

Financial Statements and
Other Financial Information

Guam Telephone Authority
(A Public Corporation)

*Years ended September 30, 2002 and 2001
with Report of Independent Auditors*

Guam Telephone Authority
(A Public Corporation)

Financial Statements and
Other Financial Information

Years ended September 30, 2002 and 2001

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Report of Independent Auditors

The Board of Directors
Guam Telephone Authority

We have audited the accompanying statement of net assets of the Guam Telephone Authority (GTA), a component unit of the Government of Guam, (a public corporation) as of September 30, 2002, and the related statements of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of GTA's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of GTA for the year ended September 30, 2001 were audited by other auditors whose report, dated April 30, 2002, expressed an unqualified opinion on those statements. We have also audited the adjustments described in Note 8 that were applied to restate the 2001 financial statements. In our opinion, such adjustments are appropriate and have been properly applied.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Guam Telephone Authority as of September 30, 2002, and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, GTA adopted Governmental Accounting Standards Board Statement (GASB) No. 34, *Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments* as amended by GASB No. 37, *Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments: Omnibus* and GASB No. 38, *Certain Financial Statement Disclosures*. The accompanying 2001 financial statements have been restated to reflect the changes required by GASB Nos. 34, 37 and 38.

Management's discussion and analysis on pages 3 through 5 is not a required part of the basic financial statements but is supplementary information required by GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information included in Schedules 1 and 2 are presented for purposes of additional analysis and is not a required part of the basic financial statements. This information is the responsibility of GTA's management. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and in our opinion, is fairly stated in all material respects, in relation to the basic financial statements taken as a whole. The supplementary information for the year ended September 30, 2001 were audited by other auditors whose report, dated April 30, 2002, expressed an unqualified opinion on such information.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 26, 2003 on our consideration of GTA's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Ernst + Young LLP

December 26, 2003, except for note 9 as to which the date is April 14, 2004

Guam Telephone Authority
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Management's Discussion and Analysis

September 30, 2002 and 2001

The following Management Discussion and Analysis of Guam Telephone Authority (the Authority) activities and financial performance provide readers with an introduction and overview to the financial statements for the fiscal year ended September 30, 2002. This discussion has been prepared by management and should be read in conjunction with the financial statements and notes, which follow this section.

Guam Telephone Authority was created by Public Law 12-44, pursuant to which the assets and liabilities of the telephone division of the Public Utility Agency of Guam (PUAG) were transferred effective April 1, 1974.

The Authority serves as a local exchange carrier providing telephone network access and call-handling features. Federal Communications Commission (FCC) regulates interstate or long distance access, while Guam Public Utilities Commission (GPUC) regulates local access and services. The Authority also provides cellular, DSL, and other communication services to Guam.

Like all businesses, the Asian economic crisis, terrorist attacks on September 11, and Typhoon Chata'an affected operating revenues. The extensive damage caused by Typhoon Chata'an disrupted network access and delayed services. The Authority is continuously working diligently to improve customer service and response time.

Using the Financial Statements

The Authority's financial statements are prepared in accordance with accounting principles generally accepted in the United States (GAAP) as applied to governmental unit. The Governmental Accounting Standards Board (GASB) establishes and sets governmental accounting and financial reporting principles for state and local governments. The Authority implemented GASB 20 and elected not to apply FASB statements and Interpretations issued after November 30, 1989.

For the year ended September 30, 2002, the Authority adopted GASB Statement No. 34 "Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments" as amended by GASB Statement No. 37, "Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments: Omnibus" and GASB No. 38, "Certain Financial Statement Disclosures".

Guam Telephone Authority
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Management's Discussion and Analysis

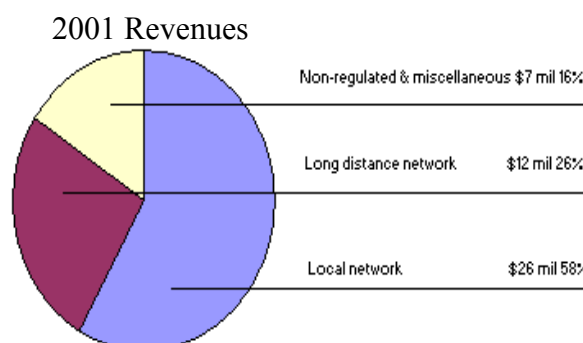
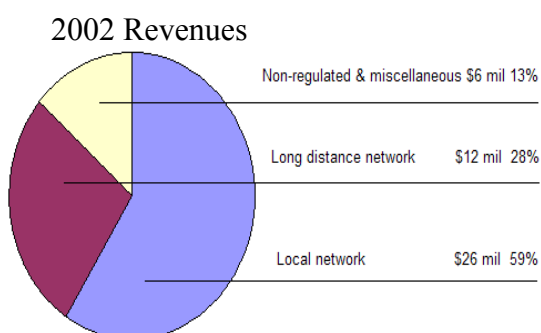
September 30, 2002 and 2001

Financial Data

	Year ended September 30, 2002	Year ended September 30, 2001	% Increase (Decrease) from 2001
Operating revenues	\$ 44,259,637	\$ 44,681,820	-0.9%
Operating expenses, excluding depreciation	25,839,612	31,479,079	-17.9%
Operating income before depreciation	18,420,025	13,202,741	39.5%
Depreciation and amortization	17,685,614	16,097,020	9.9%
Earnings (loss) from operations	734,411	(2,894,279)	125.4%
Non-operating income (expenses), net	(5,677,253)	6,456,613	-187.9%
Net (decrease) increase in net assets	\$ (4,942,842)	\$ 3,562,334	-238.8%

