PALAU INTERNATIONAL CORAL REEF CENTER
(A COMPONENT UNIT OF THE REPUBLIC OF PALAU)

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2012 AND 2011

Deloitte & Touche LLC
P.O. Box 500308
Saipan, MP 96950-0308
USA

Tel: +1 670 322 7337/0860/0861
Fax: +1 670 322 7340
www.deloitte.com

INDEPENDENT AUDITORS' REPORT

Board of Directors
Palau International Coral Reef Center:

We have audited the accompanying statements of net assets of the Palau International Coral Reef Center (the Center), a component unit of the Republic of Palau, as of September 30, 2012 and 2011, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Center's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Center as of September 30, 2012 and 2011, and changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 31, 2013 on our consideration of the Center'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* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 8 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. 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.

Deloitte & Touche LLP

May 31, 2013

PALAU INTERNATIONAL CORAL REEF CENTER

Management's Discussion and Analysis
Fiscal Year Ended September 30, 2012

This Management's Discussion and Analysis of the Palau International Coral Reef Center (the Center) provides an overview to the financial activities and performance of the Center for the fiscal year ended September 30, 2012, with selected comparative information for the fiscal years ended September 30, 2011 and 2010.

ORGANIZATION AND MISSION

The Center was created by Public Law 5-17 in November 1998 as a public nonprofit coral reef research, education and training center operating under a Board of Directors. The mission of the Center is to be an international center of excellence to support conservation and management for the perpetuation of marine and associated environments through research and education that is significant to Palau and relevant to the world. The Center is designed to assist in improving the management, use and conservation of Palau and the world's marine environment, and to serve as a direct education tool and a tourism attraction through aquarium exhibits which highlight Palau's marine ecosystems and species.

The Republic of Palau (ROP) received funding of US $7.3 million from the Government of Japan for the construction of the Center. The construction commenced in November 1999 and the facility opened in January 2001. Located on an 8,248 square meter pier, the Center features three main buildings: a research facility, visitor education and awareness exhibit areas, and an administration complex.

To achieve its mission, the Center developed and adopted its Strategic Plan 2002-2006 (phase 1) with goals and objectives to guide it towards a self-sustaining center of excellence for marine research, training and educational activities. The strategic plan focuses on the Center's activities in five program areas - research, environmental education and public awareness, aquarium exhibits, institutional development and income generation, and engineering and maintenance - as key to becoming a center of excellence in self-sustained research and educational programs.

In September 2006 when phase 1 of the Palau International Coral Reef Center Strengthening Project was completed, the Center developed and adopted Strategic Plan 2007-2012, which is phase 2 of the project with the same focus on the five program areas, but with a regional focus. That is, sharing what we have learned over the years with our neighbors in the Micronesia region by way of collaboration, sharing and transfer of knowledge, and capacity building. Activities of the Center will be locally responsive and globally significant.

In November 2012, the center adopted a more streamline five-year Strategic Plan with a clear vision and core values along with its mission.

VISION

The Center envisions people empowered with science and knowledge for effective marine conservation and management.

CORE VALUES

The Center is guided by the following core values:

1. We believe in working together in a spirit of cooperation, teamwork and partnership both within the Center and with external partners.

2. We achieve meaningful results through hard work focus and effective application of our knowledge and skills.

3. We are reliable and consistent, providing excellent service to our guests, clients and partners.

P. O. Box 7086 Koror, Republic of Palau 96940
Tel. 680.488.6950 Fax. 680.488.6951 email. picrc@picrc.org http://www.PICRC.org

CORE VALUES, CONTINUED

4. We deliver quality information and objective and innovative science in order to support sound resource management decisions and actions.

5. We are visionaries, pursuing and adapting to important trends and opportunities.

6. We invest in people and learning, creating a nurturing environment for our staff and partners and promoting cultural awareness and sensitivity, community well-being and the application of traditional knowledge.

FINANCIAL STATEMENTS

The financial statements of the Center are prepared following the provisions of the Governmental Accounting Standards Board and in compliance with accounting principles generally accepted in the United States of America as applied to governmental entities and proprietary funds. The flow of economic resources measurement focus is used as the basis of accounting for proprietary funds in which the statement of net assets includes all assets and liabilities associated with the operation of the fund. The accrual basis of accounting is the method used to record revenues when earned and expenses when incurred.

