

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

**INDEPENDENT AUDITOR'S REPORT
AND
FINANCIAL STATEMENTS**

Years Ended September 30, 2007 and 2006

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

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SEPTEMBER 30, 2007 and 2006

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Palau District Housing Authority

I have audited the accompanying combined financial statements of Palau District Housing Authority (the Authority), a component unit of the Republic of Palau (ROP), as set forth in Section I of the foregoing Table of Contents, as of September 30, 2007 and 2006, and for the years then ended. These financial statements are the responsibility of the Authority's management. My responsibility is to express an opinion on these financial statements based on my audits.

I conducted my audits 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. Those standards require that I plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, I do not express such an opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audits provide a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Palau District Housing Authority as of September 30, 2007 and 2006, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, I have also issued my report dated November 30, 2007 on my consideration of Palau District Housing Authority's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts, grants and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of my audits.

The *Management's Discussion and Analysis* on pages 3 through 11 is not a required part of the basic financial statements but is supplementary information required by the *Governmental Accounting Standards Board*. I have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, I did not audit the information and express no opinion on it.

My audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards on page 38 is presented for purposes of additional analysis, as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. This supplementary information is the responsibility of the management of the Authority. Such information has been subjected to the auditing procedures applied in my audit of the basic financial statements and, in my opinion, is fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

J. Scott Magliari & Company
Koror, Republic of Palau
November 30, 2007

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

As management of the Palau District Housing Authority (the Authority), a component unit of the Republic of Palau, we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal year ended September 30, 2007. We encourage readers to consider the information presented here in conjunction with the Authority's financial statements, which begin on page 12.

Financial Highlights

- The assets of the Authority exceeded its liabilities at September 30, 2007 by \$2,618,396 (net assets).
- The Authority's cash and cash equivalents at September 30, 2007 was \$909,545 representing an increase of \$27,960 from September 30, 2006.
- The Authority had revenues of \$172,798 and expenses of \$122,303 for the year ended September 30, 2007.

Overview of the Financial Statements

The discussion and analysis is intended to serve as an introduction to the Authority's basic financial statements. The Authority's basic financial statements are comprised of two components: 1) authority-wide financial statements and 2) notes to the financial statements. This report also contains the schedule of expenditures of federal awards as supplementary information in addition to the basic financial statements themselves.

AUTHORITY-WIDE FINANCIAL STATEMENTS

The authority-wide financial statements are designed to provide readers with a broad overview of the Authority's finances, in a manner similar to a private-sector business.

The *Statement of Net Assets* presents information on all of the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

The *Statement of Revenues, Expenses and Changes in Net Assets* presents information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., depreciation and earned but unused vacation leave).

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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

Overview of the Financial Statements, Continued

AUTHORITY-WIDE FINANCIAL STATEMENTS, Continued

The *Statement of Cash Flows* provides information about the Authority's cash receipts and cash payments during the reporting period. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities.

The authority-wide financial statements report on the function of the Authority that is principally supported by intergovernmental revenues. The Authority's function is to develop and administer low-cost housing projects and to assist in correcting housing conditions endangering the health, safety, and welfare of the people residing in the Republic of Palau, which is funded primarily with grant revenue received from the U.S. Department of Housing and Urban Development.

The authority-wide financial statements can be found on pages 12 through 16 of this report.

NOTES TO THE FINANCIAL STATEMENTS

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the authority-wide financial statements. The notes to the financial statements can be found on pages 17 through 33 of this report.

SUPPLEMENTARY INFORMATION

The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-profit Organizations*. The schedule of expenditures of federal awards can be found on page 38 of this report.

FUND FINANCIAL STATEMENTS

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is now on Major Funds rather than fund types. The Authority consists of exclusively Enterprise Funds. Enterprise funds utilize the full accrual basis of accounting. The Enterprise method of accounting is similar to accounting utilized by the private sector accounting.

Many of the funds maintained by the Authority are required by the U.S. Department of Housing and Urban Development. Others are segregated to enhance accountability and control.

PALAU DISTRICT HOUSING AUTHORITY
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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

Authority-Wide Financial Analysis

Fiscal year 2007 is the fifth year of implementation of Governmental Accounting Standards Board (GASB) Statement No. 34. The new financial statement focuses on the Authority as a whole. The Authority financial statements (see pages 12 through 16) are designed to emulate corporate presentation models whereby all Authority activities are combined into one total. The focus of the Statement of Net Assets is designed to be similar to bottom line results for the Authority. This statement combines current financial resources (short-term spendable resources) with capital assets. The Statement of Revenues, Expenses, and Changes in Net Assets focuses on both the gross costs and the net costs of Authority activities which are supported mainly by appropriations from Palau National Congress (PNC) and by other revenues. This approach is intended to summarize and simplify the user's analysis of cost of Authority services to the public.