<u>Assets</u>	September 30, 2002	September 30, 2001	% Increase (Decrease) from 2001
Current assets	\$ 18,890,767	\$ 20,462,996	-7.7%
Investments	933,800	933,800	0.0%
Property, plant and equipment	148,031,750	159,046,747	-6.9%
Other noncurrent assets, net	198,418	240,937	-17.6%
Total assets	168,054,735	180,684,480	-7.0%

<u>Liabilities and net assets</u>			
Current installments of long-term debt	5,622,570	4,691,691	19.8%
Current liabilities	12,742,745	16,215,968	-21.4%
Long-term debt	104,927,093	110,032,328	-4.6%
Accrued annual leave, less current installments	825,088	864,412	-4.5%
Total liabilities	124,117,496	131,804,399	-5.8%
Net assets*	\$ 43,937,239	\$ 48,880,081	-10.1%



Guam Telephone Authority
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Management's Discussion and Analysis

September 30, 2002 and 2001

2002 compared to 2001

Overall, there were minor changes in the market segments. The increases in the federal government's demand for basic local wire line services offset the decline in residential lines. The decline in long distance network access charges were offset by the increase in special access services, digital subscriber lines (DSL), and universal service funds. The non-regulated revenues declined mainly due to lack of market presence in wireless and to policy expectation that the Authority will not compete against private sector firms.

Operating expenses decrease significantly by 17.9% or \$5,639,467 due to reduced spending in new product introduction (DSL and prepaid services) and privatization of the Authority. The increase in depreciation is due to changes in the estimated useful life of plant equipment as ordered by GPUC.

Cash flows

Year ended September 30,	2002	2001
Cash flow provided by (used in)		
Operating activities	\$ 15,655,714	\$ 10,356,145
Investing activities	626,357	719,126
Financing activities	(17,125,470)	(18,953,538)
Decrease in cash and cash equivalents	\$ (843,399)	\$ (7,878,267)

Net cash generated from operations are used to fund network expansion, modernization, and repayment of debt. While our current liabilities are usually close to or exceed current assets, we plan to meet our ongoing operational cost and capital improvements primarily from our operations.

Privatization

Guam Telephone Authority is the last local exchange carrier to be held and operated as a governmental agency in the United States of America. As the technology on global communications is changing, it is imperative that the Agency be able to compete and change as well. As a result, P.L 26-70 was passed to privatize Guam Telephone Authority.

On February 4, 2004, P.L. 27-63 was passed to amend and reenact certain sections of P.L. 26-70 relating to the terms of the privatization. Bid opening will be held on June 7, 2004 and the sale is expected to close on April 30, 2005.

Guam Telephone Authority
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Statements of Net Assets

	September 30, <u>2002</u>	<u>2001</u> (Restated, Note 8)
Assets		
Current assets:		
Cash and cash equivalents (<i>Note 2</i>):		
General funds	\$ 4,661,149	\$ 5,382,418
Construction	<u>112,774</u>	<u>234,904</u>
Total cash and cash equivalents	4,773,923	5,617,322
Telecommunications accounts receivable, net (<i>Note 3</i>)	5,827,122	7,432,990
Materials and supplies, net	8,209,725	7,202,586
Prepayments	<u>79,997</u>	<u>210,098</u>
Total current assets	<u>18,890,767</u>	<u>20,462,996</u>
Rural Telephone Bank (RTB) stock	<u>933,800</u>	<u>933,800</u>
Property, plant and equipment (<i>Note 4</i>):		
Telecommunications plant in service	266,749,481	253,176,294
Telecommunications plant under construction	<u>8,895,822</u>	<u>16,123,590</u>
	275,645,303	269,299,884
Less accumulated depreciation	(127,613,553)	(110,253,137)
	<u>148,031,750</u>	<u>159,046,747</u>
Other noncurrent assets, net	<u>198,418</u>	<u>240,937</u>
Total assets	<u>\$168,054,735</u>	<u>\$180,684,480</u>

See accompanying notes.

Guam Telephone Authority
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Statements of Net Assets, continued

	September 30, <u>2002</u>	<u>2001</u> (Restated, Note 8)
Liabilities and net assets:		
Current liabilities:		
Current installments of long-term debt <i>(Note 5)</i>	\$ 5,622,570	\$ 4,691,691
Accounts payable	5,754,764	7,680,091
Customers' deposits and advance billings	3,926,557	3,719,161
Accrued payroll and employee benefits	1,196,436	1,061,848
Accrued interest	1,246,806	1,223,694
Other current liabilities	<u>618,182</u>	<u>2,531,174</u>
Total current liabilities	<u>18,365,315</u>	<u>20,907,659</u>
Long-term debt, less current installments <i>(Note 5)</i> :		
Rural Utilities Service mortgage notes	71,598,884	75,028,568
Federal Financing Bank mortgage notes	17,531,861	18,537,405
Rural Telephone Bank mortgage notes	<u>15,796,348</u>	<u>16,466,355</u>
	<u>104,927,093</u>	<u>110,032,328</u>
Accrued annual leave, less current installments	<u>825,088</u>	<u>864,412</u>
Total liabilities	<u>124,117,496</u>	<u>131,804,399</u>
Net assets:		
Invested in capital assets	36,235,281	43,099,034
Unrestricted	<u>7,701,958</u>	<u>5,781,047</u>
Total net assets	<u>43,937,239</u>	<u>48,880,081</u>
Commitments and contingencies <i>(Notes 7 and 9)</i>		
Total liabilities and net assets	<u>\$168,054,735</u>	<u>\$180,684,480</u>

See accompanying notes.