OVERVIEW OF FINANCIAL OPERATIONS

In fiscal year 2012,operating revenues increased by 0.49% ($673,546 in fiscal year 2012 versus $670,279 in fiscal year 2011) mainly due to increases in contractual service revenues by 394%, donations by 14%, facilities fees and admissions by 22%, boat fee by 106% and accommodation by 56%. On the other hand, grants revenues decreased by 32% because most of the multi-projects were closing this fiscal year. In fiscal year 2011, operating revenues increased by 21% ($670,279 in fiscal year 2011 versus $555,092 in fiscal year 2010) mainly due to increases in fundraising by 90%, donations by 37% and research facilities, education program fee and others by 78%, while facility use and aquarium admission fees decreased by 4%.

In fiscal year 2012 total tourist arrivals to Palau from all markets was 116,856 and the Palau Aquarium captured 15,535 of them, which is a 13% market share, a 2% increase from fiscal year 2011. Of the 15,535 visitors to the Center, only 2,362 (15%) were from the Republic of China (ROC), a 4% increase from fiscal year 2011. The Korean market brought in 18,402 visitors to Palau in 2012, of which 8,705 visited the Center which translates to a 47% share in fiscal year 2012. 37,981 Japanese tourists visited Palau in fiscal year 2012, and the Center received only 2,793 (7%) of them, which remained the same compared to fiscal year 2011.

In fiscal year 2011 total tourist arrivals to Palau from ROC increased by 67%, 37,632 versus 22,514 in fiscal year 2010. Total tourist arrivals to Palau from all markets was 109,057 in fiscal year 2011 and the Palau Aquarium captured 12,361 of them, which is an 11% market share, 8% down from fiscal year 2010. Of the 12,361 visitors to the Center, only 1,306 (11%) were from ROC, a 2% increase from fiscal year 2010. The Korean market brought in 15,681 visitors to Palau in 2011, of which 7,217 visited the Center which translates to a 46% share in fiscal year 2011, 23% less than fiscal year 2010. 37,800 Japanese tourists visited Palau in fiscal year 2011, and the Center received only 2,536 (7%) of them, which is 1% less compared to fiscal year 2010. Japanese visitors made up 21% of those who visited the Center in fiscal year 2011. All other markets made up largely of Palauan visitors, visitors from the U.S. mainland, the Philippines, the People's Republic of China (PRC) and Germany contributed 1,676 (14%) of visitors to the Center.

Operating expenses decreased by 16% from $1,091,196 in fiscal year 2011 to $921,716 in fiscal year 2012. Personnel expenses (salaries, wages and fringe benefits) decreased by 11%, from $453,083 in fiscal year 2011 to $405,233 in fiscal year 2012 as a result of unfilled vacant positions. Notable decreases in expenses include communications (65%), supplies and printing (27%) and utilities (28%). There were increases in fuel (123%), repair and maintenance (79%) and other expenses (26%). The decrease in operating costs is also attributed largely to decreases in merchandise cost (15%), sales and marketing (50%), dues and subscription (62%) and anniversary (12%). Operating expenses decreased by 12% from $1,235,767 in fiscal year 2010 to $1,091,196 in fiscal year 2011. Personnel expenses (salaries, wages and fringe benefits) decreased by 10%, from $501,465 in fiscal year 2010 to $453,083 in fiscal year 2011, as a result of drastic measures to lay-off staff and reorganize responsibilities to a sustainable level. Notable decreases in expenses include repairs and maintenance (12%), fuel (46%), supplies and printing (48%), professional services (31%) and utilities (18%). There were increases in communications (52%) and other expenses (185%). The decrease in operating costs is also attributed largely to decreases in merchandise cost (22%), sales and marketing (99%), depreciation (32%) and anniversary (50%).

OVERVIEW OF FINANCIAL OPERATIONS, CONTINUED

In fiscal year 2012, total operating loss decreased by $175,831 due to a change in management and implementation of cost cutting measures to keep the Center from running out of funds. Changes implemented resulted in an increase in net assets of $111,692. Change in net assets for fiscal year 2012 as compared to fiscal year 2011 improved by 409% from $(36,177) in fiscal year 2011 to $111,692 in fiscal year 2012. As a result, total net assets increased from $2,241,767 in fiscal year 2011 to $2,353,459 in fiscal year 2012.

In fiscal year 2011, total operating loss decreased by $260,176 due to a change in management and implementing cost cutting measures to keep the Center from running out of funds. Changes implemented resulted in a decrease in net assets of $36,177. Change in net assets for fiscal year 2011 as compared to fiscal year 2010 improved by 72 % from $(127,869) in fiscal year 2010 to $(36,177) in fiscal year 2011. As a result, total net assets decreased from $2,277,944 in fiscal year 2010, as restated, to $2,241,767 in fiscal year 2011.

