

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

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2014 AND 2013

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, 2014 and 2013, 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, 2014 and 2013, 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 7 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 April 30, 2015 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

April 30, 2015



Protected Areas Network Fund

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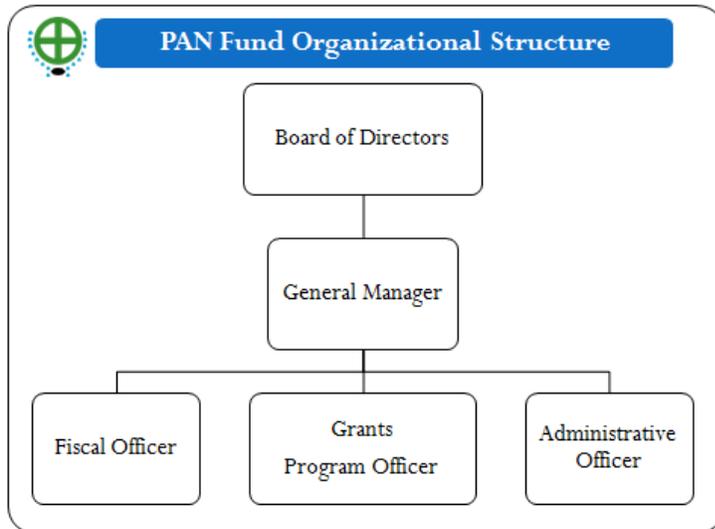
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Management's Discussion and Analysis Year Ended September 30, 2014

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, 2014, with selected comparative information for the fiscal years ended September 30, 2013 and 2012.

ORGANIZATION AND PURPOSE

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.



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

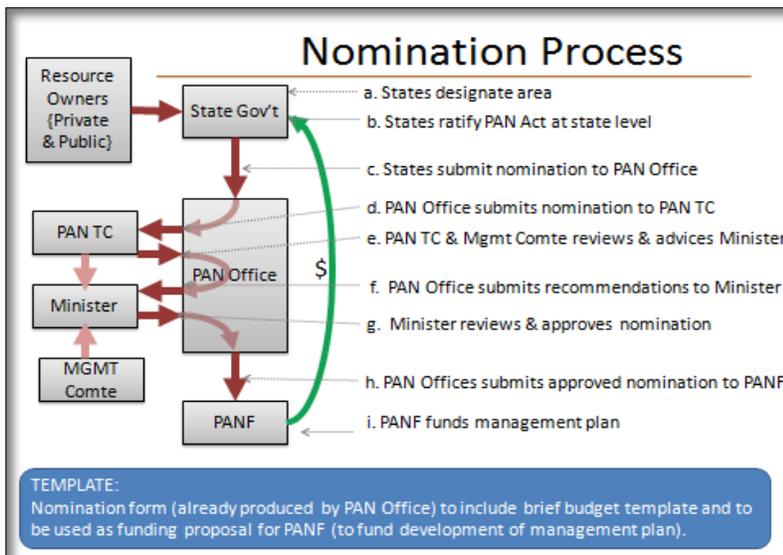
legislations were published under Title 24 PNC Chapter 34 - Protected Areas Network.

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 funding priorities for the PAN are driven by Palau's goals to establish and operationalize the PAN as promulgated by RPPL 6-39 and 7-42, where 100% of the monies are to be used to support and operationalize the PAN. The PAN serves as the national strategy to meet the goals of the Micronesia Challenge (MC) and achieve its goals on the Program of Works on Protected Areas (PoWPA) under the United Nations Convention on Biological Diversity (United Nations CBD).¹ The MC is a regional initiative with commitments by the Chief Executives of the Republic of Palau (ROP), the Federated States of Micronesia, the Republic of the Marshall Islands, the Territory of Guam and the Commonwealth of the Northern Mariana Islands with a goal to effectively conserve at least 30% of the near-shore marine and 20% of the terrestrial resources across Micronesia by the year 2020.

¹ Country Program Strategy for Palau's MC Endowment Fund

The green fee revenue is an environmental impact fee generated from two points of entry: the ocean and airports. The environmental impact fee or commonly known as “green fee” for the PAN is \$15 per non-Palauan passport holder visiting Palau. The green fee revenue is collected by the Bureau of Revenues, Customs and Taxation under the MOF. The MOF then transfers the revenues to PAN Fund in accordance with PAN regulations and established procedural agreements. The publication of Title 24 PNC Chapter 34 creating an enabling legal infrastructure for the PAN provided an opportunity and advantage for the PAN, where the green fee revenue generated and realized from previous fiscal years provides a funding source for the following year’s operation.

