

YAP FISHING AUTHORITY

**Financial Statements and
Independent Auditor's Report
Fiscal Years Ended
September 30, 2005 and 2004**



**Office of the Public Auditor
State of Yap
Federated States of Micronesia**



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YAP STATE GOVERNMENT**

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EXECUTIVE SUMMARY

Financial Audit of the
Yap Fishing Authority
for the Years ended September 30, 2005 and 2004

The Office of the Yap State Public Auditor was engaged to audit the Yap Fishing Authority for the years ended September 30, 2005 and 2004 and has issued its report dated September 7, 2006. Due to scope limitations presented by inadequate accounting records and other factors explained in the Independent Auditor's Report on page 1, I was unable to determine whether the financial position of YFA as of September 30, 2005 and 2004 nor the results of its operations and cash flows for the years then ended were fairly presented. Fiscal year 2005 is the third consecutive year that I have not been able to form an opinion on YFA's financial statements.

Moreover, YFA was unable to prepare *Management's Discussion and Analysis* which is supplementary information required by Governmental Accounting Standards Board (GASB) Statement No. 34, "*Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments*" to be presented with the basic financial statements.

The Schedule of Expenditures of Federal Awards on page 6 shows that for the years ended September 30, 2005 and 2004, YFA incurred \$1,328 and \$10,278, respectively, in expenses related to recovery efforts after Typhoon Sudal.

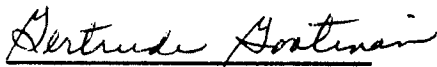
The report on internal control over financial reporting and compliance and other matters required by *Government Auditing Standards* on page 16 discusses reportable conditions at YFA. These conditions and our recommendations are presented for the information of YFA management in the Schedule of Findings beginning on page 18. Of the twelve findings, two are considered to be material weaknesses. All twelve findings are related to inadequate controls over financial reporting, seven of which are repeat findings from the prior years.

Following is a summary of the audit findings for the year ended September 30, 2005:

- (1) Finding No. 1 relates to the unavailability of minutes of meetings held by the Board.
- (2) Finding No. 2 pertains to the deposit of grant funds with local vendors. \$11,328 remained with two vendors as of September 30, 2006. As of the date of this report, the balance of funds still remaining with vendors has been significantly reduced.
- (3) Finding No. 3 cites YFA for recording adjustments without economic basis in its general ledger.
- (4) Finding No. 4 discusses a \$26,760 balance due from a Board member for equipment rental. As of the date of this report the balance was still outstanding because YFA did not require a promissory note or other means of ensuring collection of the balance due from the Board member.
- (5) Finding No. 5 discusses inadequate accounting for fixed assets.

- (6) Finding No. 6 pertains to a charge account maintained by YFA with a local vendor. We recommend that YFA close the account and adopt a purchase order system to eliminate the risk of unauthorized charges.
- (7) Finding No. 7 relates to the need for YFA to adopt a vehicle policy similar to the Government which requires vehicles to be parked at the motor pool after hours.
- (8) Finding No. 8 cites YFA for not properly reconciling its general ledger.
- (9) Finding No. 9 relates to \$658,489 in trade receivables that YFA has been carrying on its books for over ten years. The likelihood of collection on these accounts is very slim, therefore, we recommend that the Board review and identify accounts to be written off the books.
- (10) Finding No. 10 discuss the Board member invoice also discussed in Finding No. 4 of \$26,750 which was inaccurately prepared by YFA. Ten and a half hours of equipment rental services worth \$525 was not invoiced to the Board member.
- (11) Finding No. 11 pertains to a board decision to forgive the debt owed by a government office because it was considered redundant for government agencies to settle debts amongst themselves. This is a flawed reasoning that defeats the purpose of establishing enterprise funds such as YFA.
- (12) Finding No. 12 discusses the need for YFA to define vacation leave policies and ensure reliable records are maintained of employee leave balances.

A copy of this draft report was provided to the Chairman of the Board and the acting general manager on May 30, 2006. We also met and discussed the contents of the report with the Chairman of the Board and key staff members on December 5, 2006. We requested YFA to provide their written responses to the audit findings and recommendations, but despite repeated follow up on our part, YFA was not able to submit written responses.



Gertrude Gootinan
Yap State Public Auditor
February 20, 2007

YAP FISHING AUTHORITY

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Yap Fishing Authority:

I was engaged to audit the accompanying balance sheets of the Yap Fishing Authority (YFA) as of September 30, 2005 and 2004, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the YFA management.

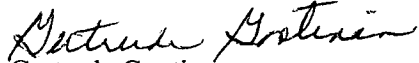
Documentation to determine the carrying value of fixed assets reported on the financial statements as of September 30, 2005 and 2004 was not available. The fiscal year 2005 and 2004 financial statements for Yap Fresh Tuna, Inc. (YFTI), a 50% owned subsidiary in which YFA is deemed to have controlling interest have not been audited. In my opinion, the financial statements of YFA should be consolidated with the financial statements of YFTI to conform with accounting principles generally accepted in the United States of America. YFA did not present Management's Discussion and Analysis that, although not a required part of the basic financial statements, is supplementary information required by the Governmental Accounting Standards Board.

I was unable to obtain properly reconciled trial balances for the years ended September 30, 2005 and 2004. The general ledger beginning balances for the year ended September 30, 2004 did not agree with the fiscal year 2003 ending balances. Moreover, the general ledger for the year ended September 30, 2005 contained many adjusting entries, some of which were found to be without economic basis. Consequently, due to inadequate accounting records and lack of concrete action taken by management to address findings and recommendations reported in an agreed-upon-procedures engagement dated October 12, 2005, I was unable to form an opinion on whether operating revenues and expenses for the years ended September 30, 2005 and 2004 were valid, complete and recorded in accordance with accounting principles generally accepted in the United States of America.

Because of the scope limitations described in the preceding paragraphs, I was unable to audit the financial statements supporting the financial activities of the Yap Fishing Authority, nor was I able to form an opinion on those financial activities by other auditing procedures. Since I did not audit the accompanying balance sheets of the Yap Fishing Authority as of September 30, 2005 and 2004 and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended, the scope of my work was not sufficient to enable me to express, and I do not express, an opinion on these financial statements.

