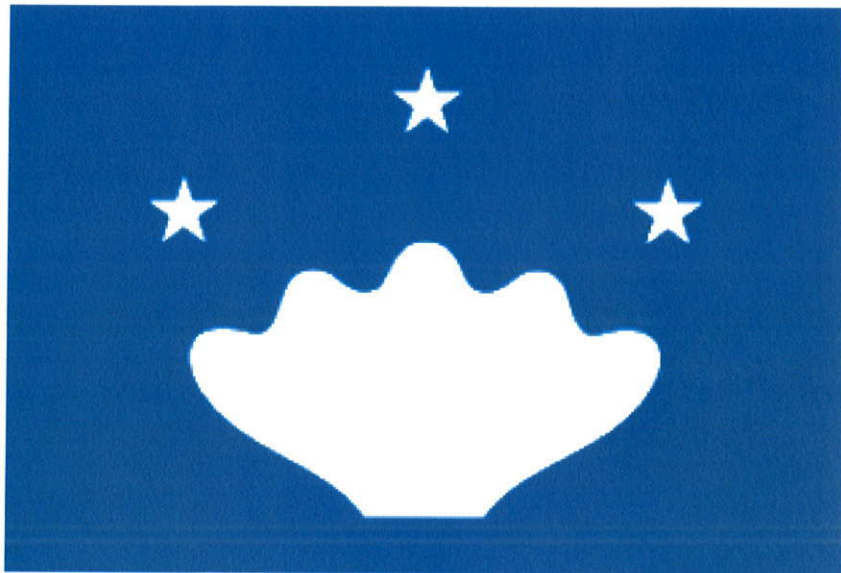




**OFFICE OF THE PUBLIC AUDITOR**  
**REPUBLIC OF PALAU**

**PERFORMANCE AUDIT REPORT**

ON



**HATOHOBEL STATE GOVERNMENT**  
**REPUBLIC OF PALAU**

**PERIOD COVERED**

**OCTOBER 1, 2006 THROUGH SEPTEMBER 30, 2008**

Performed by the Office of the Public Auditor

TOBI07-08-P02\*opa01



# REPUBLIC of PALAU

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Office of the Public Auditor

January 22, 2013  
*Serial#: opa13-036au*

Honorable Thomas Patris  
Governor  
Hatothobei State Government  
Office of the Governor  
Koror, Republic of Palau

**Subject: Final Report on the Performance Audit of Hatothobei State Government for the period from October 1, 2006 through September 30, 2008.**

Dear Governor Patris:

This report presents the results of our performance audit of Hatothobei State Government for the period from October 1, 2006 through September 30, 2008.

The Office of the Public Auditor (OPA) received your response to the draft audit report. The response (without the attachments) is published verbatim in the final report.

The OPA has established an audit recommendation tracking system to keep track of the status of recommendations issued in this report. Accordingly, the OPA will conduct follow up inspections on your responses and corrective action measures to assess their implementation and operation. On a semi-annual basis, June 30 and December 31 each year, the OPA will report the status of the recommendations to the Office of the President and Preceding Officers of the Olbiil Era Kelulau for their information and disposition.

If you have any questions regarding matters of audit findings and recommendations, the OPA will be available to discuss such matters at your request.

Sincerely,

A handwritten signature in black ink, appearing to read "Satruning Tewid", is written over a large, stylized oval flourish.

Satruning Tewid  
Acting Public Auditor  
Republic of Palau

**HATOHOBEL STATE GOVERNMENT  
Republic of Palau**

**October 1, 2006 through September 30, 2008**

**TABLE OF CONTENTS**

	<b><u>Page No.</u></b>
Executive Summary	1-4
Background	5
Objective, Scope and Methodology	5-6
Prior Audit Coverage	6
Findings and Recommendations:	
1. Outstanding Prior Year Audit Findings and Recommendations	7-8
2. Travel Vouchers Not Properly Filed to Justify \$7,666 of Travel Cost	8
3. Travel to Negotiate Purchase of Construction Materials	8-9
4. Travel Expense to Negotiate Fisheries Projects	9-10
5. \$3,078 Insurance Premium Refunds	10-11
6. Cash Receipts	11-12
7. Bank Reconciliation	12
8. Wire Transfer of Funds	12-13
9. Fixed Assets	13-14
10. Competitive Bidding	14-15
11. Personnel System	15-16
12. Account Receivables	16
13. Accounts Payable	17
14. \$18,250 Disbursements Lack Supporting Documentation	17-18
15. Housing Preservation Grant Program	19-21



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Office of the Public Auditor

January 22, 2013

Honorable Thomas Patris  
Governor  
Hatohobei State Government

Dear Governor Patris:

This audit report presents the result of our performance audit of Hatohobei State Government for the two (2)-year period ended September 30, 2008. Specifically, the audit covered the period from October 1, 2006 through September 30, 2008.

The objective of the audit was to determine whether (1) expenditures were incurred in accordance with National and State laws and regulations, (2) revenues/cash receipts were properly deposited into the State Treasury, (3) expenditures and cash receipts were supported by adequate supporting documentation, (4) earmarked CIP grants were expended for purposes for which they were authorized and appropriated, and (5) the state has established proper internal controls to ensure the proper recording of transactions and safeguarding of its properties.

