

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT

YEAR ENDED SEPTEMBER 30, 2008

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

FINANCIAL STATEMENTS  
YEAR ENDED SEPTEMBER 30, 2008

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## INDEPENDENT AUDITORS' REPORT

Honorable Sebastian Anafel  
Governor, State of Yap  
Federated States of Micronesia:

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Yap (the State) as of and for the year ended September 30, 2008, which collectively comprise the State's basic financial statements as set forth in Section II of the foregoing table of contents. These financial statements are the responsibility of the management of the State. Our responsibility is to express an opinion on the respective financial statements based on our audit.

Except as discussed in the following paragraphs, we conducted our 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

The financial statements of Public Transportation System have not been audited, and we were not engaged to audit these financial statements as part of our audit of the State's basic financial statements. The financial activities of Public Transportation System are included in the State's basic financial statements as a blended component unit and represent 100% of the assets, net assets, and revenues of the State's business-type activities and 46%, 26%, and 27%, respectively, of the assets, net assets/fund balances, and revenues of the State's aggregate remaining fund information.

The financial statements of Yap Fishing Authority have not been audited, and we were not engaged to audit these financial statements as part of our audit of the State's basic financial statements. The financial activities of Yap Fishing Authority are included in the State's basic financial statements as a discretely presented component unit and represent 10%, 13%, and 2%, respectively, of the assets, net assets, and revenues of the State's aggregate discretely presented component units.

Because of inadequacies in the accounting records, the audited financial statements of Yap Fresh Tuna, Inc., a 50%-owned subsidiary in which Yap Fishing Authority is deemed to have a controlling interest, were not available to be consolidated with the financial statements of Yap Fishing Authority. Consolidation of Yap Fresh Tuna, Inc. financial statements with the financial statements of Yap Fishing Authority is required to conform to accounting principles generally accepted in the United States of America.

In our opinion, based on our audit, except for the inability to present audited financial statements for the Public Transportation System, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Yap as of September 30, 2008, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In addition, in our opinion, based on our audit, because of the effects of the matters discussed in the fourth and fifth paragraphs above, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the aggregate discretely presented component units of the State of Yap as of September 30, 2008, and the changes in financial position thereof for the year then ended.

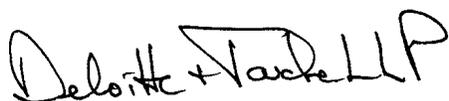
In our opinion, based on our audit, except for the inability to present audited financial statements for the Public Transportation System, such financial statements, as set forth in Section II of the foregoing table of contents, present fairly, in all material respects, the respective financial position of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Yap as of September 30, 2008, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 11 to the financial statements, the beginning net assets of the governmental activities within the accompanying financial statements has been restated.

The Management's Discussion and Analysis, on pages 3 through 8, as well as the Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund and notes thereto, on pages 44 and 45, are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the management of the State. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

Our audit was conducted for the purpose of forming an opinion on the State's respective financial statements that collectively comprise the State's basic financial statements. The combining and individual fund financial statements, as set forth in Section IV of the foregoing table of contents, which are also the responsibility of the management of the State, are presented for purposes of additional analysis and are not a required part of the basic financial statements of the State. Such additional information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 29, 2009, on our consideration of the State's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that 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 considered in assessing the results of our audit.

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is written in a cursive, stylized font.

June 29, 2009

## YAP STATE GOVERNMENT

### Management's Discussion And Analysis Year Ending September 30, 2008

This analysis, prepared by the Office of Administrative Services, offers readers of the Yap State Government's (Yap State) financial statements a narrative overview of the activities of the government for the fiscal year ended September 30, 2008. We encourage readers to consider this information in conjunction with Yap State's financial statements, which follow. Fiscal year 2007 comparative information has been included, where appropriate. This analysis is required by the Governmental Accounting Standards Board, (GASB) which provides guidelines on what must be included and excluded from this analysis.

#### FINANCIAL HIGHLIGHTS

- For the fiscal year ended September 30, 2008, Yap State's total net assets decreased by \$14.23 million (or -13.35%) from \$106.61 million in the prior year, as restated to \$92.38 million in 2008.
- During fiscal year 2008, Yap State's revenues of \$13.54 million fell short of total expenditures (\$27.77 million) by \$14.23 million. In comparison to fiscal year 2007, revenues fell by \$21.49 million (or -61.29%) although total expenditures remained at the previous year's level. The decrease in revenue is primarily due to significant losses on investments.
- Yap State ended the fiscal year with a significant operating deficit as compared to the previous years. In fiscal year 2008, revenues available for appropriation were \$11.47 million less than budgeted for the general fund which is comprised of the \$2.67 million shortfall of actual collections and the \$8.8 million of investment losses. However, actual expenditures were \$.56 million less than the final budgeted amount.
- The unreserved surplus of the General Fund decreased by \$10.19 million (-20.87%); a decrease from \$38.52 million in the prior year to \$27.60 million in fiscal year 2008. The decrease is attributable mainly to substantial losses on Yap State's investment portfolio. Investment losses realized on Yap State's general fund investments totaled \$8.8 million in fiscal year 2008, a decrease of \$18.22 million (or -192.39%) from the \$9.47 million earned in fiscal year 2007.

#### OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to Yap State's basic financial statements. Yap State's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains additional required supplementary information in the form of budgetary schedules, which are prepared on the budgetary basis of accounting, and other optional supplementary information, in addition to the basic financial statements themselves, which includes combining statements for governmental funds component units.

##### Government-Wide Financial Statements

The government-wide statements report information about Yap State as a whole using accounting methods similar to those used by private-sector companies. It provides both long-term and short-term information about the State's financial status.

The statement of net assets includes all the government's assets and liabilities. The difference in the two is called net assets. Over time, increases or decreases in the State's net assets serve as indicator to measure the State's financial position.

## YAP STATE GOVERNMENT

### Management's Discussion And Analysis Year Ending September 30, 2008

The statement of activities on the other hand, account for the State's current year's revenues and expenses regardless of when cash is received or paid.

The government-wide financial statements of Yap State are divided into three categories:

- Governmental activities -- Most of Yap State's basic services are included here, such as education, health, special appropriations, finance, judiciary, and general administration. Federal grants finance most of these activities.
- Business-type activities -- Yap State reports the operations of its Public Transportation System, which charges tariffs to help cover the costs of the transportation services it provides.
- Component Units -- Yap State includes the operating results of the Yap Visitor's Bureau, the Yap State Public Service Corporation, the Yap Fishing Authority, and The Diving Seagull, Inc. in its report. Although legally separate, these "component units" are important because Yap State is financially accountable for them.

#### Fund Financial Statements

The fund financial statements provide more detailed information about Yap State's significant funds. Funds are accounting devices that Yap State uses to keep track of specific sources of funding and spending for particular services. The State uses fund accounting to comply with financial and related legal requirements

Yap State has two types of funds:

- Governmental funds. Most of Yap State's basic services are included in governmental funds, which focus on (1) how cash and other financial assets that can be readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance Yap State programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statement, or on the subsequent page, that explains and reconciles the relationship (or differences) between them.
- Proprietary funds. Services for which Yap State charge customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both long- and short-term financial information.

#### **FINANCIAL ANALYSIS OF YAP STATE AS A WHOLE**

Net assets may serve over time as a useful indicator of a government's financial position. At the end of fiscal year 2008, Yap State's assets exceeded liabilities by \$92.38 million. Of its total net assets, \$26.88 million (29.10%) are restricted as to the purposes they can be used for. Another \$37.22 million (40.29%) can be used for or are invested in capital assets (buildings, roads, etc.). Yap State uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although Yap State's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

**YAP STATE GOVERNMENT**

Management's Discussion And Analysis  
Year Ending September 30, 2008

The following schedule summarizes Yap State's net assets as of September 30, 2008 with comparative figures for the prior year:

	<u>2008</u>	(As Restated) <u>2007</u>
Current and other non-capital assets	\$ 66,574,330	\$ 77,640,577
Capital assets	<u>37,215,377</u>	<u>39,144,521</u>
Total assets	<u>103,789,707</u>	<u>116,785,098</u>
Other liabilities	5,484,300	4,843,211
Long-term liabilities	<u>5,923,861</u>	<u>5,332,141</u>
Total liabilities	<u>12,101,876</u>	<u>10,175,352</u>
Net assets:		
Invested in capital assets, net of related debt	37,215,377	39,144,521
Restricted	26,873,226	29,341,722
Unrestricted	<u>28,282,943</u>	<u>38,123,503</u>
Total net assets	\$ <u>92,381,546</u>	\$ <u>106,609,746</u>

At the end of fiscal year 2008, Yap State's unrestricted assets show a surplus of \$28.28 million (30.61% of total net assets). These funds are included in Yap State's investment portfolio and are available for discretionary purposes subject to appropriation by the Yap State Legislature. Yap State's assets decreased by \$12.99 million (11.12%) from fiscal year 2007 levels. Key elements of the decrease and the differences from the prior year are shown in the following schedule:

	<u>2008</u>	(As Restated) <u>2007</u>
Revenues:		
Program Revenues:		
Charges for services	\$ 1,208,295	\$ 1,324,273
Operating grants and contributions	18,240,757	19,190,277
Capital Grants and contributions	(673,338)	1,229,664
General Revenues:		
Taxes	3,470,109	3,403,364
Unrestricted investment (losses) earnings	(8,754,261)	9,475,556
Other	<u>50,517</u>	<u>359,109</u>
Total revenues	<u>13,542,079</u>	<u>34,982,243</u>

## YAP STATE GOVERNMENT

### Management's Discussion And Analysis Year Ending September 30, 2008

	<u>2008</u>	(As Restated) <u>2007</u>
Expenses:		
General government	5,612,320	5,283,936
Health Services	4,613,794	4,293,830
Education	7,384,012	7,303,875
Economic development	1,408,700	1,583,352
Public Safety	449,874	628,132
Public works and transportation	5,458,934	4,094,336
Community affairs	1,106,162	892,923
Boards and commissions	50,941	78,624
Payments to components	1,030,916	1,417,913
Judiciary	189,338	163,933
Public auditor	(3,406)	2,647
Other	<u>468,694</u>	<u>1,615,233</u>
Total expenses	<u>27,770,279</u>	<u>27,358,734</u>
Change in net assets	(14,228,200)	7,623,509
Net assets at the beginning of the year	<u>106,609,746</u>	<u>98,986,237</u>
Net assets at the end of the year	<u>\$ 92,381,546</u>	<u>\$106,609,746</u>

Total revenues in fiscal year 2008 of \$13.54 million decreased from the prior year's \$34.98 million (down 61.3%) primarily due to significant investment losses.

Total expenses in fiscal year 2008 of \$27.77 million basically remained at fiscal year 2007's level of \$27.36 million.

### FINANCIAL ANALYSIS OF YAP STATE'S FUNDS

The above financial analysis incorporates a restatement which is more fully discussed in Note 11 to the accompanying financial statements. As noted earlier, Yap State uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. As of the end of fiscal year 2008, Yap State's governmental funds reported a combined fund balance of \$61.20 million, which represents a decrease of \$11.65 million (or -15.99%) in comparison with fiscal year 2007. This decrease is primarily attributable to investment losses. Of the total fund balance, \$15.22 million is reserved to indicate that it is not available for new spending because it has already been committed: 1) to generate income for future operations (\$11.82 million); 2) to liquidate contracts and purchase orders of the prior period (\$5.7 million); to fund specific general fund and compact CIP-related activities (\$2.83 million). The unreserved combined fund balance is \$40.85 million, a decrease of \$9.45 million (or -18.79%) from fiscal year 2007. The difference is mainly accounted for by the decrease in the unreserved fund balance of the general fund.

The General Fund is the chief operating fund of the State. At the end of the current fiscal year, the unreserved fund balance of the General Fund was \$27.6 million as compared with the prior year ending unreserved fund balance of \$38.5 million, a deterioration of \$10.9 million (or 28.3%), while total fund balance was \$35.8 million compared with a total fund balance of \$46 million at the end of the prior

## YAP STATE GOVERNMENT

### Management's Discussion And Analysis Year Ending September 30, 2008

fiscal year, a deterioration of \$10.2 million. The decrease in the overall fund balance of the General Fund was primarily the result of investment losses, which reflected the slump in global financial markets that commenced in January 2008.

The Foreign Assistance Grants Fund has a total fund balance of \$3.8 million, which primarily represents Compact Sector grant revenues received not yet expended at year end. The net increase in fund balance during the current year in the Foreign Assistance Grants Fund was \$1.3 million (or 53.3%), which primarily was the result of loan proceeds of \$0.6 million received under Asian Development Bank loan agreement as well as a transfer in from the General Fund and Compact Capital Projects Fund of \$0.1 million and \$0.3 million, respectively.

The Compact Capital Projects Fund has a total fund balance of \$15.3 million, which primarily represents Compact Capital Account funds under Compact I not yet expended at year end. The net decrease in fund balance during the current year in the Compact Capital Projects Fund was \$1.6 million (or 9.3%), which primarily was the result of capital-related expenditures of \$1.3 million as well as a transfer out to the Foreign Assistance Grants Fund of \$0.3 million.

The Compact Trust Fund has a total fund balance of \$5.8 million, all of which is reserved for the funding of future operations of the primary government commencing in fiscal year 2024. The net decrease in fund balance during the current year in the Compact Trust Fund was \$1.2 million (or 17.4%), which reflected the slump in global financial markets that commenced in January 2008.

#### GENERAL FUND BUDGETARY HIGHLIGHTS

Yap State budgetary condition was inevitably effected by the market downturn occurring throughout fiscal year 2008, resulting in a \$11.47 million negative variance in revenues over expenditures. Moreover, the unreserved general fund surplus decreased by \$10.19 million (down 20.87%) in fiscal year 2008; from \$38.52 million in fiscal year 2007 to \$27.60 million in 2008. This decrease was due to the \$8.75 million in investment losses in fiscal year 2008.

#### CAPITAL ASSET AND DEBT ADMINISTRATION

##### Capital Assets

Yap State's investment in capital assets for the primary government as of September 30, 2008, amounted to \$110.42 million, net of accumulated depreciation of \$73.32 million, leaving a net book value of \$37.09 million. This represents a net decrease of \$2.05 million (or 5.2%) from fiscal year 2007. The table below summarizes Yap State's capital assets:

	<u>2008</u>	(As Restated) <u>2007</u>
Land	\$ 3,120,610	\$ 3,120,610
Buildings	6,525,611	7,018,758
Equipment	1,725,633	905,837
Furniture and Fixtures	20,033	10,372
Vehicles	716,799	644,686
Boats	3,672,235	3,845,931
Infrastructure	21,313,868	23,454,001
Public Transportation	<u>-</u>	<u>144,326</u>
	<u>\$ 37,094,789</u>	<u>\$ 39,144,521</u>

## YAP STATE GOVERNMENT

### Management's Discussion And Analysis Year Ending September 30, 2008

Additional information on Yap State's capital assets can be found in Note 5 to the financial statements.

#### Long-Term Debt

Long-term debt obligations of the Yap State primary government total \$6.08 million at September 30, 2008. This debt is comprised of the non-current portion of the following ADB Loans: Early Retirement Program Loan, Private Sector Development Loan, and the Basic Social Services Loan with all three adding to \$5.25 million, liability for compensated absences of \$0.58 million and long-term payments due under land purchase agreements of \$0.25 million. Principal repayments on the outstanding ADB loans began in 2008 and are partially covered by \$2.14 million deposited in a restricted investment account jointly held with the FSM National Government.

Additional information on Yap States long-term debt obligations can be found in note 7 to the financial statements.

#### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES**

Yap State ended fiscal year 2008 with a weakened financial position as reflected in its decreased unreserved general fund surplus as compared to previous years. The global economic downturn continues and the government is facing an uncertain future with no expected economic growth in the near term. Insofar as other economic factors in the local economy remain relatively stagnant, no material growth in local taxes or fees are expected except for the potential income that new Compact Infrastructure projects may generate when such projects are implemented.

Yap State management also maintains a cautious approach with respect to funding from Compact sector grants, currently comprising 34% of Yap State's revenues. The delayed implementation of the public infrastructure grants, and the uncertainties concerning decisions made by the U.S. Department of Interior in its interpretation of the *Fiscal Procedures Agreement* --- continues to inform Yap State's prudent choices and conservative projections with respect to Compact sector funding in fiscal year 2008 and beyond.

Yap State's investment is subject to the current volatile climate in the U.S. financial markets. Fiscal Year 2008's significant investment loss of \$8.75 million made substantial impact on the financial condition of the government. The uncertainties in the financial market and downturn in global economy, Yap State's strong hold on fiscal discipline is now most needed for continued sound operating results and stable financial position during fiscal year 2009.

#### **CONTACTING YAP STATE'S FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors, a general overview of Yap State's finances to demonstrate its accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Director, Office of Administrative Services, P.O Box 610, Yap, FM 96943.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Net Assets  
September 30, 2008

	Primary Government			Component Units
	Governmental Activities	Business-Type Activities	Total	
<b>ASSETS</b>				
Current assets:				
Cash and cash equivalents	\$ 278,309	\$ 120,885	\$ 399,194	\$ 3,250,899
Cash and cash equivalents - restricted	2,097	-	2,097	-
Time certificates of deposit	-	-	-	3,004,526
Investments	51,068,408	-	51,068,408	-
Receivables, net of allowance for uncollectibles	2,530,559	205,278	2,735,837	967,930
Advances	881,537	-	881,537	-
Inventories	-	-	-	903,516
Other current assets	960,460	59,742	1,020,202	419,013
<b>Total current assets</b>	<b>55,721,370</b>	<b>385,905</b>	<b>56,107,275</b>	<b>8,545,884</b>
Noncurrent assets:				
Restricted assets:				
Investments	5,784,550	-	5,784,550	-
Investments	4,143,304	-	4,143,304	-
Loans	539,201	-	539,201	-
Capital assets, net of accumulated depreciation	37,094,789	120,588	37,215,377	12,551,657
<b>Total noncurrent assets</b>	<b>47,561,844</b>	<b>120,588</b>	<b>47,682,432</b>	<b>12,551,657</b>
<b>Total assets</b>	<b>\$ 103,283,214</b>	<b>\$ 506,493</b>	<b>\$ 103,789,707</b>	<b>\$ 21,097,541</b>
<b>LIABILITIES</b>				
Current liabilities:				
Bank overdraft	\$ 380,111	\$ -	\$ 380,111	\$ -
Current portion of long-term obligations	69,850	-	69,850	626,460
Accounts payable	1,355,198	6,241	1,361,439	3,629,627
Compensated absences payable, net of current portion	85,655	-	85,655	-
Other liabilities and accruals	249,061	219,173	468,234	573,783
Deferred revenue	3,005,720	113,291	3,119,011	-
<b>Total current liabilities</b>	<b>5,145,595</b>	<b>338,705</b>	<b>5,484,300</b>	<b>4,829,870</b>
Noncurrent liabilities:				
Noncurrent portion of long-term obligations	5,179,723	-	5,179,723	4,151,307
Compensated absences payable	494,531	-	494,531	-
Other noncurrent liabilities	249,607	-	249,607	-
<b>Total noncurrent liabilities</b>	<b>5,923,861</b>	<b>-</b>	<b>5,923,861</b>	<b>4,151,307</b>
<b>Total liabilities</b>	<b>11,069,456</b>	<b>338,705</b>	<b>11,408,161</b>	<b>8,981,177</b>
Contingencies				
<b>NET ASSETS</b>				
Invested in capital assets, net of related debt	37,094,789	120,588	37,215,377	9,758,502
Restricted for:				
Nonexpendable:				
Future operations	5,784,550	-	5,784,550	-
Expendable:				
Compact related	18,290,954	-	18,290,954	-
Debt service	2,143,304	-	2,143,304	-
Other purposes	664,458	-	664,458	-
Unrestricted	28,235,703	47,200	28,282,903	2,357,862
<b>Total net assets</b>	<b>92,213,758</b>	<b>167,788</b>	<b>92,381,546</b>	<b>12,116,364</b>
<b>Total liabilities and net assets</b>	<b>\$ 103,283,214</b>	<b>\$ 506,493</b>	<b>\$ 103,789,707</b>	<b>\$ 21,097,541</b>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Activities  
Year Ended September 30, 2008

Functions/Programs	Program Revenues				Net (Expenses) Revenues and Changes in Net Assets			
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government			Component Units
					Governmental Activities	Business-type Activities	Total	
Primary government:								
Governmental activities:								
Judiciary	\$ 189,338	\$ -	\$ -	\$ -	\$ (189,338)	\$ -	\$ (189,338)	\$ -
Councils of traditional leaders	201,582	-	-	-	(201,582)	-	(201,582)	-
Public auditor	(3,406)	-	-	-	3,406	-	3,406	-
General government	5,612,320	834,470	4,506,106	201,710	(70,034)	-	(70,034)	-
Economic development	1,408,700	-	1,131,747	42,864	(234,089)	-	(234,089)	-
Public safety	449,874	-	47,183	-	(402,691)	-	(402,691)	-
Community affairs	1,106,162	-	49,983	253,275	(802,904)	-	(802,904)	-
Education	7,384,012	67,172	7,790,872	-	474,032	-	474,032	-
Public works and transportation	5,023,988	-	107,110	50,654	(4,866,224)	-	(4,866,224)	-
Health services	4,613,794	35,571	4,125,669	-	(452,554)	-	(452,554)	-
Boards and commissions	50,941	-	-	-	(50,941)	-	(50,941)	-
Payments to components	1,030,916	-	400,110	-	(630,806)	-	(630,806)	-
Future operations	-	-	-	(1,221,841)	(1,221,841)	-	(1,221,841)	-
Other appropriations	267,112	-	-	-	(267,112)	-	(267,112)	-
Total governmental activities	<u>27,335,333</u>	<u>937,213</u>	<u>18,158,780</u>	<u>(673,338)</u>	<u>(8,912,678)</u>	<u>-</u>	<u>(8,912,678)</u>	<u>-</u>
Business-type activities:								
Public Transportation System	434,946	271,082	81,977	-	-	(81,887)	(81,887)	-
Total primary government	<u>\$ 27,770,279</u>	<u>\$ 1,208,295</u>	<u>\$ 18,240,757</u>	<u>\$ (673,338)</u>	<u>(8,912,678)</u>	<u>(81,887)</u>	<u>(8,994,565)</u>	<u>-</u>
Component units:								
Yap Visitor's Bureau	\$ 314,037	\$ 1,086	\$ -	\$ -	-	-	-	(312,951)
Yap State Public Service Corporation	4,642,048	1,023,556	-	-	-	-	-	(3,618,492)
Yap Fishing Authority	387,846	243,098	-	-	-	-	-	(144,748)
The Diving Seagull, Inc.	7,379,526	8,256,692	-	-	-	-	-	877,166
Total component units	<u>\$ 12,723,457</u>	<u>\$ 9,524,432</u>	<u>\$ -</u>	<u>\$ -</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(3,199,025)</u>
General revenues:								
Taxes:								
Revenue sharing					2,163,763	-	2,163,763	-
Excise taxes					1,306,346	-	1,306,346	-
Unrestricted investment earnings					(8,754,261)	-	(8,754,261)	83,692
Contributions from primary government					-	-	-	560,013
Other					44,818	5,699	50,517	-
Total general revenues and special items					<u>(5,239,334)</u>	<u>5,699</u>	<u>(5,233,635)</u>	<u>643,705</u>
Change in net assets					<u>(14,152,012)</u>	<u>(76,188)</u>	<u>(14,228,200)</u>	<u>(2,555,320)</u>
Net assets at the beginning of the year					<u>106,365,770</u>	<u>243,976</u>	<u>106,609,746</u>	<u>14,671,684</u>
Net assets at the end of the year					<u>\$ 92,213,758</u>	<u>\$ 167,788</u>	<u>\$ 92,381,546</u>	<u>\$ 12,116,364</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Balance Sheet  
Governmental Funds  
September 30, 2008