The accompanying Schedule of Expenditures of Federal Awards (page 6) is presented for the purpose of additional analysis and is not a required part of the financial statements. This schedule is the responsibility of YFA's management.

In accordance with *Government Auditing Standards*, I have also issued a report dated September 7, 2006 on my consideration of the Yap Fishing Authority's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, and contracts. The purpose of that report is to describe the scope of my testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of my audits.


Gertrude Gootinan
Yap State Public Auditor

September 7, 2006

YAP FISHING AUTHORITY

Balance Sheets
September 30, 2005 and 2004

ASSETS	<u>2005</u>	<u>2004</u>
Current Assets		
Cash	\$ 45,048	\$ 77,560
Investments in unconsolidated subsidiary	398,016	395,274
Trade receivables, net	21,760	5,870
Purchase order advance	11,833	69,220
Employee receivables, net	1,358	--
Due from grantor	--	10,278
	<hr/>	<hr/>
Total current assets	478,015	558,202
Property and equipment, net	<hr/>	<hr/>
	1,861,959	2,039,143
TOTAL ASSETS	\$ <u>2,339,974</u>	\$ <u>2,597,345</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable	14,016	20,095
Accrued payroll and others	2,630	1,835
Due to affiliate	41,945	41,945
Due to the State Government	35,325	35,325
	<hr/>	<hr/>
Total current liabilities	93,916	99,200
Contingencies		
Net Assets		
Invested in capital assets	1,861,959	2,039,143
Unrestricted	384,099	459,002
	<hr/>	<hr/>
Total net assets	2,246,058	2,498,145
TOTAL LIABILITIES AND NET ASSETS	\$ <u>2,339,974</u>	\$ <u>2,597,345</u>

See accompanying notes to financial statements

YAP FISHING AUTHORITY

Statements of Revenues, Expenses and Changes in Net Assets
Years ended September 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Operating revenues		
Fish & ice sales	\$ 49,037	\$ 74,782
Charter & rental income	37,100	58,106
Other income	26,934	12,230
Other sales	2,060	14,811
Fishing rights and dockage fees	<u>625</u>	<u>50</u>
Total operating revenues	115,756	159,979
Operating expenses		
Depreciation	183,184	182,184
Other	68,348	62,296
Utilities	52,785	32,478
Payroll, taxes and benefits	37,452	38,275
Contractual services	14,287	18,626
Bad debt expense	9,092	18,970
Non-YFA expense	1,052	19,955
Travel	2,681	2,373
Fleet expenses	<u>32</u>	<u>9,069</u>
Total operating expenses	368,913	384,226
Loss from operations	(253,157)	(224,247)
Nonoperating revenues/(expenses)		
Other expenses	(3,000)	--
Gain (loss) on investment in unconsolidated subsidiary	2,742	(2,458)
Intergovernmental contribution	1,328	10,278
Typhoon loss	--	(128,311)
Donations and other contributions	--	189,767
Operating subsidy	--	81,000
Inventory loss	--	(7,972)
Impairment loss in PMAir	<u>--</u>	<u>(2,000)</u>
Total nonoperating revenues/(expenses)	1,070	140,304
Net loss	<u>(252,087)</u>	<u>(83,943)</u>
Net assets at beginning of year	2,498,145	2,582,088
Net assets at end of year	<u>\$ 2,246,058</u>	<u>\$ 2,498,145</u>

See accompanying notes to financial statements

YAP FISHING AUTHORITY

Statements of Cash Flows Years ended September 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities		
Receipts from customers	\$ 70,872	\$ 142,078
Receipts from other operating activities	39,272	27,041
Cash payments for goods and services	(96,969)	(231,342)
Cash payments to employees	(38,015)	(38,254)
Net cash used for operating activities	<u>(24,840)</u>	<u>(100,477)</u>
Cash flows from noncapital financing activities		
Other expenses	(3,000)	--
FEMA grant receipts	1,328	33,330
Operating subsidy from Yap State Government	--	81,000
Purchase order advance	--	69,220
Net cash provided by (used for) noncapital financing activities	<u>(1,672)</u>	<u>183,550</u>
Cash flows used for investing activities		
Acquisition of fixed assets	(6,000)	(7,745)
Net cash used for investing activities	<u>(6,000)</u>	<u>(7,745)</u>
Net increase (decrease) in cash	(32,512)	75,328
Cash, beginning of year	<u>77,560</u>	<u>2,232</u>
Cash, end of year	<u>\$ 45,048</u>	<u>\$ 77,560</u>
Reconciliation of operating loss to net cash used for activities:		
Loss from operations	\$ (253,157)	\$ (224,247)
Adjustments to reconcile loss from operations to net cash used for operating activities		
Depreciation	183,184	182,184
(Increase)/decrease in assets		
Due from Grantor	10,278	--
Trade receivables	(15,890)	9,140
Employee receivables	(1,358)	633
Prepaid expense	57,387	(69,220)
Increase/(decrease) in liabilities		
Accounts payable	(6,079)	1,645
Accrued payroll and other	795	(612)
Net cash used for operating activities	<u>\$ (24,840)</u>	<u>\$ (100,477)</u>

See accompanying notes to financial statements

YAP FISHING AUTHORITY

Schedule of Expenditures of Federal Awards
Years ended September 30, 2005 and 2004

Grantor/CFDA #/Grantor's Program Title	CFDA #	FY05 Expenditures	FY04 Expenditures
Federal Emergency Management Agency Grant FEMA-FM-DR1511 Typhoon Sudal Public Assistance Grant – Yap Fishing Authority (Note 1)	83.516	\$1,328	\$10,278
TOTAL FEDERAL AWARDS EXPENDED		\$1,328	\$10,278

Note (1):

The FEMA Grant is passed through the FSM National Government to the State of Yap. The amount received by YFA was the result of reimbursement claims submitted to the Division of Yap State Finance.

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity – The Yap Fishing Authority (YFA), an enterprise fund of the State of Yap, was created in 1979 pursuant to Yap State Law (YSL) No. 6-13. The primary objective of YFA is to promote, develop, and support commercial utilization of living marine resources within the State of Yap.

