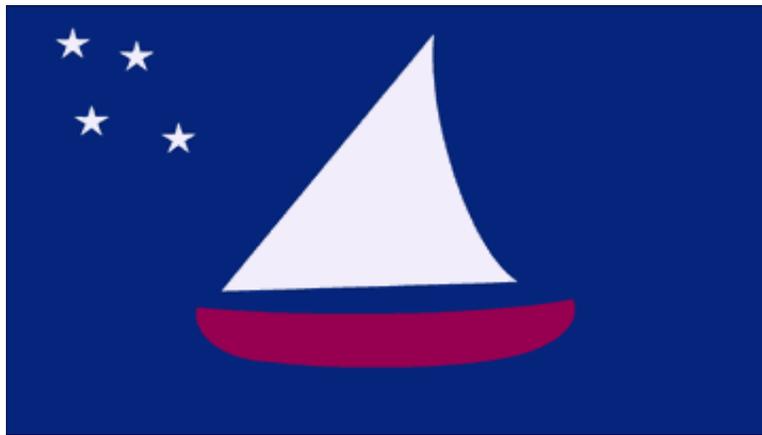


# PERFORMANCE AUDIT REPORT

On



SONSOROL STATE GOVERNMENT

REPUBLIC OF PALAU

PERIOD COVERED

October 1, 1998 to September 30, 2005

Performed by the Office of the Public Auditor



## REPUBLIC of PALAU

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October 10, 2007

**Serial#: opa08-006au**

Honorable Damian 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, 1998 through September 30, 2005.**

Dear Governor Albis:

This report presents the results of our audit of Sonsorol State Government for the period from October 1, 1998 through September 30, 2005.

The Office of the Public Auditor (OPA) received your response to the draft audit report. Your response is published together with the final audit report.

The OPA has established an audit recommendation tracking system to keep track of the status of recommendations issued in this report. The OPA will issue follow-up letters on December 31 and June 30 each year to determine what action the State has taken to implement the recommendations. The status of the recommendations are reported to the Office of the President and the Olbiil Era Kelulau on a annual basis 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**

Period from October 1, 1998 to September 30, 2005

**Table of Contents**

<u><i>Performance Audit Report on Sonsorol State Government</i></u>	<u><i>Page No.</i></u>
I. Executive Summary	1-3
II. Background	4-5
II. Objective, Scope and Methodology	5
III. Detailed Findings:	
1. Earmarked CIP Funds	6-7
2. Employee Contributions for Civil Service Pension Plan	7-9
3. Payroll System	9-10
4. Purchase of State Boat	10-12
5. Sale of the State Boats	12-14
6. Boat Charter	14
7. Bank Reconciliation	15
8. Agreement to Deliver Vessel	16-17
9. Audit of State Budget	17
10. Questioned Cost	18-19
IV. Status of Recommendations	20-23
V. Auditee's Response	24-31



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October 10, 2007

Honorable Damian Albis  
Governor  
Sonsorol State Government

Dear Governor Albis:

This audit report presents the result of our audit of Sonsorol State Government for the seven (7)-year period ended September 30, 2005. Specifically, the audit covered the period from October 1, 1998 through September 30, 2005.

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 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.

### **Findings**

First, the State expended \$9,169 of funds earmarked by the Olbiil Era Kelulau for the Sonsorol State Office renovation on other expenditures and claimed the expenditures to be for the renovation of the State office.

Secondly, the State refunded employees' pension plan contributions totaling \$4,205, contributions which were withheld from employees' pay and accumulated over an extended period, without proper authorization and supporting documentation.

Thirdly, pay increments and retroactive pay were processed and implemented without proper supporting documentation (personnel actions and other essential documents) to evidence proper authorization.

Fourth, the State entered into an agreement with a vendor to purchase a State boat for a price of \$140,000, but only paid \$120,000, with no proof of discount or reduction of the purchase price and failed to adhere to the payment remittance mechanism stipulated in the agreement.

Fifth, the State purchased two passenger/cargo boats, one in fiscal year 1995 for \$100,000 and the other in fiscal year 1999 for \$140,000, spent \$13,356 and \$51,527 respectively to repair the boats and subsequently sold both boats for \$1,500 on October 2002.

Sixth, the State chartered a boat for a trip to Sonsorol for which it paid a charter fee in addition to purchasing fuel for the boat without an agreement.

Seventh, the State did not perform periodic bank reconciliations on its bank accounts.

Eighth, the State executed a contract with a vendor after services had been rendered and paid.

Ninth, the State Legislature failed to obtain the services of an independent auditor to audit the accounts of Sonsorol State once every four years in accordance with the State Constitution.

Tenth, we questioned \$87,945 of expenditures incurred during the period from October 1, 1998 through September 30, 2005 due to insufficient or lack of supporting documentation.

## **Recommendations**

First, we recommend the Governor expend earmarked funds in accordance with the purpose for which the funds are appropriated.

Second, we recommend the Governor withhold Pension Plan contributions from employees' pay on a bi-weekly basis and remit the contributions to the Pension Plan on a timely basis.

Third, we recommend the State utilize personnel files (containing personnel actions and other essential documents) to evidence the pay rates of State employees as well as retroactive actions.

Fourth, we recommend that when major procurements are executed via contractual agreements, the State carefully consider the terms and conditions of the agreement to ensure their practicality and the ability of the State to fulfill such terms and conditions.

Fifth, we recommend that in the acquisition of capital assets that require substantial up-front outlay of funds, the State use consultants (subject-matter experts) to inspect and advise the State of the quality and performance aspect of the product before purchase.

Sixth, we recommend that future arrangements involving the procurement of goods and services of a similar nature be put into a written agreement to better protect the interest of the State and to substantiate the value of goods and services procured with State funds.

Seventh, we recommend the State reconcile its bank accounts on a monthly basis to enhance and strengthen its cash management system.

Eighth, we recommend that contracts for the provision of services be executed prior to the delivery of services.

Ninth, we recommend the State Legislature obtain the services of an independent auditor to audit the State at least once every four years in accordance with Article XII, Section 12, of the State Constitution.

Tenth, we recommend the Governor to strictly enforce the controls requiring that expenditure of State funds be supported by adequate supporting documentation (invoices, receipts, contracts, etc.) to account for and justify the official nature of expenditures.

On September 24, 2007, the Office of the Public Auditor received the Sonsorol State Government's response to the Draft Audit Report. The response essentially agrees with all recommendations in the report. Based on the response we received from the Sonsorol State Government, we consider recommendations 2, 3, 7, 8, 9, and 10 "open" pending corrective actions by the Governor to establish the necessary legislation, policies and procedures or 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 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.



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..., and 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. The Olbiil Era Kelulau (OEK) appropriated the sum of \$1,064,875 in block grants and \$297,000 for Capital Improvement Projects (CIP) for the fiscal years 1999 through 2005.