Guam Telephone Authority
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Statements of Revenues, Expenses and Changes in Net Assets

	Year ended September 30,	
	<u>2002</u>	<u>2001</u> (Restated, Note 8)
Operating revenues (<i>Note 5</i>):		
Basic local network services	\$26,360,935	\$26,220,839
Long distance net work service	12,375,714	11,847,879
Non-regulated	5,287,175	6,275,191
Miscellaneous	783,875	836,480
Less uncollectible revenues	(<u>548,062</u>)	(<u>498,569</u>)
Total operating revenues	<u>44,259,637</u>	<u>44,681,820</u>
Operating expenses (<i>Note 7</i>):		
Depreciation	17,685,614	16,097,020
Plant specific operations	11,787,356	12,944,164
Corporate operations	8,057,977	9,560,927
Customer operations	3,665,044	6,115,873
Plant non-specific operations	<u>2,329,235</u>	<u>2,858,115</u>
Total operating expenses	<u>43,525,226</u>	<u>47,576,099</u>
Earnings (loss) from operations	<u>734,411</u>	(<u>2,894,279</u>)
Other (expense) revenues:		
Interest expense on long-term debt	(6,303,609)	(6,491,871)
Other income, net (<i>Note 5</i>)	626,356	1,165,875
Unfunded retirement liability transfer (<i>Note 6</i>)	<u>---</u>	<u>11,782,609</u>
Total other (expense) revenues	(<u>5,677,253</u>)	<u>6,456,613</u>
(Decrease) increase in net assets	(4,942,842)	3,562,334
Net assets at beginning of year, as restated	<u>48,880,081</u>	<u>45,317,747</u>
Net assets at end of year	<u>\$43,937,239</u>	<u>\$48,880,081</u>

See accompanying notes.

Guam Telephone Authority
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Statements of Cash Flows

	Year ended September 30,	
	<u>2002</u>	<u>2001</u> (Restated, Note 8)
Cash flows from operating activities		
Cash received from customers	\$46,072,901	\$45,271,892
Cash payments to suppliers and employees for goods and services	(30,417,187)	(34,915,747)
Net cash provided by operating activities	<u>15,655,714</u>	<u>10,356,145</u>
Cash flows from investing activity		
Interest and dividends on investments and bank accounts	<u>626,357</u>	<u>719,126</u>
Cash flows from capital and related financing activities		
Additions to telecommunications plant	(6,670,617)	(8,685,971)
Interest paid on long-term debt	(6,280,497)	(6,529,781)
Repayments of long-term debt	(4,174,356)	(3,917,428)
Proceeds from long-term debt	<u>---</u>	<u>179,642</u>
Net cash used for capital and related financing activities	<u>(17,125,470)</u>	<u>(18,953,538)</u>
Net decrease in cash and cash equivalents	(843,399)	(7,878,267)
Cash and cash equivalents at beginning of year	<u>5,617,322</u>	<u>13,495,589</u>
Cash and cash equivalents at end of year	<u>\$ 4,773,923</u>	<u>\$ 5,617,322</u>

See accompanying notes.

Guam Telephone Authority
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Statements of Cash Flows, continued

	Year ended September 30,	
	<u>2002</u>	<u>2001</u>
		(Restated, Note 8)
Reconciliation of earnings (loss) from operations to net cash provided by operating activities:		
Earnings (loss) from operations	\$ 734,411	\$(2,894,279)
Adjustments to reconcile earnings (loss) from operations to net cash provided by operating activities:		
Provision for uncollectible receivables	548,062	498,569
Depreciation	17,685,614	16,097,020
Changes in operating assets and liabilities:		
Decrease (increase) in telecommunications accounts receivable	1,057,806	(104,608)
Increase in materials and supplies	(1,007,139)	(3,545,683)
Decrease in prepayments	130,101	240,877
Decrease in other non-current assets	42,519	38,975
Decrease in accounts payable	(1,925,327)	(298,860)
Increase in customers' deposits and advance billings	207,396	196,111
Increase (decrease) in accrued payroll and employee benefits	134,588	(365,593)
Decrease in accrued annual leave	(39,324)	(89,784)
(Decrease) increase in other current liabilities	(<u>1,912,993</u>)	<u>583,400</u>
Net cash provided by operating activities	<u>\$15,655,714</u>	<u>\$10,356,145</u>

See accompanying notes.

Guam Telephone Authority
(A Public Corporation)

Notes to Financial Statements

September 30, 2002 and 2001

1. Organization and Summary of Significant Accounting Policies

General

Guam Telephone Authority (the “Authority”) was created by Public Law 12-44, pursuant to which the assets and liabilities of the telephone division of the Public Utility Agency of Guam (PUAG) were transferred to the Authority effective April 1, 1974. In 1991, a separate non-regulated “Cellular Operations” was created utilizing funds advanced by the Authority. As a Government of Guam agency, the Authority and its Cellular Operations are classified as a component unit of the Government of Guam for financial reporting purposes and, therefore, are not subject to taxes.