A summary of operations, changes in net assets and cash flows for the fiscal years ended September 30, 2012, 2011and2010follows:

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2012, 2011 and 2010

	2012	2011	Increase (Decrease) from 2011	2010 (As Restated)
Operating revenues:				
Grants	$ 270,040	$ 394,622	-32%	$ 327,793
Facility user and admission fees	111,826	91,750	22%	95,411
Donations	66,656	58,629	14%	42,926
Merchandise sales	23,884	22,585	6%	34,295
Fund raising	33,011	41,571	-21%	21,858
Contract service	103,179	20,899	394%	-
Boat fee	27,097	13,169	106%	13,104
Accommodation	12,705	5,641	125%	7,671
Research facilities	8,822	5,609	57%	2,562
Education program fee	6,455	2,321	178%	970
Other	9,871	13,483	-27%	8,502
Total operating revenues	**673,546**	**670,279**	0.49%	**555,092**
Recoveries (bad debts)	3,084	-	100%	(418)
	676,630	**670,279**	1%	**554,674**
Operating expenses:				
Salaries, wages and fringe benefits	405,233	453,083	-11%	501,465
Depreciation	167,337	157,263	6%	232,506
Utilities	90,879	125,673	-28%	153,747
Donations	-	103,550	-100%	-
Supplies and printing	47,719	65,803	-27%	126,989
Professional services	60,135	55,363	9%	79,799
Travel	20,488	17,007	20%	38,712
Fuel	25,759	11,545	123%	21,393
Merchandise cost	12,536	14,744	-15%	18,974
Insurance	15,714	14,167	11%	15,073
Communications	7,578	21,960	-65%	14,435
Anniversary	3,472	3,959	-12%	7,987
Repairs and maintenance	10,937	6,121	79%	6,942
Training	8,509	2,550	234%	78
Dues and subscription	898	2,335	-62%	1,472
Entertainment	746	1,174	-36%	937
Postage and freight	142	262	-46%	891
Sales and marketing	15	30	-50%	2,240
Other	43,619	34,607	26%	12,127
Total operating expenses	**921,716**	**1,091,196**	**-16%**	**1,235,767**
Operating loss	**(245,086)**	**(420,917)**	**-42%**	**(681,093)**

Statements of Revenues, Expenses and Changes in Net Assets, Continued
Years Ended September 30, 2012, 2011 and 2010

	2012	2011	Increase (Decrease) from 2011	2010 (As Restated)
Nonoperating revenues:				
Appropriations	356,708	387,000	-8%	382,500
Interest income	70	105	-33%	1,166
Interest expense	-	(2,365)	-100%	-
Total nonoperating revenues	**356,778**	**384,740**	**-7%**	**383,666**
Operating loss before capital contributions	**111,692**	**(36,177)**	**-409%**	**(297,427)**
Capital contributions	-	-	0%	169,558
Change in net assets	**111,692**	**(36,177)**	**-409%**	**(127,869)**
Net assets at beginning of year	**2,241,767**	**2,277,944**	**-2%**	**2,405,813**
Net assets at end of year	**$ 2,353,459**	**$ 2,241,767**	**5%**	**$ 2,277,944**

Statements of Cash Flows
Years Ended September 30, 2012, 2011 and 2010

	2012	2011	Increase (Decrease) from 2011	2010
Cash flows from operating activities	$ (305,481)	$ (146,842)	108%	$ (384,984)
Cash flows from noncapital financing activities	356,708	387,000	-8%	382,500
Cash flows from capital and related financing activities	(33,562)	(106,649)	-69%	(21,111)
Cash flows from investing activities	70	(2,260)	-103%	1,166
Net increase (decrease) in cash	**17,735**	**131,249**	**-86%**	**(22,429)**
Cash at beginning of year	**272,300**	**141,051**	**93%**	**163,480**
Cash at end of year	**$ 290,035**	**$ 272,300**	**7%**	**$ 141,051**

OVERVIEW OF FINANCIAL POSITION

Total current assets increased by 29% in fiscal year 2012 over fiscal year 2011 ($524,603 versus $405,622), due mostly to a 108% increase in receivables at September 30, 2012 ($213,206 versus $102,324). There are no ROP receivables in fiscal year 2012. Allotments from ROP were timely received. Cash increased by 7% in fiscal year 2012 over fiscal year 2011 ($290,035 versus $272,300). Most grants are multi-year and $142,345 represents grant amounts that have been expended but not received in fiscal year 2012. Due to a decreased, yet high rate of depreciation, total assets decreased by 1% in fiscal year 2012 over fiscal year 2011 ($2,568,871 versus $2,583,665).