As a result of the audit, the Office of the Public Auditor (OPA) found a number of problems and deficiencies noted below relating to the administration of Hatohobei State funds, which we believe should be brought to the attention of management for appropriate corrective action. We also propose recommendations, which we believe, if implemented, will correct these problems/deficiencies.

**First**, we found that the Governor has not taken affirmative action to implement corrective action plan and/or to resolve audit findings contained in the Office of the Public Auditor's (OPA) previous audit report.

**Second**, travel vouchers were not properly filed to justify \$7,666 of travel cost.

**Third**, the amount of \$1,388 was spent on a trip to negotiate the purchase of construction materials in the Philippine, which eventually resulted in the purchase of local construction materials.

**Fourth**, the Governor expended \$1,272 towards negotiation for Fisheries Development Projects for which he lacked authority to negotiate.

**Fifth**, the amount of \$3,078 of insurance premiums was refunded to state employees, which refunds lacked sufficient supporting documents.

**Sixth**, cash receipts were not consistently issued to support revenue collections.

**Seventh**, bank reconciliations were not performed on a monthly basis.

**Eight**, a bank transfer was made in the amount of \$1,289 without supporting documents to show the purpose of the transfer.

**Ninth**, fixed assets are not properly recorded into the State's accounting records.

**Tenth**, certain procurements costing \$5,000 or more were not competitively bid.

**Eleventh**, the State's personnel system is not properly maintained and fully implemented.

**Twelfth**, an account receivable system has not been established to account for monies due to the State.

**Thirteenth**, the Governor has not established a system to record and keep track of State obligations.

**Fourteenth**, the sum of \$18,250 of disbursements lacked proper supporting documentation.

**Fifteenth**, the State did not comply with the terms and conditions of the Housing Preservation Grant Program.

### **Recommendations**

To correct the above deficiencies, we recommend Hatohebi State implement the following recommendations:

**First**, the Governor should take affirmative action by implementing the corrective action plans contained in his response to the prior year audit report.

**Second**, the Governor should implement and enforce Hatohebi State Travel Policies and Procedures.

**Third**, the Governor conducts cost-benefit analysis of purchasing goods and services locally versus off-island to determine which option is most economical in the use of state funds.

**Fourth**, the Governor should conduct legal research or obtain legal advice regarding the authority required prior to entering into negotiations for fishing-related development ventures.

**Fifth**, refunds to State employees should be properly supported and justified.

**Sixth**, the Governor directs the State finance office to issue cash receipts to evidence revenue collections.

**Seventh**, the Governor directs the State Treasurer to perform monthly bank reconciliation.

**Eighth**, the Governor exercises strict controls over bank transfers to ensure they are properly documented and justified.

**Ninth**, the Governor directs the State Treasurer to establish and implement a fixed asset accounting system to account for State fixed assets.

**Tenth**, the Governor ensures that State procurements greater or equal to \$5,000 shall be subject to competitive bidding.

**Eleventh**, the Governor implements all components of the personnel system to ensure that all control elements of the system are operating, including properly authorized Personnel Actions for all employees.

**Twelfth**, the Governor establishes an accounting system to properly account for the State's accounts receivable.

**Thirteenth**, the Governor establishes a system to account for, monitor, and reconcile the State's obligations.

**Fourteenth**, the Governor exercises strict controls over disbursements to ensure that expenditures contain adequate supporting documents.

**Fifteenth**, the Governor complies with the terms and conditions of grant agreements awarded to the State.


The Office of the Public Auditor has established an audit recommendation tracking system. All audit recommendations contained herein will be included in the tracking system as *open*, *resolved*, or *closed*. An *open* recommendation is one where no action or plan of action has been made by the client (state, department or agency). A *resolved* recommendation is one which OPA is satisfied that the client cannot take immediate action, but has established a reasonable plan and time frame of action. A *closed* recommendation is one which the client has taken sufficient action to meet the intent of the recommendation or OPA has withdrawn it.

On August 10, 2012 the Office of the Public Auditor received a response to the Draft Audit Report from the Governor of Hatohobei State. The response essentially agrees with all the findings and recommendations in the report. Based on the response, the Hatohobei State has provided an action plan to correct the findings and/or implement the audit recommendations. The Office of the Public Auditor will conduct follow up procedures to ensure that corrective actions are taken and/or audit recommendations are timely implemented.

Office of the Public Auditor

Finally, the Office of the Public Auditor would like to thank the staff and management of the Hatohebei State Government for the professional courtesy and cooperation extended to us during the audit.

Sincerely,



Satrunino Tewid  
Acting Public Auditor

## **BACKGROUND**

Hatothobei State is one of the sixteen (16) States in the Republic of Palau. The State's Constitution, ratified on November 13, 1983 created the constitutional government of the State of Hatothobei. The Constitution established the primary branches of the government consisting of the Executive (Office of the Governor), the Traditional Leaders, and the Legislature.

The Executive power of the state government is vested in the Governor and Lieutenant Governor who shall have the power to enforce the laws of the State, to spend money pursuant to appropriation laws, to collect taxes, and to propose an annual unified budget for the State Government, among other duties and responsibilities. The Governor and Lieutenant Governor shall be elected in a statewide election for terms of four years and shall not serve more than two consecutive terms.

