

Financial Statements and  
Other Financial Information

**Guam Telephone Authority**  
(A Public Corporation)

*Years ended September 30, 2003 and 2002  
with Report of Independent Auditors*

Guam Telephone Authority  
(A Public Corporation)

Financial Statements and  
Other Financial Information

Years ended September 30, 2003 and 2002

**Contents**

Report of Independent Auditors .....	1
Management's Discussion and Analysis .....	3
Audited Financial Statements	
Statements of Net Assets .....	6
Statements of Revenues, Expenses and Changes in Net Assets .....	8
Statements of Cash Flows .....	9
Notes to Financial Statements.....	11
Other Financial Information	
Schedules of Revenues .....	25
Schedules of Expenses .....	26

## Report of Independent Auditors

The Board of Directors  
Guam Telephone Authority

We have audited the accompanying statements of net assets of the Guam Telephone Authority (GTA, a public corporation), a component unit of the Government of Guam, as of September 30, 2003 and 2002, 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 GTA'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 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 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 Guam Telephone Authority as of September 30, 2003 and 2002, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.

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 the Government Auditing Standards Board (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 audits were 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 is 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 audits 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 19, 2004 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*

May 19, 2004, except for note 8 as to which the date is June 7, 2004

Guam Telephone Authority  
(A Public Corporation)

Management's Discussion and Analysis

September 30, 2003 and 2002

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, 2003. 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.

On July and December 2002, Guam was hit with super typhoons with winds in excess of 150 mph. The extensive damage caused by Typhoon Chata'an and Pongsona 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, 2003 and 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  
(A Public Corporation)

Management's Discussion and Analysis, continued

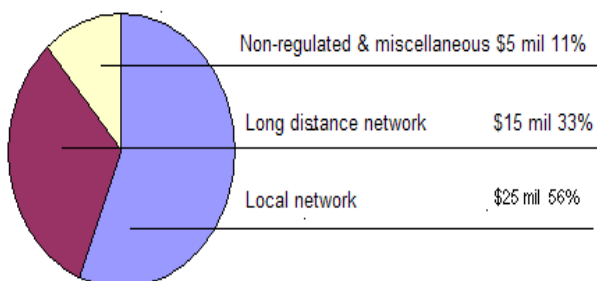
September 30, 2003 and 2002

**Financial Data**

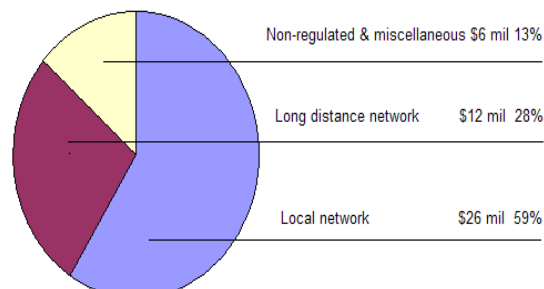
	Year ended September 30, 2003	Year ended September 30, 2002	% Increase (Decrease) from 2002
Operating revenues	\$ 42,855,794	\$ 44,259,637	-3.2%
Operating expenses, excluding depreciation	22,261,510	25,839,612	-13.8%
Operating income before depreciation	20,594,284	18,420,025	11.8%
Depreciation and amortization	18,041,328	17,685,614	2.0%
Earnings from operations	2,552,956	734,411	247.6%
Non-operating income (expenses), net	(12,251,922)	(5,677,253)	115.8%
Net decrease in net assets	\$ (9,698,966)	\$ (4,942,842)	96.2%

<u>Assets</u>	September 30, 2003	September 30, 2002	% Increase (Decrease) from 2002
Current assets	\$ 17,964,388	\$ 18,890,767	-4.9%
Investments	933,800	933,800	0.0%
Property, plant and equipment	131,556,457	148,031,750	-11.1%
Other noncurrent assets, net	155,900	198,418	-21.4%
Total assets	150,610,545	168,054,735	-10.4%
<u>Liabilities and net assets</u>			
Current installments of long-term debt	5,825,461	5,622,570	3.6%
Current liabilities	9,538,546	12,742,745	-25.1%
Long-term debt	100,342,811	104,927,093	-4.4%
Accrued annual leave, less current	665,454	825,088	-19.3%
Total liabilities	116,372,272	124,117,496	-6.2%
Net assets	\$ 34,238,273	\$ 43,937,239	-22.1%

**2003 Revenues**



**2002 Revenues**





Guam Telephone Authority  
(A Public Corporation)

Management's Discussion and Analysis, continued

September 30, 2003 and 2002

**2003 compared to 2002**

The local network and non-regulated services dropped by 4.7% and 18%, respectively. The long distance network access charges increased by 19% due to increase in special access services, digital subscriber lines (DSL), and universal service funds. The non-regulated revenues declined mainly due to the Authority's lack of market presence in wireless due to policy expectation that the Authority will not compete against private sector firms.

