

OFFICE OF THE YAP STATE PUBLIC AUDITOR
ANNUAL REPORT TO THE GOVERNOR AND THE LEGISLATURE
For the period January 1 to December 31, 2008

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INTRODUCTION

This report is submitted in accordance with 13 YSC 704 which states, "The Public Auditor shall file an annual report with the Governor and the Legislature within five days after the convening of each January regular session of the Legislature." The report focuses on the activities of the Office of the Yap State Public Auditor (Yap OPA) during the period January 01, 2008 to December 31, 2008.

The year 2008 represents the 8th consecutive year since 2000 that the Office of the Yap State Public Auditor has been in continuous operation. Since its establishment in 1983, the office has suffered closure every two years as the State Legislature searches for replacements for expatriate public auditors who generally completed their two-year contracts and vacate the office. Because of the lack of continuity in the early years, opportunities for testing the sufficiency of the Office's enabling legislation had never presented itself. As previously mentioned in the FY 2007 annual report, there were several event, activities, and circumstances which required our review of the Public Auditor Act. Such reviews have illuminated the need to revisit and revamp the Public Auditor Act, to update the language to make it more responsive to the current auditing and accounting environment and to broaden the types of engagement the Office is authorized to conduct in order for the office to effectively fulfill its mission in accordance with the FSM Strategic Development Plan.

As mentioned in the FY2007 annual report, some of the existing deficiencies of the Public Auditor Act are as follows:

- (1) The Public Auditor Act does not require the audit office to follow any recognized auditing standards.*
- (2) The Public Auditor Act appears to limit the type of audits that could be conducted by the Office to financial and financial-related audits, whereas the majority of audits conducted by government audit organizations are performance or "effectiveness and efficiency" audits.*
- (3) To comply with auditing standards, the staff as well as the Public Auditor need to be free of the confines of the Public Service System Act, but the Act appears to imply that OPA employees should be subjected to the PSSR.*
- (4) The Office of the Public Auditor should be allowed to make use of regional expertise and other available resources, including staff of regional audit offices, but the current language appears to allow the Office to cooperate only with the FSM National Public Auditor and external financial statement auditors.*

For more discussion on the above matters, we have reprinted the detailed discussion of the above mentioned that was included in the 2007 annual report, please refer to pages 8 to 9 of this report. In the coming months, we hope to be able to initiate discussion with the Executive and Legislature branches towards amendment of the Public Auditor Act.

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SUMMARY OF ACTIVITIES

The highlights of activities for the Office of the Yap State Public Auditor for calendar year 2008 are presented below:

Financial Highlights:

Our overall budget for FY08 was \$169,335 consisting only of Compact Capacity Building Sector Grant funds. Actual expended plus encumbrances at September 30, 2008 was \$126,821.20, with \$42,513.80 in unexpended balance.

Our approved budget for fiscal year 2009 is \$164,110; all from Compact Capacity Building Sector Grants. Currently, \$57,418 has been allotted of which \$32,841 has been expended or encumbered.

Audits and Other Engagements:

Compared to calendar year 2007, wherein we issued six reports consisting of five financial audits and one performance audit, for 2008, we managed to issue nine reports consisting of eight financial audits (five FY06 audits and three FY07 audits) and one performance audit. As of January 2009, only three of the FY2007 financial audits and two performance audits have yet to be finalized.

Planned Activities for Calendar Year 2009:

With the inclusion of three component units under the Single Audit Contract, we now have six component units that we must audit every year before March 31st. Previously, the deadline for the audit of the component unit was June 30 and it was only in Fiscal Year 2009 that the deadline was moved to March 31st. The audits of the component units will take priority over other requests for audits. To date, we have received two requests for audits, one from the Governor asking us to perform an audit on a locally generated fund account and one for a compliance audit of a Department. In addition, another department has requested that we audit annually a small fund maintained outside the State Treasury.

Staffing and Other Matters:

In November 2008, two staff and the Public Auditor resigned. The Audit Manager was appointed by the Legislature as the Acting Public Auditor effective November 7, 2008 up to the time a suitable replacement can be hired.