## **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 October 1, 1998 through September 30, 2005. 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.

The audit was conducted in accordance with *generally accepted government auditing standards, issued by the Comptroller General of the United States*, and the Public Auditing Act of the Republic of Palau.

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: Earmarked CIP Funds**

Funds earmarked (appropriated for a specific purpose) by the Olbiil Era Kelulau (OEK) for specific Capital Improvement Projects (CIPs) should be expended for purposes for which the funds were earmarked.

During the audit, we found that the State expended funds earmarked by the OEK for the renovation of the State Office on other expenses and claimed the expenses to be for the State Office Renovation. The State Office was destroyed in a fire on May 06, 1998 and the State began leasing Office Space in September of 1998 and continued to do so to the present time. However, the State continued to procure lumber and other building materials, which could not have been for the State Office as the office was destroyed by fire. At the end of fiscal year 1998, State records showed a balance of \$13,750 for the State Office renovation fund but as of fiscal year 2005, State records showed total expenditures of \$9,169 on State Office renovation with no structure to support the alleged renovation expenditures.

It appears that expenditures were not carefully scrutinized to ensure that only those expenses relating to the State Office renovation were paid for and charged to the State Office renovation account.

As a result, \$9,169 of funds earmarked for the State Office Building renovation may have been used for other purposes contrary to the intent of the appropriation.

We recommend the Governor expend earmarked funds in accordance with the purpose for which the funds are appropriated. In addition, we recommend the Office of the Attorney General or the Office of the Special Prosecutor to further investigate the above expenditures and take appropriate action to recover any funds that may have been illegally expended.

**Sonsorol State Government's (SSG's) Response:** *First, I concur that funds earmarked by the (OEK) for specific CIP should be expended for the purposes for which the funds were earmarked. However, in regards to Finding No. 1: Earmarked CIP Funds, you said that funds were spent for materials for renovation of the state office. After doing some research on this as this incident is the responsibility of the prior Administrations, it I found out that the earmarked CIP was divided in half as follows: Seven thousand, five hundred dollars, (\$7,500.00) was allocated for the State liaison office in Echang Koror, and the other half was allocated for the State office ononsorol Island. Note that under RPPL 4-40, on pg. 29 sub. Section 4(p),onsorol State; the language simply spells that \$15,000.00 is earmarked for repair ofonsorol State Office. Also, under SSPL No. 4-11R-1, Funds in the amount of \$7,500.00 was appropriated for the purpose of repairing the State Office ononsorol Island. This source of funding comes from the National Government earmarked under RPPL 4-40. Therefore, the funds expended for purchasing materials after the date the Liaison Office foronsorol State in Koror got burned down was used for repair of the State Office inonsorol Island; the capital ofonsorol State.*

### **Corrective Plan of Action:**

*The State has been disciplined by having imposed upon it the National Government Penalties and Interests that are imposed on state debts that affect our budget and state operations. As the incumbent Governor of Sonsorol State, I have operated within and according to the budget I have been appropriated and tried my very best to use my budget means to pay all the state obligations to the National Government so that we don't encounter future debts with the National Government. Some examples are:*

- *The state has appropriated \$15,000 from its local revenue to pay its overdue debts, including penalties and interests owed to the Social Security Administration.*
- *The state is currently paying its ROP taxes, pension plan contributions, and Social Security contributions on a timely basis.*

**OPA's Comments:** At September 30, 1998, the State showed a balance of \$13,750 of the earmarked funds for renovation of the State Office, which means the State had already used \$1,250 from the initial \$15,000 appropriation. Further, if the State used \$7,500 to renovate the State Office in Sonsorol, as stated in your response, then there still remains \$6,250 from the above \$13,750 balance to be used for renovation, which the State was unable to present documented evidence of its use. Moreover, the Office of the Public Auditor was unable to verify and physically inspect the renovation of the State Office in Sonsorol Island due to its remote distance and lack of adequate logistical support.

### **Finding No. 2: Employee Contributions for Civil Service Pension Plan**

Employee contributions to the Civil Service Pension Plan deducted from employees' pay should be remitted by the State to the Pension Plan in a timely manner. Furthermore, employee contributions withheld by the State and accumulated over an extended period of time, and not remitted to Pension Plan, should not be refunded to employees.

During the audit we found that the State had been withholding and accumulating employee contributions for Civil Service Pension Plan for a prolonged period without remitting the contributions to the Pension Plan. In 1998, the State office building was destroyed by a fire along with volumes of records and documents, some of which may have contained information regarding State employees bi-weekly contributions to Pension Plan. For reasons we have not been able to establish, in 1999 the State refunded contributions for certain employees totaling \$4,205 without supporting documents itemizing and justifying the amount of refunds for each beneficiary. In addition, the State Governor entered into an agreement with the Civil Service Pension Plan to pay back the employee as well as the employer's contributions covering the years 1987 through 1999.

We were unable to determine the reason(s) and authority under which the Governor refunded State employees' Pension Plan contributions, which the State withheld and accumulated over an extended period without remitting to the Pension Plan office.

As a result, the State refunded \$4,205 of pension contributions to certain State employees without proper supporting documents itemizing and justifying the amount refunded to each beneficiary. In addition, the Governor may have violated the Pension Plan and Retirement Fund Act by failing to remit to Pension Plan contributions withheld from employees' pay. Moreover, legal issues may arise concerning the aforementioned agreement whereby the Governor agreed to pay the employees past contributions (which the Governor refunded to employees) with State funds along with employers' contributions.

We recommend the Governor withhold Pension Plan contributions from State employees' pay on a bi-weekly basis and remit the contributions to the Pension Plan on a timely basis. In addition, we recommend the Governor consult with his legal counsel regarding the potential legal issues surrounding the agreement whereby the State agreed to pay State employees past pension contributions. Moreover, if the State has already paid the past contributions, then the State should require each employee to reimburse the State for the amount of contribution paid on behalf of the employee.