YFA is governed by a five-member Board of Directors appointed by the Governor with the advice and consent of the State Legislature.

Basis of Accounting – YFA utilizes accounting principles generally accepted in the United States of America as is applicable to proprietary funds of governmental entities. Such funds are accounted for using the flow of economic resources measurement focus. Thus, revenues are recorded when earned and liabilities at the time expenses are incurred.

Accounting Standards – Government Accounting Standards Board (GASB) Statement No. 20, “Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting” requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principle Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. YFA has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

GASB Statement No.34 (*Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*) establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into four net asset categories:

- (a) **Invested in capital assets, net of related debt** - Capital assets, net of accumulated depreciation, and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets)
- (b) **Nonexpendable** – Net assets subject to externally imposed stipulations that require the YFA to maintain them permanently.
- (c) **Expendable** – Net assets whose use by the YFA is subject to externally imposed stipulations that can be fulfilled by actions of the Bureau pursuant to those stipulations or that expire by the passage of time.
- (d) **Unrestricted** – Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

The YFA does not have restricted net assets as at September 30, 2005 and 2004.

GASB No. 34 establishes a new financial reporting model that includes management’s discussion and analysis, which is required supplementary information to the basic financial statements, and the presentation of net assets and changes in net assets in comparative financial statements.

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

Concurrent with the implementation of GASB 34, YFA also adopted GASB Statement No. 33 (*Accounting and Financial Reporting for Non-exchange Transactions*). Statement No. 33 defines and classifies non-exchange transactions into four categories and establishes the timing of recording of each category of transactions in the financial statements. Hence, operating grants received by YFA from the State of Yap are classified as voluntary non-exchange transactions as defined by GASB Statement No. 33. Thus, the grants are reported on the accompanying Statements of Revenues, Expenses and Changes in Net Assets as non-operating revenue, regardless whether such grants are used to acquire capital assets. Before the adoption of this accounting pronouncement, YFA recorded as additions to contributed capital, the portion of operating grants used to acquire capital assets.

New Accounting Standards – For fiscal year 2005, YFA implemented GASB Statement No. 40, *Deposit and Investment Risk Disclosures (an amendment to GASB Statement No. 3)*. The impact of GASB Statements No. 40 was not significant to the financial statements.

For fiscal year 2006, YFA will be implementing GASB Statement No. 46, *Net Assets Restricted by Legislation*. Management does not anticipate that implementation of GASB Statement No. 46 will have a material financial statement impact.

Cash – For purposes of the balance sheet and statement of cash flows, cash represents cash on hand and cash on deposit in a bank account. All of the balances at September 30, 2005 and 2004 are fully collateralized as such are subject to Federal Deposit Insurance Corporation (FDIC) coverage.

Depreciation – Property and equipment is stated at cost less accumulated depreciation. Routine maintenance and repairs are expensed as incurred. Depreciation is recorded in the financial statements using the straight-line method over the estimated useful lives of the assets as follows:

Buildings	3-20 years
Dock	40 years
Fishing fleet	10 years
Refrigeration & cold storage equipment	5-10 years
Motor vehicles	5-20 years
Other equipment	2-10 years
Other capital assets	2-10 years

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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.

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

2. INVESTMENT IN UNCONSOLIDATED SUBSIDIARY

At September 30, 2005 and 2004 YFA holds an investment in an unconsolidated joint venture with the National Fisheries Corporation. YFA has a 50% interest in Yap Fresh Tuna Inc. with a carrying value of \$398,016 and \$395,274 at September 30, 2005 and 2004, respectively.

In the prior years, by virtue of its management agreement with Yap State, NFC was considered to be the controlling partner; hence, YFTI was consolidated with NFC's financial statements and was carried on the equity method in YFA's financial statements.

In fiscal year 1999, NFC's management of YFTI was discontinued. Therefore, the State of Yap, through YFA, is now the controlling partner. Audits of YFTI for the years ended September 30, 2005, 2004 and 2003 have not been finalized to allow for consolidation. Adjustments to the investment account for fiscal years 2005 and 2004 are based on unaudited results of YFTI's operation. (See Note 15).

3. DUE FROM GRANTOR

In fiscal year 2004, as a result of Typhoon Sudal, YFA suffered major damages to its buildings and equipments and lost 100% of its fleet of fishing vessels. YFA sought assistance from the U.S. Federal Emergency Management Agency under FEMA DMR 1511 for the repair of the buildings and replacement of the fishing vessels. In addition, YFA was tasked under project worksheet (PW #381) to assist the U.S. Army divers remove and dispose of YFA's sunken fishing vessels at the harbor area. Total reimburseable expenses incurred by YFA under PW #381 at September 30, 2004 totaled \$10,278. The amount is recorded as a receivable due from grantor and intergovernmental contribution on the accompanying financial statements.

4. TRADE RECEIVABLE

A summary of trade receivables at September 30, 2005 and 2004 is presented below:

	<u>2005</u>	<u>2004</u>
Regular trade customers	\$ 458,887	\$ 444,272
Affiliates of YFA	107,160	108,684
Yap State departments and agencies	24,782	11,298
Officers and employees	19,437	36,774
	<u>610,266</u>	<u>601,028</u>
Less: allowance for doubtful accounts	<u>(588,506)</u>	<u>(595,158)</u>
Trade receivables, net	<u>\$ 21,760</u>	<u>\$ 5,870</u>

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

5. EMPLOYEES RECEIVABLE

A summary of employees' receivable is presented below:

	<u>2005</u>	<u>2004</u>
Employees receivable	39,040	\$ 25,395
Less: allowance for doubtful accounts	<u>(37,682)</u>	<u>(25,395)</u>
	<u>\$ 1,358</u>	<u>\$ --</u>

6. PROPERTY AND EQUIPMENT

A summary of property and equipment as of September 30, 2005 and 2004 is as follows:

	<u>Beginning Balance October 1, 2004</u>	<u>Transfers and Additions</u>	<u>Transfers and Disposal</u>	<u>Ending Balance September 30, 2005</u>
Buildings	\$ 1,600,000	\$	\$	\$ 1,600,000
Dock	2,629,778			2,629,778
Fishing fleet Refrigeration & cold storage equipments	269,986			269,986
Motor vehicles	122,799	6,000		128,799
Other equipment	122,404			122,404
Other capital asset	1,159			1,159
Total cost	<u>4,746,126</u>	<u>6,000</u>	<u> </u>	<u>4,752,126</u>
(Less): Accumulated depreciation	(2,706,983)	(183,184)		(2,890,167)
	<u>\$ 2,039,143</u>	<u>\$ (177,184)</u>	<u>\$</u>	<u>\$ 1,861,959</u>

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

PROPERTY AND EQUIPMENT (cont.)