The Authority follows accounting policies prescribed or authorized by the Federal Communications Commission of the United States of America, as provided for in the indenture agreement with the United States Rural Utilities Service (RUS), the Rural Telephone Bank (RTB) and the Federal Financing Bank (FFB). The Authority is also subject to the regulations of the Public Utility Commission of Guam (PUC).

Because of the PUC rate-making process, certain differences arise in the application of accounting principles generally accepted in the United States between regulated and non-regulated businesses. Such differences mainly concern the time at which various items enter into the determination of net earnings in order to follow the principle of matching revenues and expenses.

On May 28, 1997, the Guam Legislature (the “Legislature”) adopted Public Law 24-36 to initiate the process for the privatization of the Authority and to require legislative approval of any plan to privatize the Authority. On December 21, 2001, the Legislature adopted Public Law 26-70, which resulted in the adoption of special rules and regulations for the privatization process and the public disclosure of information relative to such process.

Guam Telephone Authority
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Notes to Financial Statements

1. Organization and Summary of Significant Accounting Policies, continued

Basis of Accounting

The financial statements of the Authority have been prepared in conformity with accounting principles generally accepted in the United States (GAAP) as applied to government units. Government Accounting Standards Board (GASB) Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting", requires that propriety 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 Authority has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

For the year ended September 30, 2002, the Authority adopted GASB Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments (GASB 34)" as amended by GASB Statement No. 37 and applied those standards on a retroactive basis. GASB Statement No. 34 establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into the following four net asset categories:

- Invested in capital assets, net of related debt - represent capital assets, net of accumulated depreciation and net of the outstanding balances of any debt attributable to the acquisition, construction or improvement of those assets.
- Restricted nonexpendable net assets - represent net assets subject to externally imposed stipulations that require the Authority to maintain them permanently.
- Restricted expendable net assets - represent net assets subject to externally imposed stipulations that can be fulfilled by actions of the Authority pursuant to those stipulations or that expire by the passage of time.
- Unrestricted net assets - represent net assets, which do not meet the definition of "restricted" or "invested in capital assets, net of related debt".

The Authority does not have restricted net assets at September 30, 2002 and 2001. At September 30, 2002 and 2001, total net assets includes \$13,557,529 in Contributions from the Government of Guam representing the net assets and liabilities transferred from PUAG in 1974.

Guam Telephone Authority
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Notes to Financial Statements

1. Organization and Summary of Significant Accounting Policies, continued

Basis of Accounting, continued

For the year ended September 30, 2002, the Authority also adopted GASB Statement No 38, which requires that certain disclosures be made in the notes to the financial statements concurrent with the implementation of Statement No. 34. While this statement did not affect amounts reported in the financial statements of the Authority, certain note disclosures have been added or amended.

Geographic Area of Customer Base

The Authority is the sole supplier of local telephone service within Guam. Overseas services are provided by Guam-based private telecommunications companies.

Cash and Cash Equivalents

For purpose of the statements of net assets and the statements of cash flows, cash and cash equivalents include cash on hand, cash in banks, cash in money market funds and time certificates of deposit with original maturity dates of ninety days or less.

Materials and Supplies

Materials and supplies are carried at the lower of cost (average pricing) or market net of a provision of \$1,284,166 and \$1,766,328 as of September 30, 2002 and 2001, respectively.

Rural Telephone Bank Stock

Rural Telephone Bank stock is issued based on the loan agreement between the Authority and RTB. The Authority's investment in RTB stock is carried at cost and consists of 933,800 shares of \$1 par value Class B stock.

Property, Plant and Equipment

Property, plant and equipment are stated at cost. Cost of plant includes an allocation of overhead, including administrative expenses. The Authority also capitalizes the cost of borrowed funds during periods of the construction of projects requiring more than one year to complete. The cost of plant retired or otherwise disposed of, net of sales proceeds plus removal cost, is charged to accumulated depreciation.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

Guam Telephone Authority
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Notes to Financial Statements

1. Organization and Summary of Significant Accounting Policies, continued

Vacation and Sick Leave

Employees are credited with vacation leave at rates of 104, 156 or 208 hours per fiscal year, depending upon their service time with the Authority. Accumulation of such vacation credits is limited to 480 hours at fiscal year end and is convertible to pay upon termination of employment. Sick leave does not vest and is not accrued.

Operating Revenues

Operating revenues consist primarily of subscriptions and other local charges and the Authority's share of overseas message tolls.

Accounting Estimates

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

Reclassifications

Certain balances in the 2001 financial statements have been reclassified to correspond to the 2002 financial statement presentation.

2. Cash and Cash Equivalents

At September 30, 2002 and 2001, the Authority has cash balances of \$4,773,923 and \$5,617,322, respectively, deposited in various checking and savings accounts. Of the total deposits, \$314,925 and \$372,639, respectively, is insured by Federal Depositary Insurance Corporation and \$3,290,660 and \$2,654,942, respectively, is deposited in trust accounts collateralized by U.S. Treasury bills and bonds. The remaining balances are not insured or collateralized.

The Authority has deposited \$85,952 and \$84,722 in money market funds, which are collateralized by open-ended U.S. Treasury Bills and U.S. Treasury Notes at September 30, 2002 and 2001, respectively. These investments are recorded at cost and earn interest at 4.87%.