	General	Special Revenue Foreign Assistance Grants	Capital Projects Compact Capital Projects	Permanent Compact Trust	Other Governmental Funds	Total
<b>ASSETS</b>						
Cash and cash equivalents	\$ 48,764	\$ -	\$ -	\$ -	\$ 229,545	\$ 278,309
Equity interest in internal investment pool	43,572,183	3,226,092	4,270,133	-	-	51,068,408
Investments	2,000,000	-	-	-	-	2,000,000
Receivables, net:						
Loans	539,201	-	-	-	-	539,201
Federal agencies	-	427,030	-	-	-	427,030
FSM National Government	434,112	1,607,725	-	-	35,563	2,077,400
Other	26,129	-	-	-	-	26,129
Due from other funds	2,359,755	4,096,508	11,009,670	-	338,552	17,804,485
Advances	303,262	578,275	-	-	-	881,537
Prepaid items	960,460	-	-	-	-	960,460
Restricted assets:						
Cash and cash equivalents	2,097	-	-	-	-	2,097
Pooled investments	2,143,304	-	-	-	-	2,143,304
Investments	-	-	-	5,784,550	-	5,784,550
Total assets	<u>\$ 52,389,267</u>	<u>\$ 9,935,630</u>	<u>\$ 15,279,803</u>	<u>\$ 5,784,550</u>	<u>\$ 603,660</u>	<u>\$ 83,992,910</u>
<b>LIABILITIES AND FUND BALANCES</b>						
Liabilities:						
Bank overdraft	\$ 380,111	\$ -	\$ -	\$ -	\$ -	\$ 380,111
Accounts payable	485,777	835,161	2,594	-	31,666	1,355,198
Other liabilities and accruals	151,321	56,034	680	-	41,026	249,061
Deferred revenue	97,490	2,908,230	-	-	-	3,005,720
Due to other funds	15,444,730	2,295,386	-	-	64,369	17,804,485
Total liabilities	<u>16,559,429</u>	<u>6,094,811</u>	<u>3,274</u>	<u>-</u>	<u>137,061</u>	<u>22,794,575</u>
Fund balances (deficits):						
Reserved for:						
Related assets	6,039,201	-	-	5,784,550	-	11,823,751
Encumbrances	2,152,664	2,662,640	692,005	-	187,270	5,694,579
Continuing appropriations	40,010	150,000	2,637,032	-	-	2,827,042
Unreserved:						
General fund	27,597,963	-	-	-	-	27,597,963
Special revenue funds	-	1,028,179	-	-	464,570	1,492,749
Capital projects funds	-	-	11,947,492	-	(185,241)	11,762,251
Total fund balances	<u>35,829,838</u>	<u>3,840,819</u>	<u>15,276,529</u>	<u>5,784,550</u>	<u>466,599</u>	<u>61,198,335</u>
Total liabilities and fund balances	<u>\$ 52,389,267</u>	<u>\$ 9,935,630</u>	<u>\$ 15,279,803</u>	<u>\$ 5,784,550</u>	<u>\$ 603,660</u>	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds

37,094,789

Long-term liabilities, including loans payable, are not due and payable in the current period and, therefore, are not reported in the funds. The liabilities include:

Long-term debt payable (5,249,573)  
Compensated absences payable (580,186)  
Land acquisition claims payable (249,607)

(6,079,366)

Net assets of governmental activities

\$ 92,213,758

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Revenues, Expenditures, and Changes in Fund Balances  
Governmental Funds  
Year Ended September 30, 2008

	General	Special Revenue Foreign Assistance Grants	Capital Projects Compact Capital Projects	Permanent Compact Trust	Other Governmental Funds	Total
Revenues:						
Compact funding	\$ -	\$ 12,688,351	\$ -	\$ -	\$ -	\$ 12,688,351
Net decrease in the fair value of investments	(8,754,261)	-	-	(1,221,841)	-	(9,976,102)
Federal contributions and other grants	-	5,423,246	-	-	-	5,423,246
Revenue sharing	2,163,763	-	-	-	-	2,163,763
Excise taxes	1,124,530	-	-	-	181,816	1,306,346
CFSM grants	-	47,183	-	-	548,503	595,686
Fees and charges	347,903	102,743	-	-	13,370	464,016
Departmental charges	473,197	-	-	-	-	473,197
Other	44,818	-	-	-	-	44,818
Total revenues	<u>(4,600,050)</u>	<u>18,261,523</u>	<u>-</u>	<u>(1,221,841)</u>	<u>743,689</u>	<u>13,183,321</u>
Expenditures:						
Current:						
Judiciary	209,797	-	-	-	-	209,797
Councils of traditional leaders	209,233	-	-	-	-	209,233
General government	868,494	4,355,183	299,315	-	201,710	5,724,702
Economic development	826	1,118,377	150,000	-	56,234	1,325,437
Public safety	505,551	47,183	-	-	-	552,734
Community affairs	307,938	49,983	33,039	-	452,432	843,392
Education	118,979	7,858,044	-	-	-	7,977,023
Public works and transportation	1,873,490	25,000	753,195	-	50,654	2,702,339
Health services	526,160	4,161,240	-	-	-	4,687,400
Boards and commissions	54,029	-	-	-	-	54,029
Payments to component units	499,676	400,110	31,130	-	-	930,916
Other appropriations	267,112	-	-	-	-	267,112
Total expenditures	<u>5,441,285</u>	<u>18,015,120</u>	<u>1,266,679</u>	<u>-</u>	<u>761,030</u>	<u>25,484,114</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(10,041,335)</u>	<u>246,403</u>	<u>(1,266,679)</u>	<u>(1,221,841)</u>	<u>(17,341)</u>	<u>(12,300,793)</u>
Other financing sources (uses):						
Loan proceeds	-	645,757	-	-	-	645,757
Operating transfers in	-	444,142	-	-	-	444,142
Operating transfers out	(146,324)	-	(297,818)	-	-	(444,142)
Total other financing sources (uses), net	<u>(146,324)</u>	<u>1,089,899</u>	<u>(297,818)</u>	<u>-</u>	<u>-</u>	<u>645,757</u>
Net change in fund balances	<u>(10,187,659)</u>	<u>1,336,302</u>	<u>(1,564,497)</u>	<u>(1,221,841)</u>	<u>(17,341)</u>	<u>(11,655,036)</u>
Fund balances at the beginning of the year	<u>46,017,497</u>	<u>2,504,517</u>	<u>16,841,026</u>	<u>7,006,391</u>	<u>483,940</u>	<u>72,853,371</u>
Fund balances at the end of the year	<u>\$ 35,829,838</u>	<u>\$ 3,840,819</u>	<u>\$ 15,276,529</u>	<u>\$ 5,784,550</u>	<u>\$ 466,599</u>	<u>\$ 61,198,335</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Reconciliation of the Statement of Revenues, Expenditures,  
and Changes in Fund Balances of Governmental Funds  
to the Statement of Activities  
Year Ended September 30, 2008

Amounts reported for governmental activities in the statement of activities on page 4 are different because:

Net change in fund balances - total governmental funds from page 12	\$ (11,655,036)
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded or are less than depreciation in the current period, including increases to construction in progress	(1,905,406)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore, are not reported as expenditures in governmental funds. These expenses include accrued annual leave and land claims payable that are reported in the statement of activities, but not in funds	(23,363)
The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction has any effect on net assets. This amount is the net effect of these differences in the treatment of long - term debt and related items	<u>(568,207)</u>
Change in net assets of governmental activities as presented on page 10.	\$ <u>(14,152,012)</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Net Assets  
Proprietary Funds  
September 30, 2008

	<u>Public Transportation System</u>
<u>ASSETS</u>	
Current assets:	
Cash and cash equivalents	\$ 120,885
Receivables, net of allowance for uncollectibles	205,278
Other current assets	59,742
Total current assets	<u>385,905</u>
Noncurrent assets:	
Capital assets, net of accumulated depreciation	<u>120,588</u>
Total assets	<u>\$ 506,493</u>
<u>LIABILITIES</u>	
Current liabilities:	
Accounts payable	\$ 6,241
Other liabilities and accruals	219,173
Deferred revenue	113,291
Total liabilities	<u>338,705</u>
<u>NET ASSETS</u>	
Invested in capital assets	120,588
Unrestricted	47,200
Total net assets	<u>167,788</u>
	<u>\$ 506,493</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Revenues, Expenses, and Changes in Net Assets  
Proprietary Funds  
Year Ended September 30, 2008

	<u>Public Transportation System</u>
Operating revenues:	
Charges for services	\$ 146,112
Sales	<u>124,970</u>
Total operating revenues	<u>271,082</u>
Operating expenses:	
Cost of services	118,676
Administration costs	288,998
Depreciation and amortization	<u>27,272</u>
Total operating expenses	<u>434,946</u>
Operating loss	<u>(163,864)</u>
Nonoperating revenues:	
Other	<u>5,699</u>
Total nonoperating expenses	<u>5,699</u>
Loss before operating transfers	(158,165)
Operating transfers in	<u>81,977</u>
Change in net assets	(76,188)
Net assets at the beginning of the year	<u>243,976</u>
Net assets at the end of the year	<u>\$ 167,788</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Cash Flows  
Proprietary Funds  
Year Ended September 30, 2008

	<u>Public Transportation System</u>
Cash flows from operating activities:	
Cash received from customers	\$ 69,452
Cash payments to employees	(113,440)
Cash payments to suppliers	(294,995)
Net cash used in operating activities	<u>(338,983)</u>
Cash flows from noncapital financing activities:	
Contributions from the primary government	383,171
Net cash provided by noncapital financing activities	<u>383,171</u>
Cash flows from capital and related financing activities:	
Purchases of capital assets	1,076
Net cash used in capital and related financing activities	<u>1,076</u>
Net change in cash and cash equivalents	45,264
Cash and cash equivalents at the beginning of the year	<u>75,621</u>
Cash and cash equivalents at the end of the year	<u>\$ 120,885</u>
Reconciliation of operating loss to net cash used in operating activities:	
Operating loss	\$ (163,864)
Adjustments to reconcile operating loss to net cash used in operating activities:	
Depreciation expense	27,272
Bad debts expense	-
Changes in assets and liabilities:	
Receivables, net	(203,850)
Other current assets	(3,176)
Accounts payable	2,415
Deferred revenue	2,220
Net cash used in operating activities	<u>\$ (338,983)</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Combining Statement of Net Assets  
Component Units  
September 30, 2008

	Yap Visitor's Bureau	Yap State Public Service Corporation	Yap Fishing Authority	The Diving Seagull, Inc.	Total
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$ 143,713	\$ 706,850	\$ 53,446	\$ 2,346,890	\$ 3,250,899
Time certificate of deposit	-	-	-	3,004,526	3,004,526
Investments	-	-	-	-	-
Receivables, net:					
General	87	767,466	20,288	-	787,841
Other	84,894	8,253	93	86,849	180,089
Inventories	-	903,516	-	-	903,516
Other current assets	-	114,873	39,629	264,511	419,013
Total current assets	<u>228,694</u>	<u>2,500,958</u>	<u>113,456</u>	<u>5,702,776</u>	<u>8,545,884</u>
Noncurrent assets:					
Capital assets, net of accumulated depreciation	42,485	9,261,337	2,035,708	1,212,127	12,551,657
Total noncurrent assets	<u>42,485</u>	<u>9,261,337</u>	<u>2,035,708</u>	<u>1,212,127</u>	<u>12,551,657</u>
Total assets	<u>\$ 271,179</u>	<u>\$ 11,762,295</u>	<u>\$ 2,149,164</u>	<u>\$ 6,914,903</u>	<u>\$ 21,097,541</u>
<b>LIABILITIES</b>					
Current liabilities:					
Current portion of long-term debt	\$ -	\$ 113,723	\$ -	\$ 512,737	\$ 626,460
Accounts payable	29,701	3,183,197	35,427	381,302	3,629,627
Other liabilities and accruals	5,482	313,252	84,038	171,011	573,783
Total current liabilities	35,183	3,610,172	119,465	1,065,050	4,829,870
Noncurrent liabilities:					
Noncurrent portion of long-term debt	-	2,679,432	-	1,471,875	4,151,307
Total liabilities	<u>35,183</u>	<u>6,289,604</u>	<u>119,465</u>	<u>2,536,925</u>	<u>8,981,177</u>
<b>NET ASSETS</b>					
Invested in capital assets, net of related debt	42,485	6,468,182	2,035,708	1,212,127	9,758,502
Unrestricted	193,511	(995,491)	(6,009)	3,165,851	2,357,862
Total net assets	<u>235,996</u>	<u>5,472,691</u>	<u>2,029,699</u>	<u>4,377,978</u>	<u>12,116,364</u>
	<u>\$ 271,179</u>	<u>\$ 11,762,295</u>	<u>\$ 2,149,164</u>	<u>\$ 6,914,903</u>	<u>\$ 21,097,541</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Combining Statement of Revenues, Expenses, and Changes in Net Assets  
Component Units  
Year Ended September 30, 2008

	Yap Visitor's Bureau	Yap State Public Service Corporation	Yap Fishing Authority	The Diving Seagull, Inc.	Total
Operating revenues:					
Charges for services	\$ 891	\$ 560,906	\$ -	\$ 8,256,692	\$ 8,818,489
Sales	195	462,650	243,098	-	705,943
Total operating revenues	<u>1,086</u>	<u>1,023,556</u>	<u>243,098</u>	<u>8,256,692</u>	<u>9,524,432</u>
Operating expenses:					
Cost of services	-	5,655,446	212,967	5,587,493	11,455,906
Administration costs	300,416	281,492	-	456,544	1,038,452
Depreciation and amortization	18,415	765,079	173,901	1,145,039	2,102,434
Total operating expenses	<u>318,831</u>	<u>6,702,017</u>	<u>386,868</u>	<u>7,189,076</u>	<u>14,596,792</u>
Operating income (loss)	<u>(317,745)</u>	<u>(5,678,461)</u>	<u>(143,770)</u>	<u>1,067,616</u>	<u>(5,072,360)</u>
Nonoperating revenues (expenses):					
Contributions from the primary government	327,047		232,966	-	560,013
Interest income	-		-	83,692	83,692
Interest expense	-	(13,034)	-	(190,450)	(203,484)
Other	4,794	2,073,003	(978)	-	2,076,819
Total nonoperating revenues (expenses), net	<u>331,841</u>	<u>2,059,969</u>	<u>231,988</u>	<u>(106,758)</u>	<u>2,517,040</u>
Change in net assets	14,096	(3,618,492)	88,218	960,858	(2,555,320)
Net assets at the beginning of the year	<u>221,900</u>	<u>9,091,183</u>	<u>1,941,481</u>	<u>3,417,120</u>	<u>14,671,684</u>
Net assets at the end of the year	<u>\$ 235,996</u>	<u>\$ 5,472,691</u>	<u>\$ 2,029,699</u>	<u>\$ 4,377,978</u>	<u>\$ 12,116,364</u>

See accompanying notes to financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies

The accompanying financial statements of the State of Yap (the State) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the State's accounting policies are described below.

A. Reporting Entity

The State is one of the four states that make up the Federated States of Micronesia (FSM), along with the states of Chuuk, Kosrae and Pohnpei. The State is a constitutional government comprised of three branches: the Legislative Branch, consisting of 10 members elected for a term of four years by qualified voters of their respective election districts; the Executive Branch, headed by the Governor and Lt. Governor who are primarily responsible for executing the laws and administering state government services; and the Judiciary Branch made up of the State Supreme Court, which consists of a Chief Justice and two Associate Justices, and other courts that may be created by law. The State also has traditional leaders that serve in the Council of Pilung and the Council of Tamol that advise the State on matters concerning customary law and traditional practice.

For financial reporting purposes, the State has included all funds, organizations, agencies, boards, commissions and institutions. The State has also considered all potential component units for which it is financially accountable as well as other entities for which the nature and significance of their relationship with the State are such that exclusion would cause the State's financial statements to be misleading or incomplete. The criteria to be considered in determining financial accountability include whether the State, as the primary government, has appointed a voting majority of an organization's governing body and either has the ability to impose its will on that organization or there is potential for the organization to provide specific financial benefits to or impose specific financial burdens on the State. Financial accountability also exists if an organization is determined to be fiscally dependent on the primary government, although the primary government does not appoint a voting majority of the organization's governing board.

Each blended and discretely presented component unit of the State has a September 30 year-end.

Once financial accountability has been determined for a potential component unit, that component unit is either blended into the primary government or discretely presented from the primary government. Potential component units that do not meet the financial accountability criteria, but where a voting majority of the governing board is appointed by the State, are deemed to be related organizations. The nature and relationship of the State's component units and related organizations are disclosed in the following section.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

i. Discretely Presented Component Units

Discretely presented component units are entities which are legally separate from the State, but are financially accountable to the State, or whose relationships with the State are such that exclusion would cause the State's basic financial statements to be misleading or incomplete. The component units' column of the basic financial statements includes the financial data of the following major component units:

Yap Visitor's Bureau (YVB): YVB was created by YSL No. 4-25 and is responsible for the promotion of Yap as a tourist destination. YVB is governed by a seven-member Board of Directors, of which five members are appointed by the Governor subject to the advice and consent of the Legislature, one member is appointed by the Speaker of the Legislature, and one member is elected by the six appointed members.

Yap State Public Service Corporation (YSPSC): YSPSC was created by YSL No. 4-4 and is responsible for the delivery of electricity, water and sewer in the State. YSPSC is governed by a seven-member Board of Directors appointed by the Governor subject to the advice and consent of the Legislature.

Yap Fishing Authority (YFA): YFA was created by Yap District Law (YDL) No. 6-13 and is responsible for the promotion, development, and supporting of commercial utilization of living marine resources within the State. YFA is governed by a five-member Board of Directors appointed by the Governor subject to the advice and consent of the Legislature.

The Diving Seagull, Inc. (DSI): DSI was incorporated in the State on March 17, 1997 and was organized primarily to pursue fishing and other fishing related activities by operating fishing vessels, marketing and selling fish, and developing cold storage and/or transshipment facilities. DSI is governed by a seven-member Board of Directors.

The State's component units, departments, and funds that are separately audited issue their own financial statements. These statements may be obtained by directly contacting the various entities or obtaining them directly from the Office of the Public Auditor at the following address:

P.O. Box 927  
Colonia, Yap, FSM 96943

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

A. Reporting Entity, Continued

ii. Omitted Component Units

The following component units have been omitted from the basic financial statements due to the lack of available financial information:

Public Transportation System (PTS) PTS was created by Yap State Law (YSL) No. 1-170 and is responsible for the provision of reliable and inexpensive transportation for those people living outside of the Colonia area. PTS is governed by a five-member Board of Directors appointed by the Governor subject to the advice and consent of the Legislature. The financial activities of this omitted component unit are not considered material to the basic financial statements.

Gagil-Tomil Water Authority (GTWA): GTWA was created by YSL No. 1-183 and is responsible for the provision of services in the operation and maintenance of the Gagil-Tomil Water System. GTWA is governed by a nine-member Board of Directors, four of which are appointed by the Gagil member of the Council of Pilung, four appointed by the Tomil member of the Council of Pilung, and one appointed by the Governor. The financial activities of this omitted component unit are not considered material to the basic financial statements.

Southern Yap Water Authority (SYWA): SYWA was created by YSL No. 1-221 and is responsible for the operation and maintenance of the Southern Yap Water System. SYWA is governed by a six-member Board of Directors, of which one is appointed by the Governor, two members who are appointed by the Municipal Chief of Rull on the Council of Pilung, one of whom shall be from either Lamer or Luwech Villages, and three members who are appointed by the municipal chiefs of Gilman, Kanifay, and Dalipebinaw on the Council of Pilung. The financial activities of this omitted component unit are not considered material to the basic financial statements.

Yap Sports Council (YSC): YSC was created by YSL No. 4-65 and is responsible for promoting and encouraging sports participation at all levels of society. YSC is governed by an eleven-member Board of Directors, of which three members are appointed by the Governor subject to the advice and consent of the Legislature, two members are appointed by the Speaker of the Legislature, two members are appointed by the Council of Pilung, two members are appointed by the Council of Tamol, and two members are appointed by the Congress of the FSM National Government. The financial activities of this omitted component unit are not considered material to the basic financial statements.

B. Government-Wide Financial Statements

The Statement of Net Assets and the Statement of Activities report financial information on all of the non-fiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been eliminated from these statements except for other charges between the primary government and the discretely presented component units. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

B. Government-Wide Financial Statements, Continued

Primary government activities are defined as either governmental or business-type activities. Governmental activities, which normally are supported by taxes, intergovernmental revenues and other non-exchange revenues, are reported separately from business-type activities, which rely to a significant extent on fees charged to external parties for goods or services. As such, business-type activities account for operations similarly to a for-profit business. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable. Discretely presented component unit activities are presented with their business-type focus.

The Statement of Net Assets presents all of the reporting entity's non-fiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt that are attributed to the acquisition, construction or improvement of those assets.
- Restricted net assets - nonexpendable consists of permanent funds in which donors or other outside sources have stipulated that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to the principal.
- Restricted net assets - expendable consists of resources in which the State is legally or contractually obligated to spend resources in accordance with restrictions either externally imposed by creditors, grantors, contributors, and the like, or imposed by law.
- Unrestricted net assets consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated (for example, internally restricted), to indicate that management does not consider them to be available for general operations.

The government-wide Statement of Net Assets reports \$26,883,266 of restricted net assets, of which \$664,458 is restricted by enabling legislation.

The Statement of Activities demonstrates the degree to which the direct expenses of given functions or segments are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function or segment. Program revenues include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items not meeting the definition of program revenues are, instead, reported as general revenue.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

C. Fund Financial Statements

The fund financial statements present a balance sheet and a statement of revenues, expenditures, and changes in fund balances for its major and aggregated non-major funds.

Major individual governmental funds are reported as separate columns in the fund financial statements pursuant to GASB reporting standards, with nonmajor governmental funds being combined into a single column.

The State reports its financial position and results of operations in funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures/expenses. Transactions between funds within a fund type, if any, have not been eliminated.

D. Measurement Focus and Basis of Accounting

The government-wide financial statements are reported using the economic resources management focus and the accrual basis of accounting, as are the proprietary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements account for the general governmental activities of the State and are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as they become susceptible to accrual; generally when they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State considers revenues to be available if they are collected within sixty days of the end of the current fiscal period.

Significant revenues susceptible to accrual include income and gross revenue taxes, federal grants, federal reimbursements and other reimbursements for use of materials and services. Miscellaneous revenues from other financing sources are recognized when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available. Investments and related investment earnings are recorded at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Expenditures generally are recorded in the period in which the related fund liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

Amounts reported as program revenue include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as general revenues rather than as program revenues. General revenue is derived from taxation, investment income and other fees that are not allocated to specific programs.