**SSG's Response:** *With respect to Finding No. 2, I have read and understood the finding and the policies pertaining to employees' contributions to the Republic's Pension Plan. I totally agree with your findings, even though I was not the Governor at the time these issues occurred. However, I have researched the issues and came to my findings that it is true that most of the documents regarding the refund of pension contributions by Sonsorol state employees were refunded to the employees. Moreover, according to my findings, I found out that between 1987 to 1995, the office of the Pension Plan was not clear on whether state governments were eligible for pension plan membership or not. In fact, most of the state governments including Koror state experienced the same confusion experienced by Sonsorol state.*

*As a result, the leadership of Sonsorol State including the state legislature did approve a legislation to authorize the disbursement of funds from the state treasury to refund the state employees for their share that was deducted from the pay checks. Attached is the copy of the state public law that authorizes the disbursement of such funds.*

*After 1995, the state was cleared by the office of Pension Plan about their employees' contributions. Therefore, in the year 1999 the state started paying their employees' contribution to Pension Plan to this date.*

*In regards to the former Governor's decision to get into agreement with the office of Pension Plan to pay off their debt with the Pension Plan, I would say that it is the decision of the Administration under their leadership. I do believe that it is the best way to resolve the problem. The agreement will end next year, and after all payments for our debt with the Pension Plan, we will require the state employees to pay the state their share to recover the expenses that the state expended for the employees share to the Pension Plan.*

### **Corrective Plan of Action:**

- *Every year the state is paying \$14,750 for the payment of its obligation with the Pension Plan Office as a payment for the contract agreement signed between Sonorol State Government and the office of Pension plan for the unpaid obligation between 1987 through 1999.*
- *The State is now currently paying its employer/employee contribution to Pension Plan in a timely manner.*
- *The state is currently compiling all the records of state employees who have contribution share with Pension Plan between the year 1987 and 1999 to require them to pay back the state for their share.*
- *The state will execute a policy that if the employee doesn't pay the state for their obligation, the state may not release their documents required for their retirement fund.*

**OPA's Comments:** The Office of the Public Auditor will monitor and follow up on the corrective action plan to ensure that it is implemented and enforced.

### **Finding No. 3: Payroll System**

The State should establish a payroll system that utilizes and maintains personnel files for State employees. The personnel file should contain such documents as employment application, personnel action forms, and other essential forms to document and support personnel actions on employees. The personnel file should contain information on employees including, but not limited to, the name of employee, position, title, service computation date, effective date, pay level, pay increment, etc.

During the audit we found that the State has not established a payroll system to document and maintain vital information on State employees. As such, the State lacked documentation to support employees' rate of pay, rate of pay was properly authorized, position, etc. To illustrate the problem, the State's budget contains appropriations for budgeted positions; however, actual pay does not always agree to amounts budgeted, and without personnel actions, it is difficult to determine the authorized pay rate. In another case, an employee was given retroactive pay of \$640, however, without a *personnel action form*, we were unable to determine if the pay was properly authorized or calculated.

The cause of the above condition is that the State has not prioritized the need to establish a payroll system for its employees.

As a result, the State does not have a system in place to ensure that pay levels and related actions for State employees are properly documented and authorized.

We recommend the Governor to render the payroll system the priority level necessary to establish and implement the system. The payroll system is critical to ensure all personnel actions (i.e. pay increments) are properly documented and authorized. The State should utilize and maintain personnel action files and forms for State employees, including part time employees who are hired under a special contract.

**SSG's Response:** *I concur with your finding Number 3 regarding the state's Payroll System. The state has done some filings on the personnel's records but they are not well organized yet. However, the Administration under my office is currently working on this matter. The Legislative branch has passed a law, SSPL 6-13-R1, which I signed into law that requires the Executive Branch within 90 days to have all employees' records in file and in a safe place.*

### **Corrective Plan of Action**

- *The state has passed a law to require the executive branch within 90 days to have all state employees' records filed and kept in a safe place.*
- *The Governor will appoint his commission members to review the state's employment system and create policies on the state's payroll system.*
- *The state staffs are currently compiling and creating files for all state employees, full and part time, including those hired under a special contract. Such files would include at a minimum such documents as signed applications, personnel action forms, and other essential forms to document and support personnel action, for good record keeping.*

**OPA's Comments:** The Office of the Public Auditor will monitor and follow up on the corrective action to ensure their implementation, including the establishment of personnel policies and procedures.

### **Finding No. 4: Purchase of State Boat**

Procurements executed through contractual agreements should adhere to the terms and conditions of the agreement and documentation pertaining to the procurement process should be maintained to protect the rights and obligations of the State.

The State received the sum of \$140,000 from the Olbill Era Kululau (OEK) during the fiscal year 1999 under RPPL No. 5-18 to purchase a new State Boat. Upon completing the bid solicitation process for the State boat, the State awarded the contract to a Japanese firm whereupon the parties entered into a purchase/sell agreement worth \$140,000. Based on supporting documents, the State paid \$120,000 but failed to substantiate the payment of the remaining \$20,000. Furthermore, there was no evidence to show that the purchase agreement was amended to reduce the purchase price of the boat. Nonetheless, State officials claim that the State paid the full purchase price of the boat (\$140,000). Moreover, Sonsorol State failed to adhere to the terms of the agreement by failing to process payments via telegraphic remittance and instead used a courier to hand carry one of the payments (\$40,000) to Japan. In addition, the State processed payments through Bank of Hawaii instead of Bank of Guam as stipulated in the agreement.

It appears the State entered into an agreement without carefully considering the payment arrangements to ensure their practicality and fulfillment; thus, the State employed alternative methods to remit payments, which did not comply with the terms of the agreement. In addition, the State failed to obtain supporting documents (invoices/receipts) to substantiate the purchase price of the boat.

As a result, the State cannot substantiate the recorded cost of the boat in its financial records. In addition, the State may have incurred additional costs by using a courier instead of telegraphic remittance to tender payments for the boat.

We recommend that when major procurements are executed via contractual agreements the state carefully consider the terms and conditions of the agreement to ensure their practicality and the ability of the State to fulfill such terms and conditions. In addition, in the procurement of assets, the State should ensure that supporting documents (invoices/receipts) are obtained and maintained to support the recorded cost of assets in the State's financial records.

**SSG's Response:** *After reviewing your description on finding no. 4, we went through all our files and searched for documents. Unfortunately, this issue was the responsibility of the prior administrations and also it has been almost 10 years since the purchase date of the said vessel. In addition to that the former Governor at that time, the late Kuterbis Kutermalei, had passed away and I cannot use him as a source of information regarding this finding.*

*However, on the basis of my treasurer's statement and my personal knowledge since I was working on that vessel at that time I will try to answer some of the issues raised to the best of our knowledge.*

- *The \$20,000 was used to repair the state boat since at the time we got the boat to Koror, the Office of Transportation did a Registration Survey on the boat and found out that the boat was not seaworthy to carry passengers and cargos on the open ocean. As a result, the Governor refused to make the final payment to the owner in Japan and informed him that he will use the fund to repair the boat. We have been trying to locate some of the communication documents but have not been able locate them. We have moved our office from the Cause Way Apartments to AM/PM Building in Meyuns and our staff may have misplaced some of our files. We ask that we submit our report at this time, try to search for the files, and if we come across some of the missing files, we will submit copies to your office right away.*

*With regards to the payment process in compliance with the terms of the contract, I cannot recommend any justification since it is clear that it is a mismanagement decision to make amendment to the terms of the contract without proper documentation. For that I concur with the findings and, since the events surrounding the purchase of these vessels occurred prior to my administration, I cannot offer any explanation or justifications for the actions or taken or not taken.*