Financial Analysis of the Authority as a Whole
Net Assets
As of September 30, 2007, 2006, and 2005

	<u>2007</u>	<u>2006</u>	<u>2005</u>
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 909,545	\$ 881,585	\$ 995,289
Notes receivable, current portion	177,668	160,071	165,876
Accounts receivable	41,052	39,162	40,842
Interest receivable	<u>9,589</u>	<u>10,376</u>	<u>10,469</u>
Total current assets	<u>1,137,854</u>	<u>1,091,194</u>	<u>1,212,476</u>
Noncurrent assets:			
Notes receivable, net of current portion	1,511,893	1,466,077	1,230,552
Allowance for doubtful accounts	(85,000)	(85,000)	(85,000)
Capital assets, net	28,175	35,481	48,713
Other assets	<u>43,041</u>	<u>52,904</u>	<u>110,179</u>
Total noncurrent assets	<u>1,498,109</u>	<u>1,469,462</u>	<u>1,304,444</u>
TOTAL ASSETS	<u><u>\$ 2,635,963</u></u>	<u><u>\$ 2,560,656</u></u>	<u><u>\$ 2,516,920</u></u>

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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

Authority-Wide Financial Analysis, Continued

Financial Analysis of the Authority as a Whole
Net Assets
As of September 30, 2007, 2006, and 2005

	2007	2006	2005
LIABILITIES			
Current Liabilities:			
Accrued expenses	\$ 17,567	\$ 17,614	\$ 17,666
Total liabilities	17,567	17,614	17,666
NET ASSETS			
Invested in capital assets	28,175	35,481	48,713
Restricted	2,312,086	2,312,086	2,312,086
Unrestricted	278,135	195,475	138,455
Total net assets	2,618,396	2,543,042	2,499,254
TOTAL LIABILITIES AND NET ASSETS	\$ 2,635,963	\$ 2,560,656	\$ 2,516,920

This schedule is prepared from the Authority's Statement of Net Assets, which is presented on an accrual basis of accounting whereby liabilities and expenses are recorded when incurred, whether paid or not, and revenue is recorded when earned, whether received or not.

Total net assets as of FY 2007 increased to \$2.62 million from \$2.54 million in FY 2006. The increase is attributed to increase in notes receivable.

Noncurrent assets increased from \$1.47 million in FY 2006 to \$1.50 million in FY 2007. The increase is attributed to increase in notes receivable. A large portion of the notes receivable is from Home Rehabilitation Loan Program.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

Authority-Wide Financial Analysis, Continued

As noted earlier, net assets may serve over time as a useful indicator of an entity's financial position. In the case of the Authority, assets exceeded liabilities by \$2,618,396 as of September 30, 2007.

By far the largest portion of the Authority's net assets (88%) reflects its restricted net assets. Restricted net assets pertain to grants received from U.S. Department of Housing and Urban Development (HUD), contributions received from the Trust Territory of the Pacific Islands and from the Republic of Palau.

With prudent fund management, the Authority was able to increase its surplus from \$195,475 in FY 2006 to a surplus of \$278,135 in FY 2007.

Statement of Revenues, Expenses, and Changes in Net Assets

**Operating Revenues for the Year Ended
September 30, 2007**

Operating revenues:	
Republic of Palau appropriations	\$ 67,000
Interest on loans	61,479
Section 8 income	15,300
National treasury income	8,500
Federal contributions	4,050
Other	<u>16,469</u>
 Total operating revenues	 <u>\$ 172,798</u>

The schedule indicates total revenues realized by the Authority in FY 2007 of \$172,798. The largest portion of revenues (\$67,000 and \$8,500) was contributed by the Olbiil Era Kelulau (Palau National Congress). The U.S. Federal Government contributed \$4,050. The Authority's revenues are largely intergovernmental revenues received from cost reimbursement grants. The Authority draws down monies from the grants' awards for allowable program expenses, except for non-cash transactions, such as depreciation expense and changes in compensated absences. The Authority's intergovernmental revenues and charges for services were sufficient to cover all expenses incurred during the year.

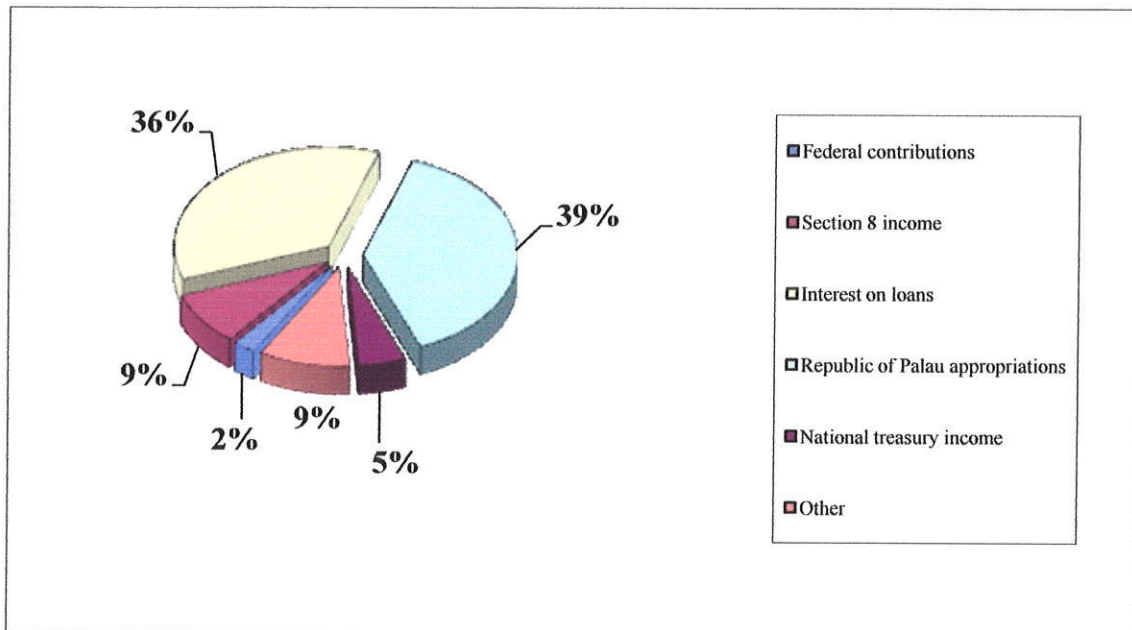
PALAU DISTRICT HOUSING AUTHORITY
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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

