

Yap Traditional Navigation Society

Financial Statements and Independent Auditor's Reports

For The Years Ended
September 30, 2007, 2008, and 2009



**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Years Ended
September 30, 2007, 2008, and 2009

TABLE OF CONTENTS

Independent Auditor's Report	1
Schedules of Cash Receipts and Disbursements	2
Notes to Financial Statements	3
Independent Auditor's Report on Internal Control	6
Schedule of Findings and Responses	8



**OFFICE OF THE STATE PUBLIC AUDITOR
YAP STATE GOVERNMENT**

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Yap Traditional Navigation Society

We were engaged to audit the accompanying statements of cash receipts and disbursements of the Yap Traditional Navigation Society (TNS) for the fiscal years ended September 30, 2007, 2008, and 2009. These financial statements are the responsibility of the management of TNS.

Because of inadequacies in TNS' accounting records, we were unable to form an opinion regarding the completeness of the amounts recorded in the accompanying statement of cash receipts and disbursements.

Due to the significance of the matter discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements referred to in the first paragraph.

As described in note 2, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

A handwritten signature in black ink, appearing to read "Ronald C. Yow", is written over a faint, illegible stamp.

Ronald C. Yow
Acting Yap State Public Auditor

September 16, 2011

YAP TRADITIONAL NAVIGATION SOCIETY

Statements of Cash Receipts and Disbursements

For the Fiscal Years ended September 30, 2007, 2008, and 2009

	<u>Year Ended</u> <u>2007</u>	<u>Year Ended</u> <u>2008</u>	<u>Year Ended</u> <u>2009</u>
Receipts			
Grant Proceeds	\$ 27,000	\$ 13,500	\$ 9,920
Yap State Government appropriation	-		30,600
Sale of Canoe - net	-	-	10,738
Interest	145	131	51
Contract services	-	8,400	2,800
Other	462	11,898	4,706
	<u>27,607</u>	<u>33,929</u>	<u>58,815</u>
Disbursements			
Contractual services	-		30,600
Instructor Fees	11,781	8,300	987
Student Stipends - net	3,098	20,622	4,756
Travel		734	
Promotion	2,442	-	-
Materials and Supplies	1,219	4,370	14,407
Buildings and Facilities	6,169	1,115	283
Office supplies	3,392	376	42
	<u>28,101</u>	<u>35,517</u>	<u>51,075</u>
Net change in cash	(494)	(1,588)	7,740
Cash at beginning of year	<u>12,643</u>	<u>12,149</u>	<u>10,561</u>
Cash at end of year	<u>\$ 12,149</u>	<u>\$ 10,561</u>	<u>\$ 18,301</u>

See accompanying notes to financial statements

**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Notes to Financial Statements
Fiscal Years Ended September 30, 2007, 2008 and 2009

(1) Organization

The Yap Traditional Navigation Society (TNS) is a nongovernmental not for profit organization incorporated under Title 23 of the Yap State Code. The primary goal of TNS is to ensure that the traditional navigation and canoe building practices, an essential part of Yap culture, are promoted and preserved. To achieve this goal, TNS founded the Yap Traditional Maritime Institute (TMI), which is dedicated to the revitalization and perpetuation of the traditional Yapese art of canoe building, sailing, and navigation. Instruction includes sailing theory and navigation skills, history of sailing and its role in Yapese history, practical courses in canoe building, and how the skill of Yapese sailing can be utilized today.

(2) Summary of Significant Accounting Policies

Basis of Accounting

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. TNS uses the cash basis of accounting. Under this method of accounting, transactions are recognized as receipts or disbursements, and noncash transactions are not recognized. The cash basis differs from accounting principles generally accepted in the United States of America primarily because receipts (revenues) are recognized when received rather than when earned and disbursements (expenses) are recognized when paid rather than when the obligation is incurred.

As described above, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

Cash

Custodial credit risk is the possibility that in the event of a bank failure TNS' deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution but not in the depositor's name. TNS does not have a deposit policy for custodial credit risk.

For the purpose of the statements of cash receipts and disbursements, cash is defined as cash in checking accounts and savings accounts. As of September 30, 2007, 2008, and 2009, \$12,149, \$10,561, and 18,301 respectively of cash was maintained in one financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance.

**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Notes to Financial Statements
Fiscal Years Ended September 30, 2007, 2008 and 2009

(3) Grants

In April 2009, TNS received a grant of \$9,920.25 under the Australian Government's AusAID Small Grants Scheme (SGS) for traditional canoe building and sailing in Ulithi. Another Ausaid grant for \$16,200 to fund community based traditional canoe building for Yapese youths was received in 2010.

