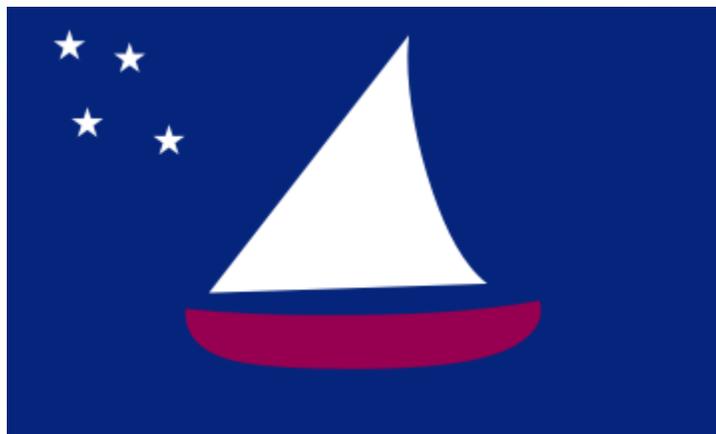




**OFFICE OF THE PUBLIC AUDITOR**  
**REPUBLIC OF PALAU**

**PERFORMANCE AUDIT REPORT**

ON



**SONSOROL STATE GOVERNMENT**  
**REPUBLIC OF PALAU**

**PERIOD COVERED**

**OCTOBER 1, 2005 THROUGH SEPTEMBER 30, 2009**

*Performed by the Office of the Public Auditor*

SON-06-09-P03



## REPUBLIC of PALAU

Office of the Public Auditor

P.O. BOX 850  
KOROR, PALAU 96940  
TEL: (680) 488-2889  
FAX: (680) 488-2194  
HOTLINE: (680) 488-5687  
E-MAIL: palauopa@palaunet.com

March 28, 2011  
*Serial#: opa11-077au*

Honorable Damian B. Albis  
Governor  
Sonsorol State Government  
Office of the Governor  
Koror, Republic of Palau

**Subject: Final Report on the Audit of Sonsorol State Government for the period from October 1, 2005 to September 30, 2009.**

Dear Governor Albis:

This report presents the results of our audit of Sonsorol State Government for the period from October 1, 2005 to September 30, 2009.

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 response 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 presiding 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 "Satrunino Tewid", is written over a horizontal line.

Satrunino Tewid  
Acting Public Auditor  
Republic of Palau

**SONSOROL STATE GOVERNMENT**  
**Republic of Palau**

**October 1, 2005 through September 30, 2009**

**TABLE OF CONTENTS**

	<b><u>Page No.</u></b>
Executive Summary	1-4
Background	5-6
Objective, Scope and Methodology	6
Findings and Recommendations:	
1. Outstanding prior year audit findings and recommendations	7
2. Purchase of a State Boat	7-9
3. \$91,946 of disbursements lack supporting documentation	9-10
4. Travel Voucher not properly filed to justify \$5,467 of travel costs	10-11
5. \$7,528 of Procurement were not competitively bid	11-12
6. Fixed Asset Accounting System	12
7. Personnel System	12-13
8. Accounts Payable System	13-14
9. Cash Receipts	14-15
10. Bank Reconciliations	15
11. \$107,029 of uncategorized expenses	16-17
12. Field Trip Expenses over Budget	17-18
Status of Recommendations	19-24



# REPUBLIC of PALAU

P.O. BOX 850  
KOROR, PALAU 96940  
TEL: (680) 488-2889  
FAX: (680) 488-2194  
HOTLINE: (680) 488-5687  
E-MAIL: palauopa@palaunet.com

Office of the Public Auditor

March 28, 2011

Honorable Damian Albis  
Governor  
Sonsorol State Government  
Koror, Republic of Palau

Dear Governor Albis:

This audit report presents the result of our audit of Sonsorol State Government for four (4) year period ended September 30, 2009. Specifically, the audit covered the period from October 1, 2005 through September 30, 2009.

The objective of the audit was to determine whether (1) expenditure were incurred in accordance with National and State laws and regulations, (2) 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 review, the Office of the Public Auditor (OPA) found a number of problems and deficiencies noted below relating to the administration of Sonsorol 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**, the State has not taken affirmative action to implement corrective action plan and/or to resolve audit findings contained in the OPA's previous audit report covering fiscal years 1999 through 2005.

**Second**, the State made an advance payment of \$90,000 to a contractor for the purchase of a State boat and later cancelled the purchase agreement and has not been refunded in full the advance payment.

**Third,** the Governor expended \$22,811 without proper supporting documents such as invoices/receipts to justify the official purpose of the expenditures.

**Fourth,** \$3,329 of State funds were used for travel and travelers failed to file travel vouchers after completion of the travel.

**Fifth,** the State procured \$7,528 of fuel for the State's ship without competitive bidding.

**Sixth,** Sonorol State has not established a system to account for its fixed assets.

**Seventh,** the State has not established a personnel system for its employees to ensure that all personnel actions are properly approved.

**Eighth,** the State does not have an accounts payable system in place to account for its purchases on credit.

**Ninth,** the State did not issue cash receipts to support revenue collections in fiscal years 2006 through 2009.

**Tenth,** the State did not consistently perform monthly bank reconciliation of its bank accounts.

**Eleventh,** the State recorded a total \$107,029 of expenditures under a classification entitled "Uncategorized Expenditures" from fiscal year 2006 through 2009, however, the State Unified Budget does not contain a line item "Uncategorized Expenditure".