The Traditional Leaders Council is composed of Romohparuh, Heimong, and Heimah; and no one may become a member of the Traditional Leaders Council unless appointed and accepted pursuant to customs and traditions. It shall be the duty of the Council to safeguard and promote the traditional ways of life of the people of Hatothobei and to advise the Governor and the Lieutenant Governor and the Hatothobei State Legislature on matters relating to and affecting customs and traditions.

The Legislative power of the state government is vested in the Hatothobei State Legislature, composed of nine (9) members, elected at large for a term of four (4) years. The legislature shall have the following powers; to enact legislation, to levy taxes, duties, and excises appropriation to the state, to borrow money on the credit of the state for public projects or to settle public obligations, to impeach the Governor or Lieutenant Governor, to promote the general welfare of the people, and to exercise such other duties and functions permitted by the state constitution and the constitution and laws of the Republic of Palau.

Compensation for the Governor, Lieutenant Governor, Council of Chiefs, and the State Legislators shall be established by law.

Article XI, Section 1 of the State's Constitution states in part: "There shall be a Hatothobei State Treasury into which shall be deposited revenues derived from taxes and other sources appropriate to the State. No funds shall be withdrawn from the treasury except by law."

## **OBJECTIVE, SCOPE AND METHODOLOGY**

The objective of the audit was to determine whether (1) expenditures were incurred in accordance with National and State laws and regulations, (2) revenues/cash receipts were properly deposited into the State Treasury, (3) expenditures and cash receipts were supported by adequate supporting documentation, (4) earmarked CIP grants were expended for purposes for



which they were authorized and appropriated, and (5) the state has established proper internal controls to ensure the proper recording of transactions and safeguarding of its properties.

The audit covered the period of fiscal years 2007 and 2008, specifically from October 1, 2006 through September 30, 2008. As this is a performance audit, we did not conduct audit procedures to assess the fairness of the financial statements of the State or any component or accounts within those financial statements and therefore express no opinion on the financial statements.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards required that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives

The Public Auditing Act of 1985 empowers the Office of the Public Auditor to specifically act to prevent fraud, waste, and abuse in the collection and expenditures of public funds. The Public Auditor may make recommendations on the prevention and/or detection of fraud, waste, and abuse of public funds.

To accomplish our audit objective, we reviewed bank reconciliations, earmarked CIP funds, account receivable and accounts payable, fixed assets, cash receipts, and non-payroll and payroll expenditures. In performing the review, we conducted tests of the aforementioned components of the State's accounting system and procedures to assess the adequacy of the State's system of internal controls. The audit involved reviewing accounting records maintained by the State as well as on-site inspection of the State's fixed assets. We also interviewed appropriate state officials and reviewed relevant accounting records maintained at the Bureau of National Treasury.

## **PRIOR AUDIT COVERAGE**

The latest performance audit of the State Government was for fiscal years 2000 through 2006. Since then, there has been no other audit, attestation or studies conducted on the State Government.

## FINDINGS AND RECOMMENDATIONS

### Finding No. 1: Outstanding Prior Year Audit Findings and Recommendations

Hatohebei State should comply with 5 PNCA §401 by implementing audit recommendations contained in the Office of the Public Auditor's (OPA) prior year audit reports.

Hatohebei State has not take affirmative action to implement corrective action plan and/or to resolve audit findings contained in the Office of the Public Auditor's (OPA) previous audit report covering fiscal years 2000 through 2006 as follows:

- Travel Policies and Procedures
- Competitive Bidding
- Wire Transfer of Funds
- State's Personnel System
- Fixed Assets
- Accounts Payable
- Bank Reconciliation
- Expenditures without Supporting Documents

The Governor responded to the prior year audit report by providing corrective action plans; however, the plans have yet to be implemented.

Hatohebei State's failure to take affirmative action to comply with prior year audit recommendations by the Office of the Public Auditor (OPA) constitutes non-compliance with 5 PNCA §401, which may result in the suspension of the State's block grants.

**Recommendation:** The Governor should take affirmative action by implementing the corrective action plans contained in his response to the prior year audit report. Doing so will strengthen internal controls over State operations and prevent possible future suspension of State's block grants.

**HSG's Response:** *The prior year audit was for the period October 1, 1999 through September 30, 2006. It was done in May 2009 and I submitted my response with corrective action plans on April 15, 2009. These action plans were being imposed beginning October 2008. When your office started the present audit, I don't have enough time to review those documents. Besides, those are from the previous administration which I believed it is unethical for me to investigate. The office of the Special Prosecutor or the Office of the Attorney General may investigate this matter. We don't receive results of their investigation from the previous audit.*

**OPA's comments:** The corrective action plans that the OPA refers to are policies and procedures issues (i.e. Travel Policies and Procedures) that the State needs to implement in order to improve and strengthen internal controls over the use of State funds. The timing and question

of which administration incurred the expenditures is not the focus of corrective action, but rather the establishment and implementation of essential policies and procedures.

**Finding No. 2: Travel Vouchers not Properly Filed to Justify \$7,666 of Travel Cost**

State Officials using Hatohobei State funds for official travel should adhere to Hatohobei State Travel Policies and Procedures as promulgated in Executive Order No. HS-01-95. Section 701 of the Travel Policies and Procedures require state officials to submit a travel voucher (travel authorization, receipts, invoices, trip report, etc.) within 30 days after completion of a trip.