TNS received a private sector development grant of \$54,000 in 2006. Funds were provided to the State of Yap through grants and loans from Asian Development Bank (ADB). The Workforce Enrichment Division (WED) of the Department of Resources and Development (R&D) was charged with determining the best use of these funds. In accordance with a Memorandum of Understanding (MOU) with R&D, a partial allocation of the funds was awarded to TNS, with payment in four installments. Payments of \$13,500, \$27,000, and \$13,500 were recorded by TNS in fiscal years 2006, 2007, and 2008 respectively. TNS used the funds to found the Maritime Institute.

(4) Contract Services

The Yap State Government in 2007 engaged TNS to reconstruct a canoe damaged by Typhoon Sudal. Pursuant to an agreement executed between TNS and the Office of Planning and Budget (OPB), TNS was contracted to receive \$11,200 in compensation for providing all supervision, labor, and materials for all work connected with the project entitled Maap Bechiyal Canoe Chugpin Project. Funding was initially provided to Yap through the U.S. Federal Emergency Management Administration (FEMA). TNS received payments of \$8,400 and \$2,800 in fiscal years 2008 and 2009 respectively.

(5) Yap State Appropriation

TNS received education sector appropriations from the Yap State Government of \$61,896 in 2009. The appropriations, allotted from the Special Revenue Fund, were designated for the purpose of funding new programs. TNS expended \$30,600 of this amount in fiscal year 2009. A further \$28,444 was subsequently expended in 2010.

(6) Sale of Canoe

In fiscal year 2009, TNS sold a full size fishing canoe to the Linden Museum in Stuttgart Germany. The museum purchased the canoe as part of an exhibition to mark the 100th anniversary of the legendary South Seas Expedition by the Hamburg Museum in 1909-10.

YAP TRADITIONAL NAVIGATION SOCIETY
Notes to Financial Statements
Fiscal Years Ended September 30, 2007, 2008 and 2009

The sale is reflected in the Statement of Cash Receipts and Disbursements net of related shipping and other costs of \$4,262.

(7) Other Cash Receipts

Consist principally of payments received from canoe tours and fees and donations collected at festivals and special events.

(8) Management Agreement

A consulting firm was engaged in October 2009 to manage the daily operations of TNS and its maritime institute, TMI. The consulting firm was paid \$6,432 from funds appropriated by the state for its services in fiscal 2010. The owner of the consulting firm, who is also a State employee, had previously performed management functions as a volunteer.

(9) Student Stipends

Traditional navigation instruction is conducted through TNS' maritime institute, TMI, free of charge. Educational allowances are provided to individuals who train as apprentices. The amount of the allowance of \$2,150 is payable in ten installments. The allowance is meant to assist with transportation costs and classroom material expenses.

(10) Related Parties

Several members of the BOD and officers of TNS hold management positions and other positions of influence with Yap State. TNS has also entered into significant transactions with members of the BOD, and with others within the organization, as discussed in Note 8.

(11) Risk Management

TNS is self-insured for all risks. Any loss or liability that may result upon the occurrence of a natural disaster, accident or litigation will be borne entirely by TNS. Management is of the opinion that no material losses have been sustained as a result of this practice during the past three years.

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL

To the Board of Directors of
Yap Traditional Navigation Society

We were engaged to audit the financial statements of the Yap Traditional Navigation Society (TNS) for the fiscal years ended September 30, 2007, 2008, and 2009 and have issued our report thereon dated September 16, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered TNS's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of TNS's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of TNS's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying *Schedule of Findings and Responses*, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct material misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of TNS's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying *Schedule of Findings and Responses* as Finding No. 1 through No. 4 to be material weaknesses.

A significant deficiency is a deficiency or combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged

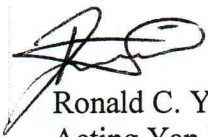
with governance. We consider the deficiencies described in the accompanying *Schedule of Findings and Responses* as Findings No. 5 and No. 6 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether TNS's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 or other matters required to be reported.

We noted certain matters that we reported to the management of TNS in a separate letter dated September 16, 2011.

This report is intended for the information of the Board of Directors, management, and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.



Ronald C. Yow
Acting Yap State Public Auditor

September 16, 2011

**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Schedule of Findings and Responses
Fiscal Years Ended September 30, 2007, 2008 and 2009

Finding No. 1 – Segregation of Duties

Criteria: Proper separation of responsibilities ensures that the work of one individual acts as a check on the work of another in the performance of incompatible functions. Persons who handle cash or other forms of payment, such as signed checks, should have no incompatible duties with respect to the recording of receipts and payables or reconciliation of cash.