**Twelfth,** the State spent \$2,965 over budget for the line item "Field Trips" in fiscal year 2009.

## **Recommendations**

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

**Second,** we recommend the Governor persist in the efforts to recover the State funds from the contractor.

**Third,** we recommend the Governor exercises strict controls over disbursements of State funds to ensure that expenditures contain adequate supporting documents.

**Fourth,** we recommend the Governor strictly enforces the requirement for filing travel vouchers after the completion of the travel.

**Fifth**, 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 are subject to competitive bidding.

**Sixth**, we recommend the Governor direct the State Treasurer to establish a system to account for State fixed assets.

**Seventh**, we recommend the Governor establish a personnel system for State employees.

**Eighth**, we recommend the Governor establish an accounts payable system to account for and keep track of state's accounts payable and other obligations.

**Ninth**, we recommend the Governor direct the State Treasurer to issue cash receipts to evidence all revenue collections.

**Tenth**, we recommend the Governor direct the State Treasurer to perform monthly bank reconciliations of State's bank accounts.

**Eleventh**, we recommend the Governor direct the State Treasurer to record and classify expenditures in accordance with the State's unified budget acts.

**Twelfth**, we recommend the Governor direct the State Treasurer to provide periodic status reports of expenditures compared to budget to enable the Governor to make timely decisions whether to propose supplemental funding or reprogramming to ensure overspending does not occur.

On February 21, 2011, the Office of the Public Auditor received Sonsorol State Government's response to the Draft Audit Report. The response essentially agrees with all the findings and recommendations in the report. Based on the response, we consider all the recommendations "open" pending corrective actions by the Governor to establish the necessary policies and procedures or other measures to remedy each finding, the person responsible for their implementation, and the time frame for implementation.

The Office of the Public Auditor (OPA) 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.

Please provide us the status of recommendation within 30 days along with documentation showing the specific actions taken. If corrective action actions will take longer than 30 days, please provide us additional information every 60 days until we notify you that the recommendation has been closed.

Finally, we would like to extend our appreciation to the management and staff of the Sonsorol State Government for their cooperation and professional courtesy extended to us during the audit.

Sincerely,

A handwritten signature in black ink, appearing to read 'Satrunino Tewid', written over a faint, large, light-colored oval shape.

Satrunino Tewid  
Acting Public Auditor

## **BACKGROUND**

Sonsorol State is one of the sixteen (16) States in the Republic of Palau. The State's Constitution, ratified on October 10, 1983, created the constitutional government of the State ofonsorol. The Constitution established the primary branches of the government consisting of the Executive (Office of the Governor), the Council of Chiefs, and the Legislature.

The Governor shall be the Chief Executive of the State Government. The Governor 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 Council of Chief is composed of each of the traditional Paramount Chiefs from the islands ofonsorol State. The Council of Chiefs shall have the following functions and powers: to request the Governor to veto any bill affecting customary law, traditional practices..., to participate in negotiations with other states or foreign companies, to select one chief from its membership to serve in the National Council of Chiefs for a term of four years..., among other powers.

The Legislative Power ofonsorol State shall be vested in theonsorol State Legislature which shall consist of one house. The Legislature shall be composed of four Paramount Chiefs from the four Municipalities inonsorol State..., two legislators to be popularly elected at-large and, for the first eight years after the effective date of the constitution, four representatives shall be popularly elected from the four Municipalities as follows: a) one shall be elected fromonsorol Municipality; b) one shall be elected from Pulo Anna Municipality; c) one shall be elected from Merir Municipality; and d) one shall be elected from Fana Municipality... The legislature shall have the following powers: to levy taxes which shall be uniformly applied throughout the state, to borrow money on the credit of the State..., to delegate authority to municipalities and their administrative offices, to enact laws..., to provide for the welfare, peace and security of State residents, among other powers.

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

Article XII, Section 1, of the State's Constitution states in part: "There shall be a State treasury and municipal treasuries for each of the municipalities withinonsorol State. All public revenues from whatever source derived shall be deposited in the appropriate treasury. No funds shall be withdrawn from any treasury except by law."

In addition, Article XII, Section 12, of the State's Constitution states: "The State Legislature shall request an auditor to audit the State Budget at least once every four years and not later than 18 months after the effective date of this constitution. The auditor shall audit the accounts of every branch and agency of the State Government as well as advise the government of proper financial management techniques..."

The major source of funding for state operations comes from appropriations from the Olbiil Era Kelulau (OEK) in the form of block grants and capital improvement projects. For fiscal year 2006 through 2009, the Olbiil Era Kelulau (OEK) appropriated the sum of \$662,500 in block grants but there were no appropriations for Capital Improvement Projects.

## **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) 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 had established proper internal controls to ensure proper safeguarding of its properties and transactions were properly recorded.

The audit covered the period from fiscal year beginning October 1, 2005 through September 30, 2009. 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 the generally accepted government auditing standards. Those standards require 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 expenditure 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, accounts receivable and accounts payable, fixed assets, cash receipts, and non-payroll and payroll expenditures. In performing the review, we conducted specific 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.