Discretely presented component units distinguish operating revenues and expenses from nonoperating items. Operating revenues generally result from providing services and producing and delivering goods in connection with a discretely presented component unit's principal ongoing operations. All other revenues are reported as nonoperating. Operating expenses includes the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

The State reports the following fund types:

1. Governmental Funds

i. General Fund

This fund is the primary operating fund of the State. It is used to account for all governmental transactions, except those required to be accounted for in another fund.

ii. Special Revenue Funds

These funds account for specific revenue sources that have been aggregated according to enabling legislation to support specific governmental activities.

iii. Capital Projects Funds

These funds account for the acquisition or construction of major State capital facilities financed primarily from loans and federal reimbursements.

iv. Permanent Fund

This fund accounts for resources that are legally restricted to the extent that only earnings, and not principal, may be used to support programs for the benefit of the government.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

D. Measurement Focus and Basis of Accounting, Continued

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - For State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - For State and Local Governments: Omnibus*, sets forth minimum criteria (percentage of the assets, liabilities, revenues or expenditures/expenses for either fund category or the governmental and enterprise combined) for the determination of major funds. Major individual governmental funds are reported as separate columns in the fund financial statements. The nonmajor funds are combined in a column in the fund financial statements and detailed in the combining statements.

The State reports the following major funds:

Foreign Assistance Grants Fund, a Governmental Fund Type Special Revenue Fund. This fund accounts for funds received under sector grants pursuant to the Amended Compact of Free Association; all financial transactions of federally assisted funds, which are subgranted to the Yap State Government, as well as other direct federal grants that the State received from the United States government, and foreign assistance grants.

Compact Capital Projects Fund, a Governmental Fund Type - Capital Projects Fund. This fund is used to account for financial transactions related to Compact Capital Account funds as provided under Section 211(a) of the Compact of Free Association.

Compact Trust Fund, a Governmental Fund Type - Permanent Fund. This fund accounts for United States Congress appropriations under United States Public Law 99-239, as amended, Title II, Article I, Section 215 and approved by the FSM Congress to provide for an additional source of revenue for the government budget that will be needed to substitute for the absence of Compact of Free Association funding. Earnings from funds invested would not be available for distribution until October 2023.

E. Reporting Standards

As allowed by GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the State's proprietary funds and discretely presented component units follow all GASB pronouncements and those Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins that were issued on or before November 30, 1989, except those that conflict with a GASB pronouncement.

F. Cash and Cash Equivalents and Time Certificates of Deposit

Cash and cash equivalents include cash held in demand accounts as well as short-term investments with a maturity date within three months of the date acquired by the State. Deposits maintained in time certificates of deposit with original maturity dates greater than three months are separately classified on the statement of net assets/balance sheet.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

G. Investments

Investments are recorded at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. When market prices of equity investments in companies are not readily determinable, the investments are carried at cost if less than twenty percent of the companies' total equity is owned, on the equity method if greater than twenty percent and less than fifty percent is owned, and on a consolidated basis if greater than fifty percent is owned.

H. Receivables

In general, tax revenue is recognized on the government-wide statements, when assessed or levied and on the governmental fund financial statements to the extent that it is both measurable and available. Receivables are stated net of estimated allowances for uncollectible accounts. Reimbursements due to the State for expenditures on federally funded reimbursement and grant programs are reported as "receivables from federal agencies".

Receivables of the primary government are primarily due from businesses and individuals residing in the State. The State establishes an allowance for doubtful accounts receivable based on the credit risk of specific customers, historical trends and other information.

I. Prepaid Items and Inventories

Certain payments made to vendors or persons for services reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

Inventories of the discretely presented component units are determined by physical count and are valued at the lower of cost or market by the first-in first-out method (FIFO).

J. Interfund Receivables/Payables

During the course of its operations, the State records transactions between individual funds for goods provided or services rendered. Receivables and payables resulting from transactions between funds are classified as "due from other funds" or "due to other funds" on the governmental fund balance sheet.

These balances result from the time lag between the dates that 1) interfund goods and services are provided or reimbursable expenditures occur, 2) transactions are recorded in the accounting system, and 3) payments between funds are made, and are scheduled to be collected in the subsequent year.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

K. Restricted Assets

Certain assets of the primary government are classified as restricted assets because their use is completely restricted through loan agreements or enabling legislation. Specifically, the State has collateralized pooled investments from Asian Development Bank loan proceeds and earnings in the amount of \$2,143,304 for the Yap State Early Retirement Scheme. Furthermore, cash and cash equivalents in the amount of \$2,097 is restricted for Compact Sector payments and investments in the amount of \$5,784,550 are restricted under the Compact of Free Association in that they are not available for distribution until October 2023.

L. Capital Assets

Capital assets, which include property, plant, equipment and infrastructure assets (e.g. roads, bridges, docks, water and sewer lines, water catchments, and other similar items), are reported in the governmental activity column of the government-wide financial statements. Such assets, whether purchased or constructed, are recorded at historical cost or estimated historical cost. Donated capital assets are recorded at estimated fair market value at the date of donation.

Machinery and equipment, other than vehicles and boats, are capitalized when the cost of individual items exceed \$50,000. Vehicles and boats, along with significant repair and maintenance qualifying as a betterment of such, are capitalized regardless of cost and depreciated. Buildings and infrastructure projects, along with significant improvements or reconstruction qualifying as a betterment of such, are capitalized when the cost of individual items or projects exceed \$100,000. The costs of normal maintenance and repairs that do not add to the value of the capital asset or materially extend capital asset lives are not capitalized.

Capital assets of the primary government and the component units are depreciated using the straight-line method over their estimated useful lives, with a full year's depreciation charged in the year of acquisition and disposal, regardless of date. Estimated useful lives are as follows:

Buildings	40 - 50 years
Infrastructure	25 - 50 years
Facilities	3 - 40 years
Machinery and equipment	3 - 25 years
Furniture and fixtures	3 - 10 years

M. Deferred Revenue

In the government-wide financial statements, deferred revenue is recognized when cash, receivables or other assets are recorded prior to being earned. In the governmental fund financial statements deferred revenue represents monies received or revenues accrued which have not been earned or do not meet the "available" criterion for revenue recognition under the modified accrual basis of accounting. The deferred revenue in the governmental fund types has primarily resulted as federal funds are received in advance of eligible expenditures.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

N. Compensated Absences

It is the government's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. There is no liability for unpaid accumulated sick leave since the government does not have a policy to pay any amounts when employees separate from service with the government. All vacation pay is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements. Annual leave accumulates at the rate of one working day per bi-weekly pay period.

O. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

The unreserved fund balances for the governmental funds represent the amount available for budgeting future operations. The reserve for related assets as of September 30, 2008, is represented by the following assets:

	<u>General</u>	U.S. Federal <u>Grants</u>	U.S. Federal <u>Grants</u>	Compact Capital <u>Projects</u>	Compact <u>Trust</u>	Other Governmental <u>Funds</u>	<u>Totals</u>
Equity interest in internal investment pool	\$1,356,696	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,356,696
Investments	2,000,000	-	-	-	-	-	2,000,000
Receivables:							
Loans	539,201	-	-	-	-	-	539,201
Restricted assets:							
Pooled investments	2,143,304	-	-	-	-	-	2,143,304
Investments	-	-	-	-	5,784,550	-	5,784,550
	<u>\$6,039,201</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$5,784,550</u>	<u>\$ -</u>	<u>\$11,823,751</u>

The reserve for related assets within the General Fund includes the amount of \$3,500,000 set aside for future repayment of the Early Retirement Program Loan.

P. Risk Financing

The State is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. It is the policy of the primary government not to purchase commercial insurance for the risks of loss to which it is exposed. Instead, State management believes it is more economical to manage its risks internally. In the event of claim settlements and judgments, the State reports all of its risk management activities in its General Fund. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. However, no material losses have been incurred as a result of this policy in the last three years.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

Q. Estimates

The preparation of financial statements in conformity with GAAP 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, expenditures and expenses during the reporting period. Actual results could differ from those estimates.

R. New Accounting Standards

During fiscal year 2008, the State implemented GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues*, and GASB Statement No. 50, *Pension Disclosures an amendment of GASB Statements No. 25 and 27*. GASB Statement No. 43 establishes uniform financial reporting for other postemployment benefit plans by state and local governments and GASB Statement No. 50 more closely aligns the financial reporting requirements for pensions with those for other post-employment benefits. GASB Statement No. 48 establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing, and includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other post employment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB Statement No. 49 provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In June 2007, GASB issued statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. GASB Statement No. 51 addresses whether and when intangible assets should be considered capital assets for financial reporting purposes. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(1) Summary of Significant Accounting Policies, Continued

R. New Accounting Standards, Continued

In November 2007, GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. GASB Statement No. 52 improves the quality of financial reporting by requiring endowments to report their land and other real estate investments at fair value, creating consistency in reporting among similar entities that exist to invest resources for the purpose of generating income. The provisions of this statement are effective for periods beginning after June 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. GASB Statement No. 53 is intended to improve how state and local governments report information about derivative instruments - financial arrangements used by governments to manage specific risks or make investments - in their financial statements. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of the State.

S. Total Columns

Total columns are presented primarily to facilitate financial analysis. The Management's Discussion and Analysis includes certain prior year summarized comparative information in total. Such information does not include sufficient detail to constitute a full comparative presentation. Accordingly, such information should be read in conjunction with the State's financial statements for the year ended September 30, 2007 from which summarized information was derived.

T. Reclassification

Due to the provisions of GASB Statement No. 34 Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments, major funds presented in the previous year may not be major funds presented in the current year. Concurrently, major funds presented in the current year may not be major funds presented in the previous year. The State has consolidated the U.S. Federal Grants Fund with the Foreign Assistance Grants Fund, whereas such was presented as a major fund in the previous year. The Compact Special Block Fund and the CFSM Grants Fund have been consolidated with the Foreign Assistance Grant Fund whereas such were presented as nonmajor governmental funds in the previous year.

(2) Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(2) Deposits and Investments, Continued

The State pools cash resources of its various funds in order to facilitate the management of cash. Unless otherwise required by law, interest income received on pooled cash accrues to the General Fund. Cash and cash equivalents applicable to a particular fund are readily identifiable. The State has invested the majority of its excess Compact Funds in a pooled investment fund which is managed under the control of the Federated Development Authority, an entity comprised of the FSM National Government and its four component states. Investment income originating from the pool accrues to the General Fund.

The deposit and investment policies of the State are governed by Title 13 of the Yap State Code. The Treasurer is responsible for ensuring that deposits of the General Fund are maintained in commercial checking or savings accounts of any financial institution whose assets are at least \$1 billion and whose deposits are subject to Federal Deposit Insurance Corporation (FDIC) insurance. The Governor is responsible for the investment of any monies of the State that are deemed not necessary for immediate use.

The Federated Development Authority has selected investment managers who are given authority to buy and sell securities. These investment managers may invest in stocks, bonds and cash equivalents, for which minimum standards of quality of such investments at the time of purchase shall be as follows:

- i. Cash equivalents - The investment manager may engage in all normally accepted short-term investment practices including, but not limited to U.S. Treasury and government agency securities, bankers acceptances, certificates of deposit, commercial paper and repurchase agreements using any of the foregoing as collateral. The following restrictions apply: (1) Commercial paper must be rated A-1/P-1 or higher by Standard & Poors Corporation and Moody's Investor Services; and (2) Certificates of deposit must be from FDIC insured banks or FSLIC insured savings and loan associations, both of which must have assets in excess of \$2 billion. Deposits in smaller institutions are acceptable, but must not exceed the amount of the insurance, unless collateralized by U.S. Treasury obligations at 102%.
- ii. Stocks - A "B" rating by a national rating service is required. Non-rated stocks, such as banks or insurance companies, must be equal in quality or higher.
- iii. Bonds – Investments in bonds are confined to issues rated "A" or higher by a national rating service, except in the case of U.S. Treasury or government agency obligations which are not rated.

The equity portfolio shall be diversified among issues and industry classifications. No more than 25% of the equity portfolio may be invested in any single classification, as described by the Standard and Poors 500 Index, unless prior approval is received from the Secretary of Finance.

No investment may be made in a single corporate entity which exceeds 5% of the total assets of the fund at the time of purchase without prior approval of the Secretary of Finance.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(2) Deposits and Investments, Continued

A. Deposits

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1 Deposits that are federally insured or collateralized with securities held by the State or its agent in the State's name;

Category 2 Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the State's name; or

Category 3 Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in the State's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the State's 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 or held by the pledging financial institution but not in the depositor-government's name. The State does not have a deposit policy for custodial credit risk.

As of September 30, 2008, the carrying amount of the primary government's total cash and cash equivalents was \$280,406 and the corresponding bank balance was \$384,940, which is maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2008, bank deposits in the amount of \$200,000 were FDIC insured. The State does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

B. Investments

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

Category 1 Investments that are insured or registered, or securities held by the State or its agent in the State's name;

Category 2 Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in the State's name; or

Category 3 Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the State's name.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(2) Deposits and Investments, Continued

B. Investments, Continued

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

As of September 30, 2008, the State's investments at fair value are as follows:

Fixed income securities:	
Domestic fixed income	\$ <u>20,204,822</u>
Other investments:	
Domestic equities	38,635,257
Cash management account	<u>156,183</u>
	<u>38,791,440</u>
	\$ <u>58,996,262</u>

As of September 30, 2008, the State's fixed income securities, including their Moody's Investors Service credit ratings, had the following maturities:

Investment Type	Rating Type	Maturity (in years)				Total
		Current	1-5	6-10	Over	
U.S treasury obligations	AAA	\$109,364	\$4,075,423	\$ 431,844	\$ 342,572	\$4,959,203
U.S. government agency obligations:						
California Water Sewer	AAA	-	-	-	27,124	27,124
Federal Farm Credit Bank	AAA	-	35,881	-	-	35,881
Federal Home Loan Bank	AAA	7,160	422,148	-	-	429,308
Federal Home Loan Mortgage Corporation	AAA	-	40,789	12,673	2,061,531	2,114,993
Federal National Mortgage Association	AAA	-	16,270	7,106	2,266,016	2,289,392
Government National Mortgage Association	AAA	-	-	-	161,159	161,159
Government National Mortgage Corporation	AAA	-	-	-	2,423,891	2,423,891
Housing Urban Development	AAA	-	7,128	-	-	7,128
Salt River Project	AAA	-	-	-	94,004	94,004
Sonoma County Pension	AAA	-	-	-	10,284	10,284
Tennessee Valley Authority	AAA	20,078	-	-	5,545	25,623
Texas Transportation	AAA	-	-	-	115,945	115,945
Corporate notes and bonds	A1	-	375,082	47,621	73,791	496,494
Corporate notes and bonds	A2	14,826	335,362	274,650	211,025	835,863
Corporate notes and bonds	A3	-	328,789	343,560	178,855	851,204
Corporate notes and bonds	AA1	-	181,016	153,675	-	334,691
Corporate notes and bonds	AA2	-	592,825	148,929	220,276	962,030
Corporate notes and bonds	AA3	2,065	124,003	244,715	144,755	515,538
Corporate notes and bonds	AAA	2,610	181,953	17,859	-	202,422
Corporate notes and bonds	B1	-	-	34,355	-	34,355

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(2) Deposits and Investments, Continued

B. Investments, Continued

Investment Type	Rating Type	Maturity (in years)				Total
		Current	1-5	6-10	Over	
Corporate notes and bonds	B2	-	2,162	-	-	2,162
Corporate notes and bonds	B3	-	-	-	67,098	67,098
Corporate notes and bonds	BA1	36,255	7,644	43,741	-	87,640
Corporate notes and bonds	BA3	-	52,456	-	-	52,456
Corporate notes and bonds	BAA1	-	879,460	580,377	44,610	1,504,447
Corporate notes and bonds	BAA2	128,088	377,072	227,769	220,037	952,966
Corporate notes and bonds	BAA3	4,952	231,764	114,071	27,569	378,356
Corporate notes and bonds	BAAI	110,000	33,200	-	-	143,200
Corporate notes and bonds	N/A	-	-	80,799	9,164	89,963
Grand Total		<u>\$435,398</u>	<u>\$8,300,427</u>	<u>\$2,763,744</u>	<u>\$8,705,251</u>	<u>\$20,204,820</u>

As of September 30, 2008, the General Fund holds 10.7% of the shares of the Bank of the Federated States of Micronesia in the amount of \$1,000,000, 24.5% of the shares of the Pacific Islands Development Bank in the amount of \$1,000,000, and an equity investment in Palau Micronesia Air (PMA) in the amount of \$500,000. As the fair market value of these investments, except for PMA, is not readily available, such have been recorded at cost. The shares in Palau Micronesia Air have been fully reserved for through an impairment loss.

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. With the exception of investments in U.S. government securities, which are explicitly or implicitly guaranteed by the United States government, all other investments must be rated in accordance with the State's investment policy.

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the State will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The State's investments are held and administered by trustees. Based on negotiated trust and custody contracts, all of these investments were held in the State's name by the State's custodial financial institutions at September 30, 2008.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the State. As of September 30, 2008, the State's investment in agency obligations of the Federal National Mortgage Association constituted 11.5% of its total investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The State does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(2) Deposits and Investments, Continued

B. Investments, Continued

Discretely Presented Component Units

The Yap Fishing Authority (YFA) holds an investment of 50% interest in Yap Fresh Tuna, Inc., an unconsolidated entity that should be consolidated into YFA in accordance with accounting principles generally accepted in the United States of America for which a related impairment loss of \$398,016 has been recognized.

(3) Receivables

Receivables as of September 30, 2008, for the primary government's individual major funds and nonmajor funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	<u>General</u>	Foreign Assistance <u>Grants</u>	Compact <u>Trust</u>	Nonmajor And Other <u>Funds</u>	<u>Totals</u>
Receivables:					
Loans	\$7,939,201	\$ -	\$ -	\$2,000,000	\$ 9,939,201
Federal agencies	-	612,182	-	-	612,182
FSM National Government	434,112	6,410,835	-	849,305	7,694,252
Taxes	171,044	-	-	-	171,044
Other	<u>251,337</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>251,337</u>
	8,795,694	7,023,017	-	2,849,305	18,668,016
Less: allowance for uncollectible accounts	<u>(7,796,252)</u>	<u>(4,988,262)</u>	<u>-</u>	<u>(2,813,742)</u>	<u>(15,598,256)</u>
Net receivables	<u>\$ 999,442</u>	<u>\$2,034,755</u>	<u>\$ -</u>	<u>\$ 35,563</u>	<u>\$ 3,069,760</u>

Loans receivable of the primary government as of September 30, 2008 are as follows:

Major Governmental Funds

General Fund:

Note receivable from the Yap Fishing Corporation, appropriated under YSL No. 2-96, uncollateralized, due and payable on or before June 11, 2004. This note has been fully provided for in the allowance for uncollectibles. \$ 6,400,000

Note receivable from the Yap Fishing Corporation, appropriated under YSL No. 3-8, uncollateralized, due September 30, 2004, interest at 6% per annum. This note has been fully provided for in the allowance for uncollectibles. 1,000,000

STATE OF YAP  
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Notes to Financial Statements  
September 30, 2008

(3) Receivables

Note receivable from the Yap State Public Service Corporation, uncollateralized, due in quarterly interest only payments through March 2003; monthly principal and interest payments of \$5,651 starting June 1, 2003; interest at 2%, maturing in May 2017.	<u>539,201</u>
	<u>7,939,201</u>

Nonmajor Governmental Funds

Note receivable from the Yap Fishing Corporation, appropriated under YSL No. 3-67, uncollateralized, non-interest bearing and payable on demand. This note has been fully provided for in the allowance for uncollectibles.	<u>2,000,000</u>
	<u>\$ 9,939,201</u>

Receivables for the State's discretely presented component units, including applicable allowances for uncollectible accounts, are as follows:

	<u>Yap Visitors Bureau</u>	<u>Yap State Public Service Corporation</u>	<u>Yap Fishing Authority</u>	<u>The Diving Seagull, Inc.</u>	<u>Totals</u>
Receivables:					
General	\$ 62,452	\$ 911,136	\$ 659,596	\$ 649,342	\$ 2,282,526
Other	<u>84,894</u>	<u>8,253</u>	<u>36,673</u>	<u>86,849</u>	<u>216,669</u>
	147,346	919,389	696,269	736,191	2,499,195
Less: allowance for uncollectible accounts	<u>(62,365)</u>	<u>(143,670)</u>	<u>(675,888)</u>	<u>(649,342)</u>	<u>(1,531,265)</u>
Net receivables	<u>\$ 84,981</u>	<u>\$ 775,719</u>	<u>\$ 20,381</u>	<u>\$ 86,849</u>	<u>\$ 967,930</u>

(4) Interfund Receivables and Payables

Receivables and payables between funds reflected as due to/from other funds in the combined balance sheet at September 30, 2008, are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Foreign Assistance Grants	\$ 4,096,508
General	Compact Capital Projects	11,009,670
General	Nonmajor governmental funds	338,552
Foreign Assistance Grants	General	2,295,386
Nonmajor governmental funds	General	<u>64,369</u>
		<u>\$ 17,804,485</u>

STATE OF YAP  
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Notes to Financial Statements  
September 30, 2008

(5) Fixed Assets

Capital asset activities of the primary government for the year ended September 30, 2008, are as follows:

	Balance October 1, 2007	Additions	Retirements	Balance September 30, 2008
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 3,120,610	\$ _____	\$ _____	\$ 3,120,610
	<u>3,120,610</u>	<u>_____</u>	<u>_____</u>	<u>3,120,610</u>
Capital assets, being depreciated:				
Buildings	13,424,788	-	-	13,424,788
Heavy equipment	3,627,746	1,076,729	-	4,704,475
Furniture and Fixtures	11,041	12,370	-	23,411
Vehicles	1,412,879	292,659	-	1,705,538
Boats	5,080,297	41,975	-	5,122,272
Infrastructure	<u>82,316,716</u>	<u>_____</u>	<u>_____</u>	<u>82,316,716</u>
Total capital assets, being depreciated	<u>105,873,467</u>	<u>1,423,733</u>	<u>_____</u>	<u>107,297,200</u>
Less accumulated depreciation for:				
Buildings	(6,406,030)	(493,147)	-	(6,899,177)
Heavy equipment	(2,721,909)	(256,933)	-	(2,978,842)
Furniture & Fixtures	(669)	(2,709)	-	(3,378)
Vehicles	(768,193)	(220,546)	-	(988,739)
Boats	(1,234,366)	(215,671)	-	(1,450,037)
Infrastructure	<u>(58,862,715)</u>	<u>(2,140,133)</u>	<u>_____</u>	<u>(61,002,848)</u>
	<u>(69,993,882)</u>	<u>(3,329,139)</u>	<u>_____</u>	<u>(73,323,021)</u>
Total capital assets, being depreciated, net	<u>38,879,585</u>	<u>(1,905,406)</u>	<u>_____</u>	<u>33,974,179</u>
Governmental activities capital assets, net	<u>\$39,000,195</u>	<u>\$(1,905,406)</u>	<u>\$ _____</u>	<u>\$37,094,789</u>

(5) Fixed Assets, Continued

Depreciation expense was charged to functions/programs of the primary government's governmental activities as follows:

Judiciary	\$ 5,113
Council of traditional leaders	5,174
Public auditor	1,544
General government	60,895
Economic development	120,635
Public safety	42,792
Community affairs	279,949
Education	287,413
Public works and transportation	2,331,521
Health services	87,226
Boards and commissions	6,877
Payment to component units	<u>100,000</u>
	<u>\$ 3,329,139</u>

STATE OF YAP  
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Notes to Financial Statements  
September 30, 2008

(6) Operating Transfers In/Out

Operating transfers in/out for each major governmental fund and nonmajor governmental funds in the aggregate, for the year ended September 30, 2008, are as follows:

<u>Source</u>	<u>Recipient</u>	<u>Transfers Out</u>	<u>Transfers In</u>
<u>Major Governmental Funds</u>			
General	Foreign Assistance Grants	\$ 146,324	\$ 146,324
Compact Capital Projects	Foreign Assistance Grants	<u>297,818</u>	<u>297,818</u>
		<u>\$ 444,142</u>	<u>\$ 444,142</u>

Transfers are used to: 1) move revenues from the fund that enabling legislation or budget requires to collect them to the fund that enabling legislation or budget requires to expend them, 2) use unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations and U.S. federal matching requirements, and 3) record reductions in interfund loans for amounts that are not expected to be repaid.