Condition: The office assistant prepares and records invoices, receives and records payments, makes deposits, and maintains cash on hand. Notwithstanding bank signatory authority rests with the Treasurer who is a member of the BOD, the office administrator prepares checks in payment of vendor invoices, delivers them to the Treasurer for signature after which they are returned to this same individual, who also mails/delivers the checks to vendors.

Cause: TNS has only one administrative employee and a manager to perform all office functions.

Effect: Failure to maintain adequate segregation of duties over payments could result in misappropriation of assets or errors that go undetected or are not timely detected

Recommendation: To reduce the risk of error and ensure adequate custody and control over cash receipts and disbursements, implement the following:

- Separate the functions of receiving and recording of cash receipts and disbursements. We understand staff size is limited. However functions may be rotated among staff.
- Closer oversight and supervision of financial transactions by the Treasurer and Board of Directors. For example, in many small organizations, it is the Treasurer that maintains the accounting records and performs bank reconciliations.

Management Response and Corrective Action Plan:

Agree, although, due to the limited staff it is difficult to separate responsibilities to different individuals. TNS Board Member/Treasurer will assist the office staff with supervising financial transactions. TNS will seek out possible intern from the local community college or other volunteer that can assist with recording cash receipts and disbursements. Planned completion date is January 2012.

YAP TRADITIONAL NAVIGATION SOCIETY
Schedule of Findings and Responses
Fiscal Years Ended September 30, 2007, 2008 and 2009

Finding No. 2 – Cash and Unrecorded Transactions

Criteria: Because cash and cash equivalents are so liquid and transferable, the risk of theft is greater than for any other asset. Cash includes cash on hand and balances with financial institutions that are immediately available for any purpose. Additionally, principles of accounting generally provide that, based on the method of accounting used, that the financial statements reflect the economic substance of transactions that occur in each accounting period reported on.

Condition: Controls over and the proper accounting of cash are lacking as follows:

- A supply of cash is maintained on hand in the office to make payments in cash. The payments are typically for small purchases, urgent items, or for payees who are in areas or locations where checks are not accepted, e.g., outer islands. The payments are made from cash collected from such activities as canoe tours. Accordingly, some of the receipts and disbursement noted above have improperly not been given accounting recognition.
- There are no procedures to verify the amount of cash and checks received to the amount deposited. Deposits are made on an irregular basis. Checks received are not immediately endorsed, only endorsed when deposited. TNS does not always issue a receipt to customers and half are unnumbered.

Cause: The limited number of staff and high turnover, coupled with a desire to accommodate those from the outer islands and others who normally only transact business in cash may have compelled TNS to follow this practice.

Effect: A lack of adequate control over cash and cash transactions could result in theft or misappropriation. Additionally, failure to record the effects of financial transactions, such as the collection of unrecorded sales and the settlement of liabilities in cash, may result in the misstatement of financial information.

Recommendation: Prohibit the practice of using cash to settle liabilities and ensure all transactions are properly recorded. In addition, ensure that:

- Prohibit the practice of maintaining any cash on hand.
- Checks are stamped with the TNS endorsement immediately upon receipt.

**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Schedule of Findings and Responses
Fiscal Years Ended September 30, 2007, 2008 and 2009

- Deposits are made daily.
- Cash is not maintained on site and, when collected, is secured at all times.

Management Response and Corrective Action Plan:

Agree. It was common practice during the audited period to use the cash from canoe tours to pay the tour staff directly. The office did not record this turnover of money as it was usually completed in a short time period. This was realized to be a bad accounting practice and has been alleviated during the Fiscal Year 2011 and is no longer practiced today. Currently, the only cash on hand is a petty cash account that is used for minor purchases. These transactions are (now)¹ recorded and tracked.

¹Inserted for clarification purposes

Finding No. 3 – Bank Reconciliations

Criteria: Periodic reconciliations of amounts recorded in an organization's cash accounts to amounts shown on bank statements are key control activities.

Condition: Monthly bank reconciliations are not performed. During our audit we requested and TNS provided four reconciliations, which we tested for completeness and accuracy.

Cause: TNS has experienced a great deal of turnover in office staff, many of which were unpaid volunteers who lacked accounting experience. This combined with the fact that responsibility for performing reconciliations appears to have never been assigned any individual or designated as part of the job description of office personnel may explain why reconciliations were not performed.

Effect: The failure to perform reconciliations of bank accounts, and to perform these timely, could result in losses due to theft or misappropriation of funds that go undetected or might not be timely detected.

Recommendation: To reduce the likelihood of errors in the recording of transactions and misappropriation of funds, ensure that bank reconciliations are timely prepared and reviewed.