Operating expense decreased by 14% or \$5.6 million due to reduced spending in payroll 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.

The Authority suffered damages totaling approximately \$2.7 million from Chata'an and \$4.9 million from Pongsona. The Authority expects much of the damages to be covered by the insurance.

**Cash flows**

Year ended September 30,

	<u>2003</u>	<u>2002</u>
<b>Cash flow provided by (used in)</b>		
Operating activities	\$ 20,930,874	\$ 15,613,195
Investing activities	185,142	626,357
Financing activities	<u>(16,105,693)</u>	<u>(17,082,951)</u>
<b>Decrease in cash and cash equivalents</b>	<u>\$ 5,010,323</u>	<u>\$ (843,399)</u>

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 5, 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 openings for the privatization of the Authority were held on June 7, 2004. Bid evaluations are currently on going and management expects to have the negotiated documents by December 31, 2004, which will be submitted to the Governor of Guam and the Guam Legislature for approval. Thereafter the documents will be provided to the FCC for approval.

Guam Telephone Authority  
(A Public Corporation)

Statements of Net Assets

	September 30,	
	<u>2003</u>	<u>2002</u>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents ( <i>Note 2</i> ):		
General funds	\$ 8,601,419	\$ 4,661,149
Construction	<u>1,182,827</u>	<u>112,774</u>
Total cash and cash equivalents	9,784,246	4,773,923
Telecommunications accounts receivable, net ( <i>Note 3</i> )	2,740,033	5,827,122
Materials and supplies, net	5,321,733	8,209,725
Prepayments	<u>118,376</u>	<u>79,997</u>
Total current assets	<u>17,964,388</u>	<u>18,890,767</u>
Rural Telephone Bank stock	<u>933,800</u>	<u>933,800</u>
Property, plant and equipment ( <i>Note 4</i> ):		
Telecommunications plant in service	271,029,946	266,749,481
Telecommunications plant under construction	<u>5,450,213</u>	<u>8,895,822</u>
	276,480,159	275,645,303
Less accumulated depreciation	(144,923,702)	(127,613,553)
	131,556,457	148,031,750
Other noncurrent assets, net	<u>155,900</u>	<u>198,418</u>
Total assets	<u>\$150,610,545</u>	<u>\$168,054,735</u>

See accompanying notes.



Guam Telephone Authority  
(A Public Corporation)

Statements of Net Assets, continued

	September 30, <u>2003</u>	<u>2002</u>
<b>Liabilities and net assets:</b>		
Current liabilities:		
Current installments of long-term debt <i>(Note 5)</i>	\$ 5,825,461	\$ 5,622,570
Accounts payable	2,728,997	5,754,764
Customers' deposits and advance billings	4,087,148	3,926,557
Accrued payroll and employee benefits	1,004,364	1,196,436
Accrued interest	1,203,854	1,246,806
Other current liabilities	<u>514,183</u>	<u>618,182</u>
Total current liabilities	<u>15,364,007</u>	<u>18,365,315</u>
Long-term debt, less current installments <i>(Note 5)</i> :		
Rural Utilities Service mortgage notes	68,483,498	71,598,884
Federal Financing Bank mortgage notes	16,456,186	17,531,861
Rural Telephone Bank mortgage notes	<u>15,403,127</u>	<u>15,796,348</u>
	<u>100,342,811</u>	<u>104,927,093</u>
Accrued annual leave, less current installments	<u>665,454</u>	<u>825,088</u>
Total liabilities	<u>116,372,272</u>	<u>124,117,496</u>
Net assets:		
Invested in capital assets	24,184,331	36,235,281
Unrestricted	<u>10,053,942</u>	<u>7,701,958</u>
Total net assets	<u>34,238,273</u>	<u>43,937,239</u>
Commitments and contingencies <i>(Notes 7 and 8)</i>		
Total liabilities and net assets	<u>\$150,610,545</u>	<u>\$168,054,735</u>

See accompanying notes.