Total current assets increased by 37% in fiscal year 2011 over fiscal year 2010 ($405,622 versus $296,710), due mostly to a 93% increase in cash at September 30, 2011 ($272,300 versus $141,051). There are no ROP receivables in fiscal year 2011. Allotments from ROP were timely received. Grants receivables decreased by 69% in fiscal year 2011 over fiscal year 2010 ($4,709 versus $15,438). Most grants are multi-year and $4,709 represents grant amounts that have been expended but not received in fiscal year 2011. Due to a decreased, yet high rate of depreciation, total assets decreased by 2% in fiscal year 2011 over fiscal year 2010, as restated ($2,583,665 versus $2,628,917).

Grant receipts are initially posted as deferred revenue waiting to be expensed as projects are implemented. Deferred revenue decreased by 75% in fiscal year 2012 over fiscal year 2011 ($29,979 versus $120,370). The Center strived to pay its debts and signed a note payable with the Palau Public Utilities Corporation (PPUC) for its outstanding electric bills. The balance of the note payable to PPUC at the end of fiscal year 2012 was $87,749 and $114,318 in fiscal year 2011. Total liabilities decreased by 37% during fiscal year 2012 from $341,898 in fiscal year 2011 to $215,412 in fiscal year 2012 and by 3% during fiscal year 2011 from $350,973 in fiscal year 2010 to $341,898 in fiscal year 2011.

OVERVIEW OF FINANCIAL POSITION, CONTINUED

As the Center continues to grow and operate, it incurs expenses and recognizes revenues as projects are implemented. As such, accounts payable decreased by 20% ($23,862 versus $29,819) in fiscal year 2012 over fiscal year 2011 and decreased by 82% ($29,819 versus $164,635) in fiscal year 2011 over fiscal year 2010 and deferred revenue decreased by 75% ($29,979 versus $120,370) in fiscal year 2012 over fiscal year 2011 and increased by 7% ($120,017 versus $112,017) in fiscal year 2011 over fiscal year 2010.

Capital Assets

At September 30, 2012, 2011 and 2010, the Center had $2,044,268, 2,178,043, and $2,332,207, respectively, invested in capital assets, net of accumulated depreciation where applicable, including buildings, mechanical, electrical, research, office, exhibit and marine equipment, aquarium, furniture and fixtures, computers and vehicles, which represents a net decrease in fiscal year 2012 of $133,775 or 6% over fiscal year 2011 and $154,164 or 7% in fiscal year 2011 over fiscal year 2010. See note 5 to the financial statements for more information on the Center's property, plant and equipment.

Long-Term Debt

At September 30, 2012 and 2011, the Center had $87,749 and $114,318, respectively, in long-term debt outstanding. See note 6 to the financial statements for more detailed information on the Center's long-term debt and changes therein.

A summary of the Center's statements of net assets at September 30, 2011, 2010 and 2009 is shown below:

Statements of Net Assets
September 30, 2012, 2011 and 2010

	2012	2011	Increase (Decrease) from 2011	2010 (As Restated)
Current assets:				
Cash	$ 290,035	$ 272,300	7%	$ 141,051
Receivables:				
Grantor agencies	142,345	4,709	2923%	15,438
Other	70,861	97,615	-27%	84,925
	213,206	102,324	108%	100,363
Less allowance for doubtful accounts	(46,556)	(56,949)	-18%	(56,949)
Total receivables, net	166,650	45,375	267%	43,414
Inventories	62,642	84,248	-26%	102,213
Prepaid expense	5,276	3,699	43%	10,032
Total current assets	**524,603**	**405,622**	**29%**	**296,710**
Property, plant and equipment, net	2,044,268	2,178,043	-6%	2,332,207
Total assets	**$ 2,568,871**	**$ 2,583,665**	**-1%**	**$ 2,628,917**
Current liabilities:				
Current portion of note payable	$ 21,565	$ 24,067	-10%	$ -
Accounts payable	23,862	29,819	-20%	164,635
Deferred revenue	29,979	120,370	-75%	112,017
Accrued expenses	73,822	77,391	-5%	74,321
Total current liabilities	**149,228**	**251,647**	**-41%**	**350,973**
Note payable, net of current portion	66,184	90,251	-27%	-
Total liabilities	**215,412**	**341,898**	**-37%**	**350,973**
Net assets:				
Invested in capital assets	2,044,268	2,178,043	-6%	2,332,207
Unrestricted	309,191	63,724	385%	(54,263)
Total net assets	**2,353,459**	**2,241,767**	**5%**	**2,277,944**
Total liabilities and net assets	**$ 2,568,871**	**$ 2,583,665**	**-1%**	**$ 2,628,917**

