Fund utilizes the flow of economic resources measurement focus. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

Estimates

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

Basis of Accounting

All proprietary funds are accounted for on a flow of economic resources, measurement focus. With this measurement focus, all assets and liabilities associated with the operation of this fund are included in the statements of net position. Proprietary fund operating statements reflect increases and decreases in net total assets and utilize the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Budget and Appropriation

In each year's national government fiscal year budget, the Olbiil Era Kelulau shall authorize and appropriate all money collected through the environmental protection arrival fee which shall be used for the sole purpose of the operation of the Protected Areas Network including authorization and appropriation of no more than ten percent (10%) of such amount to be allocated to PAN Fund for reasonable administrative costs of operation of PAN Fund. Budgetary financial statements are not considered to be a disclosure requirement by management.

Cash

For purposes of the statements of net position and of cash flows, cash is defined as cash on hand and cash in checking account. As of September 30, 2015 and 2014, cash was \$3,064,899 and \$2,732,240, respectively, and the corresponding bank balances were \$3,136,579 and \$2,895,837, respectively, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. At September 30, 2015 and 2014, bank deposits of \$500,000 were FDIC insured. Collateralization of deposits is not required; therefore, uninsured deposits are exposed to custodial credit risk.

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 PAN Fund or its agent in PAN Fund'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 PAN Fund's name; or

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

Cash, Continued

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

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

Fixed Assets

Fixed assets are stated at cost. Depreciation is calculated using the straight-line method based on the estimated useful lives of the respective assets. Current policy is to capitalize items in excess of \$100.

Retirement Plan

On August 8, 2013, PAN Fund withdrew from the Palau Civil Service Pension Trust Fund (the Fund) as the Fund considers PAN Fund to be a non-profit, non-governmental organization, and to be exempt from participation in the Fund.

Net Position

PAN Fund's net position is classified as follows:

- Invested in capital assets: capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- Restricted: net position subject to externally imposed stipulations that can be fulfilled by actions of PAN Fund pursuant to those stipulations or that expire by the passage of time. PAN Fund considers all assets, except investments in capital assets, to be restricted in accordance with the provisions of RPPL 7-42.
- Unrestricted: net position that is not subject to externally imposed stipulations. As PAN Fund considers all assets, except investments in capital assets to be restricted in accordance with the provisions of RPPL 7-42, PAN Fund does not have unrestricted net position at September 30, 2015 and 2014.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During fiscal year 2015, the following pronouncements were implemented:

- GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, which revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The implementation of this statement did not have a material effect on the accompanying financial statements as PAN Fund employees do not contribute to the Republic of Palau Civil Service Pension Trust Fund (the Plan), a defined benefit, cost sharing multi-employer plan.
- GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*, which improves accounting and financial reporting for state and local governments' combinations and disposals of government operations. Government combinations include mergers, acquisitions, and transfers of operations. A disposal of government operations can occur through a transfer to another government or a sale. The implementation of this statement did not have a material effect on the accompanying financial statements.
- GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date - an amendment of GASB Statement No. 68*, which addresses an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or nonemployer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability. The implementation of this statement did not have a material effect on the accompanying financial statements.

In February 2015, GASB issued Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and financial reporting issues related to fair value measurements and requires entities to expand their fair value disclosures by determining major categories of debt and equity securities within the fair value hierarchy on the basis of the nature and risk of the investment. The provisions in Statement No. 72 are effective for fiscal years beginning after June 15, 2015. Management believes that the implementation of this statement only requires additional disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques and will not have a material effect on the financial statements.

In June 2015, GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement No. 68, and Amendments to Certain Provisions of GASB Statements No. 67 and No. 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements No. 67 and No. 68 with the reporting requirements in Statement No. 68. The provisions in Statement No. 73 are effective for fiscal years beginning after June 15, 2015, with the exception of the provisions that address employers and governmental nonemployer contributing entities for pensions that are not within the scope of Statement No. 68, which are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and addresses financial reporting requirements for governments whose employees are provided with postemployment benefits other than pensions (other postemployment benefits or OPEB). The provisions in Statement No. 74 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2015, GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which eliminates two of the four categories of authoritative GAAP that exist under the existing hierarchy prescribed by Statement No. 55. The two categories that will remain under the new standard are (1) GASB Statements and (2) GASB technical bulletins and implementation guides in addition to AICPA guidance that the GASB clears. The provisions in Statement No. 76 are effective for fiscal years beginning after June 15, 2015. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In August 2015, GASB issued Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements. The provisions in Statement No. 77 are effective for fiscal years beginning after December 15, 2015. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