From the period November to December 2008, we were able to hire one auditor and one admin. assistant to fill-up the vacant positions. Our continuous advertisement for the

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vacant auditor position netted 5 applicants and we were able to identify the individual that can fill-up the position. The individual will be working for the office this coming January 19, 2009.

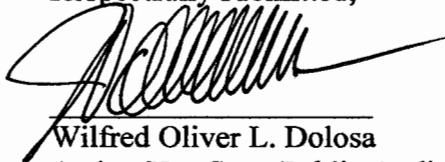
Problems and Constraints:

The main problem faced by the OPA in calendar year 2008 is the unfamiliarity of the new hires with the work at hand – in the last quarter of 2008, one auditor and the admin assistant resigned. We were able to hire their replacements and another one will be filling up the long outstanding vacant auditor’s position in January 2009.

With the current set-up on hand and the moving of Deloitte’s deadline from June 30 to March 31, there is a possibility that we might be encountering delays in the audit. But with teamwork and vigilant guidance from the lead auditors and the acting public auditor, we believe that we will be able to meet our deadlines.

As discussed in our introduction and in the previous annual report, our enabling legislation which is more than 20 years old needs to be updated and revised to reflect the changes in the auditing profession and to make it more responsive to the mission and goals of the Office of the Yap State Public Auditor. We solicit the support of the Governor and the Legislature on this endeavor.

Respectfully submitted,



Wilfred Oliver L. Dolosa
Acting Yap State Public Auditor
January 15, 2009

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FINANCIAL INFORMATION

Fiscal Year ended September 30, 2008: Our approved budget for FY08 consisted of Compact Capacity Building Sector Grants of \$169,335. The detailed financial information below as compiled from the advices of allotment obtained from the Office of Planning and Budget and the Fundware reports from Finance for the fiscal year ended September 30, 2007 is set forth hereunder.

Description	Budget	Actual Expenditures	PY Encumbrance	CY Encumbrance	Balance (Over)/Under
Personnel	\$ 111,710.00	\$ 80,364.04	\$ -0-	\$ -0-	\$ 31,345.96
Travel	14,725.00	10,397.33	-0-	-0-	4,327.67
Contractual Services	23,200.00	16,520.00	-0-	-0-	6,680.00
OCE	16,200.00	13,624.83	-0-	2,440.00	135.17
Fixed Assets	3,500.00	1,475.00	-0-	2,000.00	25.00
TOTAL	\$ 169,335.00	\$ 122,381.20	\$ -0-	\$ 4,440.00	\$ 42,513.80

The unexpended balance of 42,514 for fiscal year 2007 can be broken down as follows:

- a. Personnel Budget : \$ 31,000.00
 - aa) Salary of the Audit Manager who is getting \$22,000 as opposed to the \$25,000.00 budgeted and also due to the fact that he started in January 2008 : \$ 9,000.00
 - bb) Vacant staff auditor position, no qualified applicants yet 12,000.00
 - cc) Staff turn-over and planned salary increases under our staff training and development plan which the Attorney General's and the Personnel Offices would not allow us To implement. 10,000.00
- b. The \$4,000 unexpended in travel relates to the savings in recruitment costs for our audit manager who was recruited from Pohnpei without dependents.
- c. The \$6,000 unexpended funds in contractual services is related to funds budgeted for our peer review. The Apipa was able to obtain a grant from DOI to fund the 2008/2009 cycle of peer reviews. The Yap OPA is scheduled for its peer review in April 2009.

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Quarter Ended December 31, 2008: Our budget for fiscal year 2009 of \$164,110.00 is funded entirely from Compact Capacity Building Sector Grants. The financial information below was accumulated using the Fundware Reports from Finance as of December 31, 2008, representing allotments and expenditures to date:

Description	Budget	Actual Expenditures	PY Encumbrance	CY Encumbrance	Balance (Over)/Under
Personnel	\$ 111,710.00	\$ 12,423.90	\$ -0-	\$ -0-	\$ 99,286.10
Travel	15,000.00	-0-	-0-	-0-	15,000.00
Contr. Svcs.	18,600.00	4,450.00	-0-	13,490.00	660.00
OCE	18,800.00	1,419.71	-0-	1,057.60	16,322.69
Fixed Assets	-0-	-0-	-0-	-0-	-0-
TOTAL	\$ 164,110.00	\$ 18,293.61		\$ 14,547.60	\$ 131,268.79

AUDITS AND OTHER ENGAGEMENT ACTIVITIES

During 2008, Yap OPA released nine final and five draft reports. The finalized reports consist of 8 regularly scheduled financial audits and a financial-related audit requested by a department. More details relating to the status of audits and other engagements are provided below.