(7) Long-Term Obligations

Primary Government

Land Acquisition Claims Payable

As of September 30, 2008, \$249,607 in long-term payments due under land purchase agreements was identified by the State. This total comprises indefinite land use payments and other lease payments for which payment dates cannot be determined due to heir ship disputes.

The State implemented an Early Retirement Scheme (ERS) in which employees holding certain nonessential positions as identified by the State were retired early with a payout of the equivalent of two-years' wages. This ERS program is funded by a \$3,500,000 loan from the ADB through the FSM National Government. The activities of the ERS Program are recorded in the General Fund.

The ADB loan has a grace period of ten years with the first payment due in February 2008 and the last payment in August 2038. However, pursuant to the terms of the Financing Agreement between the State and the FSM National Government, the State is required to deposit into the ERS Trust account held in the name of the State within the FSM National Government investment portfolio, 100% of the outstanding principal balance by September 30, 2002. As of September 30, 2008, the outstanding balance is \$3,422,450.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(7) Long-term Obligations, Continued

Primary Government, Continued

Asian Development Bank (ADB) Early Retirement Program Loan

The State entered into an agreement with the Federated States of Micronesia National Government (FSM) to borrow a portion of the proceeds of the FSM Program Loan with ADB (Loan Number 1873 (SF) and Loan Number 1874 FSM (SF)), for the purpose of promoting private sector development in Yap, with interest at 1 to 1½%. The principal payments shall be made in 32 equal semi-annual payments with the first payment due on May 15, 2011 and the last payment on November 15, 2026. As of September 30, 2008, the State drewdown an additional \$286,976 of the \$1,370,910 total borrowing. The remaining increase of \$148,132 is due to a Special Drawing Rights (SDR) adjustment recorded during the year ended September 30, 2008.

The State entered into an agreement with the FSM to borrow a portion of the proceeds of the Basic Social Services Program Loan with ADB (Loan Number 1816 FSM (SF)), for the purpose of promoting basic social services in Yap, non-interest bearing with a service charge of 1% per annum on the amount of the loan withdrawn from the Loan Account. The loan is payable semiannually commencing February 1, 2009, at which time the service charge increases to 1.5% per annum, with a maturity date of August 1, 2032. As of September 30, 2008, the State drewdown an additional \$194,015 of the \$456,213 borrowing. The remaining increase of \$1,634 is due to a Special Drawing Rights (SDR) adjustment recorded during the year ended September 30, 2008.

Annual debt service requirements to maturity for principal and interest are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	\$ 69,850	\$ 51,796	\$ 121,646
2010	150,176	60,235	210,411
2011	150,176	58,331	208,507
2012	150,176	56,428	206,604
2013	150,176	170,468	320,644
2014-1018	882,044	218,243	1,100,287
2019-2023	1,176,773	147,678	1,324,451
2024-2028	1,119,862	77,308	1,197,170
2029-2033	841,733	18,962	860,695
2034-2037	<u>558,607</u>	<u>-</u>	<u>558,607</u>
	<u>\$5,249,573</u>	<u>\$859,449</u>	<u>\$6,109,022</u>

Funds for the repayment of the ADB loan are expected to be derived from the annual appropriations for salaries and wages earmarked for the positions abolished under the Early Retirement Scheme. The Financing Agreement requires the State to continue to appropriate salaries for the abolished positions and deposit the appropriate funds into the ERS Trust Account. \$3,500,000 identified for future debt service payments is included in the General Fund reserve for related assets of which \$2,143,304 is actually deposited in an investment account held jointly with the FSM National Government. That investment account is restricted for the repayment of this debt.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(7) Long-term Obligations, Continued

Primary Government, Continued

Asian Development Bank (ADB) Early Retirement Program Loan, Continued

Other long-term liabilities will be liquidated in the future from governmental funds. During the year ended September 30, 2008, the following changes occurred in the primary government's long-term liabilities in the statement of net assets:

	<u>Balance October 1, 2007</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30, 2008</u>	<u>Due Within One Year</u>
Loan payable:					
ADB loan	\$ 4,681,366	\$645,757	\$(77,550)	\$5,249,573	\$ 69,850
Other:					
Compensated absences	556,823	109,018	(85,655)	580,186	85,655
Land acquisition claims	<u>249,607</u>	<u>-</u>	<u>-</u>	<u>249,607</u>	<u>-</u>
	<u>806,430</u>	<u>109,018</u>	<u>(85,655)</u>	<u>829,793</u>	<u>85,655</u>
	<u>\$ 5,487,796</u>	<u>\$754,775</u>	<u>\$163,205</u>	<u>\$6,079,366</u>	<u>\$155,505</u>

The State was advised of a change in its ADB related debt due to the FSM National Government passing through certain foreign exchange losses. The State is currently discussing this matter with the FSM National Government and any additional adjustments that may result from this discussion will be accounted for prospectively. The increase of \$645,757 includes \$164,766 due to the Special Drawing Rights (SDR) adjustment recorded during the year ended September 30, 2008.

Discretely Presented Component Units

Yap State Public Service Corporation (YSPSC)

Loan payable to the FSM National Government for construction of certain water projects. This loan is uncollateralized and is a subsidiary loan to a loan agreement between the Asian Development Bank (ADB) and the FSM National Government, with interest at 6.82% on the outstanding balance; however, the FSM National Government has waived the interest payment requirement. The loan is repayable in Special Drawing Rights commencing August 2007 with the final payment due in February 2032. The loan is collateralized by the guarantee of the FSM National Government.

\$ 2,202,712

Uncollateralized note payable to the State; monthly principal and interest payments of \$5,651 starting June 1, 2003; interest at 2%, maturing in May 2017.

539,163

Note payable to United States of America, acting through the Rural Housing Service, for the construction of the warehouse facility and main office. The note is payable in monthly installments of \$1,075 including interest at 4.625% commencing March 26, 2003 and maturing in September 2013. The note is collateralized by YSPSC's equipment, furniture and fixtures located at YSPSC's office.

51,280

2,793,155

STATE OF YAP  
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Notes to Financial Statements  
September 30, 2008

(7) Long-term Obligations, Continued

Discretely Presented Component Units, Continued

The Diving Seagull, Inc.

On July 28, 2006, the Company signed a five-year loan agreement with the Federated States of Micronesia Development Bank (FSMDB) authorizing a maximum loan of \$1,300,000 to cover the dry-dock costs of the fishing vessel. The agreement stipulates a 1.5% loan fee and interest rate of 9%. Interest is due monthly during the six-month grace period. Interest and principal are payable in monthly installments of \$26,986 beginning January 30, 2007. Part of the loan agreement requires the Company to establish a joint account with FSMDB and to deposit \$3,000 per month until the loan is fully paid. On August 11, 2006, the Company paid-off its existing loan with FSMDB as a condition to the granting of the new loan. On February 16, 2007, a new loan was granted by FSMDB amounting to \$1,300,000 to cover additional dry dock cost of the fishing vessel at an interest rate of 9%. Interest and principal are payable in monthly installments of \$28,606 beginning June 15, 2007. The note is collateralized by a chattel mortgage on all property and equipment, including the fishing vessel Mathawmarfach.

1,984,612  
\$ 4,777,767

Annual debt service requirements to maturity for principal and interest are as follows:

<u>Year ending</u> <u>September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	\$ 626,460	\$ 166,776	\$ 793,236
2010	676,228	117,007	793,235
2011	730,555	62,680	793,235
2012	416,471	12,808	429,279
2013	112,874	5,468	118,342
2014 - 2018	580,192	9,149	589,341
2019 - 2023	605,630	-	605,630
2024 - 2028	605,630	-	605,630
2029 - 2032	<u>423,727</u>	<u>-</u>	<u>423,727</u>
	<u>\$4,777,767</u>	<u>\$373,888</u>	<u>\$5,151,655</u>

During the year ended September 30, 2008, the following changes occurred in the State's discretely presented component unit's long term liabilities.

	<u>Balance</u> <u>October 1,</u> <u>2007</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>September 30,</u> <u>2008</u>	<u>Due Within</u> <u>One Year</u>
Loan payable:					
YSPSC	\$ 2,900,597	\$ -	\$ (107,442)	\$ 2,793,155	\$ 113,723
DSI	<u>2,361,529</u>	<u>-</u>	<u>(376,917)</u>	<u>1,984,612</u>	<u>512,737</u>
	<u>\$ 5,262,126</u>	<u>\$ -</u>	<u>\$ (484,359)</u>	<u>\$ 4,777,767</u>	<u>\$ 626,460</u>

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(8) Continuing Appropriations

Continuing appropriations as of September 30, 2008, are as follows:

Major Governmental Funds

General Fund:

Autopsies (YSL No. 5-47)	\$ 18,191
Disaster/Search and Rescue (YSL No. 5-84)	1,563
YWA Daycare Bldg Matching/Yap State Scholarship (YSL No. 6-48)	<u>20,256</u>
	\$ <u>40,010</u>

Compact Capital Projects Fund:

Yap State Development Investment Loan (YSL No. 5-1)	\$ 200,000
Mobil Fuel Farm Retaining Wall (YSL No. 6-81)	397,465
Infrastructure Maintenance Fund (YSL No. 7-14)	431,567
YSPSC Fuel Subsidy and Renewable Energy Feasibility Study (YSL No. 7-34)	8,000
Loan to YSPSC (YSL No. 7-38)	<u>1,600,000</u>
	\$ <u>2,637,032</u>

Foreign Assistance Grants

Yap Community Development Program Matching (YSL No.-5-34)	\$ <u>150,000</u>
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(9) Contingencies

Sick Leave

It is the policy of the State to record expenditures for sick leave when leave is actually taken. Sick leave is compensated time for absence during working hours arising from employee illness or injury.

Insurance Coverage

The State does not maintain insurance coverage for a significant amount of fixed assets. In the event of a catastrophe, the State may be self-insured to a material extent. The State has not recognized material losses in its financial statements as a result of this matter.

Federal Grants

The State participates in a number of federally assisted grant programs. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Cumulative questioned costs of \$3,376,248 relating to fiscal years 2001 through 2007 have been set forth in the State's Single Audit Report for the year ended September 30, 2008. The ultimate disposition of these questioned costs can be determined only by final action of the respective grantor agencies. Therefore, no provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(9) Contingencies, Continued

Litigation

The State is party to several legal proceedings arising from governmental operations. Claims are filed with the State's Attorney General. Approved claims are usually paid under general appropriations to the affected government agency. At September 30, 2008, there existed several unapproved claims. The State's Attorney General is of the opinion that the State Liability Act has established claims limits of \$40,000 for wrongful injuries and \$20,000 for deaths. Current claims against the State exist but do not appear to be material. Management has not provided for such claims in the accompanying financial statements as it is not currently possible to estimate the State's potential liability, if any, arising from these claims.

Indefinite Land Use Sites

Payment obligations on rental lands termed "Indefinite Land Use Sites" were originally undertaken by the Trust Territory of the Pacific Islands (TTPI), for which obligation on these lands ceased in May, 1984. Subsequent to May 1984, responsibility to rent or purchase the sites was transferred to the State. The State's Division of Land and Surveys has estimated that the State may be responsible for funding the indefinite land use sites for back rent with interest. The State is actively attempting to negotiate purchase prices for these properties.

Federal and Other Reimbursable Costs

After the fiscal year ended September 30, 2008, the FSM National Government proposed resolution of certain long outstanding uncollected federal and other reimbursable grants. The State is considering the proposal and believes that resolution of this matter will not adversely impact the accompanying financial statements. Any recoveries arising from this resolution will be recorded in the financial statements when they become specifically measurable and are collected in cash.

(10) Creation of a Trust Fund

During fiscal year 2008, the Yap State Legislature, through YSL 7-17, allowed for the creation of a State Trust Fund, to which \$30 million of State cash and investments could be transferred. The specific assets to be transferred were not cited in the enabling legislation and management has therefore yet to transfer assets to this fund pending identification and agreement upon the assets that will be so transferred.

(11) Restatement

Subsequent to the issuance of the State's 2007 financial statements, management of the State determined that certain vehicles were not recorded as capital assets of the governmental activities. As a result of this determination, the account balances have been restated from the amounts previously reported as follows:

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Financial Statements  
September 30, 2008

(11) Restatement

	As Previously <u>Reported</u>	<u>As Restated</u>
At September 30:		
Noncurrent assets:		
Capital assets, net of accumulated depreciation	\$ <u>35,224,585</u>	\$ <u>39,000,195</u>
Net assets:		
Invested in capital assets, net of related debt	\$ <u>35,224,585</u>	\$ <u>39,000,195</u>
For the year ended September 30:		
Operating grants and contributions	\$ <u>15,414,667</u>	\$ <u>19,190,277</u>
Net assets at the end of the year	\$ <u>102,834,136</u>	\$ <u>106,365,770</u>

STATE OF YAP  
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REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2008

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Schedule of Revenues, Expenditures and Changes in Fund Balance  
Budget and Actual - General Fund  
Year Ended September 30, 2008

	Budgeted Amounts		Actual - Budgetary	Variance with Final Budget
	Original	Final	Basis (see Note 1)	
<b>Revenues:</b>				
Net decrease in the fair value of investments	-	-	(8,754,261)	(8,754,261)
Other	5,133,050	7,460,427	4,154,211	(3,306,216)
Total revenues	5,133,050	7,460,427	(4,600,050)	(12,060,477)
<b>Expenditures:</b>				
<b>Current:</b>				
Judiciary	227,365	227,365	204,974	22,391
Council of traditional leaders	212,554	218,484	211,763	6,721
General government	1,252,966	1,252,966	864,001	388,965
Economic development	71,470	99,175	(36,313)	135,488
Public safety	548,148	548,148	510,759	37,389
Community affairs	315,200	336,140	315,605	20,535
Education	16,567	16,567	-	16,567
Public works and transportation	1,781,611	2,413,215	1,915,368	497,847
Health services	216,625	536,967	537,506	(539)
Boards and commissions	43,595	43,595	47,103	(3,508)
Payments to component units	-	1,320,856	1,889,716	(568,860)
Other appropriations	274,390	274,390	266,237	8,153
Total expenditures	4,960,491	7,287,868	6,726,719	561,149
Excess (deficiency) of revenues over (under) expenditures	172,559	172,559	(11,326,769)	(11,499,328)
<b>Other financing sources (uses):</b>				
Operating transfers in	-	-	-	-
Operating transfers out	(172,559)	(172,559)	(146,324)	26,235
Total other financing sources (uses), net	(172,559)	(172,559)	(146,324)	26,235
Net change in unreserved fund balance	-	-	(11,473,093)	(11,473,093)
<b>Other changes in unreserved fund balance:</b>				
Decrease in reserve for related assets	-	-	1,115	1,115
Increase in reserve for continuing appropriations	-	-	552,751	552,751
Unreserved fund balance at the beginning of the year	38,517,190	38,517,190	38,517,190	-
Unreserved fund balance at the end of the year	<u>\$ 38,517,190</u>	<u>\$ 38,517,190</u>	<u>\$ 27,597,963</u>	<u>\$ (10,919,227)</u>

See accompanying notes to required supplementary information - budgetary reporting.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Notes to Required Supplementary Information - Budgetary Reporting  
September 30, 2008

(1) Budgetary Information

An annual appropriated budget is adopted by the State's Legislature for the General Fund and Compact Programs through an Appropriations Act. However, additional appropriations and budget modifications occur throughout the year. The majority of unencumbered appropriations lapse as of year end unless specifically extended by the State's Legislature. Budgets for special revenue funds, except the Compact Program Fund, are not included in the annual Appropriations Act. Accordingly, a budget to actual presentation for special revenue funds, except the Compact Program Fund, is not required or presented. Project-length financial plans are generally adopted for all capital project funds.

Encumbrance accounting is utilized for budgetary control purposes. Encumbrances outstanding at year-end are reported as reservations of fund balance and will be funded as expenditures in the ensuing year. Encumbrances remain as reservations of fund balance until becoming expended or canceled. If an encumbrance is subsequently canceled, the funds revert to the applicable unreserved fund balance unless otherwise required by law.

Budgetary expenditures, which are on a basis other than GAAP, represent current charges against appropriations; current charges consist of all current year liquidated and unliquidated encumbrances. Budgetary expenditures are therefore determined by subtracting both current year liquidations of prior year encumbrances and unliquidated prior year encumbrances from the combined total of current year. When reviewed in relation to respective budgets, budgetary expenditures provide the principal means of evaluating current year operating performance and management stewardship. Amounts included on the Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund (which are presented on a non-GAAP budgetary basis) are reconciled to unreserved fund balance of the Combined Balance Sheet within the other charges in unreserved fund balance section of that statement.

(2) Reconciliation – GAAP and Budgetary Bases of Accounting

Encumbrance accounting is employed in governmental funds. For budgetary purposes, the encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP reporting purposes, encumbrances outstanding at year end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be reappropriated and honored during the subsequent fiscal year.

Net change in fund balance	\$ (10,187,659)
Increase in encumbrances	<u>(1,285,434)</u>
Net change in unreserved fund balance	\$ <u>(11,473,093)</u>

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

OTHER SUPPLEMENTARY INFORMATION

YEAR ENDED SEPTEMBER 30, 2008

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Combining Schedule of Expenditures by Account  
Governmental Funds  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	General	Special Revenue	Capital	Permanent	Other Governmental Funds	Totals	
		Foreign Assistance Grants	Projects Compact Capital Projects	Compact Trust		2008	2007
Expenditures:							
Salaries and wages	\$ 2,206,250	\$ 5,550,797	\$ 44,472	\$ -	\$ 1,091	\$ 7,802,610	\$ 7,596,140
Grants and subsidies	106,651	538,970	31,130	-	177,616	854,367	1,988,064
Utilities	359,382	821,033	4,781	-	-	1,185,196	1,339,459
Contractual services	176,210	923,622	322,389	-	268,402	1,690,623	1,269,839
Supplies and materials	60,538	1,130,096	576	-	-	1,191,210	462,000
Construction	129,930	1,348,659	-	-	-	1,478,589	1,850,969
Scholarship and training	-	487,451	-	-	-	487,451	534,312
Travel	146,427	906,292	7,288	-	-	1,060,007	1,223,105
Capital outlay	83,149	1,785,222	4,044	-	46,594	1,919,009	1,695,853
Rentals	3,760	13,304	320	-	-	17,384	159,674
Food stuffs	39,545	204,199	-	-	-	243,744	208,249
Communications	92,586	179,240	1,107	-	-	272,933	283,535
Printing and reproduction	17,302	131,671	90	-	-	149,063	50,950
Medical supplies	-	942,689	-	-	-	942,689	782,611
Medical referral	448,955	85,616	-	-	-	534,571	236,682
Repairs and maintenance	30,479	667,632	64	-	9,889	708,064	193,813
Freight	4,444	178,488	69,543	-	60	252,535	391,082
Professional services	-	216,146	86,263	-	-	302,409	368,184
POL	1,185,866	267,569	568,628	-	80,180	2,102,243	695,072
Allowances	113,330	12,885	-	-	-	126,215	114,680
Leased housing	37,475	231,386	-	-	-	268,861	227,047
Other	199,006	1,392,153	125,984	-	177,198	1,894,341	2,197,533
	<u>\$ 5,441,285</u>	<u>\$ 18,015,120</u>	<u>\$ 1,266,679</u>	<u>\$ -</u>	<u>\$ 761,030</u>	<u>\$ 25,484,114</u>	<u>\$ 23,868,853</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

GENERAL FUND

September 30, 2008

The general fund is used to account for resources traditionally associated with government which are not required legally or by sound financial management to be accounted for in another fund. The United States Compact of Free Association current account and inflation adjustment funds associated with the current account are accounted for in this fund in addition to local taxes and other revenues.