### **Corrective Plan of Action**

- *The state will and must obtain and maintain good records of and supporting documents in the state's financial records, particularly as such relate to the purchase of goods and services.*
- *The state will and is currently following the applicable procurement procedures to ensure that the terms and conditions of its contracts and agreements are met.*
- *The state is already following the recommendation by the auditor regarding major procurements. The state will continue to ensure that major procurements are executed via written contractual agreements and that the State will carefully consider the terms and conditions of the agreements to ensure their practicality and the ability of the State to fulfill such terms and conditions. In addition, the State will ensure, in the procurement of assets, that supporting documents (invoices/receipts) are obtained and maintained in the appropriate files to support the recorded cost of assets in the State's financial records.*

### **Finding No. 5: Sale of State Boats**

Major acquisitions of State capital assets that require substantial up-front outlay of funds require careful evaluation and analysis to ensure the quality and durability of the product and that the investment serves and benefits the State and its citizens for a reasonable time period. In addition, when acquiring such assets, negotiations should include the provision (by vendor) of a scheduled maintenance plan to ensure that the asset, once in operation, follows the scheduled maintenance plan to extend its useful life. Moreover, any agreement associated with acquisition of a major capital asset should be reviewed by a legal expert to ensure that adequate protection are contained in the agreement to protect the State's investment.

During the period of the audit we found that Sonoma State purchased two (2) used passenger/cargo boats; namely the Southern Cross for \$100,000 in 1995 and the Santissima for \$140,000 in 1999. In 1999 the State spent \$13,856 to repair the Southern Cross and \$51,527 in 2000 to repair the Santissima. At some time before August 1, 2001, the State made a public offering for the sale of the two State boats with minimum bids as follows: Southern Cross: \$80,000 and Santissima: \$100,000. With only one bidder showing interest, the State sold both boats for the price of \$1,500 on October 2002. However, for reasons we have not been able to obtain an adequate explanation, on September 16, 2001, the successful offeror (buyer) had initially submitted a bid for \$10,000 and a bid deposit of \$1,000. However, on October 21, 2002 the State and the buyer entered into a "Boat Sale Agreement" whereby the parties agreed to a purchase price of \$1,500 for both boats.

It appears the State did not have the expertise to properly inspect the seaworthiness, structural integrity and durability of the boat before purchasing the boats. In addition, the State did not request from the seller a scheduled maintenance plan for the boat or obtain training for its

employees for the repair and maintenance of the boats. Moreover, the State did not use the services of a legal expert to review the purchase agreement for the State boats to ensure that the State's investment is adequately protected.

As a result, the State invested significant sums of money in the two boats, which required constant repair and maintenance shortly after their purchase. In addition, it would appear, especially for the Santissima, that the State made an unwise investment as it purchased the boat for a \$140,000, spent \$51,527 on repairs and sold the boat for less than \$1,500 within 3 years after purchasing the boat.

We recommend that in the acquisition of capital assets that require substantial up-front outlay of funds, the State use consultants (subject-matter experts) to inspect and advise the State of the quality and performance aspect of the product before purchase. In addition, for major asset acquisitions, State officials should require the vendor to provide a scheduled maintenance plan for the asset or provide relevant training to State employees to ensure that the asset is properly maintained and repaired to enhance its useful life and operation. Moreover, the State should consider using a legal expert to review any purchase agreements to ensure the State's investment is adequately protected. Finally, we recommend the Office of the Attorney General or the Special Prosecutor to further investigate the above procurements and sale of the State boats and take corrective action for any conduct determined to be in violation of State and National laws and regulations.

**SSG's Response:** *According to the descriptions for the findings on Sale of State Boats, I agree to the point that it was a loss to the state's Capital Asset. I also agree that the state wasted money on all the boats that it purchased. However, I still believe that these losses could be avoided if the National Government considers the State's need for transportation as the number one priority and assist the State in meeting such need.*

*As for the sale of the state boat, I interviewed former Governor Laura Ierago and I agreed with her justification for her decision to sell the boat for \$1,500.00. I was told that she advertised the sale of the boat through bidding process three times, and there was no one interested to buy the boat except the person who bought it for \$1,500.00. While awaiting the sale process, the State continued to expend funds to pay for labor to watch the boat, pay for fuel for the boat's generator to light the boat at night, and other expenses to keep the boat floating at the anchorage area in Malakal Port.*

*Therefore, the former governor made a wise decision to get rid of the boats before it sank or even spilled oil at the port that would have cost the State thousands of dollars in penalties. For these reasons, it made sense for former Governor Ierago to have decided to sell the boat for \$1,500, however small that sum may seem.*

### **Corrective Plan of Action**

- *The State has just completed a proposal for a new boat for both state of Sonsorol and Hatohobei and submitted it to the office of the President. It would be the National Government that will do all the process of getting a boat for both of the states.*
- *The leadership of Sonsorol and Hatohobei State are in the process of drafting a plan on the operation of the boat, but they are still waiting for the approval of the proposal from the Office of the President.*

**The State agrees with all of the recommendations made by the auditor with respect to this finding and will implement the procedures outlined or adopt them as part of its policies for major acquisition of State capital assets that require substantial up-front outlay of funds.**

### **Finding No. 6: Boat Charter**

Procurements should be supported by adequate supporting documentation to substantiate the quality and quantity of goods and services procured and received.

During the audit we found that the State paid Peleliu State \$1,270.00 to charter its Boat to and from Sonsorol. In addition, the State purchased \$2,730.00 worth of fuel for the boat from Shell Company for the trip. There was no written agreement stipulating the above arrangement.

We were unable to determine why the State did not require the above arrangement to be put into a written agreement.

As a result, we were unable to verify the value of the goods and services received to the amount paid.

We recommend that future arrangements involving the procurement of goods and services of a similar nature be put into a written agreement to better protect the interest of the State and to substantiate the value of goods and services procured with State funds.

**SSG's Response:** *I concur with finding No. 6 (Boat Charter) and the recommendations of the auditor for correcting the problems noted.*

### **Corrective Plan of Action**

- *I will immediately implement the recommendations of the auditor regarding this particular finding. I don't expect any further problem to arise in the future.*

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

Bank reconciliations should be performed on a monthly basis to ensure: 1) all transactions (cash receipts and disbursements) affecting the account have been recorded, 2) the accuracy of recorded transactions, 3) errors or irregularities are timely identified and corrected, and 4) the cash balance per the State's books agrees to the balance per bank.

During the audit we found certain checks that were recorded as void, however, the cancelled check (check that has cleared the bank) showed otherwise. We also found checks where the amount of the check differed from the amount recorded in the book. In addition, we found that State funds were mistakenly deposited to an individual's personal account, which was subsequently returned by the individual to the State.