Completed Engagement Activities:

Following is a list of final audit reports issued by the Office of the Public Auditor during the reporting period. Copies of the reports are provided herein as Exhibit A.

- ◆ *Yap Fishing Authority , Financial Statements and Independent Auditor’s Report for the years ended September 30, 2007 and 2006*
- ◆ *Public Transportation System, Financial Statements and Independent Auditor’s Report for the years ended September 30, 2007 and 2006*
- ◆ *Yap Community Action Program, Financial Statements and Independent Auditor’s Report for the years ended September 30,2007 and 2006*
- ◆ *Prisoner Feeding and Maintenance Fund, Schedule of Activities and Independent Auditor’s Report for year ending September 30, 2007*
- ◆ *Gagil-Tomil Water Authority, Financial Statements and Independent Auditor’s Report for the years ended September 30, 2006 and 2005.*
- ◆ *Yap Fishing Authority, Financial Statements and Independent Auditor’s Report for the years ended September 30, 2006 and 2005*

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- ◆ *Yap Sports Council, Financial Statements and Independent Auditor's Report for the years ended September 30, 2006 and 2005*
- ◆ *Public Transportation System, Financial Statements and Independent Auditor's Report for the years ended September 30, 2006 and 2005*
- ◆ *Southern Yap Water Authority, Financial Statements and Independent Auditor's Report for the years ended September 30, 2006 and 2005*

The following draft reports were issued:

- ◆ *Department of R&D, SPREP International Waters Project Acct. No. A14-30-G0503, Schedule of Activities and Independent Auditor's Report for the period January 1 to December 31, 2006*
- ◆ *Yap Sports Council, Financial Statements and Independent Auditor's Report for the years ended September 30, 2007 and 2006*
- ◆ *Southern Yap Water Authority, Financial Statements and Independent Auditor's Report for the years ended September 30, 2007 and 2006*
- ◆ *Gagil-Tomil Water Authority, Financial Statements and Independent Auditor's Report for the years ended September 30, 2007 and 2006*
- ◆ *Government Time and Attendance, a performance audit report to determine whether regular hours paid are based on actual hours worked.*

Other Ongoing Engagement Activities:

- Yap Community Action Program, Fiscal Year 2008 financial audit
- Department of Youth and Civic Affairs, compliance audit for the Fiscal Year 2008
- Yap Traditional Navigation Society, Fiscal Year 2008 financial audit

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Planned Audit and Other Engagement Activities for Calendar Year 2008

Annual Financial Audit Calendar – Of the nine component units of the State Government, three are audited annually under the Single Audit contract, and six are audited annually by the Yap OPA. The drafts for these audits need to be completed by March 31st for inclusion in the State of Yap audit report.

Requested Audits – In addition to the long list of audits requested by the Legislature several years back, we also have request for audits from departments. As previously stated in the “Other Ongoing Engagement Activities” portion, currently we are doing simultaneous audits on 2 requests. Hopefully, upon completion of audits of the component units, we will be able to finish the requested audits and can accommodate other requests.

Self-initiated Audits – The most value to the State that could be derived from the OPA should be the strengthening of internal control policies and procedures in the primary government since the bulk of funds expended each year by the Government passes through the State Finance. In 2009, though we’re hampered by the constant turnover of staff, we will try to perform at least one “effectiveness and efficiency” audit after our annual financial audit cycle is completed so as to strengthen the financial management process within the State.