Authority-Wide Financial Analysis, Continued

The following chart exhibits the breakdown of revenues for Palau District Housing Authority in FY 2007.

Operating Revenues Breakdown



**Operating Expenses for the Year Ended
September 30, 2007**

Operating expenses:	
Salaries and wages	\$ 59,907
Rent expense	11,320
Depreciation	9,606
Professional fees	9,380
Travel	7,823
Employee benefits	5,748
Communication	2,925
Repairs and maintenance	2,666
Other	<u>12,928</u>
 Total expenses	 <u>\$ 122,303</u>

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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

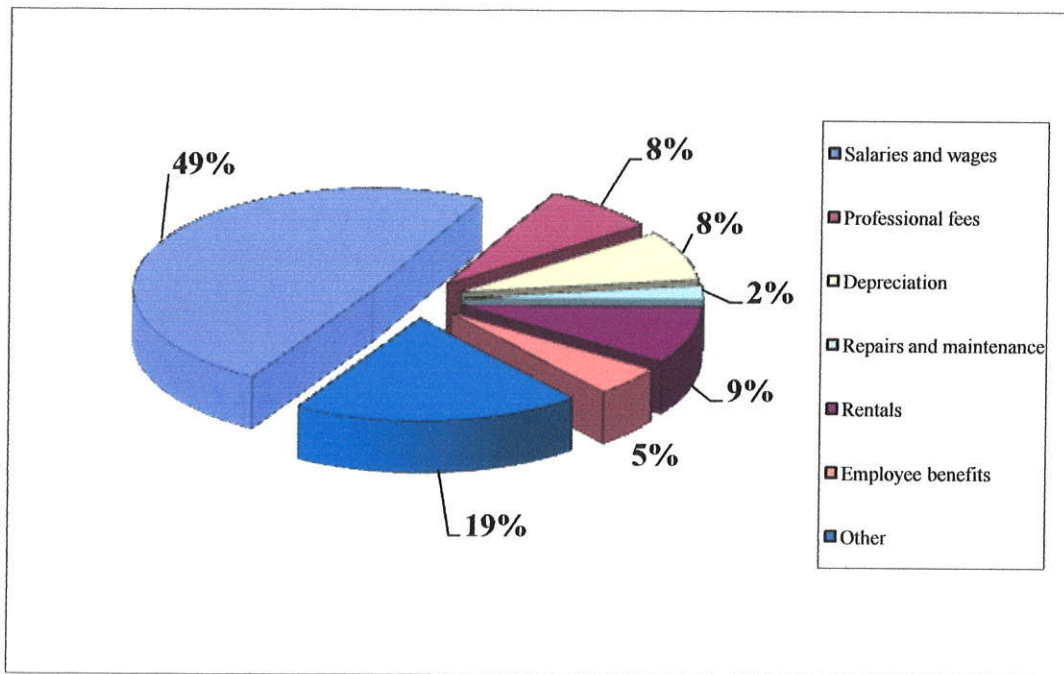
Authority-Wide Financial Analysis, Continued

Operating income	\$ 50,495
Non-operating revenues:	
Interest income	<u>24,859</u>
Change in net assets	<u>\$ 75,354</u>

The preceding schedule shows total operating expenses of \$122,303 in FY 2007. As indicated above, the Authority has surplus of \$75,354.

The biggest expenditure in FY 2007 was salaries and wages, which approximated \$60,000.

Expenses Breakdown
For Year Ended, September 30, 2007



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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

Authority-Wide Financial Analysis, Continued

CAPITAL ASSETS

As of September 30, 2007, the Authority's investment in capital assets for its business-type activities was \$28,175 (net of accumulated depreciation) as reflected in the following schedule:

	<u>(Thousands)</u>
Residential units	\$ 213
Furniture, fixtures and equipment	41
Vehicles	28
Accumulated depreciation	<u>(254)</u>
Total	<u>\$ 28</u>

Additional information on the Authority's capital assets can be found in Notes 1 and 5 of Combined Financial Statements on pages 24, 29 and 30 of this report.

Economic Factors and Next Year's Budget and Rates

The following factors were considered in preparing the Authority's budget for the 2008 fiscal year:

- An increase in the collections of loan payments. The increase will be due to additional loan disbursed.
- An increase in interest income, due to additional loan disbursed.
- Appropriation from the Palau National Government applicable to administrative and operation expenditures.
- Rental revenue derived from Section 8 rental housing units.
- Initial technical assistance grant from USDA.
- 2-year USDA grant for the implementation of the Mutual Self-Help Housing Program.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
September 30, 2007

Future Events that will Financially Impact the Authority

The Authority will continue its housing programs but will depend entirely on its limited revolving funds to fund and continue these programs.