ECONOMIC OUTLOOK

The Center's role in the region is increasing, especially in supporting the Micronesia Challenge monitoring and research. This increasing role for the Center will likely bring in more funds to support its regional role. Both the Micronesia Conservation Trust and the Nature Conservancy is committed to supporting the Center in providing technical and scientific support to the Micronesia Challenge. Through this new role, it has opened up new opportunities internationally. Furthermore, in 2012, Palau won the Future Policy Award for Shark Sanctuary legislation and PAN legislation. These legislations that were passed improved conservation of Palau unique resources, including all sharks in the waters of Palau. The Center's research department has also been publishing the results of their studies in peer reviewed international scientific journals. Because of these activities and awards, the Center is now getting more requests to house/host different research projects and is being contracted to conduct different research regionally.

With the Palau Southern Lagoon listed in the World Heritage Site, we had a slight increase in the number of visitors in fiscal year 2012. Japan visitors may increase in fiscal year 2012 and 2013 due to a rebounding economy and recovery from the devastating tsunami. The green fee increased but did not seem to have a negative impact on the number of visitors coming to our island paradise. Value added to their experiences and Palau, being a safe destination, may very well be the determining factor. Although tourists continue to increase, the Center is still facing challenges by not attracting more than 50% of this market.

A very positive outlook for the Center is its agreement with the Government of Japan, through JICA, that implemented the Capacity Enhancement Project for Coral Reef Monitoring (CEPCM) which was completed last fiscal year. For the new project, the Center and the University of Ryukyus have been awarded a competitive grant from Science and Technology Research Partnership for Sustainable Development (SATREPS). Supported by two Japanese government agencies, Japan Science and Technology Agency (JST) and the Japan International Cooperation Agency (JICA), SATREPS is a Japanese government program that promotes international joint research targeting global issues. Its core component is collaboration with other countries, stemming from the basic fact that global challenges cannot be met by a single country or region acting on its own. SATREPS works through three to five-year projects involving partnerships between researchers in Japan and researchers in another country, with a prominent focus on two primary outcomes: enhanced research capacity and scientific data that have potential for practical utilization.

CONTACTING THE CENTER'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of the Center's finances and to demonstrate the Center's accountability for the money it receives. The Management's Discussion and Analysis for the year ended September 30, 2011 is set forth in the report on the audit of the Center's financial statements which is dated February 25, 2013. That Discussion and Analysis explains the major factors impacting the 2011 financial statements. If you have questions about the 2011 or 2010 reports, or need additional information, please contact the Chief Executive Officer at the Palau International Coral Reef Center, P.O. Box 7086, Koror, Palau 96940, or e-mail ygolbuu@picrc.org or call 488-6950.

PALAU INTERNATIONAL CORAL REEF CENTER

Statements of Net Assets
September 30, 2012 and 2011

ASSETS	2012	2011
Current assets:		
Cash	$ 290,035	$ 272,300
Receivables:		
Grantor agencies	142,345	4,709
Other	70,861	97,615
	213,206	102,324
Less allowance for doubtful accounts	(46,556)	(56,949)
Total receivables, net	166,650	45,375
Inventories	62,642	84,248
Prepaid expense	5,276	3,699
Total current assets	524,603	405,622
Property, plant and equipment, net	2,044,268	2,178,043
	$ 2,568,871	$ 2,583,665

LIABILITIES AND NET ASSETS	2012	2011
Current liabilities:		
Current portion of note payable	$ 21,565	$ 24,067
Accounts payable	23,862	29,819
Deferred revenue	29,979	120,370
Accrued expenses	73,822	77,391
Total current liabilities	149,228	251,647
Note payable, net of current portion	66,184	90,251
Total liabilities	215,412	341,898
Net assets:		
Invested in capital assets	2,044,268	2,178,043
Unrestricted	309,191	63,724
Total net assets	2,353,459	2,241,767
	$ 2,568,871	$ 2,583,665

See accompanying notes to financial statements.