Title 24 PNC Chapter 34 and PAN regulations stipulate eligibility requirements for fiscal and technical support administered and entrusted to PAN Fund. The requirements include a nomination process with



scientific review and assessment of the nominated conservation area, establishment of supporting State level legislations for the conservation area and a management plan. However, the management and ownership of the natural resources remains with the State and community with vested interest for a successful and effective conservation management program. The nomination process involves the PAN institutional members such as the Management Planning Unit (MPU), which comprises of the PAN Office, the PAN Technical Committee and the PAN Management Committee. Once the nomination of the site is approved and endorsed by the Minister of MNRET, the State becomes a member of the PAN and thus

becomes eligible for “green fees” and other fiscal and/or technical support from PAN Fund. Acceptable uses of “green fees” or PAN monies include, but are not limited to, fiscal support for ecological baseline studies, management plan drafting and implementation of management plans.

In 2014, PAN Member States increased by two for a total of fifteen States, with the inclusion of Ngatpang State and Angaur State. The remaining State, pending nomination of a conservation area to PAN, is

PAN Member States/Communities	
2013	2014
Ngerchelongs State	Ngerchelongs State
Ngjwal State	Ngjwal State
Melekeok State	Melekeok State
Hatohobei State	Hatohobei State
Aimeliik State	Aimeliik State
Kayangel State	Kayangel State
Ngaraard State	Ngaraard State
Ngchesar State	Ngchesar State
Ngardmau State	Ngardmau State
Ngaremlengui State	Ngaremlengui State
Airai State	Airai State
Koror State	Koror State
Peleliu State	Peleliu State
	Ngatpang State
	Angaur State

Sonsorol State. Conservation areas/sites vary in scope and conservation management plans. Some conservation areas are either marine or terrestrial areas, watersheds, ecological services or systems from marine and/or terrestrial or “ridge to reef”, while others incorporate a network of conservation programs.

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 disbursement of funds is subject to verification of activities and program implementation with the requirement for quarterly and annual reports. The “green fee” monies are utilized to finance, support and further the PAN’s conservation programs and sustainable economic development of 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), capacity building to train and build the workforce for effective conservation management programs in areas of program management, public awareness and socialization, surveillance, enforcement programs and biological monitoring programs to achieve

the MC 30/20 goals by 2020.

OVERVIEW OF FINANCIAL STATEMENTS

PAN Fund supports measures and initiatives to minimize carbon footprints with climate change mitigation. The effort is practiced with PAN Fund's voluntary investment in energy efficient technology and equipment for operations. PAN Fund's fixed assets were \$19,122 as of September 30, 2014 as compared to \$18,684 as of September 30, 2013 and \$10,664 as of September 30, 2012. See note 3 for more detailed information on PAN Fund's fixed assets and changes therein.

Statements of Net Position:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Current assets	\$ 2,734,591	\$ 2,595,052	\$ 2,035,705
Fixed assets	<u>19,122</u>	<u>18,684</u>	<u>10,664</u>
Total assets	<u>2,753,713</u>	<u>2,613,736</u>	<u>2,046,369</u>
Current liabilities	<u>219,013</u>	<u>89,955</u>	<u>-</u>
Net position:			
Invested in capital assets	19,122	18,684	10,664
Restricted	<u>2,515,578</u>	<u>2,505,097</u>	<u>2,035,705</u>
Total net position	\$ <u>2,534,700</u>	\$ <u>2,523,781</u>	\$ <u>2,046,369</u>

Statements of Revenues, Expenses and Changes in Net Position:

Operating revenues	\$ -	\$ -	\$ -
Operating expenses	<u>1,898,207</u>	<u>1,232,842</u>	<u>2,245,612</u>
Operating loss	(1,898,207)	(1,232,842)	(2,245,612)
Nonoperating revenues	<u>1,909,126</u>	<u>1,710,254</u>	<u>1,847,920</u>
Change in net position	10,919	477,412	(397,692)
Net position at beginning of year	<u>2,523,781</u>	<u>2,046,369</u>	<u>2,444,061</u>
Net position at end of year	\$ <u>2,534,700</u>	\$ <u>2,523,781</u>	\$ <u>2,046,369</u>