Management is not properly overseeing the bank reconciliation functions to ensure that they are timely performed.

As a result, expenditures were underreported by \$1,221 and errors and other irregularities can occur without timely detection by the State.

We recommend the State reconcile its bank accounts on a monthly basis. Bank reconciliation is an essential component of the State's cash management system to ensure: 1) all transactions (cash receipts and disbursements) affecting the account have been recorded, 2) the accuracy of recorded transactions, 3) errors or irregularities are timely identified and corrected, and 4) the cash balance per the State's books agrees to the balance per bank.

**SSG's Response:** *Our treasurer is currently using Quick Books Accounting Software to keep account records of state funding operation, and I have instructed her to reconcile all bank statements and the expenditures that the State is making. However, the treasurer said that she needs the help of one of an independent expert to set up her books and ensure that the set up meets with your office's requirements. Therefore, we will start reconciling our bank statements as soon as we have an expert set our books and ready to begin reconciling.*

### **Corrective Plan of Action**

- *We will start reconciling our bank statements as soon as our books are set.*
- *I have instructed my treasurer to work with the auditor and try to reconcile our bank statements between 2004 to the present and try to find and correct the problem she had while reconciling back wards to 1998.*
- *Once our State books are properly set up and the bank statements are reconciled we will reconcile the State's bank accounts on a monthly basis.*

### **Finding No. 8: Agreement to Deliver Vessel**

Contracts for the provision of services should be executed before the delivery of services to ensure that all deliverables, rights and obligations of the parties are stipulated in the contract. More importantly, the contract has to be certified as to the availability of funds to pay for the relevant services.

During the audit we found that the State had entered into a contract with a private individual for the piloting and delivery of a State boat from Japan to Palau after the services had been rendered. In addition, the State had paid the air fare and per diem for the captain to Japan, although such arrangements were not stipulated in the agreement.

We were unable to determine why the State did not execute the contract prior to the provision of services. In addition, in its haste to process and execute the contract, the State may have overlooked to include in the contract the arrangement to provide for the air fare and per diem for the captain to Japan.

As a result, services were rendered prior to the execution of the contract and, more importantly, before certification of availability of funds to pay for the services.

We recommend that contracts for the provision of services be executed prior to the delivery of services. More importantly, contracts should be certified as to the availability of funds to pay for services before the services are rendered.

**SSG's Response:** *I have reviewed finding No. 8 and I agree with the finding. I found out that the private individual is from the state of Yap and the state paid his air fare from Yap to Japan and delivered the boat to Palau without having him sign the contract. As a result, after the boat arrived Palau, the state then executed the contract and I concur that it was for the State had decided on such course of action.*

### **Corrective Plan of Action**

- *I have reviewed the procurement and special services laws and the State has no choice but to follow them.*
- *I will be visiting the Public Auditor to discuss some issues that I am not very clear with so that the State will not encounter those difficulties in the future.*
- *I am working on creating a commission to be my Administrative Committee to assist me in creating policies for the State to follow in order to improve the operation of the State in meeting the needs of the citizens of Sonsorol State while following good management practices.*

- *The State will implement and follow the recommendations of the auditor regarding finding number 8.*

### **Finding 9: Audit of State Budget**

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...”

During the audit we found that the most recent audit of Sonora State was conducted for fiscal year 1998.

We were unable to determine why the State Legislature did not request an independent auditor to conduct an audit of the State.

As a result, the State is not in compliance with Article XII, Section 12 of its Constitution.

We recommend the State Legislature obtain the services of an independent auditor to audit the State at least once every four years in accordance with Article XII, Section 12, of the State Constitution.

**SSG’s Response:** *I concur that the State never follows the constitution to request for audit of the State at least once every 4 years. I was told by the leaders of the state legislature that due to limited funding, they were not able to allocate funds to request for a private or independent auditor.*

### **Corrective Plan of Action**

- *I will introduce a legislation to require a need to audit the State prior to the end of an administration’s term in order to ensure that the next leadership can operate the state’s services without the problems of prior administrations.*

*The law will also require the chief executive officer to present a brief report through Gubernatorial Address and reports on the progress of the Administration’s Accomplishments and the pending projects and obligations to ensure smooth transition of Administration’s Leadership.*

- **I will implement the recommendation regarding this finding.**

**Finding No. 10: Questioned Cost**

A sound system of internal control requires that expenditures be supported by adequate documentation (invoices, contracts, travel documents, competitive bidding, etc.) to justify the propriety of the expenditures.

We found the following disbursements were made without adequate supporting documentation:

<b>Date</b>	<b>Check No.</b>	<b>Amount</b>	<b>Reason</b>
01/28/1999	1385	\$ 2,000	No receipt and not in the contract
01/28/1999	1387	1,408	No supporting documents
02/01/1999	1392	1,168	No supporting documents
02/05/1999	1396	4,309	No receipt and no appropriation
02/12/1999	1433	730	No invoice
02/23/1999	1487	1,200	No invoice and receipt
03/03/1999	1474	494	State was renting a space/no appropriation
03/18/1999	1500	4,344	No ticket copies in the file
04/02/1999	1556	661	Crew to Japan received per-diem
04/04/1999	1565	1,500	No invoice/payment was made before the initiation of the contract
06/23/1999	1788	4,000	No invoice and receipt
09/16/1999	2021	217	Payment is more than charges
10/13/1999	2110	3,000	No invoice and receipt
11/16/1999	2187	1,000	No invoice and receipt
12/13/1999	2254	2,100	No budget authorization
04/13/2000	2578	1,863	No invoice and receipt
08/29/2000	2822	2,000	Invoice is per-forma and not from the vendor
03/22/2001	3478	2,400	No invoice and receipt
05/17/2001	3607	535	Invoice is per-forma and account does not exist
09/18/2001	3919	500	No files and no check copy to support expenditure
07/12/2002	4551	1,456	No files and no check copy to support expenditure
07/29/2002	4603	3,000	No invoice and no receipt
12/16/2002	4937	3,500	No invoice and receipt
01/28/2003	5031	3,000	No invoice and receipt
03/12/2003	5148	1,423	No ticket copy in the file and no voucher
03/13/2003	5149	560	No ticket copy in the file and no voucher
03/18/2003	5153	5,000	No invoice, no receipt and no bidding
03/20/2003	5178	2,000	No invoice and no receipt
08/28/2003	5547	1,690	No invoice and no receipt
12/04/2003	5813	99	Account was over expensed by the amount
03/26/2004	6103	5,000	No bidding
07/02/2004	6355	4,500	No invoice and no receipt
09/17/2004	6566	2,700	No invoice and no receipt
10/21/2004	6650	3,000	No invoice and no receipt

11/08/2004	6692	1,000	No invoice and no receipt
02/15/2005	6954	4,500	No invoice and no receipt
04/14/2005	7121	2,588	No invoice and no receipt
08/17/2005	7455	7,500	No invoice and no receipt
	<b>Total</b>	<b>\$ 87,945</b>	

Management did not ensure that all disbursements are properly supported.