PALAU INTERNATIONAL CORAL REEF CENTER

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2012 and 2011

	2012	2011
Operating revenues:		
Grants	$ 270,040	$ 394,622
Facility user and admission fees	111,826	91,750
Contract service	103,179	20,899
Donations	66,656	58,629
Fund raising	33,011	41,571
Boat fee	27,097	13,169
Merchandise sales	23,884	22,585
Research facilities	12,705	5,609
Accomodation	8,822	5,641
Education program fee	6,455	2,321
Other	9,871	13,483
Total operating revenues	673,546	670,279
Recoveries	3,084	-
	676,630	670,279
Operating expenses:		
Salaries, wages and fringe benefits	405,233	453,083
Depreciation	167,337	157,263
Utilities	90,879	125,673
Professional services	60,135	55,363
Supplies and printing	47,719	65,803
Fuel	25,759	11,545
Travel	20,488	17,007
Insurance	15,714	14,167
Merchandise cost	12,536	14,744
Repairs and maintenance	10,937	6,121
Training	8,509	2,550
Communications	7,578	21,960
Anniversary	3,472	3,959
Dues and subscriptions	898	2,335
Entertainment	746	1,174
Postage and freight	142	262
Sales and marketing	15	30
Donations of capital assets to State governments	-	103,550
Other	43,619	34,607
Total operating expenses	921,716	1,091,196
Operating loss	(245,086)	(420,917)
Nonoperating revenues (expenses):		
Appropriations	356,708	387,000
Interest income	70	105
Interest expense	-	(2,365)
Total nonoperating revenues (expenses), net	356,778	384,740
Change in net assets	111,692	(36,177)
Net assets at beginning of year	2,241,767	2,277,944
Net assets at end of year	$ 2,353,459	$ 2,241,767

See accompanying notes to financial statements.

PALAU INTERNATIONAL CORAL REEF CENTER

Statements of Cash Flows
Years Ended September 30, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Cash received from customers	$ 484,993	$ 700,969
Cash payments to suppliers for goods and services	(381,672)	(397,798)
Cash payments to employees for services	(408,802)	(450,013)
Net cash used for operating activities	(305,481)	(146,842)
Cash flows from noncapital financing activities:		
Appropriations	356,708	387,000
Net cash provided by noncapital financing activities	356,708	387,000
Cash flows from capital and related financing activities:		
Property, plant and equipment acquisitions	(33,562)	(106,649)
Net cash used for capital and related financing activities	(33,562)	(106,649)
Cash flows from investing activities:		
Interest payments	-	(2,365)
Interest received	70	105
Net cash provided by (used for) investing activities	70	(2,260)
Net increase in cash	17,735	131,249
Cash at beginning of year	272,300	141,051
Cash at end of year	$ 290,035	$ 272,300
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	$ (245,086)	$ (420,917)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	167,337	157,263
Donations of capital assets to State governments	-	103,550
Recoveries	(3,084)	-
(Increase) decrease in assets:		
Receivables grantor agencies	(137,636)	10,729
Receivables, other	19,445	(12,690)
Inventories	21,606	17,965
Prepaid expense	(1,577)	6,333
Increase (decrease) in liabilities:		
Accounts payable	(5,957)	(134,816)
Deferred revenue	(90,391)	8,353
Notes payable	(26,569)	114,318
Accrued expenses	(3,569)	3,070
Net cash used for operating activities	$ (305,481)	$ (146,842)

See accompanying notes to financial statements.

(1) Organization

The Palau International Coral Reef Center (the Center), a component unit of the Republic of Palau (ROP), was created on November 20, 1998, under the provisions of Republic of Palau Public Law (RPPL) 5-17. The Law created a wholly owned government non-profit corporation managed by a Board of Directors appointed by the President of the Republic of Palau with the advice and consent of the Senate of the Olbiil Era Kelulau (ROP National Congress). The primary purpose of the Center is to carry out marine research and educate the public about the ecological, economic and cultural importance of coral reefs and their associated marine habitats.

The Center'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 the Center conform to accounting principles generally accepted in the United States of America, as applied to government entities, specifically proprietary funds. Governmental 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 Center has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

Basis of Accounting

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 the fund are included in the statement of net assets. Proprietary fund operating statements present increases and decreases in net total assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses recorded at the time liabilities are incurred.

Cash

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 Center or its agent in the Center'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 Center's name; or

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

(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, the Center's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Center does not have a deposit policy for custodial credit risk.

For purposes of the statements of net assets and cash flows, cash is defined as cash on hand and cash held in demand accounts. As of September 30, 2012 and 2011, cash was $290,035 and $272,300, respectively, and the corresponding bank balances were $291,449 and $276,762, respectively, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance and were FDIC insured. The Center does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC coverage are uncollateralized. There were no deposit levels in excess of FDIC coverage at September 30, 2012 and 2011.