	Beginning Balance October 1, 2003	Transfer and Additions	Transfer and Disposal	Ending Balance September 30, 2004
Buildings	\$ 1,651,117	\$	\$ (51,117)	\$ 1,600,000
Dock	2,629,778			2,629,778
Fishing fleet	1,261,017		(1,261,017)	
Refrigeration & cold storage equipments	286,352	14,017	(30,383)	269,986
Motor vehicles	180,360		(57,561)	122,799
Other equipment	58,249	114,865	(50,709)	122,404
Other capital asset	52,842		(51,684)	1,159
Total cost	6,119,715	128,882	(1,502,471)	4,746,126
(Less): Accumulated depreciation	(3,898,368)	(182,184)	1,373,569	(2,706,983)
	<u>\$ 2,221,347</u>	<u>\$ (53,302)</u>	<u>\$ (128,902)</u>	<u>\$ 2,039,143</u>

Depreciation expense recognized for both fiscal years ended September 30, 2005 and 2004 is \$182,184.

7. DUE TO AFFILIATE

During fiscal year 2000, YFA added a donated used tuna long-liner to its fleet of fishing vessels. In February 2000, YFA commissioned the Yap Fresh Tuna Inc. (YFTI), a 50% owned subsidiary, to outfit, staff, and manage the fishing vessel for commercial fishing. YFTI intermittently bills YFA for expenses incurred in operating the boat. In fiscal year 2003, the fishing vessel was no longer in operation and therefore, no transaction was ever recorded in fiscal year 2004. As of September 30, 2005 and 2004, the inter-company payable to YFTI for expenses incurred and revenues earned in the operation of the boat during fiscal 2002 and 2003 is \$41,945.

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

8. CONTINGENT LIABILITIES

As of September 30, 2004 and 2003, YFA possessed a majority interest in the company of Yap Fresh Tuna, Incorporated. The minority shareholder in that company is the National Fisheries Corporation. YFTI has at all times maintained its own Board of Directors. YFTI, in turn, entered into a partnership agreement with Micronesia Petroleum Company (of Kosrae) in 1998. The venture, named MPC-Yap, continues to date. The MPC-Yap partnership has maintained its own Board of Directors at all times. In 2002, disagreements arose between MPC-Kosrae directors and Yap directors and operators of MPC-Yap. The disagreements were negotiated over time and a Memorandum of Understanding was signed on or about September 12, 2003, under which MPC-Yap would be dissolved or transformed. Litigation was threatened by MPC-Kosrae before the agreement and has been threatened if the terms of the agreement are not met.

The agreement was reaffirmed on or about September 8, 2005, with payment terms from YFTI included for YFTI to buy out MPC-Kosrae's 55% interest in partnership for a total of \$200,000, spread out over less than one year. If such information is correct, YFA's ownership interest may be estimated at about 27%. YFA's potential liability in YFTI is limited to the capital already contributed, as it was legally incorporated and no specific allegation has yet been made to pierce the corporate veil. Therefore, no claim described herein has been asserted directly against YFA. The financial information provided by MPC-Yap could not be relied on and therefore, YFA's investment in MPC-Yap could not be determined.

9. RISK MANAGEMENT

YFA is self-insured for all risks. Any loss or liability that may result upon occurrence of a natural disaster, accident or litigation will be borne entirely by YFA.

FEMA approved grant authorization for eight YFA projects worth \$339,093 under FEMA FM-DR-1511. Included in the amount is \$150,000 for the F/V Mailap, approved with the condition that YFA must first obtain and submit to FEMA proof of insurance coverage for the vessel. Project worksheets for the remaining two vessels with a combined total of \$198,000 are still pending approval upon submission of YFA's proof of insurance coverage to FEMA. Management is of the opinion that YFA cannot afford insurance coverage for the vessels. The State of Yap is currently negotiating with FEMA to waive the insurance requirement. If the State of Yap is not able to successfully negotiate a waiver from FEMA, YFA or the State of Yap may have to fund the replacement cost of the three fishing vessels worth \$348,000.

10. DONATIONS AND OTHER CONTRIBUTIONS

YFA was the recipient of the 2003/2004 Goods and Services Foreign Aid Assistance Package from the Government of Japan to the Federated States of Micronesia. Accordingly, donated equipments and tools worth \$120,547 received by YFA in November 2003 and February 2004 are included in property and equipment in the accompanying financial statements for the year ended September 30, 2005 and 2004.

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

In August 2004, YFA received \$69,220 from the Fisheries Extension Service Assistance Project funded by the Japan Overseas Fisheries Cooperation Foundation for the implementation of Fishing Recovery Project in Yap. The funds were intended for the purchase of a vehicle, outboard motor boats and fishing gears to be rented by YFA to community fishermen to allow them to fish and sell their catch back to YFA for an income. YFA advanced the total amount of \$69,220 to two local vendors for the purchase of the required assets. At September 30, 2005 and 2004, the balance of the purchase advance was \$11,833 and \$69,220, respectively.

12. OPERATING SUBSIDY

In September 2004, Yap State Legislature appropriated \$81,000 from the General Fund of Yap State under YSL 6-32 to subsidize the operation of YFA

13. INVENTORY LOSS

In fiscal year 2004, the value of fishing gear inventory was written off resulting in a loss of \$7,972.