Our audit revealed that during the period from fiscal years 2007 to 2008 the State expended \$7,666 on travel without proper supporting documents to substantiate the official purpose of the travels.

The cause of the above condition appears to be that the Governor failed to implement and enforce the State's Travel Policies and Procedures.

As a result, Hatohobei State spent \$7,666 of State funds on travel without supporting documents to justify that the funds were expended for official purpose of the State.

**Recommendation:** We recommend the Governor implement and enforce Hatohobei State Travel Policies and Procedures. Specifically, all State officials using State funds to travel on official business of the State should be required to file a travel voucher (travel authorization, receipts, invoices, trip report, etc.) within 30 days after completion of travel. In addition, we recommend the Office of the Special Prosecutor or the Office of the Attorney General further investigate the above travels and to take appropriate action for any misconduct involving state funds.

**HSG's Response:** *I concur with this finding. Most of the disbursements in questioned do not have trip reports. One of the airline tickets missing was found and more documents to support this disbursement are attached herewith. Currently, strict procedures on filing travel vouchers are being imposed. The state treasury compiled all essential documents to substantiate the purpose of the travel. Records for prior travels are being reviewed and necessary documents are being compiled.*

**OPA's Comments:** Based on additional supporting documents provided, the OPA has removed questioned costs containing adequate supporting documents.

**Finding No. 3: Travel to Negotiate Purchase of Construction Materials**

The Governor should conduct a cost-benefit analysis of procuring materials locally verses off-island to determine which option is more economical in the use of State funds.

The audit revealed that in August 2007 the State spent \$1,388 on travel to the Philippines to negotiate purchase of construction materials. After taking the trip, however, the Governor eventually decided to purchase the materials locally, rendering the trip to the Philippines unnecessary and wasteful use of funds.

The Governor failed to conduct a cost-benefit analysis to determine which option (purchase locally or off-island) is most economical in the purchase of construction materials.

As a result, the travel expenses amounting to \$1,388 did not provide any meaningful benefits to the State.

**Recommendation:** We recommend the Governor conducts cost-benefit analysis of purchasing goods or services locally or off-island to determine which option is most economical in the use of state funds. In addition, we recommend the Office of the Attorney General or the Special Prosecutor further investigate the above trip to the Philippines and take appropriate action for any misuse of State funds.

**HSG's Response:** *I concur with this finding. There was no cost-benefit analysis on file which I also believe to be very necessary. I will conduct a cost-benefit analysis of any procurement made off-island in the future. Currently, with the aid of Information Technology, I negotiate with vendors or suppliers online. I don't have to travel for negotiations. Moreover, I take extra precautions and made purchases to trustworthy companies.*

#### **Finding No. 4: Travel Expenses to Negotiate Fisheries Projects**

The power and authority to negotiate fisheries development projects and related activities is vested in the national government of the Republic of Palau. Thus, State governments venturing into fisheries development programs or projects should ensure the legal status of projects and programs before investing public funds into such ventures.

We found that the Governor expended \$1,272 in October 2006 on travel to the Philippines in part to meet with a consultant to prepare a concept paper entitled "Promoting the Exploration, Development, Exploitation, and Utilization of the Fisheries and Aquatic Resources of the Territorial Waters of the Hatohobei State Government, Republic of Palau, through the Basic Principles of Decentralization. We further found that the Governor may not have the authority to administer any fisheries development projects in the State Territorial Waters or Waters in the Republic of Palau without authorization from the National Government.

The Governor expended public funds without conducting legal research or obtaining legal advice as to the position of authority required to venture into fishing development projects or programs in the territorial waters of Hatohobei State.

Due to the lack of authority to negotiate fisheries development projects, we found the expenditures associated with the travel premature and waste of Hatohobei State funds, as we did not witness anything of value to the State arising from the discussions.

**Recommendation:** We recommend that in the future, for programs or projects of similar nature, the Governor should conduct legal research or obtain legal advice regarding the authority required to undertake such ventures before expending public funds on activities associated with the project. We further recommend the Office of the Special Prosecutor or the Office of the Attorney General further investigate the above travels and to take appropriate action for any misconduct involving state funds.

**HSG's Response:** *I concur with this finding. There was no legal research no legal advice documents on file. Currently, I withdraw fishing venture negotiations which I am about to engaged. I initiated this project in the desire to raise local revenues in connection to the suspension of Fishing Right Share and reduction of State Block Grants. Fishing venture is the most available income generating resources for our state.*

**Finding No. 5: \$3,078 Insurance Premium Refunds**

Employees' contributions for insurance premiums deducted from employees' pay should be remitted by the State to the Insurance Company in a timely manner in order to avoid any policy cancellations. In addition, if employees' contributions withheld by the State were not remitted to the Insurance Company on time causing the cancellation of the insurance policy, then the amount withheld should be refunded to the employees. Refunds should be supported with evidence from the Insurance Company as to when the policy was cancelled and a schedule of the amount withheld by the State and not remitted to the insurance company for each pay period.