**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Schedule of Findings and Responses
Fiscal Years Ended September 30, 2007, 2008 and 2009

Management Response and Corrective Action Plan:

Agree. Bank reconciliations will be prepared and reviewed monthly to ensure that errors in the recording of transactions and misappropriations of funds do not occur. This practice has been adopted during the last fiscal year and is completed each month.

Finding No. 4 – Competitive Bidding

Criteria: Yap State Law No. 6-53 requires “free and open competitive bidding, by sealed bids” for the purchase of personal property or services of \$5,000 or more, and award to the lowest possible bidder. Title 9 §523 of the Yap State Code (YSC) provides an exception to the advertising for bids where there exists a threat to public health, safety, or “convenience so declared in writing by the Governor.”

Condition: Competitive bid procedures, as required by law, were not performed in connection with a management agreement executed in October 2009. A consulting firm was engaged to manage the daily operations of TNS and its maritime institute, TMI. The firm was paid \$6,432 for its services in 2010 from funds appropriated by the state. This appears to be a sole source contract. The owner of the consulting firm is a state employee and also had previously and has subsequently performed management functions as a volunteer.

Cause: TNS failed to establish formal procurement policies and systematic processes that could have assisted in implementing competitive bid requirements in accordance with sound business practices and adherence to public law. Additionally, TNS may not have understood its duty to comply with Yap State procurement procedures upon receiving appropriated funds.

Effect: Competitive bidding of purchases helps ensure cost effective procurement of goods and services by, among other things, providing an incentive for suppliers to offer the best possible price, quality, terms, and service.

Recommendation: To ensure adherence to public law and conformity with sound business practice, establish formal procurement policies and procedures and communicate these to all staff. In executing contracts with government officials, TNS should ensure that it is complying with all applicable laws, rules, and regulations.

**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Schedule of Findings and Responses
Fiscal Years Ended September 30, 2007, 2008 and 2009

Management Response and Corrective Action Plan:

Agree. Competitive bidding and price comparisons have been instituted during the last fiscal year. TNS was unaware of the bidding requirement at that time. This has since been learned and is now a common practice.

Finding No. 5 –Unused Appropriation

Criteria: Article IX, §6, of the State Constitution prohibits the withdrawal of money from the state treasury or the obligation of funds except in accordance with law, and the Yap State Code under Title 13 further provides that expenses can be made only through the obligation of appropriated sums. In addition, appropriations contain limits on the time period during which appropriations can be used, after which, they lapse.

Condition: TNS failed to fully utilize nearly \$2,900 in available appropriated funds. An education sector appropriation of \$61,896 was received in 2009 from the Yap State Government. The appropriation lapsed September 30, 2009. However, \$8,558 was re-appropriated in 2010, with an extended deadline for obligating the funds to March 31, 2010. TNS expended \$30,600 in 2009 and \$28,444 in 2010

Cause: The expenditures may not have been properly monitored by TNS. TNS represents its sole duty was to submit supporting documentation to OAS for payment, which it did, and it followed all OAS protocols for payment.

Effect: The failure to properly monitor expenditures against available funding and fully utilize the funds could affect the organization's ability to meet its obligations, ultimately impacting the furtherance of its mission.

Recommendation: To ensure available funding is fully utilized, expenditures should be accounted for by program or funding source and timely monitored against available funding.

Management Response and Corrective Action Plan:

Agree. Due to administrative oversight a draw down request from finance was not completed in time. This caused the loss of the appropriate monies. A request was made to the office of planning of budget for a one week extension but it was not granted. This will not happen again.

**Office of the Public Auditor
State of Yap**

YAP TRADITIONAL NAVIGATION SOCIETY
Schedule of Findings and Responses
Fiscal Years Ended September 30, 2007, 2008 and 2009

Finding No. 6 – Accounting System

Criteria: A formal set of self-balancing books and accounting records helps ensure the complete and accurate recording and reporting of financial data and reduces the risk that errors go undetected, or may not be timely detected.

Condition: A double-entry bookkeeping system is not in use. Transactions are presently reported based principally on checkbook entries and manually assembled.

Cause: Management seems to have concluded that, while a formal set of books and records has not been maintained, current practices have been effective in ensuring the complete and accurate accounting, monitoring, and reporting of transactions.

Effect: Failure to maintain a proper accounting system with a self-balancing set of accounts could result in the misstatement of financial information and lack of accountability of such assets as cash, which may be subject to an increased risk of misappropriation.

Recommendation: To facilitate preparation of financial reports and ensure all transactions are properly recorded, summarized, and classified establish a double-entry accounting system which includes a general ledger, books of original entry, and suitable subsidiary records.

Management Response and Corrective Action Plan:

Agree. TNS office staff will find a viable and inexpensive accounting program for use and request the board to approve the purchase. Planned completion is December 2011.