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Revenues, Expenditures by Function,  
and Changes in Fund Balance - General Fund  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	2008	2007
Revenues:		
Revenue sharing:		
Import tax	\$ 824,311	\$ 785,883
Fuel tax	84,950	63,060
Income tax	502,231	636,531
Business gross receipts tax	752,271	808,851
Unallocated	-	(251,021)
	2,163,763	2,043,304
Excise taxes:		
Alcoholic beverages	359,493	372,058
Gasoline and diesel	83,281	108,287
Tobacco	228,050	184,263
Other excise taxes	453,706	502,827
	1,124,530	1,167,435
Fees and charges:		
Licenses and permits	92,660	87,663
Fines/sale of confiscated property	61,104	98,542
Leases and other rentals	194,139	278,685
	347,903	464,890
Departmental charges:		
Sea transportation	181,410	239,374
Hospital services	264,303	-
Other	27,484	37,004
	473,197	276,378
Interest and dividends	19,566	22,333
Net (decrease) increase in the fair value of investments	(8,773,827)	9,453,223
Other revenues	44,818	324,814
Total revenues	(4,600,050)	13,752,377
Expenditures:		
Current:		
Judiciary	209,797	171,378
Councils of Traditional Leaders:		
Council of Pilung	100,321	96,100
Council of Tamol	108,912	116,410
	209,233	212,510
Public Auditor	-	500
General government:		
Office of the Governor	198,210	159,608
State Legislature	395,642	470,717
Office of Administrative Services	164,482	414,800
Office of Planning, Budget and Statistics	110,160	88,691
Disaster relief programs	-	901
	868,494	1,134,717

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Revenues, Expenditures by Function,  
and Changes in Fund Balance - General Fund, Continued  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	2008	2007
Expenditures, continued:		
Current, continued:		
Economic Development:		
Department of Resources and Development	826	505,031
Public Safety:		
Department of Public Safety/Attorney General	505,551	582,019
Community Affairs		
Department of Public Affairs	307,938	472,613
Education:		
Department of Education	118,979	358,398
Public Works and Transportation:		
Department of Public Works and Transportation	1,873,490	1,818,198
Health Services:		
Department of Health Services	526,160	-
Boards and Commissions:		
EPA Administration Board	468	-
Farmers Home Administration	21,208	21,412
Historic Preservation Office	10,243	32,605
Yap Investment Trust	22,110	16,432
	54,029	70,449
Payments to component units:		
Yap Visitor's Bureau	-	109,304
Yap State Public Service Corporation	499,676	-
Public Transportation System	-	89,928
	499,676	199,232
Other appropriations:		
Micronesian Legal Services Corporation	41,280	50,000
Japan Overseas Cooperation Volunteers	10,853	9,191
Peace Corps Program	17,550	21,018
Yap Community Action Program	197,429	136,758
Other	-	-
	267,112	216,967
Total expenditures	5,441,285	5,742,012
Excess of revenues over expenditures	(10,041,335)	8,010,365
Other financing sources (uses):		
Operating transfers in	-	164,490
Operating transfers out	(146,324)	(1,216,620)
Total other financing sources (uses), net	(146,324)	(1,052,130)
Special Items:		
Write-off of advances	-	(788,627)
Net change in fund balance	(10,187,659)	6,169,608
Fund balance at the beginning of the year	46,017,497	39,847,889
Fund balance at the end of the year	\$ 35,829,838	\$ 46,017,497

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Revenues, Expenditures and Changes in Fund Balance  
Budget and Actual - General Fund  
Year Ended September 30, 2008

	Budgeted Amounts		Actual Amounts	Variance
	Original	Final		
<b>Revenues:</b>				
Net increase in the fair value of investments	\$ -	\$ -	\$ (8,754,261)	\$ (8,754,261)
Other revenues	5,133,050	7,460,427	4,154,211	(3,306,216)
Total revenues	<u>5,133,050</u>	<u>7,460,427</u>	<u>(4,600,050)</u>	<u>(12,060,477)</u>
<b>Expenditures:</b>				
<b>Current:</b>				
Judiciary	227,365	227,365	204,974	22,391
<b>Councils of Traditional Leaders:</b>				
Council of Pilung	106,830	106,830	102,441	4,389
Council of Tamol	105,724	111,654	109,322	2,332
	<u>212,554</u>	<u>218,484</u>	<u>211,763</u>	<u>6,721</u>
Public Auditor	-	-	-	-
<b>General government:</b>				
Office of the Governor	210,930	210,930	203,636	7,294
State Legislature	397,813	397,813	397,756	57
Office of Administrative Services	524,828	524,828	155,568	369,260
Office of Planning, Budget and Statistics	117,832	117,832	107,041	10,791
Disaster relief programs	1,563	1,563	-	1,563
	<u>1,252,966</u>	<u>1,252,966</u>	<u>864,001</u>	<u>388,965</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Statement of Revenues, Expenditures and Changes in Fund Balance  
Budget and Actual - General Fund, Continued  
Year Ended September 30, 2008

	Budgeted Amounts		Actual Amounts	Variance
	Original	Final		
Expenditures, continued:				
Current, continued:				
Economic Development:				
Department of Resources and Development	71,470	99,175	(36,313)	135,488
Public Safety:				
Department of Public Safety/Attorney General	548,148	548,148	510,759	37,389
Community Affairs:				
Department of Public Affairs	315,200	336,140	315,605	20,535
Education:				
Department of Education	16,567	16,567	-	16,567
Public Works and Transportation:				
Department of Public Works and Transportation	1,781,611	2,413,215	1,915,368	497,847
Health services:				
Department of Health Services	216,625	536,967	537,506	(539)
Boards and Commissions:				
EPA Administration Board	-	-	-	-
Farmers Home Administration	21,915	21,915	21,778	137
Historic Preservation Office	-	-	4,823	(4,823)
Yap Investment Trust	21,680	21,680	20,502	1,178
	43,595	43,595	47,103	(3,508)
Payments to component units:				
Yap Visitor's Bureau	-	-	-	-
Yap State Public Service Corporation	-	1,260,856	1,829,716	(568,860)
Public Transportation System	-	60,000	60,000	-
	-	1,320,856	1,889,716	(568,860)
Other appropriations:				
Micronesian Legal Services Corporation	41,280	41,280	41,280	-
Japan Overseas Cooperation Volunteers	16,000	16,000	10,612	5,388
Peace Corps Program	21,000	21,000	16,916	4,084
Yap CAP	196,110	196,110	197,429	(1,319)
	274,390	274,390	266,237	8,153
Total expenditures	4,960,491	7,287,868	6,726,719	561,149
Excess of revenues over expenditures	172,559	172,559	(11,326,769)	(11,499,328)
Other financing sources (uses):				
Operating transfers in				-
Operating transfers out	(172,559)	(172,559)	(146,324)	26,235
Total other financing sources (uses), net	(172,559)	(172,559)	(146,324)	26,235
Special Items:				
Write-off of investments	-	-	-	-
Net change in fund balance	-	-	(11,473,093)	(11,473,093)
Other changes in unreserved fund balance:				
Decrease in reserve for related assets	-	-	1,115	1,115
Increase in reserve for continuing appropriations	-	-	552,751	552,751
Unreserved fund balance at the beginning of the year	38,517,190	38,517,190	38,517,190	-
Unreserved fund balance at the end of the year	<u>\$ 38,517,190</u>	<u>\$ 38,517,190</u>	<u>\$ 27,597,963</u>	<u>\$ (10,919,227)</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Combined Balance Sheet  
Nonmajor Governmental Funds  
September 30, 2008  
(with comparative totals as of September 30, 2007)

	Other Special Revenue	Other Capital Projects	Totals	
			2008	2007
<u>ASSETS</u>				
Cash and cash equivalents	\$ 229,545	\$ -	\$ 229,545	\$ 229,277
Equity interest in internal investment pool	-	-	-	-
Receivables, net:				
CFSM	-	35,563	35,563	1,633
Due from other funds	254,077	84,475	338,552	382,503
Total assets	<u>\$ 483,622</u>	<u>\$ 120,038</u>	<u>\$ 603,660</u>	<u>\$ 613,413</u>
<u>LIABILITIES AND FUND BALANCES</u>				
Liabilities:				
Accounts payable	\$ 13,418	\$ 18,248	\$ 31,666	\$ 24,082
Other liabilities and accruals	4,454	36,572	41,026	41,022
Deferred revenue	-	-	-	-
Due to other funds	-	64,369	64,369	64,369
Total liabilities	<u>17,872</u>	<u>119,189</u>	<u>137,061</u>	<u>129,473</u>
Fund balances:				
Reserved for:				
Encumbrances	1,180	186,090	187,270	126,491
Continuing appropriations	-	-	-	-
Unreserved:				
Special revenue funds	464,570	-	464,570	432,470
Capital projects funds	-	(185,241)	(185,241)	(75,021)
Total fund balances	<u>465,750</u>	<u>849</u>	<u>466,599</u>	<u>483,940</u>
Total liabilities and fund balances	<u>\$ 483,622</u>	<u>\$ 120,038</u>	<u>\$ 603,660</u>	<u>\$ 613,413</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Combined Statement of Revenues, Expenditures by Function,  
and Changes in Fund Balances  
Nonmajor Governmental Funds  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	Other Special Revenue	Other Capital Projects	Totals	
			2008	2007
Revenues:				
Federal contributions and other grants	\$ -	\$ -	\$ -	\$ -
CFSM grants	-	548,503	548,503	185,173
Excise taxes	181,816	-	181,816	192,625
Fees and charges	13,370	-	13,370	13,511
Total revenues	<u>195,186</u>	<u>548,503</u>	<u>743,689</u>	<u>391,309</u>
Expenditures by function:				
Current:				
General government	106,852	94,858	201,710	313,274
Community affairs	-	452,432	452,432	-
Economic development	56,234	-	56,234	46,341
Public safety	-	-	-	-
Education	-	-	-	-
Public works and transportation	-	50,654	50,654	-
Health services	-	-	-	-
Payments to component units	-	-	-	5,000
Total expenditures	<u>163,086</u>	<u>597,944</u>	<u>761,030</u>	<u>364,615</u>
Deficiency of revenues under expenditures	<u>32,100</u>	<u>(49,441)</u>	<u>(17,341)</u>	<u>26,694</u>
Other financing sources:				
Loan Proceeds	-	-	-	-
Operating transfers in	-	-	-	-
Total other financing sources	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balances	32,100	(49,441)	(17,341)	26,694
Fund balances at the beginning of the year	<u>433,650</u>	<u>50,290</u>	<u>483,940</u>	<u>457,246</u>
Fund balances at the end of the year	<u>\$ 465,750</u>	<u>\$ 849</u>	<u>\$ 466,599</u>	<u>\$ 483,940</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Combined Statement of Revenues, Expenditures by Account,  
and Changes in Fund Balances  
Nonmajor Governmental Funds  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	Other	Other	Totals	
	Special Revenue	Capital Projects	2008	2007
Revenues:				
Federal contributions and other grants	\$ -	\$ -	\$ -	\$ -
CFSM grants	-	548,503	548,503	185,173
Excise taxes	181,816	-	181,816	192,625
Fees and charges	13,370	-	13,370	13,511
Total revenues	<u>195,186</u>	<u>548,503</u>	<u>743,689</u>	<u>391,309</u>
Expenditures by account:				
Salaries and wages	-	1,091	1,091	12,203
Grants and subsidies	77,616	100,000	177,616	85,256
Utilities	-	-	-	-
Contractual services	-	268,402	268,402	34,991
Supplies and materials	-	-	-	-
Construction	-	-	-	95,041
Scholarship and training	-	-	-	-
Travel	-	-	-	1,150
Capital outlay	16,419	30,175	46,594	2,585
Rentals	-	-	-	2,200
Food stuffs	-	-	-	1,983
Communications	-	-	-	-
Printing and reproduction	-	-	-	-
Repairs and maintenance	8,911	978	9,889	1,869
Freight	-	60	60	-
Professional services	-	-	-	38,744
POL	-	80,180	80,180	7,039
Other	60,140	117,058	177,198	81,554
Total expenditures	<u>163,086</u>	<u>597,944</u>	<u>761,030</u>	<u>364,615</u>
Deficiency of revenues under expenditures	<u>32,100</u>	<u>(49,441)</u>	<u>(17,341)</u>	<u>26,694</u>
Other financing sources:				
Loan proceeds	-	-	-	-
Operating transfers in	-	-	-	-
Total other financing sources	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balances	32,100	(49,441)	(17,341)	26,694
Fund balances at the beginning of the year	<u>433,650</u>	<u>50,290</u>	<u>483,940</u>	<u>457,246</u>
Fund balances at the end of the year	<u>\$ 465,750</u>	<u>\$ 849</u>	<u>\$ 466,599</u>	<u>\$ 483,940</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

NONMAJOR GOVERNMENTAL FUNDS - SPECIAL REVENUE FUNDS

September 30, 2008

Special revenue funds are used to account for specific revenues that are legally restricted for particular purposes. A brief discussion of the State's Nonmajor Governmental Funds - Special Revenue Funds as of September 30, 2008, follows:

Section 221(b) Special Block Grant Fund

This fund is used to account for financial transactions related to the Compact program accounts under Section 221(b) of the Compact of Free Association.

Other U.S. Grants Fund

This fund is used to account for all Federal Emergency Management Agency (FEMA) grants received directly or in a subrecipient capacity through the FSM National Government.

Non-U.S. Grants Fund

This fund is used to account for all financial transactions related to certain direct and other grants received from various world organizations.

CFSM Grants Fund

This fund is used to account for appropriations made to the State from the Congress of the Federated States of Micronesia (CFSM). These grants are earned on a reimbursable basis.

Sports Development Fund

This fund accounts for certain funds dedicated to sports development in the State.

General Services Agency Fund

This fund accounts for funds dedicated to the acquisition of certain supplies for the State.

Other Special Revenue Funds

This fund accounts for funds dedicated to certain special purposes.

See Accompanying Independent Auditors' Report.

STATE OF YAP  
 FEDERATED STATES OF MICRONESIA  
 NONMAJOR GOVERNMENTAL FUNDS  
 SPECIAL REVENUE FUNDS

Combining Balance Sheet  
 September 30, 2008  
 (with comparative totals as of September 30, 2007)

	Sports Development	General Services Agency	Other Special Revenue	Totals	
				2008	2007
<u>ASSETS</u>					
Cash and cash equivalents	\$ -	\$ -	\$ 229,545	\$ 229,545	\$ 229,277
Investment pool	-	-	-	-	-
Receivables, net:					
CFSM	-	-	-	-	-
Other	-	-	-	-	-
Due from other funds	49,150	64,622	140,305	254,077	229,766
Total assets	<u>\$ 49,150</u>	<u>\$ 64,622</u>	<u>\$ 369,850</u>	<u>\$ 483,622</u>	<u>\$ 459,043</u>
<u>LIABILITIES AND FUND BALANCES</u>					
Liabilities:					
Accounts payable	\$ 13,418	\$ -	\$ -	\$ 13,418	\$ 20,939
Other liabilities and accruals	-	4,454	-	4,454	4,454
Deferred revenue	-	-	-	-	-
Due to other funds	-	-	-	-	-
Total liabilities	<u>13,418</u>	<u>4,454</u>	<u>-</u>	<u>17,872</u>	<u>25,393</u>
Fund balances:					
Reserved for:					
Encumbrances	-	-	1,180	1,180	1,180
Continuing appropriations	-	-	-	-	-
Unreserved	35,732	60,168	368,670	464,570	432,470
Total fund balances	<u>35,732</u>	<u>60,168</u>	<u>369,850</u>	<u>465,750</u>	<u>433,650</u>
Total liabilities and fund balances	<u>\$ 49,150</u>	<u>\$ 64,622</u>	<u>\$ 369,850</u>	<u>\$ 483,622</u>	<u>\$ 459,043</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
 FEDERATED STATES OF MICRONESIA  
 NONMAJOR GOVERNMENTAL FUNDS  
 SPECIAL REVENUE FUNDS

Combining Statement of Revenues, Expenditures By Function,  
 and Changes in Fund Balances (Deficits)  
 Year Ended September 30, 2008  
 (with comparative totals for the year ended September 30, 2007)

	Sports Development	General Services Agency	Other Special Revenue	Totals	
				2008	2007
<b>Revenues:</b>					
Federal contributions and other grants	\$ -	\$ -	\$ -	\$ -	\$ -
CFSM grants	-	-	-	-	-
Excise taxes	77,616	-	104,200	181,816	192,625
Fees and charges	-	13,101	269	13,370	13,511
<b>Total revenues</b>	<b>77,616</b>	<b>13,101</b>	<b>104,469</b>	<b>195,186</b>	<b>206,136</b>
<b>Expenditures by function:</b>					
<b>Current:</b>					
General government	77,616	29,236	-	106,852	117,335
Economic development	-	-	56,234	56,234	46,341
Public safety	-	-	-	-	-
Education	-	-	-	-	-
Health services	-	-	-	-	-
<b>Total expenditures</b>	<b>77,616</b>	<b>29,236</b>	<b>56,234</b>	<b>163,086</b>	<b>163,676</b>
Excess (deficiency) of revenues over (under) expenditures	-	(16,135)	48,235	32,100	42,460
<b>Other financing sources:</b>					
Loan Proceeds	-	-	-	-	-
Operating transfers in	-	-	-	-	-
<b>Total other financing sources</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Net change in fund balances (deficit)	-	(16,135)	48,235	32,100	42,460
Fund balances (deficits) at the beginning of the year	35,732	76,303	321,615	433,650	391,190
<b>Fund balances at the end of the year</b>	<b>\$ 35,732</b>	<b>\$ 60,168</b>	<b>\$ 369,850</b>	<b>\$ 465,750</b>	<b>\$ 433,650</b>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA  
NONMAJOR GOVERNMENTAL FUNDS  
SPECIAL REVENUE FUNDS

Combining Statement of Revenues, Expenditures By Account,  
and Changes in Fund Balances (Deficits)  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	Sports Development	General Services Agency	Other Special Revenue	Totals	
				2008	2007
Revenues:					
Federal contributions and other grants	\$ -	\$ -	\$ -	\$ -	\$ -
CFSM grants	-	-	-	-	-
Excise taxes	77,616	-	104,200	181,816	192,625
Fees and charges	-	13,101	269	13,370	13,511
<b>Total revenues</b>	<b>77,616</b>	<b>13,101</b>	<b>104,469</b>	<b>195,186</b>	<b>206,136</b>
Expenditures by account:					
Salaries and wages	-	-	-	-	11,944
Grants and subsidies	77,616	-	-	77,616	85,256
Utilities	-	-	-	-	-
Contractual services	-	-	-	-	-
Supplies and materials	-	-	-	-	-
Scholarship and training	-	-	-	-	-
Travel	-	-	-	-	1,150
Capital outlay	-	16,419	-	16,419	5,285
Rentals	-	-	-	-	2,200
Food stuffs	-	-	-	-	1,983
Communications	-	-	-	-	-
Printing and reproduction	-	-	-	-	-
Repairs and maintenance	-	8,911	-	8,911	1,869
Freight	-	-	-	-	-
Professional services	-	-	-	-	6,782
POL	-	-	-	-	-
Other	-	3,906	56,234	60,140	47,207
<b>Total expenditures</b>	<b>77,616</b>	<b>29,236</b>	<b>56,234</b>	<b>163,086</b>	<b>163,676</b>
Excess (deficiency) of revenues over (under) expenditures	-	(16,135)	48,235	32,100	42,460
Other financing sources (uses):					
Loan Proceeds	-	-	-	-	-
Operating transfers in	-	-	-	-	-
Operating transfers out	-	-	-	-	-
<b>Total other financing sources (uses), net</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Net change in fund balances (deficit)</b>	<b>-</b>	<b>(16,135)</b>	<b>48,235</b>	<b>32,100</b>	<b>42,460</b>
Fund balances (deficits) at the beginning of the year	35,732	76,303	321,615	433,650	391,190
<b>Fund balances (deficits) at the end of the year</b>	<b>\$ 35,732</b>	<b>\$ 60,168</b>	<b>\$ 369,850</b>	<b>\$ 465,750</b>	<b>\$ 433,650</b>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

NONMAJOR GOVERNMENTAL FUNDS - CAPITAL PROJECTS FUNDS

September 30, 2008

Capital projects funds are used to account for the acquisition and construction of major capital facilities other than those financed by proprietary funds and trust funds. A brief discussion of the State's Nonmajor Governmental Funds - Capital Projects Funds as of September 30, 2008, follows:

Public Infrastructure Development Fund

This fund accounts for United States Congress appropriations under United States Public Law 99-239, as amended, Title II, Article I, Section 211(d) and approved by the FSM Congress.

CFSM Capital Projects Fund

This fund is used to account for grants awarded by the Congress of the Federated States of Micronesia (CFSM) for improvement and betterment projects within the State.

Yap State Public Projects Fund

This fund is used to account for an appropriation from the FSM National Government which initially has been loaned to the Yap Fishing Corporation (through YEDA) and after repayment will be used to fund certain capital projects. Appropriations by the State's Legislature for capital improvement projects funded by the General Fund are also accounted for within this fund.

Water Development Projects Revolving Fund

This fund was established pursuant to YSL No. 4-69 to account for loan proceeds and other funds designated for State Water Development Projects.

See Accompanying Independent Auditors' Report.

STATE OF YAP  
 FEDERATED STATES OF MICRONESIA  
 NONMAJOR GOVERNMENTAL FUNDS  
 CAPITAL PROJECTS FUNDS

Combining Balance Sheet  
 September 30, 2008  
 (with comparative totals as of September 30, 2007)

	Public Infrastructure Development	CFSM Capital Projects	Yap State Public Projects	Water Development Projects Revolving	Totals	
					2008	2007
<u>ASSETS</u>						
Receivables:						
CFSM	\$ -	\$ 35,563	\$ -	\$ -	\$ 35,563	\$ 1,633
Due from other funds	-	44,805	-	39,670	84,475	152,737
	<u>\$ -</u>	<u>\$ 80,368</u>	<u>\$ -</u>	<u>\$ 39,670</u>	<u>\$ 120,038</u>	<u>\$ 154,370</u>
 <u>LIABILITIES AND FUND BALANCES (DEFICITS)</u>						
Liabilities:						
Accounts payable	\$ -	\$ 18,248	\$ -	\$ -	\$ 18,248	\$ 3,143
Other liabilities and accruals	-	36,572	-	-	36,572	36,568
Due to other funds	-	-	64,369	-	64,369	64,369
Total liabilities	<u>-</u>	<u>54,820</u>	<u>64,369</u>	<u>-</u>	<u>119,189</u>	<u>104,080</u>
Fund balances (deficits):						
Reserved for:						
Encumbrances	-	186,090	-	-	186,090	125,311
Unreserved	-	(160,542)	(64,369)	39,670	(185,241)	(75,021)
Total fund balances (deficits)	<u>-</u>	<u>25,548</u>	<u>(64,369)</u>	<u>39,670</u>	<u>849</u>	<u>50,290</u>
Total liabilities and fund balances (deficits)	<u>\$ -</u>	<u>\$ 80,368</u>	<u>\$ -</u>	<u>\$ 39,670</u>	<u>\$ 120,038</u>	<u>\$ 154,370</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

NONMAJOR GOVERNMENTAL FUNDS  
CAPITAL PROJECTS FUNDS

Combining Statement of Expenditures by Function,  
and Changes in Fund Balances (Deficits)  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	Public Infrastructure Development	CFSM Capital Projects	Yap State Public Projects	Water Development Projects Revolving	Totals	
					2008	2007
Revenues:						
CFSM grants	\$ -	\$ 503,086	\$ -	\$ 45,417	\$ 548,503	\$ 185,173
	<u>-</u>	<u>503,086</u>	<u>-</u>	<u>45,417</u>	<u>548,503</u>	<u>185,173</u>
Expenditures by function:						
Current:						
General government	-	-	-	94,858	94,858	195,939
Community affairs	-	452,432	-	-	452,432	-
Public works and transportation	-	50,654	-	-	50,654	-
Payments to component units	-	-	-	-	-	5,000
Total expenditures	<u>-</u>	<u>503,086</u>	<u>-</u>	<u>94,858</u>	<u>597,944</u>	<u>200,939</u>
Excess (deficiency) of revenues over (under) expenditures	<u>-</u>	<u>-</u>	<u>-</u>	<u>(49,441)</u>	<u>(49,441)</u>	<u>(15,766)</u>
Other financing sources (uses):						
Operating transfers in	-	-	-	-	-	-
Total other financing sources	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balances (deficits)	<u>-</u>	<u>-</u>	<u>-</u>	<u>(49,441)</u>	<u>(49,441)</u>	<u>(15,766)</u>
Fund balances (deficits) at the beginning of the year	<u>-</u>	<u>25,548</u>	<u>(64,369)</u>	<u>89,111</u>	<u>50,290</u>	<u>66,056</u>
Fund balances (deficits) at the end of the year	<u>\$ -</u>	<u>\$ 25,548</u>	<u>\$ (64,369)</u>	<u>\$ 39,670</u>	<u>\$ 849</u>	<u>\$ 50,290</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

NONMAJOR GOVERNMENTAL FUNDS  
CAPITAL PROJECTS FUNDS

Combining Statement of Expenditures by Account,  
and Changes in Fund Balances (Deficits)  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	Public Infrastructure Development	CFSM Capital Projects	Yap State Public Projects	Water Development Projects Revolving	Totals	
					2008	2007
Revenues:						
CFSM grants	\$ -	\$ 503,086	\$ -	\$ 45,417	\$ 548,503	\$ 185,173
	<u>-</u>	<u>503,086</u>	<u>-</u>	<u>45,417</u>	<u>548,503</u>	<u>185,173</u>
Expenditures by account:						
Contractual services	-	268,402	-	-	268,402	34,991
Capital outlay	-	30,175	-	-	30,175	(2,700)
Construction	-	-	-	-	-	95,041
Grants and subsidies	-	100,000	-	-	100,000	-
Salaries and wages	-	1,091	-	-	1,091	259
Repairs and maintenance	-	978	-	-	978	-
Freight	-	60	-	-	60	-
Professional services	-	-	-	-	-	38,744
POL	-	80,180	-	-	80,180	257
Other	-	22,200	-	94,858	117,058	34,347
Total expenditures	<u>-</u>	<u>503,086</u>	<u>-</u>	<u>94,858</u>	<u>597,944</u>	<u>200,939</u>
Excess (deficiency) of revenues over (under) expenditures	<u>-</u>	<u>-</u>	<u>-</u>	<u>(49,441)</u>	<u>(49,441)</u>	<u>(15,766)</u>
Other financing sources:						
Operating transfers in	-	-	-	-	-	-
Total other financing sources	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balances (deficits)	<u>-</u>	<u>-</u>	<u>-</u>	<u>(49,441)</u>	<u>(49,441)</u>	<u>(15,766)</u>
Fund balances (deficits) at the beginning of the year	<u>-</u>	<u>25,548</u>	<u>(64,369)</u>	<u>89,111</u>	<u>50,290</u>	<u>66,056</u>
Fund balances (deficits) at the end of the year	<u>\$ -</u>	<u>\$ 25,548</u>	<u>\$ (64,369)</u>	<u>\$ 39,670</u>	<u>\$ 849</u>	<u>\$ 50,290</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Foreign Assistance Grants Fund