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

Sonsorol 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.

Sonsorol State has not taken affirmative action to implement corrective action plan and/or to resolve audit findings contained in the OPA's previous audit reports covering fiscal years 1999 through 2005 as follows:

- Employee contributions for Civil Service Pension Plan
- Payroll system
- Bank Reconciliations
- Agreement to deliver vessel
- Audit of State budget
- Expenditures not properly supported

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

Sonsorol State's failure to take affirmative action to comply with prior year audit recommendations by the 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.

**SSG's Response:** *First, I concur to audit finding No. 1 that the state has outstanding prior audit findings, and the office of the Governor did provided corrective action plans and yet has not provided corrective actions. I promise that we will submit our progress report on the accomplishments of our audit follow ups of our pending audit findings of fiscal years 1999 to 2005.*

## **Finding No. 2: Purchase of State Boat**

The Republic of Palau Procurement Law and Regulations prescribe guidelines for use in procurement of goods and services to maximize competition towards ensuring increased economy and purchasing value of public funds. For State Governments, competitive bidding is required for goods or services costing \$5,000 or more. In the use of Request for Proposals (RFP), bid proposals should parallel the instructions and specifications in the RFP and, upon contract award, the eventual contractual agreement should coincide with terms and conditions of the RFP and the bid proposal

On December 29, 2006, Sonsorol State issued a Request for Proposal (RFP) soliciting proposals from qualified firms to provide a passenger/cargo vessel for Sonsorol State. The scope of work is defined in the RFP as follows:

- A. Provide a steel made passenger/cargo vessel that is not more than 20 years old.
- B. Contractor shall lease the vessel from Sonsorol State Government for at least 6 years.
- C. Contractor shall manage and operate the passenger/cargo ship
- D. Contractor shall provide at least 6 field trips to transport passengers, equipment and projects to the islands in Sonsorol state.
- E. Provide all technical and system information needed for securing all registration and licenses.
- F. Provide technical support needed for the first 4 years during the leasing period.

We found that only one (1) bid proposal was received by the State in response to the RFP. The bid proposal was submitted by a former Delegate of the State (to the Olbiil Era Kelulau) on behalf of TS Seacruiser Shipping Lines Ltd. operating out of Philippines. Subsequently, on January 22, 2007, a “Notice of Award” was issued to TS Seacruiser Shipping Lines Ltd. A contract was entered into between Sonsorol State and TS Seacruiser Shipping Lines Ltd. on March 15, 2007.

In the intervening period between April 19 and July 4, 2007, the State disbursed four checks in varying amounts totaling \$90,000 as payment for the State boat via the intermediary. However, the \$90,000 amount does not agree to the purchase price stipulated in the contract. The contract calls for the owner (State) to pay \$100,000 and the contractor pays the balance of \$80,000 and recovers the cost (contractor) through collection of revenues from operation of the owner’s passenger boat. In addition, the State advanced the \$90,000 through the middleman prior to obtaining transfer of the ownership of the boat from the contractor contrary to the terms of the contract. Moreover, the contractor failed to execute and provide a performance bond as required under Article X (7) of the contract. According to a letter dated February 9, 2009 to TS Seacruiser Shipping Lines, Governor Damian Albis terminated the contract for non-performance by the contractor. However, as of November 2009, Sonsorol State has not received the passenger/cargo boat or refunded its money in full.

It appears the Governor prematurely disbursed the money upfront to the intermediary before the transfer of ownership of the boat and inspection of the vessel. In addition, the OPA questions the use of the intermediary as he was used mainly as a conduit for the disbursement of funds to the contractor, which the State could have easily done. Once the State released the funds to the middleman, it lost control to the use of funds as leverage to force the contractor to perform obligations under the contract, as the State had no agreement with the middleman with respect to disbursement of funds to the contractor.

As a result, Sonsorol State is still without a passenger/cargo boat, denied the use of the \$90,000 and potential interest earnings, and still has to expend State resources to recoup the money from the contractor.

## Recommendation

The OPA recommends the Governor persist in the efforts to recover State funds from the contractor. In the future, the State should negotiate purchase agreements directly with a supplier instead of using an intermediary.

**SSG's Response:** *I have reviewed findings No. 2 and I concur to the findings and recommendations by the public auditor. Sossorol state will recover the state fund from the contractor.*

**OPA's Comments:** *The State should establish a repayment schedule with the Contractor, to include interests if the Contractor fails to make the required payments, in order to establish a definite timeline by which the money will be repaid. The Office of the Public Auditor will monitor and follow up with the State to ensure that the funds are recovered by the State.*

## Finding No. 3: \$22,811 of 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 accounting system of the state.

Our audit revealed that the Governor expended \$22,811 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>
2006	\$ 2,051
2007	\$11,831
2008	\$ 1,458
2009	\$ 7,471
<b>Total</b>	<b>\$22,811</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 \$22,811 of expenditures.

