POHNPEI TRANSPORTATION AUTHORITY

AUDIT REPORT NO. 004-17

SEPTEMBER 30, 2016

POHNPEI STATE GOVERNMENT
OFFICE OF THE PUBLIC AUDITOR

State Public Auditor
P.O. Box 370
Kolonia, Pohnpei
Federated States of Micronesia

POHNPEI TRANSPORTATION AUTHORITY
AUDIT REPORT
SEPTEMBER 30, 2016

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June 26, 2017

The Honorable Marcelo Peterson, Governor, State of Pohnpei
The Honorable Fernando Scaliem, Speaker, Pohnpei State Legislature
The Honorable Members of the Pohnpei State Legislature
The Board of Directors, Pohnpei Transportation Authority
Mr. Sadorino Martin, Commissioner, Pohnpei Transportation Authority

EXECUTIVE SUMMARY

We are pleased to submit the financial audit report of Pohnpei Transportation Authority (PTA) as of and for the year ended September 30, 2016. The audit was conducted in accordance with auditing standards generally accepted in the United States of America and the *Government Auditing Standards*, issued by the Comptroller General of the United States. The audit was also performed pursuant to Article 11, Section 8 (2) of the Pohnpei State Constitution and Pohnpei State Law No. 1L-10-79, and other laws enacted relative thereafter.

The objectives of our audit were:

1. The expression of an opinion concerning whether the financial statements present fairly, in all material respects, the financial position, result of operations, and cash flows of Pohnpei Transportation Authority as of September 30, 2016;
2. Reporting on the internal control relevant to an audit of the financial statements; and
3. Reporting on the PTA's compliance with laws and regulations, which could have a material effect on the financial statements.

The highlights of the report are as follows:

- The financial statements present fairly, in all material respects, the financial position of the Pohnpei Transportation Authority, as of September 30, 2016, and the result of its operations, and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

operation but the Board of Directors and Management needs to exert efforts to be able to reduce the Due to Primary Government of $1,393,066 as of the end of FY 2016.

A draft of this report was provided to and discussed with the management of PTA and the auditee's response is included hereto as Exhibit I on pages 26 to 27.

In the report, we have offered our recommendations to the findings that we believe once implemented, PTA's operations could be improved. In this regard, we request management to promptly identify corrective measures and to implement the audit recommendations to fully resolve the findings.

Lastly, we extend our appreciation to the management and members of the PTA workforce for the assistance they extended to us during the course of our audit.

Sincerely,

Iso Ihlen K. Joseph
State Public Auditor

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INDEPENDENT AUDITOR'S REPORT

Mr. Robert Hadley
Chairman
Board of Directors
Pohnpei Transportation Authority
Kolonia, Pohnpei State, FM 96941

We have audited the accompanying statement of net assets of Pohnpei Transportation Authority (PTA), a component unit of the State of Pohnpei, as of September 30, 2016, and the related statements of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of PTA's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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 the *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 PTA'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 opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of PTA, as of September 30, 2016, and the result of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that PTA will continue as a going concern. As discussed in Note 6 to the financial statements, the agency has suffered recurring losses from operations during the prior years. The current year revenue performance has improved considerably but PTA still has net liability which would require considerable amount of time for PTA to recover. Management's plans in regard to these matters are also described in Note 6. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

The Management's Discussion and Analysis on pages 3 to 4 is not a required part of the basic financial statements but is supplementary information required by the Governmental

POHNPEI TRANSPORTATION AUTHORITY

Management's Discussion and Analysis
Year Ended September 30, 2016

This section of the Pohnpei Transportation Authority's financial report presents our Management's Discussion and Analysis (MD&A) for the fiscal year ended September 30, 2016. This MD&A is prepared in compliance with the GASB 34 requirement. Readers are requested to read this MD&A in conjunction with the PTA's financial statements, which follows this section.

Financial Highlights

- Operating revenues for the year is $912,982, a decrease by 6.2% or $60,814 compared to prior fiscal year of $973,796.
- Operating expenses increased by 6.2% or $50,655, from $817,486 to $868,141. More than 60% of the total operating expense was expended for payroll related costs.
- Net income this year is $44,841, a decrease by 71% or $111,469 compared to prior year.
- Due to Primary Government dropped by .2% or $2,964 to $1,393,066 as a result of net income.