Combining Balance Sheet  
September 30, 2008

(with comparative totals as of September 30, 2007)

	Section 221(b) Special Block Grant	Non-U.S. Grants	CFSM Grants	Other U.S. Grants	Department of Homeland Security Grants	Education Sector	Health Sector	Private Sector Development	Environment Sector	Capacity Building Sector	Supplemental Education	Totals		
												2008	2007	
<b>ASSETS</b>														
Investment pool	\$ 3,226,092	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,226,092	\$ 3,226,092
Receivables:														
Federal agencies	-	-	-	427,030	-	-	-	-	-	-	-	-	427,030	26,130
CFSM	-	-	83,907	550,620	211,028	640,459	-	121,711	-	-	-	-	1,607,725	585,144
Other	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Due from other funds	-	174,615	-	813,601	1,293,053	-	750,030	203,373	235,291	495,422	131,123	-	4,096,508	4,159,218
Advances	-	-	-	-	-	29,751	340,818	18,061	7,282	75,430	106,933	-	578,275	-
	<u>\$ 3,226,092</u>	<u>\$ 174,615</u>	<u>\$ 83,907</u>	<u>\$ 1,791,251</u>	<u>\$ 1,504,081</u>	<u>\$ 670,210</u>	<u>\$ 1,090,848</u>	<u>\$ 343,145</u>	<u>\$ 242,573</u>	<u>\$ 570,852</u>	<u>\$ 238,056</u>		<u>\$ 9,935,630</u>	<u>\$ 7,996,584</u>
<b>LIABILITIES AND FUND BALANCES (DEFICITS)</b>														
Liabilities:														
Accounts payable	\$ 1,098	\$ 13,566	\$ 6,488	\$ 73,277	\$ 200,346	\$ 82,730	\$ 183,124	\$ 95,859	\$ 14,853	\$ 12,778	\$ 151,042	\$ -	\$ 835,161	\$ 450,271
Other liabilities and accruals	12,636	50	1,812	8,485	1,005	14,306	9,149	733	608	696	6,554	-	56,034	14,512
Deferred revenue	-	51,079	8,169	769,030	1,302,730	-	141,341	-	204,828	350,593	80,460	-	2,908,230	2,789,936
Due to other funds	1,434,376	-	18,320	273,103	-	569,587	-	-	-	-	-	-	2,295,386	2,237,348
Total liabilities	<u>1,448,110</u>	<u>64,695</u>	<u>34,789</u>	<u>1,123,895</u>	<u>1,504,081</u>	<u>666,623</u>	<u>333,614</u>	<u>96,592</u>	<u>220,289</u>	<u>364,067</u>	<u>238,056</u>		<u>6,094,811</u>	<u>5,492,067</u>
Fund balances (deficits):														
Reserved for:														
Encumbrances	163,054	73,267	10,010	305,227	790,681	257,417	698,973	54,078	38,909	120,391	150,633	-	2,662,640	5,603,762
Continuing appropriations	150,000	-	-	-	-	-	-	-	-	-	-	-	150,000	150,000
Unreserved	1,464,928	36,653	39,108	362,129	(790,681)	(253,830)	58,261	192,475	(16,625)	86,394	(150,633)	-	1,028,179	(3,249,245)
Total fund balances (deficits)	<u>1,777,982</u>	<u>109,920</u>	<u>49,118</u>	<u>667,356</u>	<u>-</u>	<u>3,587</u>	<u>757,234</u>	<u>246,553</u>	<u>22,284</u>	<u>206,785</u>	<u>-</u>		<u>3,840,819</u>	<u>2,504,517</u>
Total liabilities and fund balances	<u>\$ 3,226,092</u>	<u>\$ 174,615</u>	<u>\$ 83,907</u>	<u>\$ 1,791,251</u>	<u>\$ 1,504,081</u>	<u>\$ 670,210</u>	<u>\$ 1,090,848</u>	<u>\$ 343,145</u>	<u>\$ 242,573</u>	<u>\$ 570,852</u>	<u>\$ 238,056</u>		<u>\$ 9,935,630</u>	<u>\$ 7,996,584</u>

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Foreign Assistance Grants Fund

Combining Statement of Revenues, Expenditures by Function, and Changes in Fund Balances (Deficits)  
Year Ended September 30, 2008  
(with comparative totals for the year ended September 30, 2007)

	Section 221(b) Special Block Grant	Non-U.S. Grants	CFSM Grants	Other U.S. Grants	Department of Homeland Security Grants	Education Sector	Health Sector	Private Sector Development	Environment Sector	Capacity Building Sector	Supplemental Education	Totals		
												2008	2007	
<b>Revenues:</b>														
Compact funding	\$ -	\$ -	\$ -	\$ 257,355	\$ -	\$ 5,116,608	\$ 3,010,927	\$ 803,794	\$ 382,271	\$ 367,794	\$ 2,749,602	\$ 12,688,351	\$ 10,779,584	
Federal contributions and other grants	-	17,096	-	2,444,176	2,936,240	-	-	25,734	-	-	-	5,423,246	4,306,806	
CFSM grants	-	-	47,183	-	-	-	-	-	-	-	-	47,183	109,783	
Fees and charges	-	54,554	-	19,542	1,000	2,012	1,258	23,019	201	302	855	102,743	386,235	
	<u>-</u>	<u>71,650</u>	<u>47,183</u>	<u>2,721,073</u>	<u>2,937,240</u>	<u>5,118,620</u>	<u>3,012,185</u>	<u>852,547</u>	<u>382,472</u>	<u>368,096</u>	<u>2,750,457</u>	<u>18,261,523</u>	<u>15,582,408</u>	
<b>Expenditures by function:</b>														
<b>Current:</b>														
General government	-	117,149	-	130,396	3,357,570	-	-	-	382,472	367,596	-	4,355,183	3,618,656	
Economic development	-	544,621	-	-	-	-	-	573,756	-	-	-	1,118,377	1,033,048	
Public Safety	-	-	47,183	-	-	-	-	-	-	-	-	47,183	47,297	
Community affairs	-	-	-	49,983	-	-	-	-	-	-	-	49,983	86,989	
Education	-	-	-	886,379	-	5,026,957	-	-	-	-	1,944,708	7,858,044	6,958,388	
Public Works and transportation	-	25,000	-	-	-	-	-	-	-	-	-	25,000	-	
Health services	-	17,468	-	1,139,606	-	-	3,004,166	-	-	-	-	4,161,240	4,333,938	
Payment to component units	-	-	-	-	29,656	91,663	-	278,791	-	-	-	400,110	1,111,048	
Other	-	-	-	-	-	-	-	-	-	-	-	-	50,316	
	<u>-</u>	<u>704,238</u>	<u>47,183</u>	<u>2,206,364</u>	<u>3,387,226</u>	<u>5,118,620</u>	<u>3,004,166</u>	<u>852,547</u>	<u>382,472</u>	<u>367,596</u>	<u>1,944,708</u>	<u>18,015,120</u>	<u>17,239,680</u>	
Excess (deficiency) of revenues over (under) expenditures	-	(632,588)	-	514,709	(449,986)	-	8,019	-	-	500	805,749	246,403	(1,657,272)	
<b>Other financing sources (uses):</b>														
Loan Proceeds	-	645,757	-	-	-	-	-	-	-	-	-	645,757	784,351	
Operating transfers in	-	-	-	-	444,142	-	-	-	-	-	-	444,142	1,445,121	
Operating transfers out	-	-	-	-	-	-	-	-	-	-	-	-	(164,490)	
	<u>-</u>	<u>645,757</u>	<u>-</u>	<u>-</u>	<u>444,142</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,089,899</u>	<u>2,064,982</u>	
Net change in fund balances (deficits)	-	13,169	-	514,709	(5,844)	-	8,019	-	-	500	805,749	1,336,302	407,710	
Fund balances (deficits) at the beginning of the year	1,777,982	96,751	49,118	152,647	5,844	3,587	749,215	246,553	22,284	206,285	(805,749)	2,504,517	2,096,807	
Fund balances (deficits) at the end of the year	<u>\$ 1,777,982</u>	<u>\$ 109,920</u>	<u>\$ 49,118</u>	<u>\$ 667,356</u>	<u>\$ -</u>	<u>\$ 3,587</u>	<u>\$ 757,234</u>	<u>\$ 246,553</u>	<u>\$ 22,284</u>	<u>\$ 206,785</u>	<u>\$ -</u>	<u>\$ 3,840,819</u>	<u>\$ 2,504,517</u>	

See Accompanying Independent Auditors' Report.

STATE OF YAP  
FEDERATED STATES OF MICRONESIA

Foreign Assistance Grants Fund

Combining Statement of Revenues, Expenditures by Account, and Changes in Fund Balances (Deficits)  
and Changes in Fund Balances (Deficits)

Year Ended September 30, 2008

(with comparative totals for the year ended September 30, 2007)

	Section 221(b) Special Block Grant	Non-U.S. Grants	CFSM Grants	Other U.S. Grants	Department of Homeland Security Grants	Education Sector	Health Sector	Private Sector Development	Environment Sector	Capacity Building Sector	Supplemental Education	Totals		
												2008	2007	
<b>Revenues:</b>														
Compact funding	\$ -	\$ -	\$ -	\$ 257,355	\$ -	\$ 5,116,608	\$ 3,010,927	\$ 803,794	\$ 382,271	\$ 367,794	\$ 2,749,602	\$ 12,688,351	\$ 10,779,584	
Federal contributions and other grants	-	17,096.00	-	2,444,176	2,936,240	-	-	25,734	-	-	-	5,423,246	4,306,806	
CFSM grants	-	-	47,183	-	-	-	-	-	-	-	-	47,183	109,783	
Fees and charges	-	54,554	-	19,542	1,000	2,012	1,258	23,019	201	302	855	102,743	386,235	
	<u>-</u>	<u>71,650</u>	<u>47,183</u>	<u>2,721,073</u>	<u>2,937,240</u>	<u>5,118,620</u>	<u>3,012,185</u>	<u>852,547</u>	<u>382,472</u>	<u>368,096</u>	<u>2,750,457</u>	<u>18,261,523</u>	<u>15,582,408</u>	
<b>Expenditures by account:</b>														
Salaries and wages	-	16,549	13,733	1,075,609	98,181	1,886,542	1,016,902	276,830	180,748	120,463	865,240	5,550,797	5,110,227	
Grants and subsidies	-	-	100	500	29,452	120,823	-	388,095	-	-	-	538,970	1,475,462	
Utilities	-	-	-	23,060	1,844	378,102	323,351	36,108	22,039	6,812	29,717	821,033	828,980	
Contractual services	-	28,084	7,798	117,128	563,144	74,290	76,047	5,534	50,629	716	252	923,622	882,681	
Supplies and materials	-	5,210	1,315	46,154	394,733	473,604	9,286	6,498	5,734	7,169	180,393	1,130,096	380,461	
Construction	-	-	-	-	933,144	415,515	-	-	-	-	-	1,348,659	1,297,994	
Scholarship and training	-	-	-	414	-	468,060	1,200	-	-	-	17,777	487,451	534,312	
Travel	-	8,928	-	276,888	6,962	66,222	47,949	41,914	25,978	69,518	361,933	906,292	1,013,323	
Capital outlay	-	1,786	10,899	370,349	546,836	551,519	76,087	30,485	13,683	60,860	122,718	1,785,222	1,370,562	
Rentals	-	70	-	9,065	539	850	178	50	2,202	-	350	13,304	187,280	
Food stuffs	-	833	-	1,791	27,731	70,090	8,063	142	573	-	94,976	204,199	158,602	
Communications	-	-	-	9,569	5,924	98,440	19,049	21,610	14,561	3,162	6,925	179,240	168,259	
Printing and reproduction	-	3,287	-	17,918	279	56,976	13,445	2,975	3,363	3,029	30,399	131,671	40,954	
Medical supplies	-	-	-	84,495	-	-	858,194	-	-	-	-	942,689	782,502	
Medical referral	-	-	-	-	-	-	85,616	-	-	-	-	85,616	236,682	
Repairs and maintenance	-	-	339	10,322	566,092	63,755	6,622	3,443	5,022	2,699	9,338	667,632	160,573	
Freight	-	573	12	15,832	4,207	32,113	104,196	238	1,890	7	19,420	178,488	372,533	
Professional services	-	-	-	-	-	15,000	52,097	-	-	60,710	88,339	216,146	311,613	
POL	-	6,048	-	45,930	10,175	106,589	49,688	4,996	18,490	465	25,188	267,569	97,585	
Allowances	-	-	-	12,885	-	-	-	-	-	-	-	12,885	3,930	
Leased housing	-	-	11,350	-	6,000	72,506	71,960	-	7,200	21,520	40,850	231,386	189,693	
Other	-	632,870	1,637	88,455	191,983	167,624	184,236	33,629	30,360	10,466	50,893	1,392,153	1,635,472	
<b>Total expenditures</b>	<u>-</u>	<u>704,238</u>	<u>47,183</u>	<u>2,206,364</u>	<u>3,387,226</u>	<u>5,118,620</u>	<u>3,004,166</u>	<u>852,547</u>	<u>382,472</u>	<u>367,596</u>	<u>1,944,708</u>	<u>18,015,120</u>	<u>17,239,680</u>	
<b>Excess (deficiency) of revenues over (under) expenditures</b>	<u>-</u>	<u>(632,588)</u>	<u>-</u>	<u>514,709</u>	<u>(449,986)</u>	<u>-</u>	<u>8,019</u>	<u>-</u>	<u>-</u>	<u>500</u>	<u>805,749</u>	<u>246,403</u>	<u>(1,657,272)</u>	
<b>Other financing sources (uses):</b>														
Loan Proceeds	-	645,757	-	-	-	-	-	-	-	-	-	645,757	784,351	
Operating transfers in	-	-	-	-	444,142	-	-	-	-	-	-	444,142	1,445,121	
Operating transfers out	-	-	-	-	-	-	-	-	-	-	-	-	(164,490)	
<b>Total other financing sources (uses), net</b>	<u>-</u>	<u>645,757</u>	<u>-</u>	<u>-</u>	<u>444,142</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,089,899</u>	<u>2,064,982</u>	
<b>Net change in fund balances (deficits)</b>	<u>-</u>	<u>13,169</u>	<u>-</u>	<u>514,709</u>	<u>(5,844)</u>	<u>-</u>	<u>8,019</u>	<u>-</u>	<u>-</u>	<u>500</u>	<u>805,749</u>	<u>1,336,302</u>	<u>407,710</u>	
<b>Fund balances at the beginning of year</b>	<u>1,777,982</u>	<u>96,751</u>	<u>49,118</u>	<u>152,647</u>	<u>5,844</u>	<u>3,587</u>	<u>749,215</u>	<u>246,553</u>	<u>22,284</u>	<u>206,285</u>	<u>(805,749)</u>	<u>2,504,517</u>	<u>2,096,807</u>	
<b>Fund balances (deficits) at the end of year</b>	<u>\$ 1,777,982</u>	<u>\$ 109,920</u>	<u>\$ 49,118</u>	<u>\$ 667,356</u>	<u>\$ -</u>	<u>\$ 3,587</u>	<u>\$ 757,234</u>	<u>\$ 246,553</u>	<u>\$ 22,284</u>	<u>\$ 206,785</u>	<u>\$ -</u>	<u>\$ 3,840,819</u>	<u>\$ 2,504,517</u>	

See Accompanying Independent Auditors' Report.

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Honorable Sebastian Anafel  
Governor, State of Yap  
Federated States of Micronesia:

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Yap (the State) as of and for the year ended September 30, 2008, which collectively comprise the State's basic financial statements and have issued our report thereon dated June 29, 2009. Our report expressed a qualified opinion due to the lack of audited financial statements of Public Transportation System and an adverse opinion on the aggregate discretely presented component units due to the lack of audited financial statements of Yap Fishing Authority and Yap Fresh Tuna, Inc. Except as discussed in the preceding sentence, we conducted our 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.

For purposes of this report, our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants, and other matters did not include the Yap State Public Service Corporation, the Yap Visitors Bureau and The Diving Seagull, Inc., which were all audited by us. We have issued separate reports on our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters for these entities. The findings, if any, included in those reports are not included herein.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the State'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 the State's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the State'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 would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* 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 misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs (pages 79 through 104) as items 2008-10 and 2008-12 through 2008-14 to be significant deficiencies in internal control over financial reporting.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 2008-13 and 2008-14 to be material weaknesses.

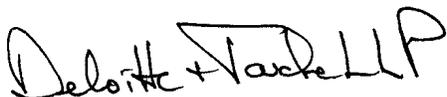
#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State'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 one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards*, and which is described in the accompanying Schedule of Findings and Questioned Costs as item 2008-11.

We noted certain matters that we reported to management of the State in a separate letter dated June 29, 2009.

The State's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the State's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the management of the State, others within the entity, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be and should not be used by anyone other than those specified parties.

  
June 29, 2009

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS  
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER  
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 AND ON THE  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

Honorable Sebastian Anafel  
Governor, State of Yap  
Federated States of Micronesia:

Compliance

We have audited the compliance of the State of Yap (the State) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2008. The State's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs (pages 79 through 104). Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the State's management. Our responsibility is to express an opinion on the State's compliance based on our audit.

As discussed in Note 2b to the Schedule of Expenditures of Federal Awards, the State's basic financial statements include the operations of certain entities whose federal awards are not included in the Schedule of Expenditures of Federal Awards for the year ended September 30, 2008. Our audit, described below, did not include the operations of the entities identified in Note 2b as these entities conducted separate audits in accordance with OMB Circular A-133, if required.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of Yap's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the State's compliance with those requirements.

As described in items 2008-01 through 2008-10 in the accompanying Schedule of Findings and Questioned Costs, the State did not comply with requirements regarding allowable costs/cost principles; cash management; equipment and real property management; matching, level of effort, earmarking; period of availability of federal funds, and procurement and suspension and debarment, that are applicable to its major programs, respectively, as described in the Federal Award Findings and Questioned Cost Section of the accompanying Schedule of Findings and Questioned Costs (page 80). Compliance with such requirements is necessary, in our opinion, for the State to comply with the requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the State complied, in all material respects, with the requirements referred to above that are applicable to its CFDA # 15.875 Compact of Free Association Sector Grants major program, its CFDA # 84.027 Special Education Grants to States major program, its CFDA # 93.224 Consolidated Health Centers major program, its CFDA # 97.036 Disaster Grants - Public Assistance (Presidentially Declared Disasters) major program and its CFDA # 97.039 Hazard Mitigation Grant major program. Also, in our opinion, the State complied, in all material respects with the requirements referred to above that are applicable to its CFDA# 15.875 Compact of Free Association Section 211A Capital Projects major program for the year ended September 30, 2008. The results of our auditing procedures also disclosed one other instance of noncompliance with those requirements, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying Schedule of Findings and Questioned Costs as item 2008-11.

#### Internal Control Over Compliance

The management of the State is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the State's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the State's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies and others that we consider to be material weaknesses.

A *control deficiency* in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 2008-01 through 2008-10 to be significant deficiencies.

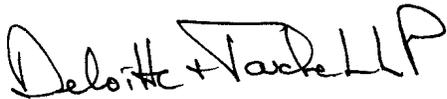
A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs, we consider items 2008-01 through 2008-10 to be material weaknesses.

The State's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the State's responses and, accordingly, we express no opinion on them.

#### Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State as of and for the year ended September 30, 2008, and have issued our report thereon dated June 29, 2009. Our report expressed a qualified opinion due to the lack of audited financial statements of Public Transportation System and an adverse opinion on the aggregate discretely presented component units due to the lack of audited financial statements of Yap Fishing Authority and Yap Fresh Tuna, Inc. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the State of Yap's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards (pages 74 through 76) is presented for the purpose of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of the management of the State. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the management of the State, others within the entity, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies, and is not intended to be, and should not be, used by anyone other than those specified parties.



June 29, 2009

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards  
Foreign Assistance Grants Fund  
Year Ended September 30, 2008

Grantor Program Title	CFDA No./ Grant No.	2008 Fiscal Year Expenditures
<u>U.S. Department of Education:</u>		
Special Education-Grants to States	84.027	\$ 886,285
Career and Technical Education -- Basic Grants to States	84.048	95
Total U.S. Department of Education		<u>886,380</u>
<u>U.S. Department of Agriculture:</u>		
Cooperative Forestry Assistance	10.664	55,395
Community Facilities Loans and Grants	10.766	75,000
Total U.S. Department of Agriculture		<u>130,395</u>
<u>U.S. Department of the Interior:</u>		
Historic Prevention Fund Grant-in-Aid	15.904	49,983
Compact of Free Association, Sector Grants	15.875	11,670,109
Total U.S. Department of the Interior		<u>11,720,092</u>
<u>U.S. Department of Health and Human Services:</u>		
Maternal and Child Health Federal Consolidated Programs Project Grants and Cooperative Agreements for Tuberculosis Control Programs	93.110	3,817
Family Planning-Services	93.116	16,088
Consolidated Health Centers	93.217	42,940
Immunization Grants	93.224	767,212
HIV Prevention Activities-Health Department Based Epidemiologic Research Studies of AIDS and HIV Infection in Selected Population Groups	93.268	46,753
Cooperative Agreements for State-Based Diabetes Control Programs and Evaluation of Surveillance Systems	93.940	5,938
Preventive Health and Health Services Block Grant	93.943	13,217
Maternal and Child Health Services Block Grant to the States CDC and Prevention - Investigations and Technical Assistance	93.988	12,423
Block Grants for Prevention and Treatment of Substance Abuse	93.991	11,534
Maternal and Child Health Services Block Grant to the States CDC and Prevention - Investigations and Technical Assistance	93.994	67,671
Block Grants for Prevention and Treatment of Substance Abuse	93.283	82,638
Block Grants for Prevention and Treatment of Substance Abuse	93.959	69,375
Total U.S. Department of Health and Human Services		<u>1,139,606</u>
<u>U.S. Department of Homeland Security:</u>		
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	2,717,826
Hazard Mitigation Grant	97.039	669,400
Total U.S. Department of Homeland Security		<u>3,387,226</u>

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Foreign Assistance Grants Fund  
Year Ended September 30, 2008

Grantor Program Title	CFDA No./ Grant No.	2008 Fiscal Year Expenditures
Reconciliation to financial statements:		
Foreign Assistance Grant Fund		\$ 18,015,120
Less:		
Non-U.S. Grants Fund		(704,238)
CFSM Grants Fund		<u>(47,183)</u>
		<u>\$ 17,263,699</u>

Note: With the exception of CFDA #84.048, CFDA #10.766 and CFDA #93.224 which are received in a direct capacity from the U.S. Department of Education, U.S. Department of Agriculture, and U.S. Department of Health and Human Services, respectively, all other awards are received in a subrecipient capacity through the FSM National Government. Additionally, expenditures reported under the Department of Homeland Security represent the federal share of expenditures, net of the State of Yap's matching share.