The Section 8 public housing program is sustainable and the land lease issue is pending awaiting approval from Koror State Public Land Authority (KSPLA). Upon approval of the lease extension, the Authority plans to conduct major repairs and improvements to the six housing units.

The Palau District Housing Authority was awarded a Self-Help Technical Assistance Pre-Development Grant in the amount of \$10,000 in March 2007 to prepare a final application. Once the final application is approved, the initial grant funding will be provided to run the Self-Help Housing Program for a period of two years.

The initial pilot project will consist of twenty housing projects funded by USDA through the Mutual Self-Help Housing Program. The Authority will administer the program with the assistance and guidance from the state level.

The Authority was fortunate to receive a Housing Preservation Grant from USDA for fiscal year 2007 to supplement its Home Improvement and Repair Assistance Program. This funding together with the existing funding will help provide additional funds for fiscal year 2008 and beyond.

Contacting the Authority's Financial Management

The financial report is designed to provide a general overview of the Authority's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Executive Director, Palau District Housing Authority, PO Box 197, Koror, Republic of Palau, 96940, or call (680) 488-6207.

PALAU DISTRICT HOUSING AUTHORITY
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Combined Statements of Net Assets with Combining Information
September 30, 2007 and 2006

	Major Enterprise Funds				Total 2007	Total 2006
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
ASSETS						
Current assets:						
Cash and cash equivalents (Notes 1 and 2)	\$ 137,445	\$ 439,266	\$ 58,379	\$ 274,455	\$ 909,545	\$ 881,585
Notes receivable, current portion (Notes 1, 3 and 8)	-	162,631	10,357	4,680	177,668	160,071
Accounts receivable	24,255	-	-	16,797	41,052	39,162
Interest receivable	-	7,791	1,798	-	9,589	10,376
Due from (to) other fund (Note 4)	-	-	(25,000)	25,000	-	-
	161,700	609,688	45,534	320,932	1,137,854	1,091,194
Noncurrent assets:						
Notes receivable, net of current portion (Notes 1, 3 and 8)	-	1,373,336	80,197	58,360	1,511,893	1,466,077
Allowance for loan losses (Notes 1 and 3)	-	(78,000)	(1,500)	(5,500)	(85,000)	(85,000)
	-	1,295,336	78,697	52,860	1,426,893	1,381,077
Capital assets, net (Notes 1 and 5)	28,046	-	-	129	28,175	35,481
Other assets	-	43,041	-	-	43,041	52,904
	28,046	1,338,377	78,697	52,989	1,498,109	1,469,462
Total noncurrent assets	28,046	1,338,377	78,697	52,989	1,498,109	1,469,462
Total assets	\$ 189,746	\$ 1,948,065	\$ 124,231	\$ 373,921	\$ 2,635,963	\$ 2,560,656

The accompanying notes are an integral part of these financial statements.

PALAU DISTRICT HOUSING AUTHORITY
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Combined Statements of Net Assets with Combining Information, Continued
September 30, 2007 and 2006

	Major Enterprise Funds				Total 2007	Total 2006
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
LIABILITIES						
Current Liabilities:						
Accrued expenses	\$ 1,759	\$ -	\$ -	\$ 15,808	\$ 17,567	\$ 17,614
Total liabilities	1,759	-	-	15,808	17,567	17,614
NET ASSETS						
Invested in capital assets (Note 1)	28,046	-	-	129	28,175	35,481
Restricted (Note 1)	-	1,801,186	260,900	250,000	2,312,086	2,312,086
Unrestricted (Note 1)	159,941	146,879	(136,669)	107,984	278,135	195,475
Total net assets	187,987	1,948,065	124,231	358,113	2,618,396	2,543,042
Total liabilities and net assets	\$ 189,746	\$ 1,948,065	\$ 124,231	\$ 373,921	\$ 2,635,963	\$ 2,560,656

The accompanying notes are an integral part of these financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Combined Statements of Revenues, Expenses and Changes in Net Assets and Combining Information
Years Ended September 30, 2007 and 2006