During the audit we found that the amount of \$3,078 of insurance premiums was refunded to three State employees due to the cancellation of their insurance policy for lack of payment. The amounts refunded lacked sufficient documentation with respect to date of policy cancellation and schedule of premium deductions from employees pay which the State failed to remit to the Insurance Company. The refunds were made as follows:

Check Date	Check No.	Amount
1/5/07	16672	\$ 1,353.88
1/8/07	16675	1,081.80
4/10/07	16878	642.00
	<b>Total</b>	<b>\$ 3,077.68</b>

The Governor, as one of the recipients, did not ensure that the refunds were supported by adequate supporting documents.

As a result, the amount of \$3,078 refunded to the employees lack proper supporting documentation and, without which, we were unable to determine if employees were entitled to the amount of the refund.

**Recommendation:** We recommend that any deductions withheld from employees' pay be remitted to the designated allottee in a timely manner. In addition, reimbursements to employees for allotments not remitted by the State to a designated allottee should require a schedule showing each pay period wherein deductions were withheld and not remitted. In this instance, the schedule should have been prepared for each reimbursed employee along with evidence of insurance policy cancellation. Finally, due to the lack of documentation surrounding the reimbursements, we recommend the Office of the Special Prosecutor or the Office of the Attorney General further investigate the above refunds and to take appropriate action for any reimbursements that the employees may not have been entitled to.

**HSG's Response:** *I concur with this finding. There was no schedule of premium deductions from employees pay and there was no evidence of the date the policy was cancelled. Inquiries were made to the Insurance Company. A copy of the policy cancellation was requested but it was denied. The insured person is the one to personally request from the company. The state has requested those concerned employees but until now we don't receive response. However, if concerned employees would not cooperate, I will send request letter to the Insurance Company. The process will take time since this matter will be handled by the company's mother company in Guam. Moreover, the state accountant is posting every transaction done in the past and is doing an account reconciliation to verify this finding. Whenever unnecessary refund will be find out, I will instruct the state treasury to collect back the said amount. Collection letters will be sent to each employee involved.*

#### **Finding No. 6: Cash Receipts**

A proper system of internal control dictates the issuance of cash receipts to evidence revenue collections.

During the audit we found that the State does not consistently issue cash receipts when revenues are received.

It appears the Governor does not understand the significance of cash receipts as a system of internal control and therefore has not directed the State finance office to establish the system to support revenue collections.

As a result, we were unable to determine if all revenue collections were properly deposited to the State's bank account(s) in a timely manner.

**Recommendation:** We recommend the Governor establish a system of cash receipts as part of the State's system of internal controls to support revenue collections. Upon establishing the

system, the Governor should direct the State finance office to issue cash receipts to evidence revenue collections.

**HSG's Response:** *In concur with this findings, the issuance of the cash receipts was not consistent. Currently, a system of cash receipts has been established beginning October 1, 2008. From there onward, issuance of cash receipts is consistently observed. The state obtained it own official receipt book in order to have continuous number sequence. Timely deposit is strictly observed and deposit procedure has been properly performed.*

### **Finding No. 7: Bank Reconciliation**

Effective cash management requires that monthly bank reconciliation be performed to establish a reliable and accurate system to account for and monitor the State's cash activities.

Our audit revealed that the State did not perform monthly bank reconciliation for its bank account in fiscal years 2007 and 2008.

The Governor did not ensure that essential internal controls over cash management are performed such as bank reconciliation.

As a result, the State incurred bank overdraft charges in the amount of \$60 in May 2008. Without bank reconciliation, the State may not be carrying an accurate balance of its account which may lead to issuance of checks from an account with insufficient funds and incurring overdraft charges.

**Recommendation:** We recommend the Governor direct the State Treasurer to perform monthly bank reconciliation. On a monthly basis, the Treasurer should reconcile the balance of cash (checking account) per the State's records to the balance per bank. The reconciliation process would enable the State to maintain an accurate balance of its accounts to avoid issuing checks from an account with insufficient funds and incurring overdraft charges. In addition, bank reconciliation would enable the State to identify errors and other irregularities and to adjust State records accordingly.

**HSG's Response:** *I concur with this finding. There was no record on file showing the performance of monthly bank reconciliation. Beginning September 2008, bank reconciliation was being performed. I will continue to strictly implement this process. Currently, bank reconciliation is updated and maintained.*

### **Finding No. 8: Wire Transfer of Funds**

Procurement of goods and services should contain proper supporting documents to justify the purpose of the expenditure; the amount (cost, quantity, and description, etc.) of goods and services being purchased, and the recording of transactions in the accounting system.

During the audit we found that a wire transfer was made on June 7, 2007 in the amount of \$1,289 without supporting documents (invoices/receipts) to show the purpose of the transfer, to whom, and the nature and cost of goods or services being purchased.

The cause of the above condition is lapse in controls to ensure that proper supporting documents (invoices/receipts) are obtained to support expenditure of state funds.

As a result, we were unable to determine the purpose and public benefit derived from the \$1,289 wire transfer.

**Recommendation:** We recommend the Governor exercises strict controls over procurements to ensure they contain adequate supporting documents (invoices/receipts). The supporting documents should show the description of the items purchased, date, costs, and quantities. In addition, we recommend to the Office of the Special Prosecutor or the Office of the Attorney General further investigate the above wire transfers and to take appropriate action for any misuse of state funds.