Guam Telephone Authority  
(A Public Corporation)

Statements of Revenues, Expenses and Changes in Net Assets

	Year ended September 30,	
	<u>2003</u>	<u>2002</u>
Operating revenues ( <i>Note 5</i> ):		
Basic local network services	\$25,132,933	\$26,360,935
Long distance network services	14,736,784	12,375,714
Non-regulated	4,336,069	5,287,175
Miscellaneous	761,067	783,875
Less uncollectible revenues	( <u>2,111,059</u> )	( <u>548,062</u> )
Total operating revenues	<u>42,855,794</u>	<u>44,259,637</u>
Operating expenses ( <i>Note 7</i> ):		
Depreciation and amortization ( <i>Note 4</i> )	18,041,328	17,685,614
Plant specific operations	10,323,622	11,787,356
Corporate operations	5,173,586	8,057,977
Plant non-specific operations	3,416,688	2,329,235
Customer operations	<u>3,347,614</u>	<u>3,665,044</u>
Total operating expenses	<u>40,302,838</u>	<u>43,525,226</u>
Earnings from operations	<u>2,552,956</u>	<u>734,411</u>
Other (expense) revenues:		
Interest expense on long-term debt	( 6,030,909 )	( 6,303,609 )
Disaster casualty loss ( <i>Note 7</i> )	( 3,999,805 )	---
Materials and supplies valuation loss	( 2,406,350 )	---
Other income, net	<u>185,142</u>	<u>626,356</u>
Total other (expense) revenues	( <u>12,251,922</u> )	( <u>5,677,253</u> )
Decrease in net assets	( <u>9,698,966</u> )	( <u>4,942,842</u> )
Net assets at beginning of year	<u>43,937,239</u>	<u>48,880,081</u>
Net assets at end of year	<u>\$34,238,273</u>	<u>\$43,937,239</u>

*See accompanying notes.*

Guam Telephone Authority  
(A Public Corporation)

Statements of Cash Flows

	Year ended September 30,	
	<u>2003</u>	<u>2002</u>
<b>Cash flows from operating activities</b>		
Cash received from customers	\$46,103,474	\$46,072,901
Cash payments to suppliers and employees for goods and services	( <u>25,172,600</u> )	( <u>30,459,706</u> )
Net cash provided by operating activities	<u>20,930,874</u>	<u>15,613,195</u>
<b>Cash flows from investing activity</b>		
Interest and dividends on investments and bank accounts	<u>185,142</u>	<u>626,357</u>
<b>Cash flows from capital and related financing activities</b>		
Additions to telecommunications plant	( 5,650,441)	( 6,628,098)
Interest paid on long-term debt	( 6,073,861)	( 6,280,497)
Repayments of long-term debt	( <u>4,381,391</u> )	( <u>4,174,356</u> )
Net cash used for capital and related financing activities	( <u>16,105,693</u> )	( <u>17,082,951</u> )
Net increase (decrease) in cash and cash equivalents	5,010,323	( 843,399)
Cash and cash equivalents at beginning of year	<u>4,773,923</u>	<u>5,617,322</u>
Cash and cash equivalents at end of year	<u>\$ 9,784,246</u>	<u>\$ 4,773,923</u>

*See accompanying notes.*

Guam Telephone Authority  
(A Public Corporation)

Statements of Cash Flows, continued

	Year ended September 30,	
	<u>2003</u>	<u>2002</u>
<b>Reconciliation of earnings from operations to net cash provided by operating activities:</b>		
Earnings from operations	\$ 2,552,956	\$ 734,411
Adjustments to reconcile earnings from operations to net cash provided by operating activities:		
Depreciation and amortization	18,041,328	17,685,614
Provision for uncollectible receivables	2,111,059	548,062
Loss from retirement of telecommunication equipment	127,119	---
Write-off of telecommunication accounts receivables	( 2,827,234)	---
Changes in operating assets and liabilities:		
Decrease in telecommunications accounts receivable	3,803,264	1,057,806
Decrease (increase) in materials and supplies	481,642	( 1,007,139)
(Increase) decrease in prepayments	( 38,379)	130,101
Decrease in accounts payable	( 3,025,767)	( 1,925,327)
Increase in customers' deposits and advance billings	160,591	207,396
(Decrease) increase in accrued payroll and employee benefits	( 192,072)	134,588
Decrease in accrued annual leave	( 159,634)	( 39,324)
Decrease in other current liabilities	( <u>103,999</u> )	( <u>1,912,993</u> )
Net cash provided by operating activities	<u>\$20,930,874</u>	<u>\$15,613,195</u>

See accompanying notes.