Statements of Cash Flows:

Cash flows from operating activities	\$ (1,803,276)	\$ (1,143,473)	\$ (2,245,612)
Cash flows from noncapital financing activities	2,416,798	3,111,759	2,422,280
Cash flows from capital financing activities	<u>(5,116)</u>	<u>(10,456)</u>	<u>(10,664)</u>
Net increase in cash	608,406	1,957,830	166,004
Cash at beginning of year	<u>2,123,834</u>	<u>166,004</u>	<u>-</u>
Cash at end of year	\$ <u>2,732,240</u>	\$ <u>2,123,834</u>	\$ <u>166,004</u>

FINANCIAL HIGHLIGHTS

Green fee revenues of \$1,882,024 increased by 10% in fiscal year 2014 compared to \$1,706,923 in fiscal year 2013 and decreased by 8% in fiscal year 2013 compared to \$1,847,920 in fiscal year 2012. Green fee revenues of \$1,847,920 from fiscal year 2012 financed PAN Fund's operations in fiscal year 2013, while \$1,706,923 from fiscal year 2013 financed PAN Fund's operations in fiscal year 2014 and \$1,882,024 from fiscal year 2014 are restricted to finance PAN Fund's operations in fiscal year 2015. However, based on prioritization of programs and activities per work plans, operating monies supported and maintained the institutional and system-wide network of conservation programs.

Total liabilities of \$219,013 increased by 143% in fiscal year 2014 compared to \$89,955 in fiscal year 2013. The increase in liabilities factors in 5% or \$96,750 payable to Palau's endowment account with MCT and \$39,476 payable to ROP.

Total operating expenses of \$1,898,207 in fiscal year 2014 increased by 54% compared to \$1,232,842 in fiscal year 2013 and decreased in fiscal year 2013 by 45% compared to \$2,245,612 in fiscal year 2012. Contributing factors for the increase in expenses include PAN Member States financial support of \$1,311,115 in fiscal year 2014 compared to \$813,416 in fiscal year 2013. The increase in the PAN Member States' expense is reflective of the increase in the number of PAN Member States from thirteen to fifteen, the cumulative work plans for the thirteen communities/PAN Member States and support of management plans for the new members.

FINANCIAL HIGHLIGHTS, CONTINUED

Additional increases in operating expenses include PAN Institutional System by 57% from \$129,354 in fiscal year 2013 compared to \$203,435 in fiscal year 2014. PAN Institutional System expense is reflective of the MPU's operating work plan with financial support of 9.95% from the fiscal year 2013 green fee revenue, thereby operating within the RPPL 9-15 amendment to PAN regulations. The additional \$25,000 for the MPU is a first tranche support from the Global Environment Facility/Small Grants Programme (GEF/SGP) to implement the Management Program Assessment and Effectiveness Tool (MPAME). The MPAME is a tool utilized to evaluate and assess the status of PAN Member States' conservation management programs. Other contributing factors for the 54% increase in operating expenses include allocations with disbursements towards the sustainable financial mechanism of PAN. Emergency funding support of \$31,210 was disbursed to PAN Member States to assist with recovery efforts from Typhoon Haiyan.

Net cash at the end of the year of \$2,732,240 is inclusive of ROP's transfer in of \$2,389,696, green fee revenue of \$1,882,024, receivable from ROP of \$468,196 from fiscal year 2013; and a due to ROP of \$39,476. The cash balance at the end of the year is earmarked for allocations and funding for PAN. The encumbrance on 2014 allocations and schedules of disbursement of funds are reflective of the degrees and stages of program mobilization or implementation by the PAN Member States and competitive grant programs, as disbursements are on a quarterly basis and subject to acceptable quarterly and annual reports.

ECONOMIC OUTLOOK

Palau's promotion and branding of "Pristine Palau" by the Palau Visitor's Authority, combined with the international interest and support for Palau's shark sanctuary and the initiative for a marine sanctuary, provide a positive outlook for the tourism industry and the generation of "green fee" revenue and financial support for PAN Fund. The target market for "high end" tourism lends towards trajectories of a sustainable tourism industry that balances impacts on the environment and economic development, with safeguards and preservation of the environment with its natural resources and ecological biodiversity.