**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 or services purchased.

**SSG's Response:** *I concur to your finding Number 3 regarding the state's failure to provide adequate supporting documents to justify disbursements. After responding to the audit findings of 2006, I have instructed my treasurer to make sure all disbursements are fully supported before she files them. I further instructed her to separate incomplete supporting documents into separate file to be completed at a later date prior to filing them into completed check files. However, with our limited funding and budget, we are still unable to hire more staff to assist our treasurer in her hard task. Consequently, we are working hard to locate all the missing documents to complete our filing of our disbursement file records and submit copies to your office and at the same time complete our files.*

**OPA's Comments:** *The initial amount of questioned costs as reported in the Draft Audit Report was \$91,946, however; subsequently, the State was able to locate and provide to the OPA additional supporting documents to resolve a majority of the Questioned Costs thereby reducing the amount down to \$22,811. The State may continue to provide to the OPA the other supporting documents to resolve the remaining unresolved Questioned Costs as they are located.*

#### **Finding No. 4: Travel Vouchers not Filed to Justify \$3,329 of Travel Costs**

Travel Policies and Procedures provide important guidelines on how State funds are used to fund official travel of the State including per diem rates of travel destination, authorized travel expenses, submission of travel vouchers after completion of travel, trip reports, etc.

The audit revealed that \$3,329 of State funds was used for travel, however, travelers failed to file travel vouchers after completion of travel. The filing of a travel voucher (with related supporting documents such as invoices/receipts) is essential as it documents expenses incurred during travel, travel destinations, and other necessary information to justify the use of public funds.

The Governor did not ensure that travelers filed their travel vouchers with supporting documents such as invoices/receipts, ticket copies, trip reports, etc. after completion of travel.

Due to lack of travel vouchers, we were unable to determine the propriety of travel expenditures and whether the purpose of travel was accomplished.

**Recommendation:** We recommend the Governor strictly enforce the requirement for filing travel vouchers after completion of travel. A travel voucher (consisting of a Travel Authorization, invoices/receipts, ticket stubs, boarding passes, trip report, etc.) should be filed within thirty (30) days after completion of travel. A traveler who fails to file a travel voucher within the required filing period should have the cost of travel garnished from his pay on a bi-weekly basis. In addition, an official who fails to file a travel voucher should be prohibited from further travel until he/she fulfills the filing requirements.

**SSG's Response:** *I have read and concurred to the audit finding No. 4 regarding travel vouchers not filed. I have located my ticket copies, boarding pass, created our trip report, and receipts and enclosed with our travel authorization forms and the check copies.*

However, our speaker needs to file his ticket copies and his boarding pass and I will submit the copy as soon as I receive it.

**OPA's Comments:** *The Governor should meet with the leadership and employees of Sonsorol State to discuss the requirements of the National Government's Executive Branch Travel Policies and Procedures. In particular, it should be explained that travelers using State funds to travel are required to file a travel voucher within 30 days after completion of travel. In addition, it also should be discussed that failure of traveler to file a travel voucher will result in the garnishing from employees' bi-weekly pay a predetermined amount until the travel advance issued to the employee is recovered in full. Finally, the policies and procedures further prohibit an employee or official with outstanding travel advance from future travel until the travel advance is cleared.*

**Finding No. 5: \$7,528 of Procurements Lack Competitive Bidding**

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

We found the State procured fuel for the State's ship in the amount of \$7,528 without competitive bidding as shown below:

Check Date	Check No.	Amount	Services or Goods
3/13/06	8027	\$ 7,528	Fuel for field trip

The Governor failed to comply with the Republic of Palau's Procurement Law and Regulations.

As a result, we were unable to determine if the State obtained the lowest price for fuel without competitive procurement.

**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 are subject to competitive bidding.

**SSG's Response:** *I have read and understood the Public Auditor's finding No. 5 regarding Sonsorol State's failure to comply with the National Procurement Law. Sonsorol State did procure fuel for state's ship in the amount \$7,528 without competitive bidding.*

*I would like to justify that our procurement of fuel dated 3/13/06 was based on our memorandum of understanding with Hatohobei State that both states should share the cost and expenses of combined trips in order to obtain minimum expenses for field trips to the Southwest Islands.*

*However, Hatohobei state owns the boat that we had been using for field trips to south west islands. In addition to that, Hatohobei state has a discount card with Shell Company that we have been sharing to procure fuel for field trips. Consequently, when we schedule field trips,*

*Hatohobei State usually arrange for the fuel for their ship, and we pay our share of the fuel directly to shell company with the discount from Hatohobei's invoice.*

**OPA's Comments:** *Sonsorol State should have requested Hatohobei State to obtain price quotations for the volume of fuel required for the trip to ensure that it was getting the best price for the money it paid.*

### **Finding No. 6: Fixed Asset Accounting System**

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 2006 through 2009 and, although the State provided a schedule, we found during the fieldwork fixed assets that were not on the listing; such as a brush cutter, chainsaw, a 25 horsepower outboard motor engine, etc.

It appears the State is not conducting periodic physical inventory of State properties to ensure all fixed assets are properly recorded, determine their location and condition, and to remove assets that are no longer in operation.

As a result, the State is unable to maintain an accurate listing of fixed assets purchased. In addition, it is unable to reconcile the listing of fixed assets to actual physical inventory due to the absence of periodic physical inventory.

**Recommendation:** We recommend the Governor direct the State Treasurer to establish a system to account for State fixed assets. The system should include a process for recording fixed assets, conduct of periodic physical inventory, and inspections to determine location and condition of fixed asset. In addition, assets that are no longer operational should be removed from the fixed asset listing.