Guam Telephone Authority
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Notes to Financial Statements

3. Telecommunications Accounts Receivable

Telecommunications accounts receivable at September 30, 2002 and 2001, are summarized as follows:

	<u>2002</u>	<u>2001</u>
Active	\$ 6,461,341	\$ 6,592,016
Inactive	<u>4,346,694</u>	<u>4,822,095</u>
	10,808,035	11,414,111
Interstate	1,625,618	2,173,236
Others	<u>1,701,170</u>	<u>1,841,329</u>
	14,134,823	15,428,676
Less allowance for doubtful accounts	<u>8,307,701</u>	<u>7,995,686</u>
	<u>\$ 5,827,122</u>	<u>\$ 7,432,990</u>

4. Property, Plant and Equipment

Property, plant and equipment as of September 30, 2002 and 2001 are summarized as follows:

	<u>Beginning Balance October 1, 2001</u>	<u>Transfers and Additions</u>	<u>Transfers and Deletions</u>	<u>Ending Balance September 30, 2002</u>
Poles, cables and wire	\$122,126,918	\$4,282,909	\$ ---	\$126,409,827
Central office equipment	76,636,826	5,392,450	---	82,029,276
Buildings	21,729,118	171,545	(74,237)	21,826,426
Customer premise equipment	14,332,826	538,157	(201,870)	14,669,113
Cellular radio facilities	5,148,672	3,255,607	---	8,404,279
Furniture and office equipment	7,329,815	303,694	(95,068)	7,538,441
Motor vehicles	3,184,196	---	---	3,184,196
Other equipment	<u>1,857,406</u>	<u>---</u>	<u>---</u>	<u>1,857,406</u>
	252,345,777	13,944,362	(371,175)	265,918,964
Less accumulated depreciation	<u>(110,253,137)</u>	<u>(17,685,614)</u>	<u>325,198</u>	<u>(127,613,553)</u>
	142,092,640	(3,741,252)	(45,977)	138,305,411
Plant under construction	16,123,590	9,539,737	(16,767,505)	8,895,822
Land	<u>830,517</u>	<u>---</u>	<u>---</u>	<u>830,517</u>
	<u>\$159,046,747</u>	<u>\$ 5,798,485</u>	<u>\$(16,813,482)</u>	<u>\$148,031,750</u>

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Notes to Financial Statements

4. Property, Plant and Equipment, continued

The provision for depreciation, as a percentage of the average balance of telephone plant in service, was 6.8% and 7.0% in 2002 and 2001, respectively. Individual plant depreciable rates for 2002 and 2001 are as follows:

Poles, cables and wire	4%-10%
Central office equipment	5%
Customer premise equipment	2%
Buildings	3%-10%
Furniture and office equipment	10%
Motor vehicles	20%
Cellular radio facilities	8%
Other equipment	20%

5. Long-Term Debt

Long-term debt at September 30, 2002 and 2001 consisted of the following:

	<u>2002</u>	<u>2001</u>
RUS, at 5% per annum, payable in semi-annual installments of:		
\$1,557,000, including interest, due May 2025	\$ 41,150,329	\$ 42,148,199
\$659,000, including interest, due October 2020	15,462,183	15,991,234
\$526,000, including interest, due May 2011	7,701,082	8,351,320
\$308,000, including interest, due April 2017	6,178,768	6,477,553
\$176,000, including interest, due April 2012	2,678,197	2,891,555
\$162,000, including interest, due May 2011	2,389,891	2,589,776
FFB, due December 2014, payable in quarterly installments of:		
\$155,000, including interest at 7.647%	4,918,430	5,154,136
\$114,000, including interest at 5.643%	4,013,549	4,235,889
\$58,200, including interest at 7.496%	1,931,322	2,024,905
\$60,600, including interest at 7.301%	1,873,139	1,965,317
\$26,900, including interest at 6.171%	920,109	969,185
\$27,700, including interest at 7.887%	864,319	905,017
\$22,100, including interest at 6.604%	738,704	776,896
\$19,400, including interest at 7.581%	615,754	645,406
\$15,400, including interest at 5.784%	537,070	566,524
\$15,300, including interest at 6.151%	523,218	551,167
\$14,400, including interest at 5.621%	506,256	534,344
\$13,000, including interest at 6.402%	438,739	461,755

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Notes to Financial Statements

5. Long-Term Debt, continued

	<u>2002</u>	<u>2001</u>
FFB, due December 2014, payable in quarterly installments of, continued:		
\$5,300, including interest at 6.214%	\$181,497	\$191,149
\$5,100, including interest at 7.111%	166,104	174,383
\$4,800, including interest at 6.490%	159,672	167,996
\$4,300, including interest at 7.399%	137,986	144,721
\$300, including interest at 5.865%	11,495	12,121
RTB, payable in semi-annual installments of:		
\$177,000, including interest at 9.5%, due October 2020	3,018,372	3,080,302
\$117,000, including interest at 6.04%, due May 2025	2,721,591	2,775,385
\$104,000, including interest at 6.05%, due May 2025	2,461,793	2,515,289
\$82,000, including interest at 6.05%, due May 2025	1,836,064	1,871,678
\$79,000, including interest at 6.05%, due May 2025	1,727,178	1,779,020
\$49,500, including interest at 6.26%, due May 2025	1,222,623	1,247,752
\$44,700, including interest at 5.56%, due May 2025	1,122,374	1,143,991
\$46,000, including interest at 5.98%, due May 2025	1,092,624	1,114,102
\$31,400, including interest at 5.93%, due May 2025	781,130	796,659
\$12,000, including interest at 6.05%, due May 2025	265,031	270,531
\$7,011, including interest at 5.33%, due July 2025	180,972	175,911
\$930, including interest at 5.96%, due July 2025	<u>22,098</u>	<u>22,851</u>
	110,549,663	114,724,019
Less current installments	<u>(5,622,570)</u>	<u>(4,691,691)</u>
	<u>\$104,927,093</u>	<u>\$110,032,328</u>