In line with the Center's Strategic Plan to become self-sustaining, cash of $155,824 and $141,736 have been internally restricted as of September 30, 2012 and 2011, respectively. These restricted funds consist of solicited donations and a portion of operating revenues designated by the Board.

Inventories

Inventories of spare parts, merchandise and supplies are stated at the lower of cost (first-in, first out) or market.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is established through a provision charged to expense. Specific accounts are charged against the allowance when management believes that the collection of the balance is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing balances that may be uncollectible, based on evaluations of collectability and prior loss experience. Bad debts are written-off against the allowance based on the specific identification method.

Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is calculated using the straight-line method over the estimated useful lives of the respective assets. Current policy is to capitalize items in excess of $1,000.

Deferred Revenue

Deferred revenue is recognized when cash, receivables or other assets are recorded prior to their being earned. Deferred revenue results from funds received through various grants.

(2) Summary of Significant Accounting Policies, Continued

Retirement Plan

The Center 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 publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the Republic of Palau Civil Service Pension Trust Fund, P.O. Box 1767, Koror, Palau 96940.

The Fund provides retirement, security and other benefits to employees, and their spouses and dependents, of the Republic of Palau, Republic of Palau State Governments and Republic of Palau agencies, funds and public corporations, which are paid monthly and are two percent 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 25 years of vesting service, are entitled to retirement benefits. RPPL 2-26 is the authority under which benefit provisions are established. Member contribution rates are established by RPPL 2-26 at six percent (6%) of total payroll and matched dollar for dollar by the employer. The Center contributed $29,996, $23,411 and $24,711 to the Fund during the fiscal years 2012, 2011 and 2010, respectively, which were equal to the required contributions for each year.

Under the provisions of RPPL 2-26, the Fund's Board of Trustees adopted a Trust Fund Operation Plan 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 Center's payroll for the years ended September 30, 2012 and 2011 was covered by the Fund's pension plan. The Fund utilizes the actuarial cost method termed "agreement cost method" with actuarial assumptions used to compute the pension benefit obligation as follows: (a) a rate of return of 7.5% per year on the investment of present and future assets, (b) a 3% increase in employee salaries until retirement, and (c) members are assumed to retire at their normal retirement date.

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 effects 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.

The Fund's October 1, 2011 actuarial valuation determined the unfunded pension benefit obligation as follows:

Active participants	$ 74,716,975
Participants in pay status	62,987,516
Participants with vested deferred benefits	2,323,366
Total pension benefit obligation	140,027,857
Net assets available for benefits, at market value	36,128,666
Unfunded benefit obligation	$ 103,899,191

(2) Summary of Significant Accounting Policies, Continued

Retirement Plan, Continued

The actuarial valuation did not provide a breakdown of actuarial present value of vested and non-vested accumulated plan benefits by sponsor or net assets available for benefits by sponsor.

Compensated Absences

Vested or accumulated unpaid annual leave is accrued when earned and is included in the statement of net assets as an accrued expense. Annual leave accumulates at the rate of 6 hours biweekly, if less than 6 years of service, 7 hours biweekly, if between 7 and 14 years of service, and 8 hours biweekly if 15 years or more of service.

Taxes

RPPL 5-17 exempted the Center from all national and state non-payroll taxes or fees.

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.

Operating and Non-Operating Revenues and Expenses

Operating revenues and expenses include all direct and administrative revenues and expenses. Non-operating revenues and expenses result from investing and financing activities including operating grants.

Net Assets

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, has required the Center to establish net asset categories as follows:

- Invested in capital assets: capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- Restricted: net assets subject to externally imposed stipulations that can be fulfilled by actions of the Center pursuant to those stipulations or that expire by the passage of time. The Center does not have restricted net assets.
- Unrestricted: net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended September 30, 2012, the Center implemented the following pronouncements:

- GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which amends Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and addresses issues related to the frequency and timing of measurements for actuarial valuations first used to report funded status information in OPEB plan financial statements. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions* (an amendment of GASB Statement No. 53), which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Center.

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*, which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity*, and No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Center.

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*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the Center.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management has not yet determined the effect of implementation of this statement on the financial statements of the Center.

In April 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of the Center.

In April 2012, GASB issued 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 provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of the Center.

In June 2012, GASB issued Statement No. 67, *Financial Reporting for Pension Plans*, which revises existing guidance for the financial reports of most pension plans, and 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 67 are effective for financial statements for periods beginning after June 15, 2013. The provisions in Statement 68 are effective for fiscal years beginning after June 15, 2014. Management has not yet determined the effect of implementation of these statements on the financial statements of the Center.