As a result, \$87,945 of expenditures incurred in fiscal years 1999 through 2005 are questioned due to insufficient or lack of supporting documentation.

We recommend the Governor to strictly enforce the controls requiring the expenditure of State funds to be supported by adequate supporting documentation (invoices, receipts, contracts, etc.) to account for and justify the official nature of expenditures. In addition, supporting documents are essential evidence to support the recording and classification of expenditures in the State's accounting system pursuant to the State's appropriation laws. Finally, we recommend the Governor locate and provide to the Office of the Public Auditor supporting documents for each of the above questioned costs for its review and resolution.

**SSG's Response:** *I have enclosed supporting documents for the checks listed in the Questioned Costs findings. However, missing records from 1999 to 2003 were not under my administration's operation. I have looked through our files and am able to locate some of the documents but could not locate all relevant documents. Despite this problem, I will just turn in my report with the documents that my office staffs were able to find.*

*With regards to missing documents listed in the Questioned Cost under my administration, I have provided the documents and justification documents as attachments to this report. However, please note that some of the missing checks that I did not provide the invoices and receipts for are probably in one of the missing files that we have been trying to locate after we moved our office from the Meyuns Causeway Apartment. I tried to obtain copies of the invoices and receipts from the vendor which is Hatohobei State, but the Governor of the said state informed me that all his receipt books and invoices are with the office of the Public Auditor for Auditing of their State. Therefore, I am not able to provide them.*

### **Corrective Plan of Action**

- *We will continue to look for missing documents while we are setting up our filing systems and if we find the missing documents, we will provide copies to your office right away.*
- *We will update our documentation records through annual inventory process to ensure that all checks are complete with required supporting documents before filing.*

**Sonsorol State Government  
Performance Audit  
FY 1999 through FY 2005**

**Status of Recommendations**

<b>Recommendations</b>	<b>Agency to Act</b>	<b>Status</b>	<b>Agency Response/ Action Required</b>
1. We recommend the Governor expend earmarked funds in accordance with the purpose for which the funds are appropriated. In addition, we recommend the Office of the Attorney General or the Office of the Special Prosecutor to further investigate the above expenditures and take appropriate action to recover any funds that may have been illegally expended.	<b>SSG</b>	<b>Closed</b>	None
2. We recommend the Governor withhold Pension Plan contributions from State employees' pay on a bi-weekly basis and remit the contributions to the Pension Plan on a timely basis. In addition, we recommend the Governor consult with his legal counsel regarding the potential legal issues surrounding the agreement whereby the State agreed to pay State employees past pension contributions. Moreover, if the State has already paid the past contributions, then the State should require each employee to reimburse the State for the amount of contribution paid on behalf of the employee.	<b>SSG</b>	<b>Open</b>	Communication from Governor regarding the outcome of discussions with his legal counsel. Plan of action based on the advice of legal counsel regarding reimbursement from employees for employees share of contributions paid by the State.
3. We recommend the Governor to render the payroll system the priority level necessary to establish and implement the system. The payroll system is critical to ensure all personnel actions (i.e. pay increments) are	<b>SSG</b>	<b>Open</b>	Timeframe for creation of Commission, duties and responsibilities of the Commission, and promulgation of payroll policies and procedures.

<p>properly documented and authorized. The State should utilize and maintain personnel action files and forms for State employees, including part time employees who are hired under a special contract.</p>			
<p>4. We recommend that when major procurements are executed via contractual agreements the state carefully consider the terms and conditions of the agreement to ensure their practicality and the ability of the State to fulfill such terms and conditions. In addition, in the procurement of assets, the State should ensure that supporting documents (invoices/receipts) are obtained and maintained to support the recorded cost of assets in the State's financial records.</p>	<p><b>SSG</b></p>	<p><b>Closed</b></p>	<p>None</p>
<p>5. We recommend that in the acquisition of capital assets that require substantial up-front outlay of funds, the State use consultants (subject-matter experts) to inspect and advise the State of the quality and performance aspect of the product before purchase. In addition, for major asset acquisitions, State officials should require the vendor to provide a scheduled maintenance plan for the asset or provide relevant training to State employees to ensure that the asset is properly maintained and repaired to enhance its useful life and operation. Moreover, the State should consider using a legal expert to review any purchase agreements to ensure the State's investment is adequately protected. Finally, we recommend the Office of the Attorney General or the Special Prosecutor to further investigate the above</p>	<p><b>SSG</b></p>	<p><b>Closed</b></p>	<p>None</p>

procurements and sale of the State boats and take corrective action for any conduct determined to be in violation of State and National laws and regulations.			
6. We recommend that future arrangements involving the procurement of goods and services of a similar nature be put into a written agreement to better protect the interest of the State and to substantiate the value of goods and services procured with State funds.	<b>SSG</b>	<b>Closed</b>	None
7. We recommend the State reconcile its bank accounts on a monthly basis. Bank reconciliation is an essential component of the State's cash management system to ensure: 1) all transactions (cash receipts and disbursements) affecting the account have been recorded, 2) the accuracy of recorded transactions, 3) errors or irregularities are timely identified and corrected, and 4) the cash balance per the State's books agrees to the balance per bank.	<b>SSG</b>	<b>Open</b>	Provide timeframe for commencement of bank reconciliation, the staff responsible for the task.
8. We recommend that contracts for the provision of services be executed prior to the delivery of services. More importantly, contracts should be certified as to the availability of funds to pay for services before the services are rendered.	<b>SSG</b>	<b>Open</b>	Provide timeframe for establishment of committee, duties and responsibilities of the committee.
9. We recommend the State Legislature obtain the services of an independent auditor to audit the State at least once every four years in accordance with Article XII, Section 12, of the State Constitution.	<b>SSG</b>	<b>Open</b>	Provide timeframe for introduction of bill requiring audit during the transition period (outgoing governor and incoming governor)

<p>10. We recommend the Governor to strictly enforce the controls requiring the expenditure of State funds to be supported by adequate supporting documentation (invoices, receipts, contracts, etc.) to account for and justify the official nature of expenditures. In addition, supporting documents are essential evidence to support the recording and classification of expenditures in the State's accounting system pursuant to the State's appropriation laws. Finally, we recommend the Governor locate and provide to the Office of the Public Auditor supporting documents for each of the above questioned costs for its review and resolution.</p>	<p><b>SSG</b></p>	<p><b>Open</b></p>	<p>OPA will continue to review supporting documents as they are provided by the State and revise schedule of Questioned costs as appropriate.</p>
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# SONSOROL STATE GOVERNMENT