14. TYPHOON LOSS

In fiscal year 2004, through the effects of Typhoon Sudal, YFA suffered major damages to its buildings and equipments and lost 100% of its fleet of fishing vessels, as well as its spare parts inventory. Management prepared and submitted applications for FEMA Public Assistance Funding through the Yap State Government to which U.S. FEMA approved grant authorizations for eight YFA projects worth \$339,093. Included in the amount is \$150,000 for the *F/V Mailap* approved with the condition that YFA must first obtain and submit to FEMA proof of insurance coverage for the vessel. Project worksheets for the remaining two vessels with a combined total of \$198,000 are still pending approval upon submission of YFA's proof of insurance coverage to FEMA. During the year ended September 30, 2004, an adjustment to write off the value of spare parts inventory damaged by the storm. In addition, a loss of \$128,311 was recognized for the net book value of the fishing vessels and other assets damaged by Typhoon Sudal.

15. LOSS ON INVESTMENT IN UNCONSOLIDATED SUBSIDIARY

YFA holds 50% of the shares of Yap Fresh Tuna, Inc. (See Note 2). Condensed unaudited financial information for YFTI for the years ended September 30, 2005 and 2004 are as follows:

Balance sheet:	<u>2005</u>	<u>2004</u>
Current assets	\$ 110,924	\$ 104,080
Property, plant and equipment	4,105,747	4,105,747
	<u>4,216,671</u>	<u>4,209,827</u>

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

Current liabilities	1,160,416	1,159,057
Long-term debt	3,708,641	3,708,641
Stockholder's equity	<u>(652,386)</u>	<u>(657,871)</u>
	<u>\$ 4,216,671</u>	<u>\$ 4,209,827</u>
Statement of revenue & expenses		
Sales	13,545	28,078
Cost of sales	--	--
Operating expenses	<u>(8,061)</u>	<u>(32,994)</u>
Net income (loss)	<u>\$ 5,484</u>	<u>\$ (4,916)</u>

16. OTHER EXPENSES

Provided below is the breakdown of Other Expenses for the years ended September 30, 2005 and 2004:

	<u>2005</u>	<u>2004</u>
Gagil-Maap Grassroots project	\$ 43,127	\$ 28
Workshop expense	8,543	7,573
Communication	5,165	8,904
Miscellaneous	4,171	7,447
Cold storage expenses	3,256	35,764
Office supplies	2,878	1,543
Representation and entertainment	<u>1,208</u>	<u>1,037</u>
	<u>\$ 68,348</u>	<u>\$ 62,296</u>

17. IMPAIRMENT LOSS IN PMAIR

YFA purchased 20 shares of the common stock of Palau Micronesia Airlines (also known as Palau Rock Island Air) for \$2,000 during the year ended September 30, 2003. The shares had no stated par value. In December 23, 2004, the airline suddenly suspended its operations to reorganize and reevaluate its business strategy. It is not known when or if the airline will resume operation, therefore, YFA recorded the impairment loss of \$2,000 at September 30, 2004.

YAP FISHING AUTHORITY

Notes to Financial Statements
September 30, 2005 and 2004

18. SUBSEQUENT EVENTS

In October 2005, the Japan Government through Fisheries Development Association of the Pacific Island Nations (FDAPIN) donated equipments and spare parts worth \$25,774 to replace YFA cold storage and shop equipments damaged by Typhoon Sudal.

In a March 2006 visit to Yap, the President/CEO of the National Fisheries Corporation (NFC), proposed to YFA (and its sole owner, the State of Yap) that NFC pull out of YFTI in its entire ownership and freely transfer all its rights and obligations in YFTI to YFA. The Office of the Governor plans to hold a series of meetings with interested parties in Yap to consider the appropriate State of Yap response to the NFC's proposal.



**OFFICE OF THE PUBLIC AUDITOR
STATE OF YAP
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**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED UPON THE AUDIT IN ACCORDANCE WITH
*GOVERNMENT AUDITING STANDARDS***

To the Board of Directors of
Yap Fishing Authority:

I was engaged to audit the financial statements of the Yap Fishing Authority (YFA), as of and for the year ended September 30, 2005, and have issued my report thereon dated September 7, 2006, which report was a disclaimer due to scope limitations presented by inadequate accounting records and lack of concrete action taken by management to address findings and recommendations of an agreed-upon-procedures engagement dated October 12, 2005 and the audit of fiscal year 2004, the unavailability of audited financial data for the Yap Fresh Tuna, Inc. (YFTI), a 50% owned subsidiary, and management's discussion and analysis which, although not a required part of the basic financial statements, is supplementary information required by the Government Accounting Standards Board. I conducted the audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting


In planning and performing my audit, I considered the YFA's internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing my opinion on the financial statements and not to provide assurance on the internal control over financial reporting. My consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Of the matters reported to management in the Schedule of Findings, we consider Findings Nos. 3 and 5 to be material weaknesses.

Compliance

As part of obtaining reasonable assurance about whether the YFA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended for the information of the management and Board of Directors of the Yap Fishing Authority and is not intended to be and should not be used by anyone other than these specified parties.

A draft copy of this report was submitted to the Chairman of the Board and the acting manager of Yap Fishing Authority on May 30, 2006. We later met with the Chairman of the Board and certain staff members of the Yap Fishing Authority on December 5, 2006 to discuss the draft report, after which we solicited written comments from the management on the findings contained in the report. Despite repeated follow up, YFA was unable to submit written comments on the audit findings and recommendations, therefore, this report is issued without management's response.


Gertrude Gootinan
Yap State Public Auditor

September 7, 2006

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

FINDING NO. 1 – UNAVAILABLE MEETING MINUTES

Criteria: The Board of Directors has a responsibility to ensure that written documentation of the proceedings of each of their meetings is maintained on file for future reference.

Condition: Our review of the Board meeting minutes found that minutes for only four meetings held during fiscal year 2005 were prepared and made available on file at YFA. The minutes were for meetings held on October 13, 2004, March 3rd & 7th, and July 25th, 2005. We were aware of several meetings also held by the Board in fiscal year 2005, for which minutes were not prepared.

Cause: The person designated by the Board to act as secretary was not herself a member of the Board and, therefore, was under no obligation to attend meetings. In her absence at Board meetings, the Chairman did not assign another board member to take and transcribe minutes.