**SSG's Response:** *I concur to the Public Auditor's finding No. 6 regarding Fixed Asset Accounting System for the state. I have discussed about the finding with my treasurer and she had understood my direction.*

### **Finding No. 7: 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, evaluations, disciplinary actions, etc.

Our audit revealed that although the State has established a personnel system for State employees, the system is not properly operating. For example, we found that approval dates for

most personnel actions selected for review were dated after their effective date. Moreover, allotments were deducted from employees' paychecks without allotment authorization forms approved by employees.

It appears the State has not fully implemented the personnel system for State employees.

As a result, we were unable to determine if State employees' personnel actions forms were properly approved. In addition, allotment deductions from employees' paychecks without allotment authorizations approved by employees make the State vulnerable to potential dispute with employees over such deductions.

**Recommendation:** We recommend the Governor establish a personnel system for State employees. Each employee should have a personnel action form showing position, rate of pay, effective date of hire, and approved by the appropriate authorizing official. In addition, all allotment deductions from employees' paychecks should be evidenced by allotment authorization forms signed by employees. We further recommend that the Governor consult with the National Government's Bureau of Public Service System, Ministry of Finance, for assistance in implementing the system.

**SSG's Response:** *I concur to your audit findings No. 7 regarding the state Personnel system. Yes it is true that the state has established a personnel system. It is also true that the systems are not properly operating due to the fact that Sonorol state is not fully staffed as the other governmental agencies do. I only have one treasurer doing all the financial responsibilities. During my second term as Governor, I tried to add more administrative staffs such as an accountant, Procurement Officer/Administrative officer, and a secretary for our State. Nevertheless, with these budget constraints due to the national economic down turn and budget cuts, it is impossible to open up new positions to our state offices.*

*There are two points that I would like to justify in regards to your findings, one is regarding the personnel action forms. The personnel action forms that are signed and dated after their effective dates were personnel action forms created by the treasurer at the time I am in office because there were no personnel action files for the existing employees of the state at the time we reviewed our files, especially after we received our first audit findings back in 2005.*

*Second, as for the allotment authorization forms, we do have the files for the allotment forms, but my treasurer had them in a separate file in her office. From now on, I have instructed my treasurer to make copies of all the allotments and file them with the employee's personnel files.*

### **Finding No. 8: Accounts Payable System**

An accounts payable accounting system is essential to account for and keep track of accounts payable and other obligations of the State.

We requested a schedule of State's accounts payable as of September 30, 2009; however, the State did not provide one. Upon conducting alternative audit procedures, however, we found a number of unrecorded liabilities and, upon further inquiry, found that the State had established credit accounts with several local business establishments.

It appears the Governor has not established a system to account for and keep track of State's accounts payable and other obligations.

Without a system to keep track of State's obligations, the State is unable to conduct effective cash flow and other critical financial analysis. Furthermore, the State is unable to effectively prioritize payment of its obligations to minimize interest charges on outstanding accounts. Moreover, the absence of accurate records of State obligations impedes the process of formulating a State budget.

**Recommendation:** We recommend the Governor establish an accounts payable system to account for and keep track of state's accounts payable and other obligations. The accounts payable system will enable the State to conduct cash flow and other financial analysis critical for policy-making decisions. Furthermore, the system will also facilitate prioritizing payments of obligations in order to effectively minimize interest charges on outstanding accounts. Finally, with accurate records on accounts payable and other liabilities, the State will be able to formulate annual unified budgets that take into consideration the financial condition of the State.

**SSG's Response:** *I concur to the Public Auditor's finding No. 8 regarding the state's Accounts Payable System. I have instructed my treasurer to establish the state's accounts payable system. I have brought in an accountant from PICRC to help my treasurer and instruct her on how to create her system in the Quick books. We also have attended week training on Government Accounting Workshop with all the states accountants and budget officers.*

*I thought that we have had the system in place. At this time, I have warned my treasurer to improve her performance. I am also considering her work load so I hope we could hire more staff to take some of her responsibilities.*

### **Finding No. 9: Cash Receipts**

Cash receipts are an essential component of the State's recordkeeping system to support revenue collections and reconciliation to deposits. In addition, cash receipts serve as source documents for revenue classifications in the State's financial records.

In our examination of cash receipts we found the State did not always issue receipts to support revenues collected in fiscal years 2006 through 2009.

It appears the cause of the above condition is that cash receipts are not uniformly issued to evidence revenue collections.

As a result, we were unable to determine the propriety of all revenues collected, and whether all collections were deposited.

**Recommendation:** We recommend the Governor direct the State Treasurer to issue cash receipts to evidence all revenue collections. At the minimum, cash receipt should identify the payer, amount received, and date of receipt. In addition, cash receipts should be issued in proper numerical sequence and reconciled to deposits.

**SSG's Response:** *I concur with the Public Auditor's finding No. 9 regarding the Cash Receipts. I have discussed this issue with the staff of the Public Auditors Office Ms. Rena. Our state treasurer will issue cash receipts to all revenue collections including the allotments received from the National Treasurer.*

### **Finding No. 10: Bank Reconciliations**

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 consistently perform monthly bank reconciliation of its bank accounts. We further found that the latest bank reconciliation was performed for the month of March 2008.

It appears essential internal controls over cash are not being performed.