See accompanying notes to Schedule of Expenditures of Federal Awards.

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Expenditures of Federal Awards, Continued  
Compact of Free Association Compact Capital Projects Fund  
Section 211 (A) Capital Account (CFDA No. 15.875)  
Year Ended September 30, 2008

<u>Grantor Program Title</u>	<u>2008 Fiscal Year Expenditures</u>
<u>U.S. Department of the Interior</u>	
Other Compact Capital Projects	\$ 194,400
YFTI/MPC Settlement	150,000
YSPSC Fuel Subsidy and Renewable Energy Feasibility Study	285,154
Jet Fuel Alternative Source and Operation	637,125
Total Compact of Free Association Capital Projects Fund 211 (A)	\$ 1,266,679

The above award is received in a subrecipient capacity from the FSM National Government.

See accompanying notes to Schedule of Expenditures of Federal Awards.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Notes to Schedule of Expenditures of Federal Awards  
Year Ended September 30, 2008

(1) Scope of Audit

The Yap State Government is a governmental entity governed by its own Constitution. All significant operations of the State of Yap are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior has been designated as the State's cognizant agency for the Single Audit.

A. Programs Subject to Single Audit

- U.S. Department of Agriculture
- U.S. Department of Education
- U.S. Department of Health and Human Services
- U.S. Department of Homeland Security
- U.S. Department of the Interior
- U.S. Department of Labor

(2) Summary of Significant Accounting Policies

A. Basis of Accounting

For purposes of this report, certain accounting procedures were followed which help illustrate the expenditures of the individual programs. All expenses and capital outlays are reported as expenditures. The Schedule of Expenditures of Federal Awards is prepared on the accrual basis of accounting.

B. Reporting Entity

For purposes of complying with The Single Audit Act of 1984, as amended in 1996, the State's reporting entity is defined in Note 1A to its September 30, 2008 basic financial statements; and all of the discretely presented component units are excluded. Accordingly, the accompanying Schedule of Expenditures of Federal Awards presents the federal award programs administered by the State, as defined above, for the year ended September 30, 2008.

C. CFDA #15.875

CFDA #15.875 represents the Office of Insular Affairs (OIA), U. S. Department of the Interior. Funding from this source is subject to varying rules and regulations since OIA administers the Compact of Free Association, which is a treaty, and is not a federal program. The Compact is comprised of various funded programs, each with separate compliance requirements. To maximize audit coverage of OIA funding, the OIG has recommended that programs administered under CFDA #15.875 be grouped by like compliance requirements and such groupings be separately evaluated as major programs.

(3) Component Units

The Yap State Public Service Corporation (YSPSC) programs are received in a subrecipient capacity. No federal awards were expended in fiscal year 2007 exceeding the threshold and therefore, compliance testing was not performed.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Programs Selected for  
Audit In Accordance With OMB Circular A-133  
Year Ended September 30, 2008

<u>Grantor Program Title</u>	<u>CFDA No Grant No.</u>	<u>2008 Fiscal Year Expenditures</u>
<u>U.S. Department of the Interior</u>		
Economic, Social and Political Development of the Territories:		
Compact of Free Association, Sector Grants	15.875	\$ 11,670,109
Compact of Free Association Capital Projects Fund 211 (A)	15.875	1,266,679
<u>U.S. Department of Education</u>		
Special Education – Grants to States	84.027	886,285
<u>U.S. Department of Health and Human Services</u>		
Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, Public Housing Primary Care, and School Based Health Centers)	93.224	767,212
<u>U.S. Department of Homeland Security</u>		
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	2,717,826
Hazard Mitigation Grant	97.039	<u>669,400</u>
Total U.S. Federal program expenditures selected		\$ <u>17,977,511</u>
Total U.S. Federal program expenditures		\$ <u>18,530,378</u>
% of total U.S. Federal expenditures covered by major programs		<u>97%</u>

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs  
Year Ended September 30, 2008

**Part I - Summary of Auditors' Results Section**

*Financial Statements*

- |   |                    |
|---|--------------------|
| 1. Type of auditors' report issued:   | Qualified; Adverse |
| Internal control over financial reporting:  |                    |
| 2. Material weakness(es) identified?  | Yes                |
| 3. Significant deficiency(ies) identified that is not considered to be a material weakness? | Yes                |
| 4. Noncompliance material to the financial statements noted?                                | Yes                |

*Federal Awards*

- |  |   |
|--|---|
| Internal control over major programs:  |   |
| 5. Material weakness(es) identified?   | Yes   |
| 6. Significant deficiency(ies) identified that is not considered to be a material weakness?                                    | None reported   |
| 7. Type of auditors' report issued on compliance for major programs:   |   |
| CFDA Program 15.875 COFA-Capital Projects Fund 211 (A)   | Unqualified   |
| All other major programs   | Qualified   |
| 8. Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?      | Yes   |
| 9. The State's major programs were as follows:   |   |
| <u>CFDA Number</u> <u>Federal Program</u>  |   |
| 15.875   | Economic, Social and Political Development of the Territories:          |
| 15.875   | Compact of Free Association - Sector Grants                             |
| 84.027   | Compact of Free Association – Section 211(A) Capital Projects           |
| 93.224   | Special Education – Grants to States                                    |
| 97.036   | Consolidated Health Centers   |
| 97.039   | Disaster Grants - Public Assistance (Presidentially Declared Disasters) |
|  | Hazard Mitigation Grant   |
| 10. Dollar threshold used to distinguish between Type A and Type B Programs, as those terms are defined in OMB Circular A-133: | \$555,911   |
| 11. The State qualified as a low-risk auditee, as that term is defined in OMB Circular A-133?                                  | No  |

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

**Part II - Financial Statement Findings Section**

<u>Finding #</u>	<u>Findings</u>
2008-10	Equipment Management
2008-12	Segregation of Duties
2008-13	Timely Completion Bank Reconciliations
2008-14	Prior Year Internal Control Findings

**Part III - Federal Award Findings and Questioned Cost Section**

<u>Finding #</u>	<u>CFDA #</u>	<u>Findings</u>		<u>Questioned Costs</u>
2008-01	15.875 CSG	Procurement and Suspension and Debarment	\$	-
2008-01	93.224	Procurement and Suspension and Debarment	\$	-
2008-01	97.036	Procurement and Suspension and Debarment	\$	-
2008-01	97.039	Procurement and Suspension and Debarment	\$	-
2008-02	15.875 CSG	Allowable Costs/Cost Principles	\$	271,263
	15.875 CSG	Procurement and Suspension and Debarment	\$	359,859
2008-03	15.875 CSG	Period of Availability of Federal Funds	\$	366,994
2008-04	97.039	Allowable Costs/Cost Principles	\$	58,936
	97.039	Procurement and Suspension and Debarment	\$	175,316
2008-05	84.027	Cash Management	\$	-
	93.224	Cash Management	\$	-
	97.036	Cash Management	\$	-
	97.039	Cash Management	\$	-
2008-06	93.224	Allowable Costs/Cost Principles	\$	26,228
	93.224	Procurement and Suspension and Debarment	\$	3,543
2008-07	93.224	Matching, level of effort, earmarking	\$	59,217
2008-08	84.027	Period of Availability of Federal Funds	\$	18,119
	84.027	Procurement and Suspension and Debarment	\$	108,962
2008-09	97.036	Allowable Costs/Cost Principles	\$	251,662
	97.036	Procurement and Suspension and Debarment	\$	87,095
2008-10	15.875 CSG	Equipment and Real Property Management	\$	-
	93.224	Equipment and Real Property Management	\$	-
	97.036	Equipment and Real Property Management	\$	-
2008-11	10.766	Procurement and Suspension and Debarment	\$	75,000
	10.766	Cash Management	\$	-

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.:	2008-01
Federal Agency:	U.S. Department of the Interior
CFDA Program:	15.875 Economic, Social and Political Development of the Territories
Federal Agency:	U.S. Department of Health and Human Services
CFDA Program:	93.224 Consolidated Health Centers
Federal Agency:	U.S. Department of Homeland Security
CFDA Program:	97.036 Disaster Grants - Public Assistance (Presidentially Declared Disasters)
Federal Agency:	U.S. Department of Homeland Security
CFDA Program:	97.039 Hazard Mitigation Grant
Requirement:	Procurement and Suspension and Debarment
Questioned Cost:	\$0

Criteria: In accordance with applicable procurement requirements, for all contracts, the following provisions should be included, as applicable:

- (i) For contracts in excess of \$100,000, administrative, contractual, or legal remedies in instances where contractors violate or breach contract terms, and the provision of such sanctions and penalties, as appropriate;
- (ii) For contracts in excess of \$100,000, termination for cause and for convenience by the Grantee or Sub-Grantee, including the manner by which it will be effected and the basis for settlement;
- (iii) Compliance with local statutes regarding kickbacks and corrupt practices;
- (iv) Access by the Government of the Federated States of Micronesia and its Sub-Grantees, the Government of the United States, or any of their duly authorized representatives to any books, documents, papers, and records of the contractor which are directly pertinent to the contract for the purpose of making audit, examination, excerpts, and transcriptions;
- (v) Retention of all required records for three years after Grantees or Sub-Grantees make final payments and all other pending matters are closed; and
- (vi) Compliance with all applicable standards, orders, or requirements issued under local environmental laws.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.: 2008-01, Continued

Condition: Many of the contracts entered into by the State do not include contract provisions (iii) to (v). For contracts that we examined that were in excess of \$100,000, we noted contract provision (ii) is also generally not included.

Cause: The State did not ensure compliance with applicable procurement requirements.

Effect: The State appears to be in noncompliance with the criteria.

The conditions cited relate to the provisions in the contracts and not to amounts incurred under contracts, and therefore, no questioned costs result from this finding.

Recommendation: We recommend that the State strengthen its controls over ensuring that compliance with the criteria occurs.

Auditee Response and Corrective Action Plan: This item was brought to the attention of the Attorney General's office after the FY2007 Single Audit report was issued. The issue will again be brought to the attention of the heads of departments and agencies to work with their legal counsel in ensuring that the provisions are included in relevant contracts.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-02  
 Federal Agency: U.S. Department of the Interior  
 CFDA Program: 15.875 Economic, Social and Political Development of the Territories  
 Grant Number: CSG-FSM 2007, CSG-FSM 2006, CSG-FSM 2005, CSG-FSM 2004  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$271,263  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$359,859

Criteria: In accordance with applicable allowable costs/cost principles requirements, expenditures should be necessary and reasonable for program needs and should be in accordance with program requirements. As part of the FY08 grant requirements, the grant may not be used for any obligation or expenditure directly incurred prior to the effective date of the grant, October 1, 2007.

In accordance with applicable procurement requirements, procurements shall provide full and open competition among vendors, and allowable exceptions should be approved and be documented in procurement files.

Condition:

1. For 14 (or 15%) of 91 Compact sector non-payroll expenditures tested, there was either insufficient documentation, or none was provided, to support competitive procurement requirements.
2. For 20 (or 22%) of 91 Compact sector non-payroll expenditures transactions tested, there were either partial or no financial and/or programmatic records (i.e., contract, receiving report, invoices, boarding pass, etc.) on file to substantiate the following transactions:

	<u>Fd Name</u>	<u>REF 1</u>	<u>YR</u>	<u>Details</u>	<u>Procurement</u>	<u>Allowable Costs</u>	<u>Remarks</u>
1	Educ	39908	08	Scholarship Fall 2008	\$ -	\$ 3,000	Absence of an agreement for FALL 08 and transcript for Spring 08
2	Educ	31962	08	main office gaanelay elem - utilities	-	1,167	Absence of billings for clarification, Summary or related billings do not agree to general ledger postings
3	Educ	33776	08		-	2,370	General ledger posting does not agree with billings or summary
4	Educ	32853	07	Purchase of textbooks	55,769	-	No procurement documentation was provided
5	Educ	39646	08		-	1,494	The APV packet , which includes receiving reports and invoices could not be located
6	Educ	29700	08	275 bags of rice and 290 ramen for OIHS for feeding program	4,707	-	Procurement documentation could not be located
8	Health	17896	07		-	177,940	APV packet, which includes invoices, receiving reports, etc, could not be located.
11	Health	29983	08	Medical supplies	-	955	This was laden on board on 9/19/07, and transfer of ownership to YSG occurred upon consignment to the carrier. As this is a FY07 expense, this does not appear to be an allowable charge to the FY08 grant

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-02, Continued  
 Federal Agency: U.S. Department of the Interior  
 CFDA Program: 15.875 Economic, Social and Political Development of the Territories  
 Grant Number: CSG-FSM 2007, CSG-FSM 2006, CSG-FSM 2005, CSG-FSM 2004  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$271,263  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$359,859

Condition, Continued:

	<u>Fd Name</u>	<u>REF 1</u>	<u>YR</u>	<u>Details</u>	<u>Procurement</u>	<u>Allowable Costs</u>	<u>Remarks</u>
12	Health	J809004	08	reversal of PO advance - batteries	3,821	-	This is essentially sole source procurement and there was no local vendor on-island represented as possessing the required merchandise, and therefore, only one off-island solicitation occurred. No procurement documentation was available to support the acquisition.
13	Health	J802003	04	Medical supplies	23,668	-	
14	Health	31139	08	Security and Ambulance services for Jan to Mar 08	8,347	-	The lowest responsible bid was not accepted and there was no reason documented for this selection in file Per invoice, expenditure is for a FY07 charge; however, this was charged to FY08, Additionally hospital management advised that this charge should have been borne by the general fund.
15	Health	29615	08	Medical referral fee	-	805	Per invoice, expenditure relates to a FY07expenditure; however, this was charged to FY08, Hospital management represented that this charge should have been borne by the general fund. Also, this patient was not approved by the Medical Board for an off-island referral. It was further represented that this referral was subsequently approved by the Legislature, but no such authorization has been provided.
17	Health	29638	08	Medical referral fee	-	38,499	Per invoice, expenditure is related to FY07 however this was charged to FY08, and thus does not seem allowable as a charge to the FY08 Grant that should only be used for expenditures from 10/1/07 and management indicated that this was supposed to be charged to local revenue.
18	Health	30488	08	Medical referral fee for services occurred in August 2007	-	33,151	Final award was to an off island vendor but price solicitations only occurred on island.
19	Private	J807023	08	Weaners for Dept of Agriculture (GUAM vendor). Purchase of pigs, certified by UOG	450	-	There was no evidence of informal procurement procedures associated with these acquisitions.
20	Capacity	33435	08	Purchase of 2 used vehicles for patrol purposes (PICK-UP and sedan).	18,000	-	

**STATE OF YAP  
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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-02, Continued  
 Federal Agency: U.S. Department of the Interior  
 CFDA Program: 15.875 Economic, Social and Political Development of the Territories  
 Grant Number: CSG-FSM 2007, CSG-FSM 2006, CSG-FSM 2005, CSG-FSM 2004  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$271,263  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$359,859

Condition, Continued:

	<u>Fd Name</u>	<u>REF 1</u>	<u>YR</u>	<u>Details</u>	<u>Procurement</u>	<u>Allowable Costs</u>	<u>Remarks</u>
21	SEG	J804017	06	A2008118 YAP/GUM/HNL - return of advanced per diem as travel was cancelled, thus per diem was returned as evidenced by cash receipt. Erroneous JV. Noted airfare portion of \$2,408.06 - YSG cannot provide documentation that it was reimbursed.	-	3,282	This is a return of advanced per diem as travel was cancelled; hence, this should not have been an expense. Questioned cost occurs for both airfare and per diem as such were expensed but travel did not occur.
22	Health	28808	08	Reimbursement of water prevention supplies (noted a discount of \$300) as funding was not available and thus, no obligation was made. JV was to transfer certain FY06 expenditures from SEG 05 to SEG 06. SEG 06 is valid for exp 6/1/06 and onwards. Entry was supported by details noting transaction date is on or after 6/1/06.	1,500		Since this was a reimbursement to an individual for supplies acquired, we could not determine the manner in which informal competitive procurement occurred.
23	SEG	J806013	06		8,624		No competitive procurement documentation was available for inspection.
24	SEG	J809007	07	Purchase of educational supplies for ECE.	5,034		The lowest bidder was disqualified and no reason for the disqualification was set forth in the procurement files.
25	Health	J802003	07	Medical Supplies	2,584		We were not able to obtain an invoice for this amount to support its validity or an attendant receiving report.
26	Educ	36733	08	YAPDOE warehouse bldg project - 5th payment	-	8,600	Unallowable, obligation ref - C26842 was dated 9/13/07. FY08 grant should only be used for obligation on or after 10/1/07. Also object class used was erroneous, this was charged as repairs when this is actually a construction.
27	Educ	42683	08	General study text books for both student and teacher edition.	77,934	-	No competitive procurement documentation provided
28	Educ	41919	08	Bus purchase for PTS department. Per contract, 75% of total cost contract is due upon execution of contract.	<u>149,421</u>	-	No competitive procurement documentation provided
					<u>\$359,859</u>	<u>\$271,263</u>	

3. For one (or 3%) of 40 payroll expenditure tested, no Personnel Action Form was available for employee number 706226.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-02, Continued  
 Federal Agency: U.S. Department of the Interior  
 CFDA Program: 15.875 Economic, Social and Political Development of the Territories  
 Grant Number: CSG-FSM 2007, CSG-FSM 2006, CSG-FSM 2005, CSG-FSM 2004  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$271,263  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$359,859

Condition, Continued:

4. Scholarship payments were made solely to students although the stated policy is that checks should be made to both the student and the institution.
5. Internal controls were not effective in the following matters. However, the ineffective controls do not result in questioned costs.

<u>ACCT NAME</u>	<u>AMOUNT</u>	<u>Fd Name</u>	<u>REF 1</u>	<u>YR</u>	<u>Oblig Doc #</u>	<u>Remarks</u>
POL	\$ 30,000	education	J805018	08	p33108	Expenditure was less than the invoice by \$1,468.50, thus it appears that the recorded expense is understated.
Transfers Out	8,327	education	37684	08	None	For ck 2748, \$434.45 for payroll, employment contract does not agree to the paycheck by an immaterial amount. Included in the paycheck are taxi fares reimbursements, pending approval by the Board that such can be charged.
Vehicles	200,338	Health	10225	04		This was already recorded in FY07 as an audit adjustment and was questioned then. YSG was to revisit entries to ensure that this will be revised by year end but such did not occur until the audit process.

Cause: The State did not ensure compliance with applicable allowable costs/cost principles requirements and procurement requirements.

Effect: For conditions 1 and 2, the State appears to be in noncompliance with the criteria and questioned costs result.

For condition 3 and 5, there appears to be inconsistencies in the application of existing internal control procedures and policies.

For condition 4, there appears to be insufficient documentation of the transaction.

Recommendation: We recommend that the State comply with the criteria and that documentation supporting competitive procurement be on file. Additionally, we recommend that documentation be on file to support compliance with State requirements.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No:	2008-02, Continued
Federal Agency:	U.S. Department of the Interior
CFDA Program:	15.875 Economic, Social and Political Development of the Territories
Grant Number:	CSG-FSM 2007, CSG-FSM 2006, CSG-FSM 2005, CSG-FSM 2004
Requirement:	Allowable Costs/Cost Principles
Questioned Costs:	\$271,263
Requirement:	Procurement and Suspension and Debarment
Questioned Costs:	\$359,859

Auditee Response and Corrective Action Plan: We agree in part with this finding. We do not agree that all the costs should be questioned as we believe that adequate documentation exists to support compliance with the criteria for most of the transactions listed under this finding. However, we agree that the documents may not have been available for the auditors review. The Director of Administrative Services will obtain necessary documentation to support compliance with the criteria and will provide that documentation to the auditors or the FSM National Government within 60 days.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-03  
 Federal Agency: U.S. Department of the Interior  
 CFDA Program: 15.875 Economic, Social and Political Development of the Territories  
 Grant Number: CSG-FSM 2007 and 2006 and 2004 Carryover  
 Requirement: Period of Availability of Federal Funds  
 Questioned Costs: \$366,994

**Criteria:** Per a letter from the grantor agency, dated January 8, 2008, the reporting deadline for FY07 sector grants was extended to April 15, 2008. Expenditures charged to this grant should be charged on or before that date.

Per a letter from the grantor, dated April 9, 2008, the FY06 SEG grant was extended to June 30, 2008. Expenditures charged to this grant should be charged on or before that date.

Per a letter from the grantor, dated March 27, 2007, the 2004 Carry-over grants were extended to December 31, 2007. Expenditures charged to this grant should be charged on or before that date.

**Condition:** For five (or 3%) of 91 Compact sector non-payroll expenditures tested, the following expenditures were incurred subsequent to the period of availability (POA).

<u>Date</u>	<u>Fd Name</u>	<u>YR</u>	<u>Check No</u>	<u>Details</u>	<u>POA</u>	<u>Remarks</u>
2/13/2008	education	04	32915	YAPDOE warehouse bldg project – 2 <sup>nd</sup> payment	\$ 15,600	pending extension letter to show FY04 grant expiration is after 12/31/07
3/27/2008	education	04	33740	100% completion Falalop, Woleai Elem School Construction	167,450	pending extension letter to show FY04 grant expiration is after 12/31/07
3/27/2008	education	04	33789	100% completion Old Classroom Renovation, final pay (outer island)	74,640	pending extension letter to show FY04 grant expiration is after 12/31/07
3/31/2008	Private	07		Transfer of FY07 YVB subsidy from GF to Sector 07. JV dated 7/21/08 but posted as of 3/31/08 – transaction date. This was a PY write-up.	109,304	No letter has been provided that extends the grant to June 30, 2008. What we have on file is only to April 15, 2008. Pending updated YVB – YSG agreement to ensure compliance requirements are communicated.
9/11/2008	Education	08	36699	General study text books for both student and teacher edition.	<u>77,934</u> 444,928	P27517 obligated 9/30/07
				Already questioned at Finding 2008-02	<u>(77,934)</u> <u>\$366,994</u>	

**Cause:** There appears to be insufficient documentation to support compliance with period of availability requirements.

**Effect:** The State appears to be in noncompliance with the criteria and questioned costs result.

**Recommendation:** We recommend that the State maintain grant extension letters and ensure compliance with period of availability requirements.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No:	2008-03, Continued
Federal Agency:	U.S. Department of the Interior
CFDA Program:	15.875 Economic, Social and Political Development of the Territories
Grant Number:	CSG-FSM 2007 and 2006 and 2004 Carryover
Requirement:	Period of Availability of Federal Funds
Questioned Costs:	\$366,994

Auditee Response and Corrective Action Plan: We agree in part with this finding. We do not agree that all the costs should be questioned as we believe that adequate documentation exists to support compliance with the criteria for most of the transactions listed under this finding. However, we agree that the documents may not have been available for the auditors review. The Director of Administrative Services will obtain necessary documentation to support compliance with the criteria and will provide that documentation to the auditors or the FSM National Government within 60 days

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-04  
 Federal Agency: U.S. Department of Homeland Security  
 CFDA Program: 97.039 Hazard Mitigation Grant  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$58,936  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$175,316

**Criteria:** In accordance with applicable allowable costs/cost principles requirements, expenditures should be necessary and reasonable for program needs and should be in accordance with program requirements. In accordance with applicable procurement requirements, procurements shall provide full and open competition among vendors, and allowable exceptions should be approved and be documented in procurement files. In addition, for travel-related expenditures, travel advance policies should be followed, advances should be timely liquidated and balances owed from employees should be timely collected.