Financial Statements Preparation

PTA is a component unit of Pohnpei State Government. PTA uses proprietary funds, financed and operated in a manner similar to private business enterprises to account for its operations. The financial statements are presented using the economic resources measurement focus and utilize the accrual basis of accounting.

Financial Analysis

The Statement of Net (Deficit) Asset presents information on all of the PTA's assets and liabilities, with the difference between the two is reported as net assets if assets are higher than liabilities, otherwise it is reported as deficit. Presented below is the comparative change in net (deficit) assets as of fiscal years ended September 30.

	2016	2015	Increase (decrease)	%tage Inc(dec)
Current assets	$ 51,969	$ 7,249	$ 44,720	617%
Non-current assets	85,459	68,532	16,927	25%
	137,428	75,781	61,647	81%
Other liabilities	110,548	90,778	19,770	22%
Due to primary government	1,393,066	1,396,030	(2,964)	(.2%)
Total liabilities	1,503,614	1,486,808	16,806	1.1%
Net Deficit	$(1,366,186)	$ (1,411,027)	$ 44,841	(3.2%)

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Statement of Net Assets
September 30, 2016
(With comparative totals for September 30, 2015)

ASSETS	2016	2015
Current assets:		
Accounts receivable, net (note 2)	$ 2,921	$ 2,924
Inventory, at cost	49,048	4,325
Total Current Assets	$ 51,969	$ 7,249
Property and equipment, net (note 3)	85,459	68,532
TOTAL ASSETS	$ 137,428	$ 75,781
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts payable	$ 79,593	$ 65,615
Accrued payroll	19,704	13,911
Accrued vacation leave	8,077	8,077
Deferred revenue	3,174	3,174
Total Current Liabilities	$ 110,548	$ 90,777
Non-current Liabilities:		
Due to primary government (note 4)	$ 1,393,066	$ 1,396,030
Total Non-current Liabilities	$ 1,393,066	$ 1,396,030
Total Liabilities	$ 1,503,614	$ 1,486,808
Contingencies (note 5)	$ - 0 -	$ - 0 -
Net Assets:		
Invested in capital assets, net of related debt	$ 85,459	$ 68,532
Unrestricted	($ 1,451,645)	(1,479,559)
Total Net Assets (Liabilities)	($ 1,366,186)	($1,411,027)
TOTAL LIABILITIES AND NET ASSETS	$ 137,428	$ 75,781

See accompanying notes to financial statements.

POHNPEI TRANSPORTATION AUTHORITY

Statement of Cash Flows
September 30, 2016

Reconciliation of income from operations to net cash provided by operating activities:	
Income from operations	$44,841
Adjustments to reconcile income from operations to net cash provided by operating activities:	
Depreciation	17,967
Changes in assets and liabilities:	
Decrease in accounts receivable	3
Increase in inventories	(44,723)
Increase in accounts payable	13,978
Increase in accrued payroll	5,793
Decrease in due to primary government	(2,964)
Sub-total	$ 34,895
Add: (Less) Adjustment that affect net income	
Increase in liability/Decrease in net assets	- 0 -
Net cash provided (used) by operations	**$ 34,895**
Cash used for acquisition of property and equipment	**($ 34,895)**
Net increase (decrease) in cash and equivalents	$ - 0 -
Cash and equivalents at beginning of year	- 0 -
Cash and equivalents at end of year	$ - 0 -

See accompanying notes to financial statements.

(1) ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

B. Basis of Accounting, Continued

Net Assets

Net assets represent the residual interest in the assets after liabilities are deducted and consist of three sections: invested in capital assets, net of related debt; restricted; and unrestricted.

- Invested in capital assets, net of related debt:

  Capital assets, net of accumulated depreciation and reduced by outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted:

  Net assets constrained to a particular purpose by enabling legislation or imposed by third parties. PTA has no restricted assets.

- Unrestricted:

  Net assets that are neither subject to externally imposed stipulations nor invested in capital assets.

C. Budget

PTA operates on an annual budget from revenues generated by projects, which are accounted for by the Pohnpei State Department of Treasury and Administration. Appropriation acts require that funds be administered in accordance with the provisions of the State's Financial Management Act. The enabling legislation does provide PTA the power to expend revenues generated by projects maintained by PTA pursuant to 33 PC 2-103. Such expenditures must, however, be in accordance with the provisions of the Financial Management Act and other applicable laws and regulations.

