

OFFICE OF THE YAP STATE PUBLIC AUDITOR
ANNUAL REPORT TO THE GOVERNOR AND THE LEGISLATURE
For the period January 1 to December 31, 2009

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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, 2009 to December 31, 2009.

The year 2009 represents the 9th 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 and FY 2008 annual reports, 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 and FY2008 annual reports, 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.

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SUMMARY OF ACTIVITIES

The highlights of activities for the Office of the Yap State Public Auditor for calendar year 2009 are presented below:

Financial Highlights:

Our overall budget for FY09 was \$164,110 consisting only of Compact Capacity Building Sector Grant funds. Actual expended plus encumbrances at September 30, 2009 was \$105,029.93, with \$59,080.07 in unexpended balance.

Our approved budget for fiscal year 2010 is \$173,105; all from Compact Capacity Building Sector Grants. Currently, \$60,526 has been allotted of which \$20,832.55 has been expended or encumbered.

Audits and Other Engagements:

Compared to calendar year 2008, wherein we issued nine reports consisting of eight financial audits (Five FY06 audits and three FY07 audits) and one performance audit, In FY2009, due to manpower constraint, we were only able to issue 4 reports consisting of three financial audits (FY07 audits) and one performance audit. As of January 2010, all FY2008 audits are being finalized for exit conferences and issuance.

Planned Activities for Calendar Year 2010:

We have six component units that we must audit and submit copies of draft reports to the external auditor on or before May 31st. Previously, the deadline for the audit of the component unit was June 30 and it was only in Fiscal Year 2010 that the deadline was moved to May 31st. The audits of the component units will take priority over other requests for audits, however, we have taken steps in trying to squeeze in the request for audit of the enterprise fund and we are currently in the probing stage. With regards to the audit of one department, we have already completed the fieldwork and we might be able to finalize the report before the end of the March. For the other outstanding request and other possible request for audits, we will be tackling them after we're done with the audit of the 6 component units.

Staffing and Other Matters:

For the majority of 2009, the office encountered manpower shortage, the Public Auditor position was vacant for 11 months, one of the junior auditors resigned in August and our admin assistant was terminated in early December.

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It was only in December 8, 2009 that a new Public Auditor was appointed and we have already announced the vacant positions. Hopefully we will be able to fill-up the vacant position before the end of January 2010.


Problems and Constraints:

The main problem faced by the OPA in calendar year 2009 aside from the unfamiliarity of the new hires with the work at hand, is the fast turn-over of the staff. Hopefully, we will retain the current staff and fill-up the vacant position as soon as possible.

With the current set-up and the new external auditor's deadline of May 31st, there is a possibility that we might be encountering delays in the audit. However, it is our position that we exhaust all possible means to maintain our audit schedule and refrain from any delays.

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. For this purpose, we will be soliciting the support of the Governor and the Legislature on this endeavor.

Respectfully submitted,



Ronald C. Yow
Yap State Public Auditor
January 18, 2010

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FINANCIAL INFORMATION

Fiscal Year ended September 30, 2009: Our approved budget for FY09 consisted of Compact Capacity Building Sector Grants of \$164,110. 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	\$ 67,217.72	\$ -0-	\$ -0-	\$ 44,492.28
Travel	15,000.00	9,386.04	-0-	-0-	5,613.96
Contractual Services	18,600.00	17,905.00	-0-	-0-	695.00
OCE	17,800.00	7,256.04	-0-	2,271.13	8,272.83
Fixed Assets	1,000.00	994.00	-0-	-0-	6.00
TOTAL	\$ 164,110.00	\$ 102,758.80	\$ -0-	\$ 2,271.13	\$ 59,080.07

The unexpended balance of 59,080.07 for fiscal year 2009 can be broken down as follows:

- a. Personnel Budget : \$ 44,492.28
 - aa) Salary of the Audit Manager who is getting \$22,000 as against the \$25,000.00 budgeted \$ 3,000.00
 - bb) Vacant Public Auditor position 31,800.00
 - cc) Staff turn-over and planned salary increases under our staff training and development plan 9,692.28
- b. The \$5,613.96 unexpended in travel relates to savings in the SPASAI and APIPA conferences. For SPASAI, the Travel expenses were shouldered by ADB while for APIPA, the travel expenses of our two staff auditors were shouldered by the FSM National Public Auditor's Office.
- c. The \$8,272.83 unexpended funds in OCE is due to our Office's lower consumption in electricity and fewer purchases of supplies, since we tried to finish-up all the existing supplies before we make some purchases.