	Major Enterprise Funds				Total 2007	Total 2006
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
Operating revenues:						
Republic of Palau appropriation	\$ -	\$ -	\$ -	\$ 67,000	\$ 67,000	\$ 67,000
Interest on loans	-	57,260	1,660	2,559	61,479	45,341
Other	4,243	11,925	175	126	16,469	7,581
Section 8 income	15,300	-	-	-	15,300	13,812
National treasury income	-	-	-	8,500	8,500	8,000
Federal contributions	-	-	-	4,050	4,050	-
Total operating revenues	<u>19,543</u>	<u>69,185</u>	<u>1,835</u>	<u>82,235</u>	<u>172,798</u>	<u>141,734</u>
Operating expenses:						
Salaries and wages	9,425	-	-	50,482	59,907	54,929
Other	3,651	500	84	8,693	12,928	12,208
Rent expense	1,120	-	-	10,200	11,320	10,200
Depreciation	7,649	-	-	1,957	9,606	10,198
Professional fees	-	-	-	9,380	9,380	8,500
Travel	701	98	-	7,024	7,823	9,040
Employee benefits	826	-	-	4,922	5,748	5,309
Communication	1,737	-	-	1,188	2,925	2,919
Repairs and maintenance	1,564	-	-	1,102	2,666	3,888
Total operating expenses	<u>26,673</u>	<u>598</u>	<u>84</u>	<u>94,948</u>	<u>122,303</u>	<u>117,191</u>
Operating income	<u>(7,130)</u>	<u>68,587</u>	<u>1,751</u>	<u>(12,713)</u>	<u>50,495</u>	<u>24,543</u>
Non-operating revenue: (expense):						
Interest income	4,480	12,181	1,436	6,762	24,859	22,279
Other expense	-	-	-	-	-	(3,034)
Total non-operating revenue	<u>4,480</u>	<u>12,181</u>	<u>1,436</u>	<u>6,762</u>	<u>24,859</u>	<u>19,245</u>
Change in net assets	<u>(2,650)</u>	<u>80,768</u>	<u>3,187</u>	<u>(5,951)</u>	<u>75,354</u>	<u>43,788</u>
Total net assets at beginning of year	<u>190,637</u>	<u>1,867,297</u>	<u>121,044</u>	<u>364,064</u>	<u>2,543,042</u>	<u>2,499,254</u>
Total net assets at end of year	<u>\$ 187,987</u>	<u>\$ 1,948,065</u>	<u>\$ 124,231</u>	<u>\$ 358,113</u>	<u>\$ 2,618,396</u>	<u>\$ 2,543,042</u>

The accompanying notes are an integral part of these financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Combined Statements of Cash Flows with Combining Information
Years Ended September 30, 2007 and 2006

	Major Enterprise Funds				Total 2007	Total 2006
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
Cash flows from operating activities:						
Receipts from customers	\$ 8,039	\$ 284,425	\$ 8,606	\$ 100,148	\$ 401,218	\$ 345,454
Payments to suppliers	(6,642)	(241,302)	(39,930)	(47,940)	(335,814)	(461,199)
Payments to employees	(9,425)	-	-	(50,482)	(59,907)	(60,238)
Other cash receipts (payments)	-	-	25,000	(25,000)	-	40,000
Net cash provided (used) by operating activities	<u>(8,028)</u>	<u>43,123</u>	<u>(6,324)</u>	<u>(23,274)</u>	<u>5,497</u>	<u>(135,983)</u>
Cash flows from financing activities:						
Acquisition of capital assets	(2,179)	-	-	-	(2,179)	-
Other adjustments	(3,072)	-	-	2,854	(218)	-
Net cash provided (used) by financing activities	<u>(5,251)</u>	<u>-</u>	<u>-</u>	<u>2,854</u>	<u>(2,397)</u>	<u>-</u>
Cash flows from investing activities:						
Interest and dividends	4,481	12,181	1,436	6,762	24,860	22,279
Net cash provided by investing activities	<u>4,481</u>	<u>12,181</u>	<u>1,436</u>	<u>6,762</u>	<u>24,860</u>	<u>22,279</u>
Net increase (decrease) in cash and cash equivalents	(8,798)	55,304	(4,888)	(13,658)	27,960	(113,704)
Cash and cash equivalents at beginning of year	<u>146,243</u>	<u>383,962</u>	<u>63,267</u>	<u>288,113</u>	<u>881,585</u>	<u>995,289</u>
Cash and cash equivalents at end of year	<u>\$ 137,445</u>	<u>\$ 439,266</u>	<u>\$ 58,379</u>	<u>\$ 274,455</u>	<u>\$ 909,545</u>	<u>\$ 881,585</u>

The accompanying notes are an integral part of these financial statements.

PALAU DISTRICT HOUSING AUTHORITY
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Combined Statements of Cash Flows with Combining Information, Continued
Years Ended September 30, 2007 and 2006

	Major Enterprise Funds				Total 2007	Total 2006
	Section 8 Housing Assistance Program	Home Rehabilitation Loan Program	Low-Cost Housing Program	Non-Major Enterprise Funds		
Reconciliation of operating income (loss) to net cash provided (used by operating activities:						
Operating income (loss)	\$ (7,130)	\$ 68,587	\$ 1,751	\$ (12,713)	\$ 50,495	\$ 24,543
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities						
Depreciation	7,649	-	-	1,957	9,606	10,198
(Increase) decrease in assets:						
Accounts receivable	(8,155)	-	-	6,266	(1,889)	1,680
Notes receivable	-	(36,114)	(33,075)	5,776	(63,413)	(229,720)
Interest receivable	-	787	-	-	787	93
Due from other fund	-	-	-	(25,000)	(25,000)	-
Other assets	-	9,863	-	-	9,863	57,275
Increase (decrease) in liabilities:						
Accrued expenses	(392)	-	-	440	48	(52)
Due to other fund	-	-	25,000	-	25,000	-
Net cash provided (used) by operating activities	<u>\$ (8,028)</u>	<u>\$ 43,123</u>	<u>\$ (6,324)</u>	<u>\$ (23,274)</u>	<u>\$ 5,497</u>	<u>\$ (135,983)</u>