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Notes to Financial Statements

5. Long-Term Debt, continued

At September 30, 2002, future maturities of long-term debt principal and interest are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt Service</u>
2003	\$ 5,622,570	\$ 4,832,500	\$ 10,455,070
2004	4,697,287	5,757,783	10,455,070
2005	4,963,103	5,491,967	10,455,070
2006	5,244,497	5,210,573	10,455,070
2007	5,542,419	4,912,651	10,455,070
2008 through 2012	31,397,697	19,451,919	50,849,616
2013 through 2017	25,857,585	10,849,595	36,707,180
2018 through 2022	19,982,770	4,624,166	24,606,936
2023 through 2025	<u>7,241,735</u>	<u>378,156</u>	<u>7,619,891</u>
	<u>\$110,549,663</u>	<u>\$61,509,310</u>	<u>\$172,058,973</u>

Unadvanced loan balance as of September 30, 2002, is as follows:

<u>Federal grantor/ Program title/ Project designation</u>	<u>Authorized amount</u>	<u>Drawndown amount</u>	<u>Unadvanced amount</u>
Rural Telephone Bank Loan: Guam 501-E7, Tamuning	\$16,082,850	\$14,942,323	\$1,140,527

Public Law 21-116 set the Authority's debt limit at \$150,607,800.

Outstanding RUS, RTB and FFB bonds are special obligations of the Authority payable from and collateralized by the proceeds of the bonds, all revenues, and all funds established by the bond indenture. These bonds do not constitute a general indebtedness of the Authority or the Territory of Guam. Revenues are defined in the bond indenture as all revenues, income, rents and receipts derived from the ownership, leasing and operation of the telephone system (System), the proceeds of any insurance covering business interruption loss relating to the System, and interest or dividends received on any moneys or securities (other than the Development Fund) held pursuant to the indenture and paid to the Revenue Fund.

In accordance with the indenture, the Authority established the following trust accounts to be held and administered by the Trustee for the bondholders.

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Notes to Financial Statements

5. Long-Term Debt, continued

Development Fund - The proceeds of all bonds are to be deposited into the Development Fund. All costs of construction (including acquisitions) of all facilities are to be paid from this fund. Insurance proceeds from physical loss of or damage to any facilities of the System, and proceeds from contractors' performance bonds are to be deposited into this fund. Proceeds from sale or lease-sale of any facilities included in the System shall be maintained in this fund and used to finance future construction.

Revenue Fund – All revenues are to be deposited into the Revenue Fund. All costs relating to the system, in addition to the costs for the payment of which moneys from time to time shall have been deposited in the Development Fund and in the Debt Service Fund, are to be paid from the Revenue Fund. The Trustee shall transfer funds from the Revenue Fund to the Debt Service Fund on or before the twenty-fifth (25th) day of each calendar month, to the extent such amount is available in the Revenue Fund after paying the monthly operating expenses with respect to the System, an amount equal to one-twelfth (1/12) of the Twelve-Month Debt Service Requirement, as defined in the Indenture. Deficiencies in any month shall be transferred to the Debt Service Fund on the earliest date on which funds become available in the Revenue Fund.

Debt Service Fund – The Trustee, on behalf of the Authority, shall make all payments of principal and interest on the bonds from the Debt Service Fund.

Management of the Authority is of the opinion that it has complied with all significant bond covenants with the exception of meeting RUS tier requirements during the year ended September 30, 2002.

6. Employees' Retirement Plan

Employees of the Authority hired before October 1, 1995 are members of the Government of Guam Employees' Retirement System, a defined benefit, contributory pension plan. The plan is administered by the Government of Guam Retirement Fund, to which the Authority contributes based upon a fixed percentage of the payroll for those employees who are members of the Plan.

As a result of the most recent actuarial valuation performed as of September 30, 2001, it has been determined that for the year ended September 30, 2002, a minimum combined employer and employee contribution rate of 40.98% of covered payroll is required to appropriately fund the current cost, amortize prior service costs and provide for interest on the unfunded accrued liability. Statutory contribution rates for employees and employer contributions were 9.5% and 19.675%, respectively, for the year ended September 30, 2002.

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Notes to Financial Statements

6. Employees' Retirement Plan, continued

The defined benefit plan utilized the actuarial cost method termed "entry age normal" with an assumed rate of return of 7.5% and an assumed salary scale increase ranging from 4% per annum (for employees with over 21 years of service) to 8.5% per annum (for employees with less than 6 years of service). The most recent actuarial valuation performed as of September 30, 2001, 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.