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements

September 30, 2003 and 2002

**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 (FCC) 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.

**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.

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**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 Activities 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.

Effective 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, 2003 and 2002. At September 30, 2003 and 2002, 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  
(A Public Corporation)

Notes to Financial Statements, continued

**1. Organization and Summary of Significant Accounting Policies, continued**

**Basis of Accounting, continued**

Effective year ended September 30, 2002, the Authority also adopted GASB Statement No 38, "Certain Financial Note Disclosures" 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.

**Reclassification**

Certain reclassifications have been made to the 2002 financial statements for comparative purposes. Such reclassifications had no effect on previously reported decrease in net assets.

**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 allowance for inventory obsolescence of \$1,204,965 and \$1,284,166 as of September 30, 2003 and 2002, 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  
(A Public Corporation)

Notes to Financial Statements, continued

**1. Organization and Summary of Significant Accounting Policies, continued**

**Licensing Rights**

The FCC granted the Authority licensing rights to operate its Personal Communication Service (PCS) for Channel Blocks E on April 28, 1997. Licensing rights incurred to acquire the PCS license from the FCC are amortized after the Authority's wireless communication service became operational. The license covers an initial period of 10 years, expiring on April 28, 2007, and renewable every five years thereafter for a nominal fee. Licensing rights is reflected as other noncurrent assets, net in the accompanying statements of net assets. For each of the years ended September 30, 2003 and 2002, amortization of licensing rights amounted to \$42,519 and is shown as a component of depreciation and amortization in the accompanying statements of revenues, expenses and changes in net assets.

**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. On February 28, 2003, the Guam Legislature passed Public Law 27-5. Chapter 4 Section 4 of the law revised the maximum accumulation of annual leave to 320 hours. Prior to this public law, accumulation of such vacation credits is limited to 480 hours at fiscal year end.

Also, under Public Law 27-5, employees who have accumulated annual leave in excess of 320 hours as of February 28, 2003 shall have up to and including September 30, 2004, to use the excess amount of leave, or that portion permitted to be credited to sick leave shall be so credited and the remaining excess leave, if any, shall be lost.

**Operating Revenues**

*Basic Local Network Services* – consist mainly of the monthly recurring rates for billed local services; one time installation fees associated with the establishment of customer service and other one time non recurring charges.

Monthly fees on services are recognized as revenue on an accrual basis, based on contracted rates, as the service is provided to customers. Installation charges and other one-time fees associated with the establishment of customer service are recognized when the related installation of equipment is complete and the telephone service has been activated.

*Long Distance Network Services* – consist mainly of revenues generated for incoming and outgoing switch access for interstate and international traffic. Also included are end-user revenues from Subscriber Line Charges and the Federal Universal Service Charge that are mandated by the FCC and special access revenues.

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**1. Organization and Summary of Significant Accounting Policies, continued**

**Operating Revenues, continued**

Long distance network services are recognized based upon minutes of traffic processed and contracted fees as incurred.

*Non-regulated* – consist of revenues from wireless service derived from the sale of cellular prepaid cards to resellers; monthly service fees from postpaid subscribers, including (a) charges for calls in excess of allocated free minutes and (b) toll charges for international long distance calls; and other landline non-regulated revenues such as (a) pay phone booth revenues, (b) inside wire maintenance, (c) miscellaneous revenues for billing on damages to the Authority's cable and wire facilities by contractors and other private parties.

Revenues from the sale of prepaid cards comprise of proceeds from sales of prepaid cards to resellers. Revenue from sales of prepaid cards are recorded immediately upon sale to resellers.

Postpaid service revenue is recognized based upon minutes of traffic processed and contracted fees for services provided. Charges for value added services are recognized as they are used by the subscriber.

Revenue from pay phone booths are based on amounts collected from various paystations.

**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.

**2. Cash and Cash Equivalents**

At September 30, 2003 and 2002, the Authority has cash balances of \$9,784,246 and \$4,773,923, respectively, deposited in various checking and savings accounts. Of the total deposits, \$343,204 and \$314,925, respectively, is insured by Federal Depository Insurance Corporation and \$5,436,693 and \$3,290,660, 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 \$77,371 and \$85,952 in money market funds, which are collateralized by open-ended U.S. Treasury Bills and U.S. Treasury Notes at September 30, 2003 and 2002, respectively. These investments are recorded at cost and earn interest at 5.0% and 4.87% in 2003 and 2002, respectively.