Effect: Written documentation of proceedings of the Board were not available to ensure that decisions and actions taken by officers and employees were conducted within the confines of their legal authority.

Recommendation: In order for the Board and management to be accountable for the decisions they have made and contribute to improving government transparency, minutes of the Board meetings must be taken and filed, without exception.

Prior Year Status: A repeat finding raised in the audit report for the year ended September 30, 2004.

FINDING NO. 2 – INADEQUATE CONTROL OVER GRANT FUNDS

Criteria: As a grantee agency, YFA has the primary responsibility to ensure that special grants entrusted to its care are safeguarded against loss and abuse and are expended in accordance with program objectives.

Condition: On August 26, 2004, YFA received \$69,220 from the Japan Embassy for the Grassroots fishing project. YFA requested price quotations from two local vendors for fishing equipment and other supplies identified to be necessary. Upon receipt of the quotations, YFA proceeded to advance \$57,710 to one vendor and \$11,510 to the other for a combined advanced sum of \$69,220, the total grant funding received. Soon thereafter, YFA changed the scope of the project negating the need for some of the supplies and equipment ordered. The vendors were notified to revise the order list, but were not required to submit the balance of the purchase order advance. As of September 30, 2005, \$54,382 and \$3,000 had been expensed of the balances advanced. Cash balances of \$3,328 and \$8,000 remain with the two vendors. Both vendors stated they were willing to refund the balances to YFA upon request from the Embassy of Japan and/or official request from YFA management. But, YFA did not request reimbursement until the middle of 2006, but only after repeated follow-up by our office.

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

Finding No. 2: Inadequate Control over Grant Funds (cont.)

Cause: Except for extreme cases, disbursement of grant funds should only be effected after receipt of goods and the final supplier invoice. This would avoid the situation discussed in the condition above.

Effect: Depositing cash with vendors increases the risk that unauthorized purchases could be made against the fund balance. Moreover, expenses are misstated when payments are made based on price quotations and recorded as expenses in the accounting records.

Recommendation: We recommend that the Acting General Manager ensure that payments are made for goods only after receipt of goods and final supplier invoice.

Prior Year Status: A repeat finding raised in the audit report for the year ended September 30, 2004.

FINDING NO. 3 – TRANSACTIONS WITHOUT ECONOMIC BASIS

Criteria: Accounting principles generally accepted in the United States of America require that transactions recorded in the general ledger must be based on actual business transactions.

Condition: Our review of YFA's general ledger found some transactions were not recorded properly to reflect its true nature. For instance, adjustments were made to the receivable account and referenced to the cash receipt journal, but without actual receipt of cash. Similarly, adjusting entries were also made to the sales journal without actual sales. The accountant who resigned in February 2005 explained the entries were adjustments she made to reconcile the customers' subsidiary ledger with the general ledger. Although the adjustments had zero net effect on the general ledger, such entries inflated sales significantly.

Cause: YFA utilizes *Peachtree Accounting* to maintain its general ledgers. The software would only increase the trade customers' subsidiary ledger through the sales journal and decrease it through the cash receipts journal. YFA employees owed substantial amounts from sales on credit and cash loans in the prior years and even at September 30, 2005. Employees paid the balances due YFA through payroll allotments. According to the accounting clerk, the payroll journal could not post transactions to the customers' subsidiary ledger, hence the adjustments she made to reconcile the subsidiary ledgers to the general ledger to consider the payments received through payroll allotments. Because inadequate supporting documentation was available to justify the adjustments she made to the general ledger, we could not determine that the adjustments were valid.

Effect: The general ledger account balances appear reconciled but the information contained therein is not reliable because adjustments were not based on real economic events. We had previously recommended that management prevent employees from obtaining sales on credit and cash advances beyond their ability to repay each pay period. Yet, such practices continue. Consequently, the employees are robbing the Authority of much needed cash needed to sustain the daily operations. Because each of the employees owed considerable balances to YFA, there is an increased risk of improper adjustments to the general ledger.

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

Finding No. 3 – Transactions without Economic Basis (Cont.)

Recommendation: We recommend that the Board of Directors direct the employees of YFA, including the acting general manager to cease from obtaining fish and ice on credit. In addition, the Board should require all employees to increase their payroll deductions so that outstanding balances could be repaid on a timely basis. We also recommend that the Board increase its efforts to collect balances owed by former YFA employees.

FINDING NO. 4 – RECEIVABLE FROM BOARD MEMBER

Criteria: The Board of Directors has the responsibility to establish policies to safeguard the financial interests of the entity it governs. Such policies should be applied even to board members in order for financial transactions to be conducted at arms-length.

Condition: During the year ended September 30, 2005, YFA provided equipment rental to one board member for a personal business venture. The total amount owed by the board member to YFA for the equipment rental is \$26,750, \$9,000 of which was related to fiscal year 2005. The total amount was still outstanding as of September 2006 and there was no payment arrangement between the individual and YFA to ensure that the receivable was settled in a timely manner.

Cause: Management allowed the Board member equipment rental to use for his personal business on credit without a formal agreement to ensure prompt payment. The individual's position on the board may have influenced management to allow the equipment rental even though his ability to pay for the equipment was not assured. To allow YFA assets to be used in furtherance of a board member's financial interests without consideration of his ability to pay for the services constitutes abuse of power.

Effect: YFA provided \$26,750 worth of equipment rental services of which \$9,000 was related to fiscal year 2005. Without a written promissory note from the board member, there is a high risk YFA may not be able to collect the balance owed on the equipment rental services. In short, a board member benefited personally from his position on the board by acquiring the use of YFA equipment rental services free of charge.

YFA's inability to collect on past due trade accounts has been a finding in each of the Authority's past audit reports. Despite the recommendations in the past to disallow credit sales, YFA continued the same practice with the effect that the very stewards of YFA assets were the same individuals who were contributing to its financial hardships.

Recommendation: We, again, strongly recommend to the Board of Directors that sales on account for YFA goods and services be disallowed immediately. This policy should apply to YFA employees and board members, as well as third parties.