An added risk mitigation for PAN Fund includes the predetermined budget for the following year based on the realized "green fee" revenue from the current year. Therefore, PAN Fund and the PAN - the system-wide network - in partnership and collaboration shall continue to identify the key priorities to allocate and utilize the limited financial resources towards effective conservation management programs. Further, mechanisms in place for PAN Fund to mitigate risks and to 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. This diversification of funds is mitigation to build resilience and sustainable financial mechanisms for PAN Fund.

In addition, the strength and support from Palau's Congress and His Excellency President Tommy E. Remengesau, Jr., a champion on environment and conservation causes, provides continued commitment and support for the MC to effectively conserve 30% of marine and 20% of terrestrial areas by the year 2020², which will impart and 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 CBD, as well as the fiscal and technical support from donor communities such as The David & Lucile Packard Foundation, TNC, CI, the Global Environment Fund, the International Union for Conservation of Nature and other supporting partners and patrons lend for a positive outlook for PAN Fund. Thus, PAN Fund has the momentum and support to continue its role as a mechanism to help the people of Palau with conservation management programs for sustainable use of natural resources and cultural preservations for the people today and future generations.

CONCLUDING SUMMARY

The socialization and transfer of technology with knowledge of the PAN and PAN Fund continues to evolve and strengthen to synchronize partnerships and collaborations between the public and private sectors. PAN Fund is also continuing its effective management process for improved system-wide network management with the PAN system-wide design, utilizing Marxan for a cost effective and integrated approach towards a nationwide biological and ecological network to prioritize and strengthen the national system-wide network with scientific and social-economic approaches to support decisions for effective management of conservation programs in Palau.

² Statement for the Eight Session of the United Nations Open Working Group on Sustainable Development, Goals Delivered by H.E. Tommy Remengesau Jr., President of the Republic of Palau, on behalf of the Pacific SDG Working Group Troika and the Pacific Small Island Developing States, Represented at the United Nationals and Timor-Leste -3 February 2014, New York.

CONCLUDING SUMMARY, CONTINUED

PAN Fund is continuously evolving with the application of adaptive management to implement strategies with objectives to improve effective results. The strategic approaches include objectives to address the demand for investment and deposit policies for custodial credit risk to safeguard and mitigate risk exposure for PAN Fund's growing assets. PAN Fund will also continue to strive for effective and efficient measures and policies to respond to changes and seize opportunities to sustainably support and finance the PAN. PAN Fund shall also continue to improve and adhere to internal controls and compliance with financial, managerial and operational policies with procedures to remain a prudent fiduciary and financial trustee for the PAN.

Management's Discussion and Analysis for the year ended September 30, 2013 is set forth in PAN Fund's report on the audit of financial statements, which is dated May 5, 2014. That Discussion and Analysis explains the major factors impacting the 2013 financial statements and can be viewed at the Office of the Public Auditor's website at www.palauopa.org.

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 monies entrusted with fiduciary care. Please visit www.palaupanfund.org for more information on Palau PAN programs. Inquiries and additional information on this report may be referred to Clarinda Ziegler, General Manager, The Protected Areas Network Fund, P.O. Box 6094, Koror, Republic of Palau 96940, or via the following: Phone: (680) 488-FUND (3863) | Fax: (680) 488-1314 | Email: ctieglar@palaupanfund.org or info@palaupanfund.org.

PROTECTED AREAS NETWORK FUND

Statements of Net Position
September 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
<u>ASSETS</u>		
Current assets:		
Cash	\$ 2,732,240	\$ 2,123,834
Receivable from Republic of Palau	-	468,196
Prepaid expenses	<u>2,351</u>	<u>3,022</u>
Total current assets	2,734,591	2,595,052
Fixed assets, net	<u>19,122</u>	<u>18,684</u>
	<u>\$ 2,753,713</u>	<u>\$ 2,613,736</u>
<u>LIABILITIES AND NET POSITION</u>		
Current liabilities:		
Accounts payable	\$ 80,099	\$ -
Accrued expenses	2,688	5,359
Due to Republic of Palau	39,476	-
Due to Micronesia Conservation Trust	<u>96,750</u>	<u>84,596</u>
Total liabilities	<u>219,013</u>	<u>89,955</u>
Commitment		
Net position:		
Invested in capital assets	19,122	18,684
Restricted	<u>2,515,578</u>	<u>2,505,097</u>
Total net position	<u>2,534,700</u>	<u>2,523,781</u>
	<u>\$ 2,753,713</u>	<u>\$ 2,613,736</u>

See accompanying notes to financial statements.