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**3. Telecommunications Accounts Receivable**

Telecommunications accounts receivable at September 30, 2003 and 2002, are summarized as follows:

	<u>2003</u>	<u>2002</u>
Active	\$ 3,242,570	\$ 6,461,341
Inactive	<u>3,799,963</u>	<u>4,346,694</u>
	7,042,533	10,808,035
Interstate	1,157,103	1,625,618
Others	<u>2,132,192</u>	<u>1,701,170</u>
	10,331,828	14,134,823
Less allowance for doubtful accounts	<u>7,591,795</u>	<u>8,307,701</u>
	<u>\$ 2,740,033</u>	<u>\$ 5,827,122</u>

**4. Property, Plant and Equipment**

Property, plant and equipment as of September 30, 2003 and 2002 are summarized as follows:

	<u>Beginning Balance October 1, 2002</u>	<u>Transfers and Additions</u>	<u>Transfers and Deletions</u>	<u>Ending Balance September 30, 2003</u>
Poles, cables and wire	\$126,409,827	\$ 2,556,828	\$( 2,027)	\$128,964,628
Central office equipment	82,029,276	1,129,887	---	83,159,163
Buildings	21,826,426	216,836	( 726,991)	21,316,271
Customer premise equipment	14,669,113	168,712	( 608,292)	14,229,533
Cellular radio facilities	8,404,279	1,427,292	---	9,831,571
Furniture and office equipment	7,538,441	719,609	( 450,279)	7,807,771
Motor vehicles	3,184,196	---	( 275,309)	2,908,887
Other equipment	<u>1,857,406</u>	<u>124,199</u>	<u>---</u>	<u>1,981,605</u>
	265,918,964	6,343,363	( 2,062,898)	270,199,429
Less accumulated depreciation	<u>(127,613,553)</u>	<u>(17,998,809)</u>	<u>688,660</u>	<u>(144,923,702)</u>
	138,305,411	(11,655,446)	( 1,374,238)	125,275,727
Plant under construction	8,895,822	1,745,597	( 5,191,206)	5,450,213
Land	<u>830,517</u>	<u>---</u>	<u>---</u>	<u>830,517</u>
	<u>\$148,031,750</u>	<u>\$ (9,909,849)</u>	<u>\$ ( 6,565,444)</u>	<u>\$131,556,457</u>

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**4. Property, Plant and Equipment, continued**

The provision for depreciation, as a percentage of the average balance of telephone plant in service, was 6.7% and 6.8% in 2003 and 2002, respectively. Individual plant depreciable rates for 2003 and 2002 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%

Depreciation expense for the years ended September 30, 2003 and 2002 amounted to \$17,998,809 and \$17,643,095, respectively, and is shown as a component of depreciation and amortization in the accompanying statements of revenues, expenses and changes in net assets.

**5. Long-Term Debt**

Long-term debt at September 30, 2003 and 2002 consisted of the following:

	<u>2003</u>	<u>2002</u>
RUS, at 5% per annum, payable in semi-annual installments of:		
\$1,557,000, including interest, due May 2025	\$ 40,132,752	\$ 41,150,329
\$659,000, including interest, due October 2020	14,912,484	15,462,183
\$526,000, including interest, due May 2011	7,016,330	7,701,082
\$308,000, including interest, due April 2017	5,864,260	6,178,768
\$176,000, including interest, due April 2012	2,453,637	2,678,197
\$162,000, including interest, due May 2011	2,179,414	2,389,891
FFB, due December 2014, payable in quarterly installments of:		
\$155,000, including interest at 7.647%	4,665,251	4,918,430
\$114,000, including interest at 5.643%	3,779,043	4,013,549
\$58,200, including interest at 7.496%	1,830,939	1,931,322
\$60,600, including interest at 7.301%	1,774,552	1,873,139
\$26,900, including interest at 6.171%	868,092	920,109
\$27,700, including interest at 7.887%	820,510	864,319
\$22,100, including interest at 6.604%	698,067	738,704

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**5. Long-Term Debt, continued**