Office of the Governor

P.O. Box 1077

Koror, Republic of Palau 96940

Ph. No. 488-1237 Fax No. 488-5501

Email: [sonsorol@palaunet.com](mailto:sonsorol@palaunet.com)

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August 25, 2007

Mr. Satrunino Tewid  
Acting Public Auditor,  
Office of the Public Auditor  
Ground Floor, VIP Building  
Koror, Republic of Palau 96940

<b>Office of the Public Auditor Received</b>	
Date <u>9/24/07</u>	Time <u>10:30 am</u>
Received By <u>mmw.</u>	
No. OPA <u>07-111</u>	

RE- Reply To Your Audit Findings For Sonsorol State Government

Dear Mr. Tewid:

Let me begin by thanking you and your staffs for the hard work you've done to audit the financial operation of the State of Sonsorol. It is my great pleasure to respond to all your findings in the draft audit report. Listed below are the responses to each finding and the corrective action plans to remedy the problems noted in the draft audit report.

## SONSOROL STATE AUDIT REPORT YEAR ENDING SEPTEMBER 30, 2005

### RESPONSE TO AUDITOR'S FINDINGS:

#### Finding No. 1: Earmarked CIP Funds

First, I concur that funds earmarked by the (OEK) for specific CIP should be expended for the purposes for which the funds were earmarked. However, in regards to Finding No. 1: Earmarked CIP Funds, you said that funds were spent for materials for renovation of the state office. After doing some research on this as this incident is the responsibility of the prior Administrations, it I found out that the earmarked CIP was divided in half as

follows: Seven thousand, five hundred dollars,(\$7,500.00) was allocated for the State liaison Office in Echang Koror, and the other half was allocated for the State office on Sonsorol Island. Note that under RPPL 4-40, on pg. 29 sub. Section 4(p),Sonsorol State; the language simply spells that \$15,000.00 is earmarked for repair of Sonsorol State Office. Also, under SSPL No. 4-11R-1, Funds in the amount of \$7,500.00 was appropriated for the purpose of repairing the State Office on Sonsorol Island. This source of funding comes from the National Government earmarked under RPPL 4-40. Therefore, the funds expended for purchasing materials after the date the Liaison Office for Sonsorol State in Koror got burned down was used for repair of the State Office in Sonsorol Island; the capital of Sonsorol State.

### **Corrective Plan of Action:**

The State has been disciplined by having imposed upon it the National Government Penalties and Interests that are imposed on state debts that affect our budget and state operations. As the incumbent Governor of Sonsorol State, I have operated within and according to the budget I have been appropriated and tried my very best to use my budget means to pay all the state obligations to the National Government so that we don't encounter future debts with the National Government. Some examples are:

- The state has appropriated \$15,000 from its local revenues to pay its overdue debts, including penalties and interests owed to the Social Security Administration.
- The state is currently paying its ROP taxes, pension plan contributions, and Social Security contributions on a timely basis.

### **Finding No. 2: Employee Contributions for Service Pension Plan**

With respect to Finding No. 2, I have read and understood the finding and the policies pertaining to Employees' contributions to the Republic's Pension Plan. I totally agree with your findings, even though I was not the Governor at the time these issues occurred. However, I have researched the issues and came to my findings that it is true that most of the documents regarding the refund of pension contributions by Sonsorol state employees were refunded to the employees. Moreover, according to my findings, I found out that between 1987 to 1995, the office of Pension Plan was not clear on whether state governments were eligible for pension plan membership or not. In fact, most of the state governments including Koror state experienced the same confusion experienced by Sonsorol state.

As a result, the leadership of Sonsorol State including the state legislature did approve a legislation to authorize the disbursement of funds from the state treasury to refund the state employees for their share that was deducted from the pay checks. Attached is the copy of the state public law that authorizes the disbursement of such funds.

After 1995, the state was cleared by the office of Pension Plan about their employees' contributions. Therefore, in the year 1999 the state started paying their employees' contribution to Pension Plan to this date.

In regards to the former Governor's decision to get into agreement with the office of Pension Plan to pay off their debt with the Pension Plan, I would say that it is the decision of the Administration under their leadership. I do believe that it is the best way to resolve the problem. The Agreement will end next year, and after all payments for our debt with the Pension Plan, we will require the state employees to pay the state their share to recover the expenses that the state expended for the employees share to the Pension Plan.

#### **Corrective Plan of Action:**

- Every year the state is paying \$14,750 for the payment of its obligation with the Pension Plan Office as a payment for the contract agreement signed between Sonorol State Government and the office of Pension plan for the unpaid obligation between 1987 through 1999.
- The State is now currently paying its employer/ employee contribution to Pension Plan in a timely manner.
- The state is currently compiling all the records of state employees who have contribution share with Pension Plan between the years 1987 and 1999 to require them to pay back the state for their share.
- The state will execute a policy that if the employee doesn't pay the state for their obligation, the state may not release their documents required for their retirement fund.

#### **Finding No. 3: Payroll System**

I concur with your finding Number 3 regarding the state's Payroll System. The state has done some filings on the personnel's records but they are not well organized yet. However, the Administration under my office is currently working on this matter. The Legislative branch has passed a law, SSPL 6- 13-R1, which I signed into law that requires the Executive Branch within 90 days to have all employees' records in file and in a safe place.

#### **Corrective Plan of Action**

- The state has passed a law to require the executive branch within 90 days to have all state employees' records filed and kept in a safe place.
- The Governor will appoint his commission members to review the state's employment system and create policies on the state's payroll system.

- The state staffs are currently compiling and creating files for all state employees, full and part time, including those hired under a special contract. Such files would include at a minimum such documents as signed applications, personnel action forms, and other essential forms to document and support personnel action, for good record keeping.

**Finding No. 4: Purchase of State Boat**

After reviewing your description on finding no. 4, we went through all our files and searched for documents. Unfortunately, this issue was the responsibility of the prior administrations and also it has been almost 10 years since the purchase date of the said vessel. In addition to that the former Governor at that time, the late Kuterbis Kutermalei, had passed away and I cannot use him as a source of information regarding this finding.

However, on the basis of my treasurer’s statement and my personal knowledge since I was working on that vessel at that time I will try to answer some of the issues raised to the best of our knowledge.

- The \$20,000 was used to repair the state boat since at the time we got the boat to Koror, the Office of Transportation did a Registration Survey on the boat and found out that the boat was not seaworthy to carry passengers and cargos on the open ocean. As a result, the Governor refused to make the final payment to the owner in Japan and informed him that he will use the fund to repair the boat. We have been trying to locate some of the communication documents but have not been able locate them. We have moved our office from the Cause Way Apartments to AM/PM Building in Meyuns and our staff may have misplaced some of our files. We ask that we submit our report at this time, try to search for the files, and if we come across some of the missing files, we will submit copies to your office right away.