The absence of bank reconciliation can lead to bank errors and other irregularities affecting cash balances without timely detection. In addition, without 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 identify errors and other irregularities and to adjust State records accordingly.

**SSG's Response:** *I have read and concur to the Public Auditor's finding No. 10 regarding the state's Bank Reconciliations. Our treasurer had begun reconciling our bank statements. At this time, I have instructed our treasurer to continue and try to update our reconciling of our bank statements.*

**Finding No. 11: \$107,029 of Uncategorized Expenditures**

Article XII, Section 1, of the State’s Constitution states in part: “There shall be a State treasury and municipal treasuries for each of the municipalities within the State. All public revenues from whatever source derived shall be deposited in the appropriate treasury. No funds shall be withdrawn from any treasury except by law.”

The State Public Laws SSPL No. 6-7R-1, SSPL No. 6-23S-1, SSPL No. 6-30S-1, and SSPL No. 7-4R-1 appropriated funds to cover State operations for fiscal years 2006 through 2009. Based on our review of these appropriations laws, we found no budget activity or line item “uncategorized expenditures”. However, during the audit we found that on numerous occasions the State expended funds and charged expenditures to a category “uncategorized expenditures” in the fiscal years shown below:

<b>Fiscal Year</b>	<b>Amount</b>
2006	\$ 3,072.60
2007	\$ 91,230.48
2008	\$ 10,434.59
2009	\$ 2,291.00
<b>Total</b>	<b>\$ 107,028.67</b>

It appears the Governor is not reviewing Quarterly, Semi-annual, and Annual expenditure reports to ensure expenditures classification coincides with the State’s appropriation budget.

As a result, the \$3,072.60 expended in fiscal year 2006, \$91,230.48 expended in fiscal year 2007, \$10,434.59 expended in fiscal year 2008, and \$2,291 expended in fiscal year 2009 may be in violation of the State’s Constitution as it appears they were not properly authorized by law.

**Recommendation:** We recommend the Governor direct the State Treasurer to record and classify expenditures in accordance with the State’s unified budget acts. Furthermore, the Treasurer should be more conscientious in preparing procurement documents (APV, PO, RQ, etc.) to ensure the documents identify the correct account (budget activity) to be charged, and the Governor should not approve procurement documents unless there are sufficient funds in the account to cover the expenditures. Finally, the Governor should review Quarterly, Semi-annual, and Annual expenditures reports to ensure expenditures classification coincides with the State’s unified budget.

**SSG’s Response:** *I have read and understood the Public Auditor’s finding No. 11 and its recommendation for corrective actions. I have concurred that it is true that our record system is the cause of all the problems stated in this audit findings. First, I would like to inform you that the treasury does submit monthly reports to me on the status of our expenditures through financial report that she prints out from her quick books report on a monthly basis. However, I was not aware that the uncategorized expenses were not the proper term to be used in the accounting system. I assumed that it is in the machine and therefore it is a special section of the*

*budget report in the QuickBooks that relates the expenses to the special grant section in the budget laws and the revenue section in the financial report.*

*Therefore, I have instructed my treasurer to identify those expenses and record them and classify them in the procurement documents as to what section in the budget law does the expense was charged to. We reviewed all the expenses and found out that the expenditures were mainly sourced from special grants such as the stimulus grant, Transportation grant, other special grants and also other payments for prior year payables such as the Social Security payments that were paid after the end of a fiscal year.*

**OPA’s Comments:** *Grants are covered in the Sonsorol State’s Unified Budget as the grants have to be authorized and appropriated before they can be expended. The grants are usually designated by the grantor for a specific purpose. Therefore the State should establish separate classifications in the State’s accounting system to record and capture expenditures for each grant. This process makes reporting to the grantor more accurate as well as the State’s expenditure reports.*

**Finding No. 12: Field Trip Expenses Over Budget**

Article XII, Section1, of the State’s Constitution states in part: “There shall be a State treasury and municipal treasuries for each of the municipalities within Sonsorol State. All public revenues from whatever source derived shall be deposited in the appropriate treasury. No funds shall be withdrawn from any treasury except by law.”

The audit revealed that the Governor expended State funds for field trips to Sonsorol in excess of amounts appropriated for that purpose for each fiscal year shown below:

<b>Fiscal Year</b>	<b>Amount Appropriated</b>	<b>Amount Expended</b>	<b>Variance</b>
2009	\$ 15,224.00	\$ 18,178.83	\$ (2,964.83)

It appears the Governor did not monitor expenditures to ensure amounts were contained within appropriation limits.

As a result, the State overspent the budget for field trips to Sonsorol for fiscal year 2009 in violation of the State Constitution.

**Recommendation:** We recommend the Governor direct the State Treasurer to provide periodic (monthly, quarterly, semi-annual, annual etc.) expenditures report to update the Governor of the status of expenditures compared to budget. The status reports will provide the Governor updated information on status of expenditures compared to budget with which to reprogram funds, request for supplemental appropriation, or make other policy decisions. In addition, the status reports will also enable the Governor to control expenditures more effectively so as to prevent overspending budget activities.