D. Inventory

Inventory is stated at the lower of cost or market using the first-in, first-out (FIFO) costing method.

E. Property and Equipment

Property and equipment are stated at cost, less accumulated depreciation. Depreciation is based on the straight-line method over the estimated useful lives of the respective assets, which range from two to fifteen years depending on the nature of the asset.

(1) ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

New Accounting Standards, Continued

the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of PTA.

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*, which is designed to improve financial reporting for governmental entities by amending the requirements of Statement No. 14, *The Financial Reporting Entity,* and No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of PTA.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of PTA.

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management has not yet determined the effect of implementation of this statement on the financial statements of PTA.

In April 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012.

(3) PROPERTY AND EQUIPMENT

A summary of the PTA's property and equipment at September 30, 2016 follows:

	Estimated Useful Life	Balance October 1, 2015	Additions	Deletions	Balance September 30, 2016
Building	15 years	$ 70,000	$ -	$ -	$ 70,000
Heavy equipment	5-10 years	3,274,036	-	-	3,274,036
Vehicles	5 years	472,285	29,420	-	501,705
Furniture and fixtures	3 years	32,865	4,316	-	37,181
Machinery and tools	2 years	62,072	1,159	-	63,231
Communication equipment	2 years	27,954	-	-	27,954
		$ 3,939,212	$ 34,895	$ -	$ 3,974,107
Less accumulated depreciation		(3,870,680)	(17,968)	-	(3,888,648)
Property and equipment, net		**$ 68,532**	**$ 16,927**	$ -	**$ 85,459**

(4) DUE TO PRIMARY GOVERNMENT

The amount represents accumulated advances made by the Pohnpei State to fund PTA's operations. Changes in the account are shown below:

Balance as of October 1, 2015	$ 1,396,030
Increase (decrease) in the account as reflected in Cash Flow Statement	(2,964)
Balance as of September 30, 2016	$ 1,393,066

These advances are facilitated by the use of a 'pooled' cash account at the Pohnpei State's general fund. Cash pooling is a practice whereby for practical purposes, cash is maintained in a single bank account.

(5) CONTINGENCIES

Pohnpei Transportation Authority is a party to six legal proceedings. The Office of the Attorney General provides general legal assistance to the Authority. In addition to the assistance provided to PTA, a substantial amount of time is also spent on civil cases in litigation at the Pohnpei State Supreme Court and the FSM National Supreme Court. At the beginning of FY 2016, there were six (6) civil cases handled by the Office of the Attorney General on behalf of PTA. In one (1) of the civil cases, the State may have to pay damages pursuant to Title 58 of the Pohnpei Code. However, no provision for any liability that may result from these court cases has been made in the accompanying financial statements.

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE BASED UPON THE AUDIT IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

YEAR ENDED SEPTEMBER 30, 2016

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE BASED UPON THE AUDIT IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Mr. Robert Hadley
Chairman
Board of Directors
Pohnpei Transportation Authority
Kolonia, Pohnpei State, FM 96941

We have audited the financial statements of Pohnpei Transportation Authority (PTA), as of and for the year ended September 30, 2016, and have issued our report thereon dated June 2, 2017. 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.

Internal Control over Financial Reporting

In planning and performing our audit, we considered PTA's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect PTA's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Recommendations as finding numbers 16-001 & 16-002 on pages 18 to 21.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable conditions described above are material weaknesses.

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Schedule of Findings and Recommendations
Fiscal Year Ended September 30, 2016

Finding No. 16-001 Office files and record keeping management needs improvement

Criteria:

Pohnpei Transportation Authority (PTA) should have an organized system of files and an effective record keeping documenting the various activities and services it provides.

Condition:

Visits to the office revealed that management has not adequately maintained office files and kept important records such as:

1. Personnel Files
    - Of the 39 employees of PTA, only 16 had personnel files while 23 personnel records were not maintained at the office
    - Files of 2 employees who already left the office for more than 10 years were included in the active files while not all files of currently employed personnel were available
    - One employee has two Social Security Numbers
2. Annual Leave and Sick Leave Records were not properly updated;
3. Vendor files were not adequately maintained; and
4. Status of project files was not adequately maintained.