Prior Year Status: The above recommendation was issued to the Authority for the years 2000, 2001, 2002, 2003, 2004 and 2005.

YAP FISHING AUTHORITY

Schedule of Findings

September 30, 2005

FINDING NO. 5 – LACK OF A FIXED ASSET REGISTER

Criteria: Management is responsible to ensure that schedules are available to support general ledger balances.

Condition: A fixed asset register was not available to support the general ledger balances for fixed assets for the year ended September 30, 2005. The register that was submitted for our review was not inaccurately prepared. Prior year adjustments had not been posted and newly acquired assets and disposals were also not reflected in the register. Moreover beginning balances were not reconciled to the prior periods and depreciation expense was inaccurately calculated.

Cause: We learned from the accountant that the register had been maintained by the Office manager who was no longer with the Authority. Then the accountant herself resigned within weeks after our request for the register. A new accountant and a comptroller were hired a few days before the resignation of the former accountant. The new accountant tried to update the fixed asset register but was unsuccessful.

Effect: We could not determine whether the fixed asset balances reflected in the general ledger were fairly presented. The lack of a reliable fixed asset register to support the general ledger balances was a scope limitation which prevented us from forming an opinion on the fixed asset accounts.

Recommendation: We recommend that the acting general manager require employees to perform their assigned tasks. The new accountant contracted by the Board needs to start updating the fixed asset register for FY06 as soon as possible. The register should be maintained regularly to keep it manageable and not become an overwhelming task at the end of the year.

Prior Year Status:

A similar finding was also offered in the audit reports for the years ended September 30, 2004, 2003, 2002, 2001 and 2000.

FINDING NO. 6 – CHARGE ACCOUNT

Criteria: The financial management act – section 503 (3) prohibit government entities and departments from acquiring goods and services without first securing certification of the availability of funds.

Condition: Our review of YFA's payables found many transactions processed through an open charge account with a local vendor. We learned from the acting manager that the charge account was used on an "as-needed" basis. The documentation for the charges occurring in FY05 found items such as office supplies as well as questionable items that could be for personal use. According to the acting manager, the account was opened by the previous manager and had since been used for that purpose. We question why a charge account was necessary when YFA had a petty cash in FY05 of \$300; most of the purchases in FY05 made against the account were less than \$100.

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

Finding No. 6 – Charge Account (Cont.)

Cause: YFA lacks effective policies to manage its daily operations consistent with the State's financial management act. Moreover, the current manager is not effectively carrying out his responsibility to safeguard the assets of YFA and ensure compliance with the State financial management regulations.

Effect: The invoices and receipts we reviewed showed about \$2,000 worth of charges to the account at YCA during fiscal year 2005.

Recommendation: We strongly recommend that the Board of Directors immediately close the YCA charge account and require the Acting General Manager to immediately adopt the use of a purchase order system for all purchasing needs in excess of \$50. The petty cash should be used for purchases of less than \$50 but purchases over \$50 must be initiated with the preparation of a purchase order form indicating the Acting Manager's approval and certification of funds availability by the accounting office. The State purchase requisition form can be adapted by YFA for its use. After the funds certification and the manager's approval has been obtained, the purchase order/requisition could then be presented to the vendor to obtain goods and the final invoice. Check payments to vendors and suppliers should be prepared only upon receipt of the final invoice.

FINDING NO. 7 – LACK OF A VEHICLE POLICY

Criteria: YFA must have a vehicle policy in place consistent with the Government Vehicle Act to prevent misuse of Authority vehicles and to minimize vehicle-related expenses such as fuel and repair and maintenance costs.

Condition: We felt it was necessary to review fuel expense for fiscal year 2005 because we learned that YFA had prepaid fuel accounts at two gas stations, but also purchased fuel from two other fuel outlets. Furthermore, we learned that YFA lacked a vehicle policy restricting the use of Authority vehicles to official purposes only. YFA had three vehicles in FY05, a 4x4 pick up truck normally driven by the cold storage supervisor, a small pick up truck for the Grassroots Project which was exclusively driven by the acting manager, and a Jeep for general use.

Our review of fuel expenses during fiscal year 2005 found that, on average, YFA spent \$12 daily for fuel despite a decrease in operating activities that might require the use of vehicles. Generally, the vehicles were needed for ice delivery, taking care of administrative errands, and monitoring the activities of grass-roots fishery recovery project. But we found very little evidence of YFA's monitoring of the Grassroots Fishery Recovery project in fiscal year 2005 which may have required the use of a vehicle.

Cause: Management's general disregard for cost containment and the prevention of abuse of Authority assets has resulted in a lack of vehicle policy consistent with the Government Vehicle Act. For instance, employees were allowed to drive Authority vehicles for their personal commute to and from work increasing the risk that the vehicles and its fuel paid for by YFA could be used after hours for nonbusiness-related activities.

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

Finding No. 7 – Lack of a Vehicle Policy (Cont.)

Effect: Our review shows that YFA spent \$3,560 on vehicle fuel expense in FY05 compared to \$2,901 in FY04 for all vehicle and heavy equipment fuel, oil, and lubricants. The amount translates to \$12 worth of fuel per working day for the entire year an amount that we consider to be excessive, considering the level of activities ongoing at YFA during fiscal year 2005.

Recommendation: We recommend that YFA adopt a vehicle policy consistent with the Government Vehicle Act (GVA) to require all vehicles to be parked at the motor pool after working hours, which is defined by the State to be 7:30am – 4:30pm. Any exception must be properly authorized as stipulated in the Government Vehicle Act. Trip and fuel tickets must be authorized and justified before the use of a vehicle, along with an activity log that must be maintained for each vehicle.

FINDING NO. 8 – UNRECONCILED GENERAL LEDGER

Criteria: Accounting principles require the general ledger to be accurately maintained and properly reconciled on a periodic basis.

Condition: We reviewed disbursements to see if the general ledger was properly maintained. In general, disbursement was recorded accurately to the general ledger but we found exceptions of which the check amount did not agree to the amount recorded to the general ledger. There were invoices entered to the general ledger for one amount and later paid for a different amount, which result with unexplained variances. We found under and over recording to the general ledger.