The accompanying notes are an integral part of these financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies

The Palau District Housing Authority (the Authority), a component unit of the Republic of Palau, was established by Public Law 4-5-5 (June 20, 1970) of the Palau District Legislature (of the Trust Territory of the Pacific Islands). Its purpose is to develop and administer low cost housing and urban renewal projects and to assist in correcting housing conditions endangering the health, safety, and welfare of the people. The Authority was reorganized by Trust Territory Public Law 5-37 (April 5, 1973). Upon emergence of the Republic of Palau Constitutional Government (January 1, 1981), the Authority was transferred to the Republic. The Authority is a public corporation administered by a five-member Board of Directors appointed by the President of the Republic of Palau with the advice and consent of the Olbiil Era Kelulau (OEK – Palau National Congress).

The Authority's primary operations are comprised of a number of housing and grant programs as follows:

Major Enterprise Funds

Section 8 Housing Assistance Program

The program provides temporary housing for rental to assist low-income families who lack sufficient income to obtain safe, decent, and sanitary housing. The program was originally funded through the U.S. Department of Housing and Urban Development (HUD), until it phased-out in December 2004. However, with prudent fund management, the program has been able to sustain and continue to provide this service.

Home Rehabilitation Loan Program

The Home Rehabilitation Loan Program provides long-term financing to low income and moderate income families to rehabilitate existing dwellings or construct new single-family housing units. This program is made possible through the initial funding from the U.S. Department of Housing and Urban Development (HUD).

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Major Enterprise Funds, Continued

Low-Cost Housing Program

The U.S. Department of Housing and Urban Development (HUD) was the primary source of funds for the Loan Fund Housing Program. The program initially provided funding for loans to low-income families for up to \$12,000, payable over a period of 30 years, at an interest rate of 3 percent per year to rehabilitate/construct their housing unit.

Currently, under this loan program and with the initial funding from HUD and USDA, the Home Improvement and Repair Assistance Program was established specifically to provide low cost and long-term loans to low income and very low-income senior citizens, 60 years old and over, to rehabilitate their homes.

Non-Major Enterprise Funds

The following funds were determined to be non-major enterprise funds for the year ended September 30, 2007:

Emergency Housing Revolving Loan Program

The Emergency Housing Revolving Loan Program has been established as an Emergency Loan Program by the Republic of Palau to citizens whose homes are destroyed by natural disaster or fire. The Program was funded by a \$500,000 appropriation from the Republic of Palau. Pursuant to Republic of Palau Public Law 6-26, § 4, the program was initially established to provide loans to private homeowners whose homes were destroyed or made uninhabitable because of damage done by storm Utor. Loans are available from a minimum amount of \$500 to a maximum amount of \$30,000, and are to be repaid over 3 to 30 year periods at an interest rate of 3 percent per year. During the fiscal year ending September 30, 2002, the Authority remitted \$250,000 of the initial funding back to the Republic of Palau National Government.

Transitional/Emergency Shelter Program

The program provides short-term temporary housing to individuals or families who become victims of domestic violence or abuse and whose homes are destroyed due to fire or natural disaster. The program was originally funded through the U.S. Department of Housing and Urban Development (HUD).

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Local Funds

Local funds consist of appropriations from Republic of Palau for general operations of the Authority.

Measurement Focus, Basis of Accounting, and Basis of Presentation

During 2003, the Authority implemented GASB Statement No. 34, "*Basic Financial Statements and Management's Discussion and Analysis – for State and Local Government*", GASB Statement No. 37, "*Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus*", GASB Statement No. 38, "*Certain Financial Statement Note Disclosures*", and GASB Interpretation No. 6 "*Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements.*"

GASB Statement No. 34 creates new basic financial statements for reporting on the Authority's financial activities. The financial statements now include government-wide financial statements prepared on an accrual basis of accounting and fund accounting which present information for individual major funds rather than by fund type. Requirements in order to comply also include adopting depreciation on capital assets and classifying assets and liabilities as current and non-current.

GASB Statement No. 37 clarifies certain provisions of GASB Statement No. 34, including the required content of the Management Discussion and Analysis, the classification of program revenues and the criteria for determining major funds. GASB Statement No. 38 modifies, establishes and rescinds certain financial statement note disclosures. GASB Interpretation No. 6 clarifies the application of standards for modified accrual recognition of certain liabilities and expenditures in areas where differences have arisen, or potentially could arise, in interpretation and practice.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

The accounts of the Authority are organized and operated on the basis of funds and grant programs. A fund is an independent fiscal year and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions. The minimum number of funds is maintained consistent with legal and managerial requirements.

The Authority has elected to use proprietary fund types as its principal reporting. Proprietary funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Authority's proprietary funds are enterprise funds used to account for those operations that are financed and operated in a manner similar to private business or where the Authority has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability.

The general purpose financial statements of the Palau District Housing Authority have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. Government Accounting Standards Board (GASB) Statement No. 20, "*Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*", requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. The Palau Housing and Urban Renewal Authority has implemented GASB No. 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the organization's audited financial statements for the year ended September 30, 2006, from which the summarized information was derived.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

New Accounting Standards

In April 2004, GASB issued Statement No. 43, "*Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*". This Statement establishes uniform financial reporting for other postemployment benefit plans by State and Local governments. The provisions of GASB Statement No. 43 are effective for reporting periods beginning after December 15, 2007. The Authority does not believe that the implementation of this Statement will have a material effect on its financial statements.