**SSG's Response:** *I have read and understood the Public Auditor's finding No. 12 regarding the over budget of filed trip expenses. We found out that the variance given in your report does not agree with our records. We reviewed all our records and the records that we submitted to the Auditor's office and found out the reasons for our differences. One reason was that our treasurer did not submit supplemental budget laws for FY 2007 and 2009. Consequently, we are transmitting the copies of the budget laws with this report.*

*As for FY 2006, we found out that the budget variance given in your report resulted from the problems of our accounting system. Our review revealed that during FY 2006 we received field trip refunds from other agencies that we shared costs of field trips to South West islands. For example, on 2/22/06 we received \$3,865.66 from Dini Faruya Organization for their share of our field trip. On 3/21/06 we received \$3,706.68 from the National Treasury for refund of Bureau of Land & Survey's share. We ran a field trip and due to the procurement process of the National Government, we had a oral agreement the Minister of Resources and Development at that time that Sonsorol State will accommodate the National surveyors on the regular South west field trip during 2006, and BLS will refund Sonsorol State for their share. Then on 9/22/06, we received \$4,500 from Dini Faruya for their share of fuel cost for filed trip to the South west islands.*

*I believe that our treasurer did not make any cash receipt for this collection to identify and classify the source of revenue collected.*

*However, our treasurer for her part said that she did the adjustments in her Quick books and the amount in the report that she submitted to my office showed no sign of over expenditure.*

**OPA's Comments:** *We have reviewed public laws and the accounting system as well as bank statements to locate the cost sharing of the field trips and have adjusted the over expenditures of the field trips at which only fiscal year 2009 showed the over expenditures for the transportation. Public Laws should be provided at the beginning of the audit and cash receipts issued when revenues are collected so that funds are easily tracked.*

## SONSOROL STATE GOVERNMENT

### STATUS OF RECOMMENDATIONS

**FOR THE PERIOD OF OCTOBER 1, 2005 THROUGH SEPTEMBER 30, 2009**

No.	Recommendation	Status	Plan of Action to implement Recommendation
1	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.	<b>Open</b>	<ul style="list-style-type: none"> <li>• The state has paid in full all the state debt with Pension Plan.</li> <li>• The state is currently paying its pension plan contributions to the office of the Civil Service Pension Plan on a timely basis to date.</li> <li>• Sonsorol State has no prior obligation or debt with pension plan office since we responded to the Public Auditor in 2007 until today.</li> <li>• The next action that we need to do this fiscal year is to execute contracts with the state employees who have refunded their withheld pension contributions between October of fiscal year 1987 to 1999 to pay back the office of the Civil Service Pension Plan through written contract from fiscal year 2002 to 2010.</li> <li>• Sonsorol State will continue to report to the office of the Public Auditor on progress of their contracts and collections.</li> </ul>
2	The OPA recommends the Governor persist in the efforts to recover State funds from the contractor. In the future, the State should negotiate purchase agreements directly	<b>Open</b>	<ul style="list-style-type: none"> <li>• I will work hard to recover the state fund that the state had disbursed to the contractor. Currently we have recovered \$34,000.00 and I will continue to recover the remaining</li> </ul>

	with a supplier instead of using an intermediary.		<p>balance prior to the end of my term.</p> <ul style="list-style-type: none"> <li>The state will follow the auditor's recommendation that the state should negotiate purchase agreements directly with a supplier and not to use intermediary.</li> </ul>
3	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 or services purchased.	<b>Open</b>	<ul style="list-style-type: none"> <li>We have located most of the missing documents and submitting with this audit response.</li> <li>The state will work hard to locate possible funding to hire more executive staffs to improve the work of the administrative duties of the executive branch of Sonsorol State Government.</li> </ul>
4	We recommend the Governor strictly enforce the requirement for filing travel vouchers after completion of travel. A travel voucher (consisting of a Travel Authorization, invoices/receipts, ticket stubs, boarding passes, trip report, etc.) should be filed within thirty (30) days after completion of travel. A traveler who fails to file a travel voucher within the required filing period should have the cost of travel garnished from his pay on a bi-weekly basis. In addition, an official who fails to file a travel voucher should be prohibited from further travel until he/she fulfills the filing requirements.	<b>Open</b>	<ul style="list-style-type: none"> <li>The state will and must follow the travel policy of the National Government as the state has no policy of its own in regards to Travel policies.</li> <li>The state will make sure that all travels must obtain a complete travel voucher with in the 30 days time and have it filed for good record keeping.</li> </ul>
5	We recommend the Governor adhere to the Republic of Palau's Procurement Law and Regulations by ensuring that	<b>Open</b>	<ul style="list-style-type: none"> <li>Governor will submit copy of the memorandum of understanding signed by the</li> </ul>

