

**PUBLIC UTILITIES CORPORATION  
(A COMPONENT UNIT OF THE REPUBLIC OF PALAU)**

**INDEPENDENT AUDITORS' REPORT ON  
INTERNAL CONTROL AND ON COMPLIANCE**

**YEAR ENDED SEPTEMBER 30, 2011**

**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  
Public Utilities Corporation:

We have audited the financial statements of the Public Utilities Corporation (PUC), as of and for the year ended September 30, 2011, and have issued our report thereon dated August 11, 2012. 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

Management of the PUC is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered PUC'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 PUC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of PUC's internal control over financial reporting.

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings and Responses as items 2011-1 and 2011-2 that we consider to be significant deficiencies in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether PUC's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed two instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as items 2011-1 and 2011-2.

We noted certain matters that we reported to management of PUC in a separate letter dated August 11, 2012.

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

This report is intended solely for the information and use of the management, the Board of Directors and others within PUC, and the Office of the Public Auditor, and is not intended to be and should not be used by anyone other than these specified parties.

*Deloitte & Touche LLP*

August 11, 2012

PUBLIC UTILITIES CORPORATION

Schedule of Findings and Responses  
Year Ended September 30, 2011

Loans Payable

Finding No. 2011-1

Criteria: As a condition of the National Development of Bank of Palau (NDBP) loan, PUC agreed to implement a tariff by August 2010 which is to include a component sufficient to repay the loan.

Condition: At September 30, 2011, PUC has not been able to address the NDBP loan condition.

Cause: The cause of the above condition is varying interpretations of this requirement.

Effect: The effect of the above condition is potential noncompliance with the criteria.

Prior Year Status: Noncompliance with the criteria was reported as a finding in the audit of PUC in 2010.

Recommendation: We recommend that PUC consult with NDBP regarding the criteria.

Auditee Response and Corrective Action Plan: PUC acknowledges the above finding. The PUC Board of Directors held public hearings in April 2012 on a new tariff schedule that should generate sufficient revenues to cover PUC's debt service requirements and subsequently passed a resolution to implement the tariff at the latest by October 1, 2012.

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Schedule of Findings and Responses  
Year Ended September 30, 2011

Minutes of Board of Directors Meetings

Finding No. 2011-2

Criteria: Minutes of Board of Directors meetings are considered public record and should include documentation of approval of significant business decisions and events. Further, such are reviewed and approved on a timely manner.

Condition: Minutes of PUC Board of Directors meetings did not include certain significant business decisions and events such as the declaration of emergency status and approval of certain significant procurement actions.

In addition, minutes of meetings from January 4, 2011 to August 3, 2011 were in draft form while minute summaries were not available for the period from August 4, 2011 to December 2011.

Cause: The cause of the above is untimely recordation and approval of minutes.

Effect: The effect of the above condition is potentially inadequate documentation supporting significant business decisions and events.

Recommendation: We recommend that meeting minutes include information on significant procurement decisions, approval of management initiatives, and other significant business decisions. In addition, we recommend that all minutes be reviewed, be formally approved at the following board meeting, and be properly filed.

Auditee Response and Corrective Action Plan: The PUC Board minutes are now being documented and reviewed in a more timely manner with the Public Information Officer assuming the responsibilities of the former Board Secretary. We believe the above condition has been resolved effective February 2012.

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Unresolved Prior Year Findings  
Year Ended September 30, 2011

The status of unresolved prior year findings are disclosed within the Schedule of Findings and Responses section of this report (page 3).