In June 2004, GASB issued Statement No. 45, "*Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*". This Statement establishes standards for the measurement, recognition, and display of other postemployment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of State and Local governmental employers. The provisions of this Statement are effective for reporting periods beginning after December 15, 2008. The Authority does not believe that the implementation of this Statement will have a material effect on its financial statements.

In December 2004, GASB issued Statement No. 46, "*Net Assets Restricted by Enabling Legislation*", an amendment of GASB Statement No. 34, which will be effective for the Authority beginning with its fiscal year ending September 30, 2007. The provisions of this Statement clarifies that a legally enforceable enabling legislation is on that a party external to a government, such as citizens, public interest groups or the judiciary, can compel a government to honor. There is no financial impact to the Authority for the fiscal year ended September 30, 2007 as a result of the implementation of this statement.

In September 2006, the GASB issued Statement No. 48, "*Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*". This statement addresses accounting and financial reporting standards for transactions where governments exchange an interest in their expected cash flows from collecting specific receivables or specific future revenues for immediate cash payments. This statement establishes criteria and reporting standards regarding the exchange as either a sale or collateralized borrowing, resulting in a liability. This statement is not effective until June 30, 2008. The Authority does not believe that the implementation of this Statement will have a material effect on its financial statements.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

New Accounting Standards, Continued

In May 2007, GASB issued Statement No. 50, "*Pension Disclosures — an amendment of GASB Statements No. 25 and No. 27*". This statement more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits (OPEB) and, in doing so, enhances information disclosed in notes to financial statements or presented as required supplementary information (RSI) by pension plans and by employers that provide pension benefits. This statement is not effective until June 30, 2008. The Authority does not believe that the implementation of this Statement will have a material effect on its financial statements.

In June 2007, GASB issued Statement No. 51, "*Accounting and Financial Reporting for Intangible Assets*". This statement establishes accounting and financial reporting standards for many different types of assets that may be considered intangible assets, including easements, water rights, timber rights, patents, trademarks, and computer software. This statement is not effective until June 30, 2010. The Authority does not believe that the implementation of this Statement will have a material effect on its financial statements.

Budgets – Budgets are prepared on an annual basis for each major operating program and are used as a management tool throughout the accounting cycle. Budgets, however are not legally adopted nor legally required for financial statement presentation.

The Authority's governing body, the Board of Directors, adopts budgets on a program or fund level basis. These budgets are submitted by the Authority's Executive Director, and approved by resolutions of the Board of Directors.

Annual budgets are adopted for all Enterprise Funds. Throughout the fiscal year, the Authority monitors and evaluates expenditures rates and patterns. However, timely notice is not given to executive management regarding forthcoming changes in objectives or other conditions that may cause significant variations from approved budget-defined plans.

The Authority's Board of Directors may authorize revisions to the budget based on the availability of financial resources. Formal budget revisions are authorized in the same manner as original budget submissions.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Management's Use of Estimates – The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents – For the purposes of the Statement of Net Assets and Statement of Cash Flows, the Authority considers cash and cash equivalents to be cash on hand, cash in checking and savings accounts, and time certificates of deposit of less than ninety-day maturities. All of the Authority's cash and cash equivalents are with a federally insured bank, \$100,000 of which is subject to coverage by federal insurance with the remaining balance exceeding insurable limits. The Authority does not require collateralization of its bank accounts and, therefore, amounts in excess of insurable limits are uncollateralized. Deposits in excess of federal depository insurance are considered uncollateralized by GASB Statement No. 40. Custodial credit risk for deposits is the risk that in the event of a bank failure, the government's deposits may not be returned to it. At September 30, 2007 and 2006, uninsured and uncollateralized bank balance of \$705,823 and \$281,048, respectively was exposed to credit risk. The Authority has not experienced any losses in such accounts.

Loans and Allowance for Loan Losses – Loans are stated at the amount of unpaid principal, reduced by an allowance for loan losses. Interest on loans is calculated by using the simple interest method on daily balances of the principal amount outstanding. The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collection of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans that may be uncollectible, based on evaluation of the collectibility of loans and prior loan loss experience. The evaluation takes into consideration such factors as specific problem loans and current economic conditions that may affect the borrowers' ability to pay. The Authority recognizes bad debts using the allowance method and is only written-off after approval by management and subsequent reporting to the Board of Directors.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Capital Assets and Depreciation – All capital assets with a value greater than \$500 and a useful life over one year are capitalized.

The cost of repairs and maintenance is charged to operations as incurred and improvements are capitalized. Depreciation of capital assets is computed using the straight-line method over the estimated useful lives of the assets. Assets are depreciated using the following depreciation guidelines:

<u>Category</u>	<u>Useful Life - Years</u>
Residential units	28
Furniture, fixtures and equipment	5
Vehicles	5

Upon retirement or other disposition of capital assets recorded, the cost and related accumulated depreciation are removed from the respective program's or fund's accounts and any gain or loss is included in the respective program's or fund's current operations.