PROTECTED AREAS NETWORK FUND

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Operating revenues	\$ -	\$ -
Operating expenses:		
PAN site/states	1,311,115	813,460
PAN Institutional System	203,435	129,354
Micronesia Conservation Trust contribution	96,750	84,596
Salaries and wages	65,765	52,660
Competitive grant expense	37,219	44,226
Emergency disbursement	31,210	-
Grants	25,000	-
Professional fees	22,468	17,364
Outreach/awareness meetings	20,953	9,012
Employee benefits	17,176	22,327
Travel and conferences	12,958	11,526
Rent	12,600	7,200
Communications	8,002	9,558
Depreciation	4,678	2,436
Utilities	2,848	3,739
Advertisements	2,424	3,063
Repairs and maintenance	2,230	783
Professional development	122	11,482
Other	21,254	10,056
	<u>1,898,207</u>	<u>1,232,842</u>
Total operating expenses		
	<u>(1,898,207)</u>	<u>(1,232,842)</u>
Operating loss		
Nonoperating revenues:		
Transfer in from Republic of Palau	1,882,024	1,706,923
Grant revenue	25,000	-
Other income	2,102	3,331
	<u>1,909,126</u>	<u>1,710,254</u>
Total nonoperating revenues		
Change in net position	10,919	477,412
Net position at beginning of year	<u>2,523,781</u>	<u>2,046,369</u>
Net position at end of year	<u>\$ 2,534,700</u>	<u>\$ 2,523,781</u>

See accompanying notes to financial statements.

PROTECTED AREAS NETWORK FUND

Statements of Cash Flows
Years Ended September 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Cash flows from operating activities:		
Micronesia Conservation Trust contribution	\$ (84,596)	\$ -
Cash payments to PAN sites/States and institutional system	(1,514,550)	(942,814)
Cash payments to suppliers for goods and services	(123,877)	(130,122)
Cash payments to employees for services	<u>(80,253)</u>	<u>(70,537)</u>
Net cash used for operating activities	<u>(1,803,276)</u>	<u>(1,143,473)</u>
Cash flows from noncapital financing activities:		
Transfer in from Republic of Palau	2,389,696	3,108,428
Grant revenue	25,000	-
Other income	<u>2,102</u>	<u>3,331</u>
Net cash provided by noncapital financing activities	<u>2,416,798</u>	<u>3,111,759</u>
Cash flows from capital financing activities:		
Fixed asset acquisitions	<u>(5,116)</u>	<u>(10,456)</u>
Net cash used for capital financing activities	<u>(5,116)</u>	<u>(10,456)</u>
Net increase in cash	608,406	1,957,830
Cash at beginning of year	<u>2,123,834</u>	<u>166,004</u>
Cash at end of year	<u>\$ 2,732,240</u>	<u>\$ 2,123,834</u>
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (1,898,207)	\$ (1,232,842)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	4,678	2,436
(Increase) decrease in assets:		
Prepaid expenses	671	(3,022)
Increase (decrease) in liabilities:		
Accounts payable	80,099	-
Accrued expenses	(2,671)	5,359
Due to Micronesia Conservation Trust	<u>12,154</u>	<u>84,596</u>
Net cash used for operating activities	<u>\$ (1,803,276)</u>	<u>\$ (1,143,473)</u>

See accompanying notes to financial statements.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2014 and 2013

(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, 2014 and 2013, MOF collected \$1,874,524 and \$1,691,923, respectively, for this purpose, which PAN Fund recorded as transfers in from ROP Green Fees. PAN Fund recorded ROP Green Fees receivable of \$-0- and \$466,696 and Green Fees payable of \$39,476 and \$-0- as of September 2014 and 2013, respectively. PAN Fund recorded \$7,500 and \$15,000 as other transfers in from ROP for audit expense reimbursement, of which \$-0- and \$1,500 was receivable, as of and for the years ended September 30, 2014 and 2013, respectively. The receivables 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 \$96,750 and \$84,596 for the years ended September 30, 2014 and 2013, 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, 2014 and 2013;
- 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, 2014 and 2013

(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;
- The undertaking of necessary research and educational activities substantially related to carrying out the provisions of RPPL No. 7-42; and
- 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, 2014 and 2013, PAN Fund provided funding for activities specified in an annual work plan of PAN Office in the amounts of \$143,435 and \$129,354, 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 \$60,000 and \$-0- for the years ended September 30, 2014 and 2013, respectively, is recorded as PAN Institutional System expense in the accompanying Statements of Revenues, Expenses and Changes in Net Position.
- Emergency funding to help PAN sites address exceptional needs arising from natural disasters or accidents. During the years ended September 30, 2014 and 2013, PAN Fund provided funding for the repair, assistance and relief efforts for PAN sites affected by Typhoon Haiyan in the amounts of \$31,210 and \$-0-, 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.