With regards to the payment process in compliance with the terms of the contract, I cannot recommend any justification since it is clear that it is a mismanagement decision to make amendment to the terms of the contract without proper documentation. For that I concur with the findings and, since the events surrounding the purchase of these vessels occurred prior to my administration, I cannot offer any explanation or justifications for the actions or taken or not taken.

**Corrective Plan of Action**

- The state will and must obtain and maintain good records of and supporting documents in the state’s financial records, particularly as such relate to the purchase of goods and services.
- The state will and is currently following the applicable procurement procedures to ensure that the terms and conditions of its contracts and agreements are met.

- The State is already following the recommendation by the auditor regarding major procurements. The State will continue to ensure that major procurements are executed via written contractual agreements and that the State will carefully consider the terms and conditions of the agreements to ensure their practicality and the ability of the State to fulfill such terms and conditions. In addition, the State will ensure, in the procurement of assets, that supporting documents (invoices/receipts) are obtained and maintained in the appropriate files to support the recorded cost of assets in the State's financial records.

### **Finding No. 5: Sale of State Boats**

According to the descriptions for the findings on Sale of State Boats, I agree to the point that it was a loss to the state's Capital Asset. I also agree that the state wasted money on all the boats that it purchased. However, I still believe that these losses could be avoided if the National Government considers the State's need for transportation as the number one priority and assist the State in meeting such need.

As for the sale of the state boat, I interviewed former Governor Laura Ierago and I agreed with her justification for her decision to sell the boat for \$1,500.00. I was told that she advertised the sale of the boat through bidding process three times, and there was no one interested to buy the boat except the person who bought it for \$1,500.00. While awaiting the sale process, the State continued to expend funds to pay for labor to watch the boat, pay for fuel for the boat's generator to light the boat at night, and other expenses to keep the boat floating at the anchorage area in Malakal Port.

Therefore, the former governor made a wise decision to get rid of the boats before it sank or even spilled oil at the port that would have cost the State thousands of dollars in penalties. For these reasons, it made sense for former Governor Ierago to have decided to sell the boat for \$1,500.00, however small that sum may seem.

### **Corrective Plan of Action**

- The State has just completed a proposal for a new boat for both state of Sonsorol and Hatohobei and submitted it to the office of the President. It would be the National Government that will do all the process of getting a boat for both of the states.
- The leadership of Sonsorol State and Hatohobei State are in the process of drafting a plan on the operation of the boat, but they are still waiting for the approval of the proposal from the Office of the President.

**The State agrees with all of the recommendations made by the auditor with respect to this finding and will implement the procedures outlined or adopt them as part of its policies for major acquisition of State capital assets that require substantial up-front outlay of funds.**

### **Finding No. 6: Boat Charter**

I concur with finding No. 6 (Boat Charter) and the recommendations of the auditor for correcting the problems noted..

#### **Corrective Plan of Action**

- I will immediately implement the recommendations of the auditor regarding this particular finding. I don't expect any further problem to arise in the future.

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

Our treasurer is currently using Quick Books Accounting Software to keep account records of state funding operation, and. I have instructed her to reconcile all bank statements and the expenditures that the State is making. However, the treasurer said that she needs the help of one of an independent expert to set up her books and ensure that the set up meets with your office's requirements. Therefore, we will start reconciling our bank statements as soon as we have an expert set our books and ready to begin reconciling.

#### **Corrective Plan of Action**

- We will start reconciling our bank statements as soon as our books are set.
- I have instructed my treasurer to work with the auditor and try to reconcile our bank statements between 2004 to the present and try to find and correct the problem she had while reconciling back wards to 1998.
- Once our State books are properly set up and the bank statements are reconciled we will reconcile the State's bank accounts on a monthly basis.

### **Finding No.8: Agreement to Deliver Vessel**

I have reviewed finding No. 8 and I agree with the finding. I found out that the private individual is from the state of Yap and the state paid his air fare from Yap to Japan and delivered the boat to Palau without having him sign the contract. As a result, after the boat arrived Palau, the state then executed the contract and I concur that it was for the State had decided on such course of action.

#### **Corrective Plan of Action**

- I have reviewed the procurement and special services laws and the State has no choice but to follow them.
- I will be visiting the Public Auditor to discuss some issues that I am not very clear with so that the State will not encounter those difficulties in the future.
- I am working on creating a commission to be my Administrative Committee to assist me in creating policies for the State to follow in order to improve the operation of the State in meeting the needs of the citizens of Sonora State while following good management practices.
- The State will implement and follow the recommendations of the auditor regarding finding number 8.

### **Finding No. 9: Audit of State Budget**

I concur that the State never follows the constitution to request for audit of the State at least once every 4 years. I was told by the leaders of the state legislature that due to limited funding, they were not able to allocate funds to request for a private or independent auditor.

### **Corrective Plan of Action**

- I will introduce a legislation to require a need to audit the State prior to the end of an administration's leadership's term in order to ensure that the next leadership can operate the state's services without the problems of prior administrations.

The law will also require the chief executive officer to present a brief report through Gubernatorial Address and reports on the progress of the Administration's Accomplishments and the pending projects and obligations to ensure smooth transition of Administration's Leadership.

- **I will implement the recommendation regarding this finding,**

### **Finding No. 10: Questioned Cost**

I have enclosed supporting documents for the checks listed in the Questioned Cost findings. However, missing records from 1999 to 2003 were not under my administration's operation. I have looked through our files and am able to locate some of the documents but could not locate all relevant documents. Despite this problem, I will just turn in my report with the documents that my office staffs were able to find.

With regards to missing documents listed in the Questioned Cost under my administration, I have provided the documents and justification documents as attachments to this report. However, please note that some of the missing checks that I

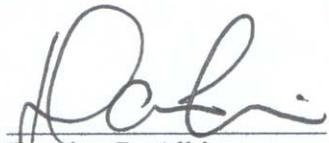
did not provide the invoices and receipts for are probably in one of the missing files that we have been trying to locate after we moved our office from the Meyuns Causeway Apartment. I tried to obtain copies of the invoices and receipts from the vendor which is Hatohebei State, but the Governor of the said state informed me that all his receipt books and invoices are with the office of the Public Auditor for Auditing of their State. Therefore, I am not able to provide them.

**Corrective Plan of Action**

- We will continue to look for missing documents while we are setting up our filing systems and if we find the missing documents, we will provide copies to your office right away
- We will update our documentation records through annual inventory process to ensure that all checks are complete with required supporting documents before filing.

Thank you and please don't hesitate to contact me if you have any questions.

Truly Yours,



Damian B. Albis  
Governor, Sonsorol State

Enclosures: Various documents

Cc: File