**HSG's Response:** *I concur to this finding. There were no documents on file supporting this wire transfer. Inquiry from the bank has been made but is unable to provide the necessary documents given the time to be five years ago. The Office of the Special Prosecutor and the Office of the Attorney General may further investigate this matter.*

### **Finding No. 9: Fixed Assets**

A fixed asset accounting system is essential to properly account for, safeguard, and identify State properties.

During the audit we requested a listing of State properties purchased for the period from fiscal year 2007 and 2008. Although the State provided a schedule of fixed assets, we found fixed assets that were not on the listing; such as a water pump and an air compressor.

It appears the controls over fixed assets are not operating in all its elements.

As a result, the State is unable to maintain an accurate listing of its fixed assets, and which may not be adequately safeguarded against loss or unauthorized use.

**Recommendation:** We recommend the Governor establish and implement a fixed asset accounting system to account for and monitor the acquisition and disposal of the State's fixed assets. In addition, the State should conduct periodic inventory of State properties to determine their location and condition. The fixed assets accounting system should include the following:

1. Procedures to record fixed assets acquisition, which includes the acquisition date, description, acquisition cost, vendor, location and condition.



2. Procedures to record the disposal of fixed assets.
3. Procedure to identify, monitor and conduct periodic inventory of the fixed assets.
4. Finally, the State should conduct a comprehensive inventory of fixed assets purchased in prior years which includes a description, cost or best estimate of cost, location and condition of the assets.

**HSG’s Response:** *I concur with this finding. Currently, the state accountant is maintaining a fixed asset accounting system beginning October 1, 2008. A regular fixed asset inventory is being performed. Fixed assets are being stored at the state office in Malakal and in the island. Unauthorized uses of these assets are strictly prohibited.*

**Finding No. 10: Competitive Bidding**

40 PNCA § 625 (b) requires that any purchases by the State Government greater or equal to \$5,000 shall be subject to competitive bidding.

During the audit we found that the State procured fuel for the State boat, construction labor, and barge rental, the value of which exceeded \$5,000, without competitive bidding. Details of the expenditures are shown below:

Check Date	Check Number	Amount	Vendor	Description
8/23/07	17035	\$ 7,113	Shell Palau	Fuel for Atoll Way
9/28/07	17082	7,500	CTK Company	Labor Contract
12/21/07	17142	7,500	CTK Company	Labor Contract
5/7/08	17290	5,811	Shell Palau	Fuel for Atoll Way
5/15/08	17301	5,364	Shell Palau	Fuel for Atoll Way
	<b>Total</b>	<b>\$ 33,288</b>		

The cause of the above condition is that the Governor failed to enforce the Republic of Palau’s Procurement Law and Regulations.

As a result, we were unable to determine if the State obtained the lowest price or best quality product or service without competitive bidding.

**Recommendation:** We recommend the Governor adhere to the Republic of Palau’s Procurement Law and Regulations by ensuring that State procurements greater or equal to \$5,000 shall be subject to competitive bidding.

**HSG’s Response:** *I concur with this finding. There was no record on file documenting the performance of bidding. A Commercial Supply Agreement for the period March 03, 2010 to March 02, 2012 is attached herewith to support fuel procurement. This is a renewal of the*

*previous agreement that the fuel supplier and the state executed. However, I just realized that before the renewal took place, I should issue another Request for Proposal. On the barge rental, it is anticipated that only one company here in Palau has offered this service.*

**OPA's comments:** Based on additional documents provided, certain expenditures have been resolved and removed as questioned costs.

### **Finding No. 11: Personnel System**

A sound system of internal control dictates that the State maintains personnel files for each employee which contain, at a minimum, employment application, a personnel action form, employment contract, allotment forms, employee evaluations, etc.

Our audit revealed that although the State has established a personnel system for State employees, the system is not properly maintained. For example, we found the deficiencies in the system:

- (1) State employees were compensated a total of \$2,287 but their Personnel Actions were approved after their effective dates.
- (2) \$250 (CK#16516) was paid as a travel/salary advance for an employee, however, evidence was lacking that the employee paid back the advance
- (3) In 2007, for pay period #9, a number of employees received double compensation, one by the State Government and the other by the Bureau of National Treasury, and although the employees paid back the amount of \$675, no documentation was provided to substantiate the deposit of these reimbursements into the State's bank account.

Although a personnel system is in place, the system has not been fully implemented to ensure that all inherent controls are operating as intended.

As a result, the personnel system is not operating in all its elements and, consequently, the controls intended to strengthen payroll processes were not followed.

**Recommendation:** We recommend the Governor implement all components of the personnel system to ensure that all control elements of the system are operating, including properly authorized Personnel Actions for all employees. In addition, the Governor should direct the State Treasurer to monitor payroll and related advances to ensure that employees pay back in full such advances. Moreover, the Treasurer should ensure that personnel files contain all appropriate documents to support any personnel actions for and against employees. Finally, the Governor should further investigate the above transactions and take appropriate action to recover state funds that employees may otherwise not be entitled to.