	<u>2003</u>	<u>2002</u>
FFB, due December 2014, payable in quarterly installments of, continued:		
\$19,400, including interest at 7.581%	583,923	615,754
\$15,400, including interest at 5.784%	505,964	537,070
\$15,300, including interest at 6.151%	493,602	523,218
\$14,400, including interest at 5.621%	476,636	506,256
\$13,000, including interest at 6.402%	414,293	438,739
\$5,300, including interest at 6.214%	171,264	181,497
\$5,100, including interest at 7.111%	157,256	166,104
\$4,800, including interest at 6.490%	150,822	159,672
\$4,300, including interest at 7.399%	130,770	137,986
\$300, including interest at 5.865%	10,833	11,495
RTB, payable in semi-annual installments of:		
\$177,000, including interest at 9.5%, due October 2020	2,950,419	3,018,372
\$117,000, including interest at 6.04%, due May 2025	2,664,499	2,721,591
\$104,000, including interest at 6.05%, due May 2025	2,405,011	2,461,793
\$82,000, including interest at 6.05%, due May 2025	1,798,263	1,836,064
\$79,000, including interest at 6.05%, due May 2025	1,672,152	1,727,178
\$49,500, including interest at 6.26%, due May 2025	1,195,973	1,222,623
\$44,700, including interest at 5.56%, due May 2025	1,099,451	1,122,374
\$46,000, including interest at 5.98%, due May 2025	1,069,842	1,092,624
\$31,400, including interest at 5.93%, due May 2025	764,662	781,130
\$12,000, including interest at 6.05%, due May 2025	259,194	265,031
\$7,011, including interest at 5.33%, due July 2025	176,812	180,972
\$930, including interest at 5.96%, due July 2025	<u>21,300</u>	<u>22,098</u>
	106,168,272	110,549,663
Less current installments	( <u>5,825,461</u> )	( <u>5,622,570</u> )
	<u>\$100,342,811</u>	<u>\$104,927,093</u>

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**5. Long-Term Debt, continued**

At September 30, 2003, 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>
2004	\$ 5,825,461	\$ 4,629,611	\$ 10,455,072
2005	4,956,781	5,498,291	10,455,072
2006	5,237,801	5,217,271	10,455,072
2007	5,535,329	4,919,743	10,455,072
2008	5,850,373	4,604,699	10,455,072
2009 through 2013	31,420,905	17,709,245	49,130,150
2014 through 2018	24,367,907	9,482,516	33,850,423
2019 through 2023	19,282,217	3,665,451	22,947,668
2024 through 2025	<u>3,691,498</u>	<u>121,043</u>	<u>3,812,541</u>
	<u>\$106,168,272</u>	<u>\$55,847,870</u>	<u>\$162,016,142</u>

Unadvanced loan balance as of September 30, 2003, 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.

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**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 (25<sup>th</sup>) 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, 2003.

**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 years ended September 30, 2003 and 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 years ended September 30, 2003 and 2002.



Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**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, 2003 and 2002 amounted to \$2,725,277 and \$3,011,406, respectively.

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's unfunded retirement costs are now recorded within the financial statements of the Government of Guam.

In 2002, the Government of Guam adopted the provisions of GASB No. 27, "Accounting for Pensions by State and Local Governmental Employees".

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**7. Commitments and Contingencies**

*Lease*

Rent expense for operating leases totaled \$296,933 and \$356,817, for the years ended September 30, 2003 and 2002, 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.

*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.

*Typhoon Damages*

On July 5, 2002 and December 8, 2002, the island of Guam was struck by typhoon Chata'an and super-typhoon Pongsona, respectively. As a result, the Authority suffered damages totaling approximately \$2,711,000 (from typhoon Chata'an) and \$4,890,000 (from super-typhoon Pongsona) to its telecommunication. The Authority expects much of the damage to be covered by insurance or reimbursements from the Federal Emergency Management Agency (FEMA). For the year ended September 30, 2003, typhoon casualty loss, in excess of recoverable amount totaled \$3,999,805 and is reflected as disaster casualty loss in the accompanying 2003 statement of revenues, expenses and changes in net assets.

During 2003, the Authority received approximately \$475,000 in insurance proceeds for typhoon Chata'an and approximately \$321,000 and \$16,000 from FEMA for typhoon Chata'an and super-typhoon Pongsona, respectively. In addition, subsequent to fiscal year ended September 30, 2003, the Authority received approximately \$576,000 in insurance proceeds and \$24,000 from FEMA for super-typhoon Pongsona. However, the ultimate amount collectible is uncertain.