Cause:

The causes of the conditions were attributed to the following:

1. There was lack of clearly defined duties and responsibilities of key staffs. Each staff needs to be informed of his/her roles in the organization including related duties and responsibilities.
2. Staffs were not adequately supervised and reports prepared by staffs were not signed by Supervisor or reviewer. There were instances where time sheets were not signed by Supervisors, leave forms were not properly filled out and not also reviewed by supervisors.
3. The lack of training and appropriate education of staffs contributed to the office records weaknesses.

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Schedule of Findings and Recommendations
Fiscal Year Ended September 30, 2016

Finding No. 16-002 Inventory control system and bookkeeping needs improvement

Criteria:

An efficient system of inventory control is necessary to properly account for supplies and materials of the Authority. A reliable bookkeeping system and reporting system is needed to ensure efficiency in operations.

Condition:

A visit to the office and interview conducted revealed the following weaknesses:

- Inventory files were not properly maintained.
- Records of inventory on hand, issued and balances were not updated and monitored.
- Subsidiary ledger files of customer accounts were not properly maintained.
- Vendor files to trace items purchased, quantity and prices of the purchases were not available.

Cause:

Interview of key staff revealed the following:

- Office staffs have limited knowledge on inventory controls and record keeping.
- The Authority also relies on the records at the State Finance to serve as files.
- Office staffs have limited understanding of accounting and until this time the Authority do not have a qualified Accountant to perform bookkeeping work.

Effect:

The conditions resulted to:

- Management is not able to monitor the use of supplies and materials.
- The annual inventory of supplies and materials was not also prepared on time.
- The customer accounts were not reconciled.

Recommendation:

We are recommending management to consider the following:

- Key staffs assigned to maintain inventory records must be properly trained on inventory controls system by keeping accurate and complete records of inventory receipts, issued and balances.

POHNPEI TRANSPORTATION AUTHORITY

Schedule of Findings and Recommendations
Fiscal Year Ended September 30, 2016

Finding No. 16-003 Unresolved Prior Year's Findings:

Criteria:

Pursuant to Pohnpei State Law No. 5L-08-00, the Authority is required to submit to the Auditor a report on the progress in clearing the deficiencies cited in the audit report until such time that all the deficiencies have been cleared, which period shall not exceed six months.

Condition:

The table that follows shows the status of the implementation of prior year's recommendations:

Audit Findings	Status of Implementation of Recommendation	Auditor's Remarks
Finding No. 14-001 Inventory control system and record keeping needs improvement Key staffs assigned to maintain inventory records must be properly trained. Ensure that reports prepared by staffs and reviewed by supervisors.	Management has not improved the inventory control system and records were not properly maintained.	Interview of key staff showed that management tried to recruit an Accountant to help improve the inventory and record keeping system but unsuccessful to hire an Accountant until this report date.
Finding No. 14-002 Property Management Accountability Management should prepare the list of property and equipment. An annual inventory of fixed assets needs to be conducted. Management needs to develop and implement a Property Maintenance Plan to ensure that property is in good condition.	Management did not update the Fixed Assets Register for fiscal year 2016. Site Inspection conducted revealed that management is able to keep track and designate employee responsible for the use of the equipment.	The Authority acquired an equipment and vehicles needed for operations. In order to ensure that equipment use will be maximized and improve useful life of equipment, we are recommending that a Property Maintenance Plan be developed and implemented.

Finding No. 16-003 Unresolved Prior Year's Findings, continued:

Cause:

Management did not develop and implement corrective measures to resolve prior audit finding on the improvement of record keeping and inventory system. Management was not also able to prepare the Property Maintenance Plan.

Effect:

The non resolution of the prior audit finding results to non compliance to Pohnpei State Law No. 5L-08-00 and lack of a reliable inventory list.

Recommendation:

We recommend management to give priority consideration in resolving the prior year's findings.

Auditee Response and Corrective Action Plan:

Please refer to Exhibit I.

POHNPEI TRANSPORTATION AUTHORITY

AUDITEE RESPONSE (EXHIBIT I)

YEAR ENDED SEPTEMBER 30, 2016

Management is committed to continue working hard to ensure adequate revenues are earned to keep PTA operation as a going concern. Current year funding (FY16) for CFSM amounts to $2.08 million. All these project monies are allotted directly to the Authority. Reoccurring deficits due to lack of projects will not be an issue for the current and coming year.

I will be available to answer and clarify issues on any and all of the above responses.

Respectfully,

Sadorino Martin
PTA, Commissioner

cc: Chairman, Board of Directors
File