STRENGTHENING THE AUDIT OFFICE

Beginning in fiscal year 2007 and continuing in 2008 and beyond, we have begun efforts to strengthen the audit office to better meet its objectives. The first step was the rewording of our mission statement to align it with the Public Sector Management section of the FSM Strategic Development Plan. We used the new mission statement in our budget for FY09 which reads as follows: *“To enhance governance, accountability, and performance in the public sector through delivery of independent assurance and investigative services.”* Previously, our mission statement had read as follow: *“To foster financial responsibility and integrity to ensure the proper use of public resources.”*

As previously mentioned in the FY 2007 annual report, there were several event, activities, and circumstances which required our review of the Public Auditor Act. Such reviews have illuminated the need to revisit and revamp the Public Auditor Act, to update the language to make it more responsive to the current auditing and accounting environment and to broaden the types of engagement the Office is authorized to conduct in order for the office to effectively fulfill its mission in accordance with the FSM Strategic Development Plan. Below, is the re-issued portion of the FY2007 annual report that delves on the event, issues and discussions about the Public Auditors Act.

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In July 2007, the U.S. Comptroller General issued the latest revision to *Government Auditing Standards*, more commonly known as the “Yellow Book” or GAGAS (generally accepted government auditing standards). The new standards, among others:

- (1) Heightened the emphasis on ethical principles that should guide the work of those who audit government programs and operations.
- (2) Clarified and discussed the impact of non-audit services on auditor independence.
- (3) Enhanced and clarified the requirements of the audit organization’s system of internal control by specifying the elements that the organization’s policies and procedures should address.
- (4) Enhanced performance auditing standards to better explain the concepts of reasonable assurance and its relationship to audit risk, significance, and the levels of evidence used to support findings and conclusions.
- (5) Reinforced the key role of auditing to maintaining accountability and good governance.

The above developments necessitated a review of our enabling legislation which found the language to be in need of revision to better meet the changing audit environment.

Some of the areas where the Act has been found to be deficient are discussed below:

1. The Act does not require the Public Auditor to follow any professional accounting or auditing standards. This is primarily because *Government Auditing Standards* (the “Yellow Book”) was not issued by the Comptroller General until 1988 whereas the Public Auditor Act was promulgated in 1983. The latest revision to the Yellow Book dated July 2007 has totally changed the face of government auditing, putting additional burden on the audit organization to ensure that it conducts high quality audits with competence, integrity, objectivity, and independence.

Although our enabling legislation does not require us to follow any kind of auditing or accounting standards, we have elected to adopt *Government Auditing Standards* mostly due to the fact that we are performing financial statement audits of the component units for inclusion in the State of Yap financial statements which are audited by other auditors. If we did not follow *Government Auditing Standards*, the State’s financial statement auditors would not accept our audits of the component units, thereby, requiring the State to expend additional funds to procure audits of those component units.

Moreover, given the media blitz on the failure of the auditors of Enron and World Com in recent years and its consequences on the stakeholders of those companies and the auditing firm involved, the public is suspect of any audit reports issued without reference to recognized standards. Therefore, if the law is not amended to require the office to follow generally accepted government auditing standards such as those promulgated by the U.S. Comptroller General, it leaves the office and the State vulnerable to future

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auditors who may elect to take the easy road and revert to issuing reports outside the framework of generally accepted auditing standards.

2. The Public Auditor Act appears to limit the type of audits that could be conducted by the Office to financial statement and financial-related audits. Section 703 of the Public Auditor Act provides only for financial or financial-related audits. This is only two types of audits contained in *Government Auditing Standards*. Other types of audits or engagements covered by the Yellow Book are performance audits (also known as “effectiveness and efficiency audits”) and attestation engagements which are different in scope than audits. During the seven years that I’ve been Public Auditor, we have had to performed non-financial audits based on requests from departments and agencies. Therefore, there is a clear need to revise the language of the Act to broaden the types of audits that the office can conduct and recommendations (Section 705), it can issue.

3. To comply with auditing standards, the staff as well as the Public Auditor need to be free of the confines of the Public Service System Act. Section 141 of Title 8, specifically exempts the Public Auditor from the Public Service System. But, the employees of the Office are not likewise exempted. Accordingly, we have had difficulty recruiting and retaining qualified individuals for the positions within the office. Moreover, the protection that the PSS accords to employees prevents the office from enforcing the basic principles of independence, objectivity, confidentiality, and integrity critical for staff members. Should a staff member breach an office policy relating to such principles, he could not be removed without first going through the PSS disciplinary and grievance process which could take months.

