

PALAU INTERNATIONAL CORAL REEF CENTER  
(A COMPONENT UNIT OF THE REPUBLIC OF PALAU)

INDEPENDENT AUDITORS' REPORT ON  
INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2009

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

Board of Directors  
Palau International Coral Reef Center:

We have audited the financial statements of the Palau International Coral Reef Center (the Center) as of and for the year ended September 30, 2009, and have issued our report thereon dated May 27, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Center's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Center's financial statements that is more than inconsequential will not be prevented or detected by the Center's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Responses (pages 3 and 4) to be significant deficiencies in internal control over financial reporting as items 2009-1 and 2009-2.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 2009-1 to be a material weakness.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Center's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings and Responses as item 2009-1.

We noted certain matters that we reported to management of the Center in a separate letter dated May 27, 2010.

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

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

*Deloitte & Touche LLC*

May 27, 2010

PALAU INTERNATIONAL CORAL REEF CENTER

Schedule of Findings and Responses  
Year Ended September 30, 2009

Deferred Revenue

Finding No. 2009-1

Criteria: Grant funds received should be used for purposes stipulated in the grant agreement.

Condition: The Center has deferred revenue of \$212,026 related to grant funds received, which is in excess of total cash at September 30, 2009, indicating that grant funds received are being used for purposes unrelated to the grant. Additionally, the Center has internally restricted cash of \$104,109 at September 30, 2009. Significant deferred revenue balances noted are as follows:

<u>Grant Name</u>	<u>Amount</u>
Fund 201C: NOAA Coral Monitoring - 2008	\$ 46,020
Fund 253: Packard MPA	\$ 54,859

Cause: The cause of the above condition is the use of grant funds for purposes unrelated to the grant.

Effect: The effect of the above condition is the potential violation of grant terms and conditions.

Recommendation: We recommend that the Center establish policies and procedures to assist in ensuring that grant monies are used for purposes stipulated in the grant agreement and that unexpended grant funds are monitored.

Prior Year Status: The lack of policies and procedures in monitoring the use of grant monies was reported as a finding in the audits of the Center for fiscal years 2007 and 2008.

Auditee Response and Corrective Action Plan:

**Name of Contact Person:** Fabian B. Iyar, Chief Executive Officer

**Corrective Action Plan:** Some grants are multi-year grants, and so when we receive them in advance, they have to be deferred until such time that projects are implemented and corresponding expenses are incurred and revenues recognized. Also, cash on hand fluctuates every month and the year-end balance is usually less than deferred revenues if the multi-year grants are still in their early stages. Due to cash flow shortages, we are forced to use grant money for regular operations, but they all get reimbursed when cash allotments are received. We will assess each grant fund, and formulate policies to make sure that grant funds are truly restricted and can only be used for intended purposes/allowable costs under the respective grants. We are already creating separate bank accounts for major grants received, which will be used in line with the stipulations set by the respective grants.

**Proposed Completion Date:** December 2010

PALAU INTERNATIONAL CORAL REEF CENTER

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2009

Inventory

Finding No. 2009-2

Criteria: An inventory monitoring system should ensure completeness of periodic counts, inventory unit costs should be determined based on the Center's costing method, and inventory prices should be approved by management.

Condition: Tests of inventory noted the following:

- In the spare parts inventory listing provided by the Center, unit price was not assigned to one (1) 25 mm hose adapter.
- Different unit costs were assigned to spare parts with similar descriptions and mode/code number. Also, similar items were not consolidated in the final spare parts valuation with one unit cost assigned.
- Our testing identified that unit costs were not updated when purchases were made and no documentation existed regarding unit cost determination.

Cause: The cause of the above condition is the lack of inventory monitoring.

Effect: The effect of the above condition is the potential misappropriation and misstatement of inventory.

Recommendation: We recommend that the Center maintain an inventory listing that is accurate and updated. The Center should ensure that invoices are on file to support inventory costing. Further, mark-ups on inventory should be based on the cost per invoice with management's directive.

Prior Year Status: The lack of an inventory monitoring system, unsupported unit costs, and unauthorized inventory prices was reported as a finding in the audits of the Center for fiscal years 2005 through 2008.

Auditee Response and Corrective Action Plan:

**Name of Contact Person:** Fabian B. Iyar, Chief Executive Officer

**Corrective Action Plan:** For the inventory monitoring system, we will make sure that we perform timely reconciliation of inventory on hand with inventory records, and make sure invoices are available on file to support inventory costing. We will also make sure that physical count sheets are on file to support the final inventory listing and that procedures are implemented to ensure completeness of the count at year end. We have created a purchase list showing mark-ups on inventory which is based on the cost per invoice and with management approval. We will also make sure that staff assigned to conduct the inventory can do it correctly the first time.

**Proposed Completion Date:** December 2010

PALAU INTERNATIONAL CORAL REEF CENTER

Unresolved Prior Year Comments  
Year Ended September 30, 2009

The status of unresolved prior year internal control findings is disclosed within the Schedule of Findings and Responses section of this report (pages 3 and 4).