Reclassification

Certain 2014 balances in the accompanying financial statements have been reclassified to conform to the 2015 presentation.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements September 30, 2015 and 2014

(3) Fixed Assets

Fixed assets of PAN Fund as of September 30, 2015 and 2014, are summarized below:

	<u>Estimated Useful Lives</u>	Balance at October 1, 2014	<u>Additions</u>	<u>Deletions</u>	Balance at September 30, 2015
Furniture, fixtures and equipment	3 years	\$ 19,234	\$ 3,059	\$ (1,599)	\$ 20,694
Vehicle	3 years	<u>7,000</u>	<u>-</u>	<u>-</u>	<u>7,000</u>
		26,234	3,059	(1,599)	27,694
Less accumulated depreciation		<u>(7,112)</u>	<u>(5,442)</u>	<u>1,599</u>	<u>(10,955)</u>
		\$ <u>19,122</u>	\$ <u>(2,383)</u>	\$ <u>-</u>	\$ <u>16,739</u>
		Balance at October 1, 2013	<u>Additions</u>	<u>Deletions</u>	Balance at September 30, 2014
Furniture, fixtures and equipment	3 years	\$ 14,120	\$ 5,116	\$ (2)	\$ 19,234
Vehicle	3 years	<u>7,000</u>	<u>-</u>	<u>-</u>	<u>7,000</u>
		21,120	5,116	(2)	26,234
Less accumulated depreciation		<u>(2,436)</u>	<u>(4,678)</u>	<u>2</u>	<u>(7,112)</u>
		\$ <u>18,684</u>	\$ <u>438</u>	\$ <u>-</u>	\$ <u>19,122</u>

(4) Contributions

The Micronesia Challenge (MC) is a commitment by the Chief Executives of the Republic of Palau, the Federated States of Micronesia (FSM), the Republic of the Marshall Islands, the U.S. Territory of Guam and the U.S. Commonwealth of the Northern Mariana Islands to effectively conserve at least 30% of the near-shore marine resources and 20% of the terrestrial resources across Micronesia by 2020.

Micronesia Conservation Trust (MCT) is a non-profit trust corporation registered in the FSM whose mission is to support biodiversity conservation and related sustainable development of the people of Micronesia by providing long-term sustained funding opportunities, management and investment services. MCT holds MC assets in restricted endowment funds. During the years ended September 30, 2015, 2014, 2013 and 2012, PAN Fund contributed \$98,177, \$96,750, \$84,596 and \$1,400,000, respectively, to the MC endowment funds held by MCT. In previous years the Republic of Palau, The Nature Conservancy and Global Environmental Facility made contributions to MCT of \$400,000, \$2,000,000 and \$1,684,848, respectively, and during the year ended September 30, 2014, Conservation International made contributions to MCT of \$1,000,000, on Palau's behalf. PAN Fund has determined that investment income will not be available for use until total contributions plus investment income totals \$10,000,000, and thus PAN Fund has not recognized related investment income in the accompanying financial statements. At September 30, 2015 and 2014, the Palau portion of MC endowment funds held by MCT was \$8,144,013 and \$8,455,615, respectively.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2015 and 2014

(4) Contributions, Continued

In accordance with RPPL 7-42, to support network wide activities, PAN Fund and/or PAN Office have entered into grants with the Palau International Coral Reef Center (PICRC) and the Palau Conservation Society (PCS) in the amounts of \$50,000 and \$54,931, respectively. The grant to PICRC, a component unit of ROP, is for strengthening and streamlining technical assistance on ecological monitoring for PAN States/Sites. The grant to PCS is for support with enabling legislation and capacity building for effective management of conservation programs for PAN States/Sites. During the years ended September 30, 2015 and 2014, \$23,486 and \$37,219, respectively, were disbursed for these grants which are recorded as competitive grant expense in the accompanying Statements of Revenues, Expenses and Changes in Net Position.

(5) Commitment

PAN Fund leases office space in Koror, Palau. Total future minimum lease payments under this lease for subsequent years ending September 30 are as follows:

Year ending September 30,

2016	\$ 14,400
2017	<u>3,600</u>
	<u>\$ 18,000</u>