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**7. Commitments and Contingencies, continued**

*Litigation*

The Authority is a defendant in various lawsuits and proceedings arising in the normal course of business. While the outcome of these lawsuits and proceedings cannot be predicted with certainty and could have a material adverse effect on the Authority's financial position, results of operations and cash flows, it is the opinion of management, after consulting with legal counsel, that the ultimate disposition of such lawsuits and proceedings will not have a material adverse effect, therefore, no provision for any liability that may result from these claims have been made in the financial statements.

*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, 2003 and 2002, the Authority was not in compliance with this requirement. The impact on the financial statements is not currently determinable.

**8. Subsequent Events**

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 were held on June 7, 2004. Bid evaluations are currently ongoing and management expects to have the negotiated documents by December 31, 2004, which will be submitted to the Governor of Guam and the Guam Legislature for approval. Thereafter the documents will be provided to the FCC for approval.

Guam Telephone Authority  
(A Public Corporation)

Notes to Financial Statements, continued

**9. New Accounting Standards**

For fiscal year 2004, the Authority will be implementing GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, and GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3). For fiscal year 2005, the Authority will be implementing GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. As of the date of the opinion, the Authority has not evaluated the financial statement impact of GASB Statement Nos. 39, 40, 42.

## Other Financial Information

Guam Telephone Authority  
(A Public Corporation)

Schedule 1

Schedules of Revenues  
Years ended September 30, 2003 and 2002

<u>2003</u>	Basic Local Revenue	Long Distance	Non - Regulated Revenues	Total
Residential	\$ 8,368,058	\$ 2,930,240	\$ 1,286,412	\$ 12,584,710
Business	12,110,164	10,724,015	1,737,535	24,571,714
Government	3,740,171	961,327	250,439	4,951,937
Federal Government	914,540	121,202	124,146	1,159,888
Other Non-Regulated	---	---	937,537	937,537
	<u>\$ 25,132,933</u>	<u>\$ 14,736,784</u>	<u>\$ 4,336,069</u>	<u>\$ 44,205,786</u>
<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>

Guam Telephone Authority  
(A Public Corporation)

Schedule 2

Schedules of Expenses  
Years ended September 30, 2003 and 2002

	<u>2003</u>	<u>2002</u>
Plant specific operations:		
Salaries, wages and benefits	\$ 6,150,663	\$ 6,879,999
Materials and supplies	755,944	1,094,922
Telephone expense	527,984	481,552
Miscellaneous	488,159	651,526
Utilities	427,360	545,289
Overtime	385,678	166,490
Repairs and maintenance	355,742	560,921
800 Query Dips	341,183	448,905
Leased facilities	285,172	339,175
Outsourcing	161,147	192,208
Fuel and oil	146,839	164,622
Custodial service	125,961	119,127
Auto parts and supplies	112,869	120,357
Tools and equipment	58,921	22,263
	<u>10,323,622</u>	<u>11,787,356</u>
Corporate operations:		
Salaries, wages and benefits	2,310,835	2,560,499
Insurance	1,354,451	835,537
Miscellaneous	1,150,267	705,671
Professional fees	142,068	210,921
Consulting - other	75,378	35,479
Overtime	38,451	122,362
Training	29,544	60,825
Material and supplies	26,122	44,262
Legal fees - off and on island attorneys	23,090	81,764
Telephone expense	23,063	25,435
Consulting - privatization	300	3,083,313
Computer hardware maintenance	17	291,909
	<u>5,173,586</u>	<u>8,057,977</u>
Plant non-specific operations:		
Salaries, wages and benefits	1,997,055	2,238,720
Miscellaneous	826,545	(638,745)
Utilities	439,734	476,439
Material and supplies	72,943	(58,032)
Overtime	72,365	21,127
Consulting	8,046	289,726
	<u>3,416,688</u>	<u>2,329,235</u>
Customer operations:		
Salaries, wages and benefits	2,663,218	3,141,775
Postage and advertising	293,826	375,864
Price and costs studies	178,491	15,592
Material and supplies	84,033	30,072
Overtime	66,801	15,434
Telephone services	40,072	61,612
Product implementation	19,176	23,124
Miscellaneous	1,997	1,571
	<u>3,347,614</u>	<u>3,665,044</u>
Total	<u>\$ 22,261,510</u>	<u>\$ 25,839,612</u>
Total employees at end of year	367	390