	State procurements greater or equal to \$5,000 are subject to competitive bidding.		<p>leadership of both states of Sonsorol and Hatohobei with our check copy.</p> <ul style="list-style-type: none"> <li>• Governor will also obtain copy of the invoice from Hatohobei State and submit with this report.</li> <li>• Sonsorol State will enact a state law that will regulate proper procedure in running field trips in order to practice a legal procedure in procuring field trip services and expenses to the farthest states of Sonsorol and Hatohobei States.</li> </ul>
6	We recommend the Governor direct the State Treasurer to establish a system to account for State fixed assets. The system should include a process for recording fixed assets, conduct of periodic physical inventory, and inspections to determine location and condition of fixed asset. In addition, assets that are no longer operational should be removed from the fixed asset listing.	<b>Open</b>	<ul style="list-style-type: none"> <li>• The treasurer will improve her establishment of the state fixed assets by removing all state assets that are no longer operational.</li> <li>• The treasurer and the staffs will conduct a physical inventory of the state assets and periodically inspect, locate, and record conditions of the state's properties.</li> </ul>
7	We recommend the Governor establish a personnel system for State employees. Each employee should have a personnel action form showing position, rate of pay, effective date of hire, and approved by the appropriate authorizing official. In addition, all allotment deductions from employees' paychecks should be evidenced by allotment authorization forms signed by employees. We further recommend that the Governor	<b>Open</b>	<ul style="list-style-type: none"> <li>• The state will follow the recommendation of the Public Auditor and seek assistance from the office of Public Service System in training our staff to improve and have our personnel system implemented well.</li> <li>• Our state treasurer will make copies of all the allotment authorization forms for the state employees and filed them with the Personnel files.</li> </ul>

	consult with the National Government's Bureau of Public Service System, Ministry of Finance, for assistance in implementing the system.		
8	We recommend the Governor establish an accounts payable system to account for and keep track of state's accounts payable and other obligations. The accounts payable system will enable the State to conduct cash flow and other financial analysis critical for policy-making decisions. Furthermore, the system will also facilitate prioritizing payments of obligations in order to effectively minimize interest charges on outstanding accounts. Finally, with accurate records on accounts payable and other liabilities, the State will be able to formulate annual unified budgets that take into consideration the financial condition of the State.	<b>Open</b>	<ul style="list-style-type: none"> <li>I have directed my treasurer to establish our accounts payable system and from now on she is going to be submitting a complete financial report to my office on a monthly basis.</li> </ul>
9	We recommend the Governor direct the State Treasurer to issue cash receipts to evidence all revenue collections. At the minimum, cash receipt should identify the payer, amount received, and date of receipt. In addition, cash receipts should be issued in proper numerical sequence and reconciled to deposits.	<b>Open</b>	<ul style="list-style-type: none"> <li>The state treasurer will issue cash receipts to evidence all revenue collections. She will also issue cash receipts in a proper numerical sequence and reconciled to every deposit.</li> </ul>
10	We recommend the Governor direct the State Treasurer to perform monthly bank reconciliation. On a monthly basis, the Treasurer should	<b>Open</b>	<ul style="list-style-type: none"> <li>The state treasurer will continue to reconcile our bank statements on a monthly basis.</li> </ul>

	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 identify errors and other irregularities and to adjust State records accordingly.		
11	We recommend the Governor direct the State Treasurer to record and classify expenditures in accordance with the State's unified budget acts. Furthermore, the Treasurer should be more conscientious in preparing procurement documents (APV, PO, RQ, etc.) to ensure the documents identify the correct account (budget activity) to be charged, and the Governor should not approve procurement documents unless there are sufficient funds in the account to cover the expenditures. Finally, the Governor should review Quarterly, Semi-annual, and Annual expenditures reports to ensure expenditures classification coincides with the State's unified budget.	<b>Open</b>	<ul style="list-style-type: none"> <li>• The state will follow the recommendation of the Public Auditor and this time we will obtain all the proper documents and proper forms prepared for complete procurement documentation.</li> <li>• Our state treasurer will record and classify all the uncategorized expenditures in the audit findings and report to the public auditor as soon as possible.</li> <li>• We will create forms that fit our state that will serve as a encumbrance with the governor's approval for certified sufficient fund in the budget law prior to procurement approval in the APV form.</li> </ul>
12	We recommend the Governor direct the State Treasurer to provide periodic (monthly, quarterly, semi-annual, annual etc.) expenditures report to update the Governor of the status of expenditures compared to budget. The status reports will provide the Governor updated information on status of expenditures compared to budget with which to reprogram funds,	<b>Open</b>	<ul style="list-style-type: none"> <li>• We will work with the Public Auditors Office to see if the findings were actually an over expenditure or was it a lack of supporting documents and justification submitted.</li> <li>• Sonsorol State will improve its accounting system and record keeping in order to improve its report and recommendations from its audit report.</li> </ul>

	request for supplemental appropriation, or make other policy decisions. In addition, the status reports will also enable the Governor to control expenditures more effectively so as to prevent overspending budget activities.		
--	---	--	--

**Status of Recommendations**

**Open – An open recommendation is one where no action or plan of action has been made by the client (state, department or agency).**

**Resolved– A resolved is one which OPA is satisfied that the client cannot take immediate action, but has established a reasonable plan and time frame of action.**

**Closed – A closed recommendation is one which the client has taken sufficient action to meet the intent of the recommendation or OPA has withdrawn it.**

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

**OFFICE OF THE PUBLIC AUDITOR  
REPUBLIC OF PALAU  
P. O. BOX 850  
KOROR, REPUBLIC OF PALAU 96940**

**Ground Floor  
Orakiruu Professional Building  
Madalaii, Koror, Palau**

**TELEPHONE NOS: (680) 488-2889/5687  
FACSIMILE NO: (680) 488-2194  
E-MAIL ADDRESS: [palaupa@palaunet.com](mailto:palaupa@palaunet.com)**

**MONDAY THRU FRIDAY  
7:30 a.m. - 4:30 p.m.**

**(Closed on Legal Holidays)**