4. The Office of the Public Auditor should be allowed to make use of regional expertise and other available resource, including staff of regional audit offices. In December 2007, an ADB consultant visited our office as part of a technical assistance package to strengthen pacific islands audit offices. One of the potential means of cooperation between audit offices within the region that was being entertained was the sharing of information and staff members. Technological innovations have now made possible the sharing of technical information at nominal costs between audit office within the Pacific regional and even all over the world. However, the OPA enabling Act in Section 713 authorizes the office to only cooperate with private accounting firms and the FSM National Public Auditors office. The Office’s access to experts and specialists could be greatly improved if the enabling Act expands the sphere of cooperation allowed between the OPA and other audit organizations.

These are only sections of the Public Auditor Act that we have identified in the course of the eight years of operation. However, our review of the Act has been cursory at best. I believe that if careful attention is given to the language of the Office’s enabling legislation, we can better identify the areas requiring improvements. It is a goal of the office to work with the Executive and Legislature Branches of Government in the coming years to update and strengthen the Act to better meet the needs of the State of Yap.

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STAFF RECRUITMENT, DEVELOPMENT AND TRAINING:

Staff Movements

During calendar year 2008, the Office lost one of its auditors. Kate L. Mulalap, a Staff Auditor I, left the Office at the end October to continue her studies in Hawaii. Kate had been with the Office for almost 2 years and had made valuable contribution in achieving the objectives of the Office. Linda Teteth, the Admin/Auditor-trainee, also left at the end of October for personal reasons.

Our current staff members consist of the following individuals – Maria Mitrad, a Staff Auditor II (Dev.) who has been with us for over five years; Brian Y. Dabgusiy, a Junior Auditor, who just completed a year with the Office; Joan Alice Pinerof, came in November as a replacement of Kate Mulalap; and Berlinda Margaret Mimew, our administrative assistant/audit trainee, who replaced Linda Tetet in October. We will be filling out the long vacant auditor come January of 2009.

Ms. Gertrude Gootinan resigned as Public Auditor as of November 7, 2008 and Legislature appointed Audit Manager Wilfred Oliver L. Dolosa as the Acting Public Auditor as of November 7, 2008.

Though we are a bit shorthanded at the moment, we still believe that all of our goals will be achieve thru teamwork. We are also in the process of developing an updated manual with the help of the former Public Auditor, on a consultancy basis. Once the manual is finished it will be a great help especially to the new recruits. In addition, we hope to be able to conduct more frequent staff evaluations which will also aid in the development and retention of staff members.

Local Training Workshop

In addition to the regular on the job training that is provided to staff members, we are coordinating with some government entities as to the trainings that might come to the island. Our plan is to let auditors attend the training and echo out what they learned thru an in-house seminar that they will be facilitating. In so doing, all of the auditors will be at par with each other as to the knowledge they gained thru these seminars.

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Off-island Training Workshop

To comply with Government Auditing Standards' continuing professional education requirements, the Public Auditor and staff auditors participated in the following off-island training workshops during the year:

APIPA Training Conference – 2 staff auditors and the Audit Manager participated in the annual Association of Pacific Islands Public Auditors conference held in CNMI last July 2008.

Mini PEIC Conference – One staff auditor Pacific Emerging Issues conference in Guam last July 2008.

Planned Activities for Next Year:

- WIGAF/PEIC - The Acting Public Auditor will be attending the conference in Hawaii in July 2008
- PASAI Conference - One to two staff auditors will be attending the conference in Palau in July 2009.
- APIPA Annual Conference – The 2009 APIPA Conference will follow the PASAI conference to be held in Guam. The Acting Public Auditor and four staff auditors will be attending.
- USDA's Executive Leadership Development Program – One staff auditor was chosen to be a participant of the program. It started in 2008 and will be continuing up to the third quarter of 2009.
- We are still in the process of trying to identify free seminars sponsored by SPASAI that we could send our staff auditors to further hone up their skills.