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.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2014 and 2013

(2) Summary of Significant Accounting Policies, Continued

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, 2014 and 2013, cash was \$2,732,240 and \$2,123,834, respectively, and the corresponding bank balances were \$2,895,837 and \$2,172,105, respectively, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. At September 30, 2014 and 2013, bank deposits of \$500,000 and \$416,365 were FDIC insured, respectively. 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
- 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.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2014 and 2013

(2) Summary of Significant Accounting Policies, Continued

Cash, Continued

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, 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.

Contribution refunds of \$5,405 were reimbursed by the Fund to PAN Fund on August 21, 2013 for the year ended September 30, 2013, 50% of which were refunded to contributing employees. There were no contribution refunds reimbursed by the Fund to PAN Fund for the year ended September 30, 2014. The net amount refunded is recorded as other income in the accompanying Statements of Revenues, Expenses and Changes in Net Position.

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, 2014 and 2013.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2014 and 2013

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended September 30, 2014, PAN Fund implemented the following pronouncements:

- GASB Statement No. 66, *Technical Corrections - 2012*, which enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The implementation of this statement did not have a material effect on the accompanying financial statements.
- GASB Statement No. 67, *Financial Reporting for Pension Plans*, which revises existing guidance for the financial reports of most pension plans. The implementation of this statement did not have a material effect on the accompanying financial statements.
- GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, which requires a state or local government guarantor that offers a nonexchange financial guarantee to another organization or government to recognize a liability on its financial statements when it is more likely than not that the guarantor will be required to make a payment to the obligation holders under the agreement. The implementation of this statement did not have a material effect on the accompanying financial statements.

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions*, which revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The provisions in Statement 68 are effective for fiscal years beginning after June 15, 2014. Management does not believe that the implementation of this statement will have a material effect on the financial statements of PAN Fund.

In January 2013, GASB issued 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 provisions in Statement 69 are effective for fiscal years beginning after December 15, 2013. Management has not yet determined the effect of implementation of this statement on the financial statements of PAN Fund.

In November 2013, GASB issued 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 provisions in Statement 71 are effective for fiscal years beginning after June 15, 2014. Management does not believe that the implementation of this statement will have a material effect on the financial statements of PAN Fund.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements September 30, 2014 and 2013

(3) Fixed Assets

Fixed assets of PAN Fund as of September 30, 2014 and 2013, are summarized below:

	<u>Estimated Useful Lives</u>	<u>Balance at October 1, 2013</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at September 30, 2014</u>
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>
		<u>\$ 10,664</u>	<u>\$ 3,456</u>	<u>\$ -</u>	<u>\$ 14,120</u>
Furniture, fixtures and equipment	3 years	\$ 10,664	\$ 3,456	\$ -	\$ 14,120
Vehicle	3 years	<u>-</u>	<u>7,000</u>	<u>-</u>	<u>7,000</u>
		10,664	10,456	-	21,120
Less accumulated depreciation		<u>-</u>	<u>(2,436)</u>	<u>-</u>	<u>(2,436)</u>
		<u>\$ 10,664</u>	<u>\$ 8,020</u>	<u>\$ -</u>	<u>\$ 18,684</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, 2014, 2013 and 2012, PAN Fund contributed \$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 investment income in the accompanying financial statements. At September 30, 2014 and 2013, the Palau portion of MC endowment funds held by MCT was \$8,455,615 and \$6,888,443, respectively.

PROTECTED AREAS NETWORK FUND

Notes to Financial Statements
September 30, 2014 and 2013

(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, 2014 and 2013, \$37,219 and \$44,226, 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,

2015	\$ 14,400
2016	14,400
2017	<u>3,600</u>
	\$ <u><u>32,400</u></u>