(3) Due From Grantor Agencies

The Center is a direct recipient of a contract award received from the Australian Institute of Marine Science, the David and Lucile Packard Foundation, the United Nations Educational, Scientific, and Cultural Organization, Micronesia Conservation Trust, the University of New Hampshire, the University of South Pacific and the University of Hawaii. Excess grant disbursements over receipts are recognized as due from grantor agencies until such funds are received in accordance with grant terms and conditions.

Changes in the due from grantor agency account for the years ended September 30, 2012 and 2011 are as follows:

	2012	2011
Balance at beginning of year	$ 4,709	$ 15,438
Deductions - cash receipts from grantor agency	(52,173)	(415,412)
Additions - program outlays	280,200	396,330
Increase (decrease) in deferred revenue	(90,391)	8,353
Balance at end of year	$ 142,345	$ 4,709

(4) Inventories

Inventories as of September 30, 2012 and 2011, consist of the following:

	2012	2011
Spare parts	$ 41,700	$ 66,442
Merchandise	20,942	17,806
	$ 62,642	$ 84,248

(5) Property, Plant and Equipment

Property, plant and equipment as of September 30, 2012 and 2011, consist of the following:

	Estimated Useful Lives	Balance at October 1, 2011	Additions	Deletions	Balance at September 30, 2012
Buildings	10 - 30 years	$ 3,674,115	$ 20,800	$ -	$ 3,694,915
Mechanical, electrical, research, office, exhibit and marine equipment	2 - 15 years	2,140,207	3,150	(541,156)	1,602,201
Aquarium	7 years	1,588,537	3,397	-	1,591,934
Furniture and fixtures	5 years	177,590	-	(22,267)	155,323
Computers	5 years	91,952	-	(69,184)	22,768
Vehicles	3 years	126,752	6,215	(2,500)	130,467
		7,799,153	33,562	(635,107)	7,197,608
Less accumulated depreciation		(5,621,110)	(167,337)	635,107	(5,153,340)
		$ 2,178,043	$ (133,775)	$ -	$ 2,044,268

	Estimated Useful Lives	Balance at October 1, 2010	Additions	Deletions	Balance at September 30, 2011
Buildings	10 - 30 years	$ 3,663,840	$ 10,275	$ -	$ 3,674,115
Mechanical, electrical, research, office, exhibit and marine equipment	2 - 15 years	2,152,132	91,625	(103,550)	2,140,207
Aquarium	7 years	1,588,537	-	-	1,588,537
Furniture and fixtures	5 years	175,341	2,249	-	177,590
Computers	5 years	91,952	-	-	91,952
Vehicles	3 years	124,252	2,500	-	126,752
		7,796,054	106,649	(103,550)	7,799,153
Less accumulated depreciation		(5,463,847)	(157,263)	-	(5,621,110)
		$ 2,332,207	$ (50,614)	$ (103,550)	$ 2,178,043

(6) Note Payable

	2012	2011
During the year ended September 30, 2011, accounts payable to the Palau Public Utilities Corporation (PPUC) were converted to a note payable, non-interest bearing, due over sixty-three months beginning April 2011, with a fixed monthly payment of $2,006.	$ 87,749	$ 114,318
Less current installment	(21,565)	(24,067)
Long-term debt	$ 66,184	$ 90,251

(6) Note Payable, Continued

Total future repayments for the years ending September 30 are as follows:

Years ending	
2013	$ 21,565
2014	24,067
2015	24,067
2016	18,050
	$ 87,749

Changes in note payable for the years ended September 30, 2012 and 2011, are as follows:

	Balance October 1, 2011	Additions	Reductions	Balance September 30, 2012	Due Within One Year
PPUC	$ 114,318	$ -	$ (26,569)	$ 87,749	$ 21,565

	Balance October 1, 2010	Additions	Reductions	Balance September 30, 2011	Due Within One Year
PPUC	$ -	$ 126,349	$ (12,031)	$ 114,318	$ 24,067

(7) Republic of Palau

During the years ended September 30, 2012 and 2011, the Center received appropriations for operations of $356,708 through RPPL 8-40 and $387,000 through RPPLs 8-18 and 8-29, respectively.

The Center conducts its operations on land without charge in the State of Koror, through a land settlement agreement dated February 3, 1997 between ROP, the Palau Public Lands Authority, the Koror State Government and the Koror State Public Lands Authority. The land settlement agreement stipulates that ROP will retain the use of the land for as long as it is used for the Center and as long as no commercial or other profit-making ventures are conducted on the premises.

(8) Risk Management

The Center 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 Center has elected to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage during the past three years.