**HSG's Response:** *I concur with this findings, the following corrective action plan will be implemented:*

Office of the Public Auditor

1. *Personnel actions will be examined and whenever there is any deficiency, collection will be done.*
2. *Documents on the change of name are attached herewith. Issues related to this will be reconciled and corrective actions will be done.*
3. *Termination letter cannot be found after efforts or searched. A copy of the letter and of travel authorization are attached herewith to support that the employee was truly terminated. Currently, personnel file is been reviewed and necessary documents were compiled to ensure proper personnel system.*
4. *The state accountant is currently performing account reconciliation. Collection letter will be sent whenever payment evidence is not found.*
5. *The state treasury already began collecting the overpayment. Please see attached agreement and collection receipts. The state accountant is currently performing account reconciliation to verify other issues of overpayment. A collection letter will be sent to individual employees.*

**OPA's Comments:** Based on additional documents provided, certain expenditures have been resolved and removed as questioned costs.

**Finding No. 12: Account Receivables**

The State should establish an accounting system to properly account for the State's account receivables.

During the audit, we found that the State has not established an accounting system to properly record accounts receivable. There is no system in place to keep track of monies owed the State including payroll and related advances to employees.

It appears management does not understand the importance of having a system in place to keep track of accounts receivable and therefore has not established such a system.

As a result, the state lacks records showing accounts receivable activities during the period of the review. In addition, without records of accounts receivable, the State is disadvantaged in providing effective monitoring and collection on outstanding accounts due the State.

**Recommendation:** We recommend the Governor establish an accounting system to properly record the State's account receivables. The records should show the balance of each account, payments on account, and balance forward. Thus, the State, at any point in time, should be able to determine who owes the State money and in what amounts.

**HSG's Response:** *I concur with this finding. Currently, the state treasury has established an accounting system for account receivables. Account receivable ledger has been maintained and collected.*

**Finding No. 13: Accounts Payable**

A sound system of internal control dictates that the State should establish a system to account for and keep track of its obligations.

During the audit we found the Governor has not established a system to record and keep track of State obligations. Although the State would, at times, make purchases on credit, there was no system in place to ensure that the resulting obligations are recorded, monitored, and reconciled.

As such, we found subsequent disbursements in fiscal year 2008 that relate to fiscal year 2007 obligations and the same in 2009 relating to 2008 obligations that were not recorded.

It appears the Governor did not ensure that a system is established to properly record, monitored and keep track of State's obligations.

As a result, the State is unable to effectively keep track of its obligations. In addition, the lack of an accounting system affects the availability, timeliness, and accuracy of financial information critical for decision making purpose (i.e., budget).

**Recommendation:** We recommend the Governor establish a system to account for, monitor, and reconcile the State's obligations. All credit purchases and payment on account should be properly recorded and reconciled. The system would enable the State to maintain timely and accurate information on State obligations for decision making purposes.

**HSG's Response:** *I concur with this finding. The state accountant is posting all invoices and bills to record accrued expenses. Account reconciliation has been performed regularly to confirm payments. State obligations has been filed and recorded regularly.*

**Finding No. 14: \$ 18,250 Disbursements Lack Supporting Documentation**

A sound system of internal control dictates that expenditures contain proper supporting documents to justify the purpose of the expenditures, the amount (cost and quantities) of goods and services purchased, and the recording of transactions in the underlying accounting system.

Our audit revealed that the Governor expended \$18,250.50 of state funds without proper supporting documents such as invoices and receipts to justify the official purpose of the expenditures. The expenditures were incurred in fiscal years shown below:

<b>Fiscal Year</b>	<b>Amount</b>
2007	\$ 14,707.45
2008	3,543.05
<b>Total</b>	<b>\$ 18,250.50</b>

The Governor failed to enforce controls over expenditures to ensure they contain proper supporting documents (invoices/receipts) to justify the purpose and amounts of expenditures.

Without vendor invoices and receipts, we were unable to substantiate the propriety of \$18,250.50 of expenditures and their recording in the financial records of the State.

**Recommendation:** We recommend the Governor exercises strict controls over disbursements to ensure that expenditures contain adequate supporting documents. Each disbursement should contain proper supporting documents (invoices/receipts) to substantiate the nature, cost, and quantities of goods and services purchased. In addition, the records support the recording and classification of expenditures in the financial statements.

**HSG's Response:** *I concur with this finding. Although most of the checks in questioned had already provided with receipts but documentation as to the description and purpose of the expenditures were not provided. Copies of invoices were requested from the vendors and are attach to response. Please find the following:*

1. *Invoice, statement and letters related to the expenditure of check number 16902*
2. *Billing statements and invoices to support the amount of \$1,460.00as a part of the payment made by check number 17168*
3. *Copy of a letter which may justify the legitimacy of the expenditure made by check number 17171*
4. *Receipt and copy of the quarterly tax report to support the payment made by check number 17219*
5. *Copy of Bill No. 3-8r-37, D3 and copy of the response letter from the Office of the Governor which may support the payment made by check number 17232. Affidavit from the payee will be provided.*
6. *Amount of check number 17307 did not coincide with the statement of account. The amount being paid is only for the first four invoices because the rest were already paid. However, there were no documents on file to fully support the purpose of this expenditure. Currently, the state treasury is compiling all necessary documents to sufficiently support this kind of expenses including meeting minutes, attendance sheets and invitation letters.*
7. *A request for an electronic copy was sent by e-mail to the off-island vendor, but has not replied yet.*
8. *Efforts to look for receipts were being done but we failed to find to support payment made by check numbers 16610 and 16940*
9. *Malakal Commeria Port ID badge is required for all the crew of our State owned vessel. During that time, the state have six crews; 1 captain, 1 chief engineer, 2 oilers, and 2 deckhands. Copies of their badges were not copied for file. Currently, the state compiled all the necessary documents to support this kind of expenditures.*

**OPA's Comments:** Based on additional documents provided, certain expenditures have been resolved and removed as questioned costs.