Cause: The accountant was careless to record each payment to the general ledger accurately and in agreement with the underlying documentation. Given the lack of periodic reconciliation of the general ledger, errors remained uncorrected.

Effect: Among our selections of detailed transactions were two transactions that were over recorded for the sum of \$725.33 and two transactions that were under recorded for the sum of \$95.74, for the net effect of \$629.59 of over recording.

Recommendation: We recommend the Board of Directors require the management and accounting staff of YFA to prepare and maintain the Authority's financial and accounting records in accordance with generally accepted accounting standards. Such standards require periodic reconciliation of the general ledger information with sales invoices, cash receipts and disbursement records and with schedules providing details of the general ledger balance sheet accounts.

Prior Year Status: Poorly maintained accounting records has been a finding in the audit reports for YFA for the years ended September 30, 2000 through 2004.

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

FINDING NO. 9 – OUTSTANDING RECEIVABLES

Criteria: The Board of Directors is responsible for adopting policies to effect the collection of balances due to YFA, especially accounts outstanding over 365 days.

Condition: YFA had been carrying a significant amount of trade account receivables on its books. As of September 30, 2005, the amount was \$658,489 of which \$635,542 or 97% consists of outstanding trade receivables over 365 days. A large number of these accounts are over ten years old with very little supporting documentation still available at YFA to effect collection. The remaining \$22,947 or 3% are for trade receivables related to FY05. The majority of these receivables had been reserved as doubtful for many years now and the Board had not taken any decisive action to try to collect them or write them off the books. In the meantime, management continue to allow credit sales every year, even despite the Authority's dismal collection record.

Cause: YFA operated for many years without oversight from a Board of Directors. The people named to serve on the Board failed to meet regularly but were never replaced by the Governor. Finally in 2005, the Governor appointed the current Board of Directors. Given the state of the accounting records at YFA, this new Board has not addressed the issue of outstanding trade receivables.

Effect: Over half of a million dollars in customer receivables, including former and current employees of YFA is reserved as uncollectible and the amount continues to increase each year. Most of these receivables are for people who are currently employed, either by the Government or by the private sector.

Recommendation: The Board needs to make a tough decision of what to do with receivables outstanding over 365 days. If a decision is reached to pursue collection, then viable collection methods must be considered, including legal action if necessary. Otherwise, non-collectable debt must be written off the book.

Prior Year Status: YFA's inability to collect on past due accounts has been a finding in its audit reports since fiscal year 2000.

FINDING NO. 10 – INACCURATE INVOICE

Criteria: Care must be taken to ensure that accounting information is accurate.

Condition: We found during our review of receivables that a member of the Board had received about \$26,750 worth of equipment rental services from YFA in FY05 and FY06 (see also Finding #2.) Our review of the invoice YFA prepared for the equipment rental was inconsistent with supporting equipment rental log sheet kept by the Shop. The log showed ten and a half more hours than was billed on the invoice for unbilled services worth \$525.

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

Finding No. 10 – Inaccurate Invoice (Cont.)

Cause: The accountant was careless in preparing the invoice and did not take the time to review and verify the log sheet details to make sure it matched the invoice. Because there was no secondary review of work performed by the accountant, the error went undetected.

Effect: YFA billed the customer (member of the Board) \$525 less than it should have for equipment rental.

Recommendation: We recommend that since the Board hired an individual and gave him the title of Comptroller, the general manager require the individual to review the work of the accounting staff to ensure that accounting information is accurate and complete.

FINDING NO. 11 – FORGIVEN DEBT

Criteria: The Board of Directors must act in the best interest of YFA.

Condition: In our attempt to confirm outstanding balances of some trade receivables, we learned that balance owed by the Office of Planning and Budget of \$8,065 was forgiven by the Board in response to a waiver request initiated by the Director of OPB. The waiver essentially requested YFA to forgive OPB's debt on the basis that both entities belong to the same government therefore unnecessary to transfer fund from one account to another. The Office of Planning & Budget is one of many departments that owe money to YFA

Cause: The Board of Directors decided to forgive OPB's debt on the basis that the transaction was unnecessary between Government entities and components, without regards to the primary objectives of setting up YFA as an enterprise fund to generate revenue through sales to the public and other governmental entities.

Effect: The Board's decision to forgive OPB's debt might set precedence for other departments and agencies to contest paying their debt which would not in the best interests of YFA.

Recommendation: We recommend to the Board to seriously consider the basis and implications of debt forgiveness before taking any such action. Moreover, we recommend that the Board require OPB to repay all balances due to YFA since by not requiring OPB to pay for the goods and services it received from YFA, YFA would in essence be footing part of the cost of the operations of the Office of Planning and Budget.

FINDING NO. 12 – ANNUAL LEAVE BALANCES

Criteria: YFA should have a leave policy in place or at least follow the Yap State Government policy on annual leave accruals.

Condition: Our review of annual leave payable found that employees who were no longer employed at YFA still had leave balances worth \$1044.80 as of September 30, 2005.

YAP FISHING AUTHORITY

Schedule of Findings September 30, 2005

Finding No. 12 – Annual Leave Balances (Cont.)

It was noted in FY04 audit that a former employee contested repaying his receivable until it was adjusted with the balance of his annual leave. The matter was not resolved and carried on to FY05. It was evident from our discussion with the new management that YFA had all along a personnel manual in which leave policies were explained, but it had been misplaced and, therefore, had not been followed for several years.

Cause: Apparently, management and the office staff did not know the whereabouts of the personnel manual and therefore were not clear what YFA's leave policy was. According to a former office manager, a former manager took away the manual to revise it but never return it. As a result, YFA had no guidelines specifying leave policy. Recently, a copy of the personnel manual was found among some old records. According to the acting general manager, it would require only minor changes to restore it as the personnel policy manual for the Authority.

Effect:

Annual leave balances of former employees were not settled after the end of their employment with YFA which increases potential liability to the Authority.

Recommendation:

The Board of Directors should review and revise the existing personnel policy manual as necessary to ensure consistency with personnel and other policies of the Yap State Government and formally adopt it for the Authority.

Prior Year Status:

Related finding was also offered in the audit report for the year ended September 30, 2004.