On September 29, 1995, the Guam Legislature passed Public Law 23-43, which created the Defined Contribution Retirement System (DCRS). All employees of the Authority, hired after October 1, 1995, are members of the DCRS, a defined contribution, contributory pension plan. The Board of Trustees of the Government of Guam Retirement Fund is responsible for the administration of the DCRS. Investment management and plan administration services for the DCRS are performed by a private firm contracted by the Board of Trustees.

Contributions into the DCRS by members are based on an automatic deduction of 5% of the member's regular base pay. The contribution is periodically deposited into an individual annuity account within the DCRS. Employees are afforded the opportunity to select from different annuity accounts available under the DCRS.

Employer contributions into the DCRS are based on a statutory amount of 19.675% of the member's regular base pay. Of the amount contributed by the employer, only 5% of the member's regular base pay is deposited into the member's individual annuity account. The remaining 14.675% is contributed towards the unfunded liability of the defined benefit plan.

Members of the DCRS who have completed five years of government service have a vested balance of 100% of both member and employer contributions plus any earnings thereon.

The cost to the Authority for retirement contributions for the years ended September 30, 2002 and 2001 is as follows:

	<u>2002</u>	<u>2001</u>
Cash contribution	\$3,011,406	\$2,313,609
Reduction of accrued unfunded liability	<u>---</u>	(<u>336,085</u>)
	<u>\$3,011,406</u>	<u>\$1,977,524</u>

Guam Telephone Authority
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Notes to Financial Statements

6. Employees' Retirement Plan, continued

Public Law 26-70 states that the Authority has no further responsibility to record future unfunded retirement costs and its deferred liability to the Government of Guam was transferred to the Government of Guam primary account. The Authority recorded other income of \$11,782,609 during the year ended September 30, 2001, upon implementation of this law. The Authority's unfunded retirement costs are now recorded within the financial statements of the Government of Guam. As of September 30, 2001, the Government of Guam has accrued approximately \$11,782,609 for the Authority's cumulative unfunded retirement liability.

In 2002, the Government of Guam adopted the provisions of GASB No. 27, "Accounting for Pensions by State and Local Governmental Employees". The effect of this change, which was retroactively applied, restated the unfunded retirement liability in 2001 from \$203,295,336 to \$34,005,640.

As of September 30, 2002, the Government of Guam's unfunded retirement liability totaled \$31,983,283. However, the amount accrued by the Government of Guam for the Authority's share of the unfunded retirement liability is not readily determinable.

7. Commitments and Contingencies

Lease

Rent expense for operating leases totaled \$152,380 and \$165,691, respectively, for the years ended September 30, 2002 and 2001, respectively. These expenses are included as components of operating expenses in the accompanying statements of revenues, expenses and changes in net assets. Future obligations under such leases are not significant.

Medicare

The Government of Guam and its component units, including the Authority, began withholding and remitting funds to the U.S. Social Security System for the health insurance component of its salaries and wages effective October 1998. Prior to that date, the Government of Guam did not withhold or remit Medicare payments to the U.S. Social Security System. If the Government is found to be liable for Medicare payments on salaries and wages prior to October 1998, an indeterminate liability could result. It has been the practice of the Authority and all other component units of the Government of Guam that payment of this health insurance component is optional prior to October 1998. Therefore, no liability for any amount, which may ultimately arise from this matter has been recorded in the accompanying financial statements.

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Notes to Financial Statements

7. Commitments and Contingencies, continued

Insurance

The Authority has commercial insurance coverage for owners, landlords and tenants liability, fidelity and forgery, robbery/safe burglary, workmen's compensation, automobile and comprehensive liability. The Authority also has commercial property insurance coverage for 95% of the total net book value of fixed assets.

Typhoon Damages

On July 5, 2002, the island of Guam was struck by typhoon Chata'an. As a result, the Authority suffered damages totaling approximately \$2,711,000 to its telecommunications plant. The Authority's insurance coverage is expected to cover such losses, less a 2% deductible. Subsequent to year end the Authority received approximately \$475,000 in insurance proceeds from the typhoon Chata'an claims. However, the amount ultimately collectible is uncertain.

Debt Covenant

Article IV, Section 22 of the supplemental RUS Loan Agreement (see Note 5), sets out certain financial ratio requirements. During the years ended September 30, 2002 and 2001, the Authority was not in compliance with this requirement. The impact on the financial statements is not currently determinable.

8. Prior Period Adjustment

Net assets as of September 30, 2000 and 2001 have been restated to properly state RTB stock at cost. As of September 30, 2000, the Authority received \$4,713,936 in patronage refunds from RTB in the form of Class B RTB stock. During 2001, refunds received totaled \$1,449,473. The refunds were previously recorded by the Authority as an increase in RTB stock, other income and net assets. Although the stocks are backed by the full faith and credit of the US Government they are not publicly traded and there are no quoted market prices. As a result, they should be valued at cost.

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Notes to Financial Statements

8. Prior Period Adjustment, continued

The effect of the restatements resulted in a \$4,713,936 decrease in beginning net assets as of September 30, 2000, a \$1,449,473 decrease in other income for 2001, and a \$6,163,409 decrease in RTB stock and ending net assets as of September 30, 2001. The restatements in net assets are summarized as follows:

Net assets at September 30, 2000, as previously stated	\$50,031,683
Prior period adjustment to properly state RTB stock at cost	(<u>4,713,936</u>)
Net assets, as restated	<u>\$45,317,747</u>
Net assets at September 30, 2001, as previously stated	\$55,043,490
Prior period adjustment	(<u>6,163,409</u>)
Net assets, as restated	<u>\$48,880,081</u>

9. Subsequent Events

On December 8, 2002, super-typhoon Pongsona struck Guam with destructive winds of approximately 180 miles per hour. As a result, the Authority suffered damages totaling approximately \$4,890,000 to its telecommunications plant. The Authority expects much of the damage to be covered by insurance. However, the total insurance settlement and amount ultimately collectible are not presently determinable.