**Finding No. 15: Housing Preservation Grant Program**

The State received the sum of \$32,037.04 in the form of financial assistance for housing programs to assist the residence of Hatohobei with low income and with equal matching funds by the State.

The Table below shows disbursements for the U.S. federal share of the housing program:

<b>Revenues:</b>			
Housing Preservation Funds			<b>\$ 32,037.04</b>
<b>Expenditures:</b>			
<b>Vendor</b>	<b>Check No.</b>	<b>Amount</b>	
Longshoremment's Lumber	17183	900	
Dominic Emilio	16566	130.86	
Ananias Victor	16568	56.81	
Dominic Emilio	16703	109.06	
Ananias Victor	16705	94.68	
<b>Total Equipment and Tools</b>		<b>1,291.41</b>	<b>1,291.41</b>
WCTC Ace Hardware	17083	2,352.05	
Mason's Hardware	17084	2,182.30	
Longshoremen's Lumber	17085	4,873.94	
HIDC	17086	2,872.05	
Koror Wholesalers	17091	1,827.47	
Mason's Hardware	17093	2,927.30	
Surangel & Son's Co.	17090	7,500.00	
Mason's Hardware	17204	1,123.65	
Mason's Hardware	17205	767.52	
Mason's Hardware	17206	72.58	
WCTC Ace Hardware	17211	254.57	
Shell Co.		3,861.00	
Shell Co.		131.20	
<b>Total Materials, Supplies and Shipping Cost</b>		<b>\$30,745.63</b>	<b>\$30,745.63</b>
<b>Total Expenses</b>			<b>\$32,037.04</b>

The Terms and Conditions of the Housing Preservation grant assistance are as follows:

1. Approved applicants will receive materials and supplies at no more than \$3,960 per applicant.
2. Program recipients will be selected by a five-member Board of Hatohobei State Economic Development Authority
3. Household income is less than \$7,500 per annum.

4. All units to be assisted will be thoroughly inspected by a qualified inspector who will be responsible for preparing rehabilitation work write-ups and justification.
5. Staff member of the state government will monitor and inspect the work performed.
6. Governor and Legislature will receive quarterly reports regarding all expenditures from the system.

During the audit we found the following:

1. There were six recipients of housing assistance but there were no evidence to support their selection (meeting eligibility) by the Hatohebei State Economic Development Authority,
2. Recipients' applications were not approved by the Governor,
3. One recipient's annual income is more than \$7,500,
4. We were unable to determine the amount of materials and supplies issued to each recipient,
5. There were no rehabilitation work write-ups and justification for material needs for each unit,
6. Monitoring and inspections were not performed,
7. Quarterly reports regarding expenditures were not provided to the Governor and the Legislature.

In addition, we found that one of the recipients claimed to be a student; however, there was no evidence of school enrollment on file.

We further found that the following expenditures were charged against the grant when they should have been charged against the State's matching share as prescribed in the state's grant application.

<b>Vendor</b>	<b>Check No.</b>	<b>Amount</b>
Longshoremment's Lumber	17183	900
Dominic Emilio	16566	130.86
Ananias Victor	16568	56.81
Dominic Emilio	16703	109.06
Ananias Victor	16705	94.68
Shell Co.		3,861.00
Shell Co.		131.20
	<b>Total</b>	<b>\$ 5,283.61</b>

We also found the sum of \$2,573 charged against the State's matching share which we believe do not relate to the purpose of the program and, thus, reduces the State's matching share. Moreover, the amount of \$32.28 lacked invoices to evidence that purchases relate to the grant and therefore is questioned.

The cause of the above condition appears to be that the Governor (Grant Administrator) failed to comply with the grant terms and conditions as prescribed in the grant agreement.

As a result, we questioned the amount of \$5,315.89 (\$5,283.61+32.28) as not legitimate charges to the low income housing assistance program. In addition, there appears to be other eligible applicants who were denied assistance while ineligible applicants were approved assistance. Finally, failure to comply with the grant terms and conditions may jeopardize future application for U.S. federal financial assistance.

**Recommendation:** We recommend that when the State receives U.S. federal financial assistance that it complies with the terms and conditions of the grant to avoid penalties (i.e., reimbursements) and to continue its eligibility for future financial assistance.

**HSG's Response:** *I concur with this finding. I may unable to submit the complete documents for this grant for those were only recovered on file. I believe that documentation was properly submitted to the grantor otherwise reimbursement may not be received. Approval for reimbursement was based on the grantees reports submitted to the grantor. Currently, compliance to the terms and conditions of the grant is being observed for the ongoing project. Permission for the grantor was acquired first, whenever changes are made.*

**OPA's comments:** Based on additional documents provided, certain expenditures have been resolved and removed as questioned costs.





**ILLEGAL OR WASTEFUL ACTIVITIES  
SHOULD BE REPORTED TO:**

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