**Condition:**

1. For one (or 20%) of five non-payroll expenditures tested, there was either insufficient documentation or none was provided to support competitive procurement requirements.
2. For two (or 40%) of five non-payroll expenditures transactions tested, there were either partial or no financial and/or programmatic records (i.e., contract, receiving report, invoices, boarding pass, etc.) on file to substantiate the following transactions.

<u>Nature</u>	<u>Ref</u>	<u>Ck No</u>	<u>Procurement</u>	<u>Allowable Costs</u>	<u>Remarks</u>
Construction of Typhoon Shutters	29580	32196	\$164,871	\$ -	A change order was executed for a new project without evidence of competitive procurement.
Construction of Typhoon Shutters	21692	33565		55,636	Completion reports for Kanikay and Ganelay were missing, shutters at Gilman Elem School were not installed as the building is not complete but 100% of the project was disbursed.
Construction	39656		-	3,300	Replacement check and APV packet, which include invoices, receiving reports, etc. was not located.
Food supplies	J801032	13054	3,084	-	No procurement documentation provided.
Food supplies	J801032	13054	<u>7,361</u>	-	No procurement documentation provided.
			<u>\$175,316</u>	<u>\$58,936</u>	

**Cause:** The State did not ensure compliance with applicable allowable costs/cost principles requirements and procurement requirements.

**Effect:** The State appears to be noncompliant with the criteria, and questioned costs result.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No:	2008-04, Continued
Federal Agency:	U.S. Department of Homeland Security
CFDA Program:	97.039 Hazard Mitigation Grant
Requirement:	Allowable Costs/Cost Principles
Questioned Costs:	\$58,936
Requirement:	Procurement and Suspension and Debarment
Questioned Costs:	\$175,316

Recommendation: We recommend that the State comply with the criteria and that documentation supporting competitive procurement be on file. Additionally, we recommend that documentation be on file.

Auditee Response and Corrective Action Plan: We agree with this finding. The Director of Administrative Services will work with the Yap Public Assistance Office and the Office of Planning and Budget to resolve these questioned costs.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.: 2008-05  
CFDA Program: U.S. ED 84.027 Special Education– Grants to States (as sub-grantee of FSMNG)  
U.S. HHS 93.224 Consolidated Health Centers  
U.S. DHS 97.036 Disaster Grants – Public Assistance (as sub-grantee of FSMNG)  
U.S. DHS 97.039 Hazard Mitigation Program (as sub-grantee of FSMNG)  
Requirement: Cash Management  
Questioned Costs: \$0

Criteria: In accordance with applicable cash management requirements, the time elapsed between the receipt of Federal funds and the clearing of the applicable check should be minimized and any amounts for interest from advances in excess of the minimum allowable should be returned to the federal government.

Condition: For all of CFDA #84.027, CFDA #93.224, CFDA#97.036, and CFDA #97.039, the State could not provide documented details of the basis of its GAPS drawdowns. Therefore, it is not possible to ensure and test compliance with cash management requirements. All programs indicated, except for CFDA #93.224 which is a direct grant, are sub-granted from the FSM National Government.

Cause: The State did not monitor drawdowns for compliance with applicable cash management requirements.

Effect: The effect of the above condition is noncompliance with applicable cash management requirements. However, no questioned costs are presented as we cannot determine the impact of this matter due to the lack of documentation.

Recommendation: We recommend that the Yap State Government establish internal controls over cash management that ensure compliance with federal requirements.

Auditee Response and Corrective Action Plan: We agree in part with this finding. All drawdowns made on the direct grant (U.S. HHS 93.224 Consolidated Health Centers) are supported by expenditure reports. The Director of Administrative Services will obtain necessary documentation to support compliance with the criteria and will provide that documentation to the auditors or the FSM National Government within 60 days. The Director will also obtain from Finance Office the details of the drawdown for the other grants to determine the cause of the non-compliance and establish procedures to prevent future occurrences.

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FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.: 2008-06  
 Federal Agency: U.S. Department Of Health and Services  
 FDA Program: 93.224 Community Health Center  
 Grant Number: H80CS06653 and H80CS06653  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$26,228  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$3,543

**Criteria:** In accordance with applicable allowable costs/cost principles requirements, expenditures should be necessary and reasonable for program needs and should be in accordance with program requirements. Furthermore, financial and programmatic records should be maintained on file for at least three years. Also, in accordance with applicable procurement requirements, procurements shall provide full and open competition among vendor and allowable exceptions should be approved and be documented in the procurement file.

**Condition:** For one (or 3%) of 32 non-payroll expenditures tested, there was insufficient documentation to support competitive procurement requirements.

For two (or 6%) of 32 non payroll expenditures tested, there was insufficient documentation (i.e., accounts payable vouchers, invoices, receiving reports, travel liquidation documents and obligating documents) to support allowable requirements.

Moreover, we noted more than three employees attended training when only two were allowed per the FY 2007 budget. The Government was not able to provide the rationale for this matter.

<u>ACCT_NAME</u>	<u>Posted Amount</u>	<u>Ck No</u>	<u>Procurement</u>	<u>Allowable Costs</u>	<u>Remarks</u>
Medical Supplies	\$2,880	33098	\$3,543	\$ -	No competitive procurement documentation; Solicited three local vendors and final vendor was off-island; No other solicitations off island occurred. Therefore, this is tantamount to sole source procurement.
Medical Supplies	2,905			2,905	No contract/PO/invoice or evidence of competitive procurement documentation was on file.
Utilities	779	32666		779	Billings were not locatable to substantiate the charge.
Travel & Expense (UDS Training)	2,402	31658	-	3,356	Three people attended UDS training when only two were allowed per the FY 07 budget. The amount questioned represents the excess travel cost over the approved budget
General Contractual Srvc	8,311	36911	-	19,188	No receiving report documentation provided.
			<u>\$3,543</u>	<u>\$ 26,228</u>	

**Cause:** The State did not ensure compliance with applicable allowable costs/cost principles requirements and procurement requirements.

**Effect:** The State appears to be in noncompliance with the criteria and questioned costs result. The procurement finding is reportable as the potential questioned costs exceed the threshold.

**STATE OF YAP  
FEDERATED STATES OF MICRONESIA**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.:	2008-06, Continued
Federal Agency:	U.S. Department Of Health and Services
FDA Program:	93.224 Community Health Center
Grant Number:	H80CS06653 and H80CS06653
Requirement:	Allowable Costs/Cost Principles
Questioned Costs:	\$26,228
Requirement:	Procurement and Suspension and Debarment
Questioned Costs:	\$3,543

Recommendation: The Yap State Governments should comply with relevant grant requirements.

Auditee Response and Corrective Action Plan: We agree with this finding. The Director of Administrative Services will contact the Director of the Waab Community Health Center Program to review and resolve this finding.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.: 2008-07  
Federal Agency: U.S. Department of Health and Human Services  
CFDA Program: 93.224 Consolidated Health Centers  
Grant Number: H80CS06653  
Requirement: Matching, Level of Effort, Earmarking  
Questioned Cost: \$59,217

Criteria: In accordance with applicable matching requirements, a matching or cost-sharing requirement may be met by either (1) allowable costs incurred by the grantee, subgrantee or cost-type contractor under the assistance agreement. This includes allowable costs borne by non-Federal grants or other cash donations by other non-federal third parties. For this purpose, Compact sector grants are eligible for matching purposes. (2) The value of third-party in-kind contributions applicable to the period, through which the cost-sharing or matching requirement applies.

Condition: Program management represented that an in-kind match occurred, and an overall statement of the match components was presented. However, details in support of the match components could not be provided. Therefore, we were not able to be able to conduct sufficient tests to ensure that the match occurred.

Cause: The State did not ensure compliance with applicable matching requirements.

Effect: The State appears to be in noncompliance with the criteria, and questioned costs result.

Prior Year Status: This has been written up in the prior year

Recommendation: We recommend that the State provide documentation substantiating the details of the match components.

Auditee Response and Corrective Action Plan: We agree with this finding. Certain documentations that were meant to substantiate the matching components of the grant were submitted to the Office of Administrative Services after the FY2007 Single Audit was issued. The Director of Administrative Services will work with director of the Waab Community Health Center Program to provide further details that will sufficiently resolve this finding.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.: 2008-08  
 Federal Agency: U.S. Department of Education  
 CFDA Program: 84.027 Special Education – Grants to States  
 Requirement: Period of Availability of Federal Funds  
 Questioned Costs: \$18,119  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$108,962

**Criteria:** In accordance with applicable period of availability requirements, any funds that are not obligated at the end of the federal funding period shall remain available for obligation for an additional period of 12 months. Also, in accordance with applicable procurement requirements, procurements shall provide full and open competition among vendors and allowable exceptions should be approved and documented in procurement files.

**Condition:** For one (or 4%) of 25 non-payroll expenditures tested, there was insufficient documentation to support competitive procurement requirements.

For three (or 12%) of 25 non-payroll expenditures, the Program was charged after the fund’s period of availability.

<u>ACCT NAME</u>	Grant		<u>Date</u>	<u>Procurement</u>	Period of	<u>Remarks</u>
	<u>Year</u>	<u>Ck No</u>			<u>Availability</u>	
Vehicles	2006	31435	11/15/07	\$108,962	\$ -	FY 2006 Grant Award and Budget were not provided for us to determine if such is allowable.
Travel & Trans Expense	2006		4/10/08	-	2,409	Grant expired 12/31/07
General Contractual Srvc	2006	33184	2/27/08	-	10,473	Grant expired 12/31/07
General Contractual Srvc	2006	34552	5/20/08	-	5,237	Grant expired 12/31/07
				<u>\$108,962</u>	<u>\$18,119</u>	

**Cause:** The State did not monitor transactions sufficiently to ensure compliance with applicable period of availability requirements and procurement requirements.

**Effect:** The State appears to be in noncompliance with the criteria, and questioned costs result.

**Recommendation:** The State should comply with grant requirements.

**Auditee Response and Corrective Action Plan:** We agree with this finding. The Director of Administrative Services will review the findings with the Director of Education to determine action plan that will resolve these findings.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-09  
 Federal Agency: U.S. Department of Homeland Security  
 CFDA Program: 97.036 Disaster Grants - Public Assistance (Presidentially Declared Disasters)  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$251,662  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$87,095

**Criteria:** In accordance with applicable allowable costs/cost principles requirements, expenditures should be necessary and reasonable for program needs and should be in accordance with program requirements. Approval in the change of scope from the project worksheets should be documented. In accordance with applicable procurement requirements, procurements shall provide full and open competition among vendors and allowable exceptions should be approved and documented in procurement files.

**Condition:**

1. For two (or 3%) of 69 non-payroll expenditures tested, there was either insufficient documentation or none was provided to support competitive procurement requirements.
2. For six (or 9%) of 69 non-payroll expenditure transactions tested, there were only partial financial and/or programmatic records (i.e., approval of the change in scope of the project worksheet and completion reports that correspond to the payment made) on file to substantiate that expenditures charged to the project worksheets are allowable.

<u>Date</u>	<u>Ref</u>	<u>Details</u>	<u>PW #</u>	<u>Procurement</u>	<u>Allowable Costs</u>	<u>Remarks</u>
						Other bidder proposals and approvals of the change of scope were not provided.
03/11/08	34107	COM Yap Campus Science Lab Bldg - 1st payment	90,95 & 531	\$ -	\$ 64,328	PW - 95 replaced damaged land Grant Bldg, PW 90 - Replaced 3 classrooms
04/09/08	35823	COM Yap Campus Science Lab Bldg - 2nd progress @ 28%	90,95 & 531	-	39,228	T1, T2, T3 and PW 531 - replacement of bldg contents, however all three PWs were lumped together to build the COM Science Bldg.
04/09/08	35823	COM Yap Campus Science Lab Bldg - 2nd progress @ 28%	90,95 & 531	-	26,130	same as above
07/22/08	39922	COM Yap Campus Science Lab Bldg - 3rd progress billing	90,95 & 531	-	50,074	same as above
07/24/08	40344	COM Yap Campus Science Lab Bldg - release of Performance Bond after 50% completion	90,95 & 531	-	16,211	same as above
09/09/08	42532	COM Yap Campus Science Lab - bldg	90,95 & 531	-	45,243	same as above
02/19/08	33137 18151 &	Colonia Community Center Improvement Project 2nd payment	140 & 171	-	871	As of 4/9/08, which was the grant expiration date, the project was only 98% complete. thus the remaining 2% of the contract is questioned.
11/22/07	28683	YAP EPA Office bldg Project	35	15,644	-	We could not locate evidence of competitive procurement occurring

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-09, Continued  
 Federal Agency: U.S. Department of Homeland Security  
 CFDA Program: 97.036 Disaster Grants - Public Assistance (Presidentially Declared Disasters)  
 Requirement: Allowable Costs/Cost Principles  
 Questioned Costs: \$251,662  
 Requirement: Procurement and Suspension and Debarment  
 Questioned Costs: \$87,095

Condition, Continued:

<u>Date</u>	<u>Ref</u>	<u>Details</u>	<u>PW #</u>	<u>Procurement</u>	<u>Allowable Costs</u>	<u>Remarks</u>
						There were inconsistencies of procurement rationale associated with this transaction.
						Informal quotations from three local business entities were on file, but none had an available unit. However, per a memo, the price ranges of the quotations received were between \$23k and \$35k. This appears contrary to the summary of quotations that indicated that no items were in stock and no quotations received.
04/28/08	35732	2004 Mitsubishi Outlander Vehicle for disaster and relief mobilization used by Office of Planning and Budget.		18,000	-	No competitive procurement documentation provided
02/26/08	33634	Office contents for YVB.	66	7,174	-	No competitive procurement documentation provided
05/22/08	33547	Office contents for YVB	66	43,572	-	No documents were located to support the expenditure
11/29/07	J802003		379	-	6,705	No competitive procurement documentation provided
10/10/07	27565	Office desk and living room for airport terminal contents Reimbursement to YVB for payroll. This is for cleaning & relocation to temporary office.	434	2,705	=	Per compliance supplement, for debris removal, regular salaries are not eligible.
/9/2008	35768		66	-	2,872	
				<u>\$87,095</u>	<u>\$251,662</u>	

3. For three (or 4%) of 69 non-payroll expenditures transactions tested, there were partial or no documentation to document approval of the change of scope in the project worksheet for the following transactions. It is our understanding that a verbal approval was obtained from the grantor.

<u>Date</u>	<u>Ref</u>	<u>Details</u>	<u>PW</u>	<u>Amount</u>	<u>Remarks</u>
10/29/07	23375	10 deskstop computers for DOE/ECE w/ 80% DP	284 & 301	\$ 11,550	PW scope was for purchase of minivan; however, expenditure charges pertain to bldg contents. The minivan was purchased by other funding due to untimely approval of PW.
01/15/08	21054	Dell Powerredge Server	164	5,577	The PW includes \$13k roof repair, due to delay in the approval of PW, YSG paid for the repair of the Archive's Office roof. Instead of repaying YSG, the PW funds were used to purchase Office contents by the Archive office.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No:	2008-09, Continued
Federal Agency:	U.S. Department of Homeland Security
CFDA Program:	97.036 Disaster Grants - Public Assistance (Presidentially Declared Disasters)
Requirement:	Allowable Costs/Cost Principles
Questioned Costs:	\$251,662
Requirement:	Procurement and Suspension and Debarment
Questioned Costs:	\$87,095

Cause: The State did not ensure compliance with applicable allowable costs/cost principles requirements and procurement requirements.

Effect: For condition 1 and 2, the State appears to be in noncompliance with the criteria, and questioned costs result.

For condition 3, we were not able to substantiate approval by the grantor or sub-grantee; however, no questioned cost will be raised as the expenditures benefitted the program and the untimely availability of funds appears to have rationalized the procedure conducted.

Recommendation: We recommend that the State comply with the criteria and that documentation supporting competitive procurement be on file. Additionally, we recommend that approvals obtained be documented in writing.

Auditee Response and Corrective Action Plan: We agree in part with this finding. We do not agree that all the costs should be questioned as we believe that adequate documentation exists to support compliance with the criteria for most of the transactions listed under this finding. However, we agree that the documents may not have been available for the auditors review. The Director of Administrative Services will obtain necessary documentation to support compliance with the criteria and will provide that documentation to the auditors or the FSM National Government within 60 days

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No: 2008-10

CFDA Program: U.S. DOI 15.875 Economic, Social and Political Development of the Territories  
Grant Number: Compact of Free Association - Sector Grants

CFDA Program: U.S. HHS 93.224 Consolidated Health Centers

CFDA Program: U.S. DHS 97.036 Disaster Grants - Public Assistance

Requirement: Equipment and Real Property Management  
Questioned Cost: \$0

Criteria: In accordance with applicable equipment management requirements, adequate maintenance procedures shall be developed to keep property in good condition. Additionally, a bi-annual inventory should be conducted and the results reconciled with underlying fixed asset records.

Condition: No formal maintenance procedures for equipment are established and we could not determine the manner in which maintenance responsibilities are carried out. Additionally, the State has not conducted an inventory of capital assets in the last two years, and it has not reconciled its last physical inventory that it conducted to its fixed asset subsidiary records.

Cause: It appears that a formal maintenance policy has not been adopted, an inventory has yet to be currently conducted and a prior inventory has yet to be reconciled to fixed asset records.

Effect: The effect of this condition is noncompliance with equipment management requirements. We are unable to quantify resulting questioned costs, if any.

Prior Year Status: This condition was cited in the 2007 Single Audit.

Recommendation: A formal maintenance program should be developed in accordance with federal compliance requirements.

Additionally an inventory of fixed assets should be conducted and be reconciled with underlying records.

Auditee Response and Corrective Action Plan: We agree with this finding. The Office of Administrative Services (Division of Procurement & Property Mgmt) will begin a physical inventory in July 2009 to reconcile its fixed asset list with those of the departments and offices. The scheduled timeline for the inventory intends to complete the inventory in Yap main island by the end of the calendar year. This undertaking is aimed to ultimately eliminate this repeated finding.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.: 2008-11  
Federal Agency: U.S. Department of Agriculture  
CFDA Program: 10.766 Community Facilities Loans and Grants  
Requirement: Procurement and Suspension and Debarment  
Requirement: Cash Management  
Questioned Costs: \$75,000

Criteria: In accordance with applicable procurement requirements, procurements shall provide full and open competition among vendors, and any allowable exceptions should be approved and documented in the procurement file.

Condition: The item tested represents 100% of expenditures charged to this federal program. There was insufficient documentation to support competitive procurement requirements. Additionally, an unknown amount of cash management issue exists as the State received the funding in 2004, but only expended the funds in 2008. Details of the item questioned are as follows:

<u>Fund</u>	<u>REF</u>	<u>Description</u>
21	23053	Purchase of Refuse Truck YA-08375. An advance payment was made in FY05 with a final payment of \$75k in 2008

Cause: The State did not ensure compliance with applicable procurement requirements.

Effect: The State appears to be in noncompliance with the criteria and questioned costs result.

Recommendation: The Yap State Governments should comply with applicable grant requirements.

Auditee Response and Corrective Action Plan: We agree with this finding. The Director of Administrative Services will contact the head of Public Works and Transportation to work with the Rural Development Program office in Yap to determine how this finding may be resolved.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No. 2008-12 - Segregation Of Duties

Criteria: A functioning system of internal controls requires that appropriate segregation of duties be implemented among those who (a) execute transactions (handling of cash), (b) approve transactions, (c) have access to the assets or the ability to issue disbursements or handle collections, and (d) post or reconcile related accounting records.

Condition: The employee responsible for the bank reconciliations also has access to cash.

Cause: It appears that the Yap State Government has not adequately considered segregation of duties in the assignment of tasks.

Effect: The effect of this condition is that there is no assurance that assets are safeguarded against irregularities.

Recommendation: Segregation of incompatible duties is important to provide assurance that assets are safeguarded against irregularities. Fundamentally, persons who have access to assets such as cash should not be responsible for posting and reconciling the cash account.

Auditee Response and Corrective Action Plan: We agree with this finding. The Director of Administrative Services will review with the Chief of Finance the current staffing situation to determine how duties and tasks may be reassigned to resolve this finding.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No. 2008-13 - Timely Completion of Bank Reconciliations

Criteria: A functioning system of internal controls requires that bank reconciliations be prepared on a monthly basis to allow identification of irregularities.

Condition: As of October 2008, the payroll bank reconciliation is not updated to reconcile transactions for the prior nine months.

Cause: It appears that the Yap State Government does not prepare bank reconciliations on a timely basis.

Effect: The effect of this condition is that there is no timely identification and resolution of irregularities and adjustments to the financial statements, if any.

Recommendation: Bank reconciliations should be prepared on a monthly basis to allow timely identification and resolution of irregularities and to ensure that all disbursements and receipts are recorded in the underlying accounting records. YSG may consider delegating certain areas of the bank reconciliation to other accounting personnel, instead of having the Chief accountant perform all the work, while maintaining segregation of duties.

Auditee Response and Corrective Action Plan: We agree with this finding. The Director of Administrative Services will review with the Chief of Finance the current staffing situation to determine how duties and tasks may be reassigned to resolve this finding.

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Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2008

Finding No.: 2008-14  
Area: Prior Year Internal Control Findings

Criteria: Prior year internal control findings should be timely resolved through appropriate corrective action.

Condition: The following internal control findings from fiscal year 2005 have not been corrected during the year ended September 30, 2008:

Finding 2005-02	Equipment and Real Property Management
Finding 2005-04	Travel Advances
Finding 2005-05	Approval of Payroll Master File Changes
Finding 2005-07	Approval of Journal Vouchers
Finding 2005-08	Purchase Advances

Cause: The cause of this condition is that inadequate corrective action occurred during fiscal year 2008.

Effect: The effect of this condition is the same cited in each of the abovementioned prior year internal control findings.

Recommendation: The Department of Administration should ensure that corrective action occurs to resolve the abovementioned issues.

Auditee Response and Corrective Action Plan: We agree with this finding. Some new procedures had been established that if maintained and enforced, would be the initial steps to resolve all of these repeat findings.

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Unresolved Prior Year Findings and Questioned Costs  
Year Ended September 30, 2008

QUESTIONED COSTS

For the year ended September 30, 2008, the following questioned costs remain unresolved.

	Questioned Costs Set Forth in Prior Audit Report <u>2007</u>	<u>Questioned Costs Resolved</u>	<u>Questioned Costs at September 30, 2008</u>
Unresolved Questioned Costs FY 01	\$ 41,829	\$ 41,829	\$ -
Unresolved Questioned Costs FY 03	101,558	101,558	-
Unresolved Questioned Costs FY 04	12,446	12,446	-
Unresolved Questioned Costs FY 05	22,008	22,008	-
Unresolved Questioned Costs FY 06	576,358	-	576,358
Unresolved Questioned Costs FY 07	<u>1,282,244</u>	<u>344,548</u>	<u>937,696</u>
	\$ <u>2,036,443</u>	\$ <u>522,389</u>	1,514,054
Questioned Costs FY 08			<u>1,862,194</u>
			\$ <u>3,376,248</u>

During the year ended September 30, 2008, the FSM National Government resolved the above questioned costs of \$522,389.

The prior year status of findings is contained in the accompanying Schedule of Findings and Questioned Costs (pages 72 through 104).