On December 17, 2003, the President signed into law the Compact of Free Association Amendments Act of 2003 or House Joint Resolution 63, Public Law 108-188. A new provision in the law authorizes the President, at the request of the Governor of Guam, to release, reduce, or waive, in whole or in part, any amounts owed by the Government of Guam to the United States Government, such as a \$105 million debt owed by the Guam Telephone Authority to the U.S. Department of Agriculture, as an offset for past un-reimbursed Compact-Impact costs. On April 14, 2004, the Government of Guam issued a report to the U.S. Department of Interior identifying \$269 million in un-reimbursed Compact-Impact costs. The Governor may now request the President to exercise his authority by notifying Congress by December 31, 2004, of his intent to exercise his authority. The total debt by the Authority, which may ultimately be offset, is not currently determinable.

On February 4, 2004, the Legislature adopted Public Law 27-63 to amend certain sections of Public Law 26-70. The amendments were made to account for current economic and market concerns and permits the Authority to proceed with the privatization process. Bid openings for the privatization of the Authority will be held on June 7, 2004 and the sale is expected to close on April 30, 2005.

Other Financial Information

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Schedule 1

Schedules of Revenues
Years ended September 30, 2002 and 2001

<u>2002</u>	Basic Local Revenue	Long Distance	Non - Regulated Revenues	Total
Residential	\$ 8,625,703	\$ 2,617,070	\$ 1,383,106	\$ 12,625,879
Business	12,765,841	8,642,648	2,560,540	23,969,029
Government	3,922,021	990,584	332,054	5,244,659
Federal Government	1,047,370	125,412	173,362	1,346,144
Other Non-Regulated	---	---	838,113	838,113
	<u>\$ 26,360,935</u>	<u>\$ 12,375,714</u>	<u>\$ 5,287,175</u>	<u>\$ 44,023,824</u>
<u>2001</u>	Basic Local Revenue	Long Distance	Non - Regulated Revenues	Total
Residential	\$ 8,859,934	\$ 1,869,466	\$ 1,549,217	\$ 12,278,617
Business	12,532,444	9,288,719	3,237,816	25,058,979
Government	3,928,826	604,796	323,882	4,857,504
Federal Government	899,635	84,898	137,520	1,122,053
Other Non-Regulated	---	---	1,026,756	1,026,756
	<u>\$ 26,220,839</u>	<u>\$ 11,847,879</u>	<u>\$ 6,275,191</u>	<u>\$ 44,343,909</u>

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Schedule 2

Schedules of Expenses
Years ended September 30, 2002 and 2001

	<u>2002</u>	<u>2001</u>
Plant specific operations:		
Salaries, wages and benefits	\$ 6,879,999	\$ 6,720,413
Materials and supplies	1,094,922	1,422,000
Miscellaneous	651,526	627,660
Repairs and maintenance	560,921	468,413
Utilities	545,289	545,154
Telephone expense	481,552	880,425
800 Query dips	448,905	500,238
Leased facilities	339,175	713,600
Outsourcing	192,208	224,903
Overtime	166,490	354,764
Fuel and oil	164,622	163,892
Auto parts and supplies	120,357	114,763
Custodial service	119,127	119,992
Tools and equipment	<u>22,263</u>	<u>87,947</u>
	<u>11,787,356</u>	<u>12,944,164</u>
Corporate operations:		
Consulting - privatization	3,083,313	4,143,145
Salaries, wages and benefits	2,560,499	2,354,301
Insurance	835,537	716,939
Miscellaneous	705,671	872,714
Computer hardware maintenance	291,909	216,113
Professional fees	210,921	333,570
Overtime	122,362	24,411
Legal fees - off and on island attorneys	81,764	263,885
Training	60,825	320,634
Material and supplies	44,262	50,867
Consulting - other	35,479	21,765
Telephone expense	<u>25,435</u>	<u>242,583</u>
	<u>8,057,977</u>	<u>9,560,927</u>
Customer operations:		
Salaries, wages and benefits	3,141,775	3,222,915
Postage and advertising	375,864	187,624
Telephone services	61,612	402,916
Material and supplies	30,072	41,083
Product implementation	23,124	1,662,888
Price and costs studies	15,592	523,206
Overtime	15,434	74,946
Miscellaneous	<u>1,571</u>	<u>295</u>
	<u>3,665,044</u>	<u>6,115,873</u>
Plant non-specific operations:		
Salaries, wages and benefits	2,238,720	1,694,377
Utilities	476,439	662,503
Consulting	289,726	(3,131)
Overtime	21,127	8,116
Material and supplies	(58,032)	271,240
Miscellaneous	<u>(638,745)</u>	<u>225,010</u>
	<u>2,329,235</u>	<u>2,858,115</u>
Total	<u>\$ 25,839,612</u>	<u>\$ 31,479,079</u>
Total employees at end of year	390	414