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Quarter Ended December 31, 2010: Our budget for fiscal year 2010 of \$173,105 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, 2009, representing allotments and expenditures to date:

Description	Budget	Actual Expenditures	PY Encumbrance	CY Encumbrance	Balance (Over)/Under
Personnel	\$ 111,710.00	\$ 13,560.22	\$ -0-	\$ -0-	\$ 98,144.78
Travel	22,000.00	-0-	-0-	-0-	22,000.00
Contr. Svcs.	18,800.00	1,500.00	-0-	4,500.00	12,800.00
OCE	18,600.00	1,238.83	-0-	33.50	17,327.67
Fixed Assets	2,000.00	-0-	-0-	-0-	2,000.00
TOTAL	\$ 164,110.00	\$ 16,299.05		\$ 4,533.50	\$ 152,272.45

AUDITS AND OTHER ENGAGEMENT ACTIVITIES

During 2009, Yap OPA released four final and seven draft reports. The finalized reports consist of three FY2008 regularly scheduled financial audits and a performance audit. 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 Sports Council , 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.*
- ◆ *Southern Yap Water Authority, Financial Statements and Independent Auditor's Report for the years ended September 30, 2007 and 2006*
- ◆ *Government Time and Attendance Report's Executive Summary*

The following draft reports were issued:

- ◆ *Yap Sports Council, Financial Statements and Independent Auditor's Report for the years ended September 30, 2008 and 2007*
- ◆ *Southern Yap Water Authority, Financial Statements and Independent Auditor's Report for the years ended September 30, 2008 and 2007*

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- ◆ *Gagil-Tomil Water Authority, Financial Statements and Independent Auditor's Report for the years ended September 30, 2008 and 2007*
- ◆ *Yap Community Action Program, Financial Statements and Independent Auditor's Report for the years ended September 30, 2008 and 2007*
- ◆ *Public Transportation System, Financial Statements and Independent Auditor's Report for the years ended September 30, 2008 and 2007.*
- ◆ *Yap Fishing Authority, Financial Statements and Independent Auditor's Report for the years ended September 30, 2008 and 2007*
- ◆ *Prisoner Feeding and Maintenance Fund, Schedule of Activities and Independent Auditor's Report for year ending September 30, 2008*

Other Ongoing Engagement Activities:

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

Planned Audit and Other Engagement Activities for Calendar Year 2010

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 May 31st for inclusion in the State of Yap single 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 engaged in simultaneous audits on 2 requests. Hopefully, upon completion of audits of the component units, we will be able to finalize the requested audits and thereafter, accommodate other requests.

Of the audits requested by the Legislature, we have started the preliminary phase of our SDF audit in late December and we have already coordinated with the Director of OAS on subject matter for records, computation and relevant documents.

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, we weren't able to perform such audit due to

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manpower constraint. However, since we are in the process of recruiting for the vacant positions before the end of January 2010, we will try to perform at least one “effectiveness and efficiency” audit after our annual financial audit cycle is completed.

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.

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:

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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 suspicious 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 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. For the past 9 years, the Office only 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

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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 nine years of operation. However, our review of the Act has been cursory at best. We 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.

STAFF RECRUITMENT, DEVELOPMENT AND TRAINING:

Staff Movements

During calendar year 2009, the Office lost one of its auditors. Joan Alice Pinerof, a Junior Auditor , left the Office at the end July to work at one of the Banks. Joan had been with the Office for almost a year and had made valuable contribution in achieving the objectives of the Office. Angelina Filenguy, the Admin/Auditor-trainee, was terminated in the first week of December.

Our current staff members consist of the following individuals – Maria Mitrad, a Staff Auditor II (Dev.) who has been with us for over six years; Brian Y. Dabgusiy, a Junior Auditor, who has been with us for over two years; Berlinda Margaret Mimew, who has been with us for over a year. Hopefully we will be able to fill out the vacant auditor and admin assistant positions before the end of January of 2010.

Mr. Ronald C. Yow was appointed by the Yap State Legislature as the new Yap State Public Auditor effective Dec. 8, 2009. Mr. Wilfred Oliver L. Dolosa, who was the Acting Public Auditor from November 7, 2008 to December 4, 2009, resumed his post as Audit Manager.

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Though we are shorthanded at the moment, we still believe that all of our goals will be achieved through 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 completed it will help clarify guidelines and procedures for each audit. Furthermore, we hope 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 provided to staff members, we are coordinating with some government entities for staff development trainings that may be provided locally. Our plan is to let auditors attend the training and echo out what they learned through an in-house seminar which 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.

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:

SPASAI Conference – The Audit Manager, then the Acting Public Auditor, attended the conference held in Palau in the third week of July 2009.

APIPA Training Conference – 4 staff auditors and the Audit Manager participated in the annual Association of Pacific Islands Public Auditors conference held in Guam in the last week of July 2009.

Procurement and Grant Fraud Training Seminar – 3 staff attended the seminar that was held in Guam on Oct. 28 to 30, 2009.

USDA's Executive Leadership Development Program – One staff auditor was chosen to be a participant of the program. It started in 2008 and was concluded in the third quarter of 2009.

Planned Activities for FY2010:

- WIGAF/PEIC - The Public Auditor will be attending the conference possibly in Hawaii in the latter part of 2010.

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- APIPA Annual Conference – The 2010 APIPA Conference will be held in Pohnpei. The Public Auditor, Audit Manager and the 4 staff auditors will be attending.
- USDA's Executive Leadership Development Program - We will try to nominate one or two of our staff auditors to join the 2nd program when it starts in the latter part of 2010
- We are still in the process of trying to identify free seminars sponsored that we could send our staff auditors to further hone their skills.