Compensated Absences – Compensated absences are those absences for which employees will be paid, such as vacation and sick leave. Employees are credited 55, 208 or 280 hours per fiscal year, based on their lengths of service. The accumulation of vacation and sick credits is limited to 360 at fiscal year-end and is convertible to pay upon termination of employment. The Authority recognizes as a liability all vested vacation and sick leave benefits accrued by its employees. When the employees use vacation and sick leave benefits, the liability account is reduced accordingly. At September 30, 2007 and 2006, compensated absences payable to employees were \$13,604 and 9,815, respectively.

Income Tax - Based on 34 PNC 7006, the Authority is exempt from all national and state non-payroll taxes or fees.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Measurement Focus, Basis of Accounting, and Basis of Presentation, Continued

Net Assets - The Authority's net assets are classified as follows:

Invested in capital assets - This represents the Authority's total investment in capital assets, net of accumulated depreciation.

Restricted net assets – This includes grants from HUD and contributions received from the Trust Territory of the Pacific Islands for the establishment of the Home Rehabilitation Revolving Loan Program and the Low-Cost Housing Revolving Loan program, respectively. It also includes contributions received from the Republic of Palau National Government for the establishment of Emergency Loan Program.

Unrestricted net assets – This includes resources derived from government appropriations. These resources are used for transactions relating to the general operations of the Authority and may be used at the discretion of the governing board to meet current expenses for any purpose.

Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. This statement also requires disclosure of formal policies related to deposit and investment risks.

Deposits:

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

- | | |
|------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Category 1 | Deposits that are federally insured or collateralized with securities held by the Authority or its agent in the Authority's name; |
| Category 2 | Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in the Authority's name; or |

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, Continued

Deposits and Investments, Continued:

Deposits, Continued:

Category 3 Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in Authority's name and noncollateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. The Authority has an investment and deposit policy for custodial credit risk. For deposits, a general depository agreement pursuant to HUD regulations, must be executed by the Authority and the depository. The depository bank must be a bank or financial institution whose deposits are insured by FDIC, Federal Savings and Loan Insurance Corporation or the National Credit Union Administration and all deposits must be fully collateralized by U.S. securities.

For credit risk in the case of deposits, there is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. As of September 30, 2007 and 2006, the carrying amount of the Authority's total cash and cash equivalents was \$909,545 and \$881,585, respectively with a corresponding bank balance of \$909,445 and \$881,585, respectively which is insured by the Federal Deposit Insurance Corporation (FDIC). From these deposits, \$206,904 and \$600,437 at September 30, 2007 and 2006, respectively was subject to coverage by FDIC with the remaining balance exceeding insurable limits. The uninsured bank balance as of September 30, 2007 and 2006 was \$705,823 and \$281,048, respectively. The Authority does not require collateralization of bank accounts, and therefore, amounts in excess of insurable limits are uncollateralized and are subject to custodial credit risk.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(1) Summary of Significant Accounting Policies, continued

Deposits and Investments, continued

Investments:

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

- Category 1 Investments that are insured or registered, or securities held by the Authority or its agent in the Authority's name;
- Category 2 Investments that are uninsured and unregistered for which the securities are held by the counterparty's trust department or agent in the Authority's name; or
- Category 3 Investments that are uninsured and unregistered, with securities held by the counterparty's trust department or agent but not in Authority's name.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial risk in GASB Statement No. 3.

As of September 30, 2007 and 2006, the Authority did not have any investments subject to GASB Statement No. 40.

(2) Cash and cash equivalents

Cash and cash equivalents at September 30, 2007 and 2006 consist of the following:

	<u>2007</u>	<u>2006</u>
Cash	\$ 258,173	\$ 183,571
Time certificates of deposit	<u>651,372</u>	<u>698,014</u>
	<u>\$ 909,545</u>	<u>\$ 881,585</u>

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(3) Notes Receivable

The Authority extends loans to qualifying residents of the Republic of Palau for rehabilitating existing dwellings or for constructing approved low-cost housing. The loans have terms from five to thirty years at an interest rate of 3% and 4.5%. Loans are restricted to a maximum ninety percent (90%) debt (aggregate of all debts associated with the property) to the appraised value of the property ratio or ninety percent (90%) of the estimated replacement cost, whichever is lower. The loans are collateralized by the property being rehabilitated.

A summary of notes receivable at September 30, 2007 and 2006 follows:

	<u>2007</u>	<u>2006</u>
Home Rehabilitation loans	\$ 1,535,967	\$ 1,499,853
Emergency Loan Revolving Fund loans	63,040	68,816
Low-Cost Housing loans	<u>90,554</u>	<u>57,479</u>
	1,689,561	1,626,148
Less current portion	<u>(177,668)</u>	<u>(160,071)</u>
Long-term notes receivable, net of current portion	1,511,893	1,466,077
Less allowance for loan losses	<u>(85,000)</u>	<u>(85,000)</u>
Long-term notes receivable, net of allowance for loan losses	<u>\$ 1,426,893</u>	<u>\$ 1,381,077</u>

(4) Due from (to) other fund

During the year, Low-Cost Housing Program advances cash from Emergency Housing Revolving Loan Fund to provide additional funding to the Home Improvement Assistance Program. As of September 30, 2007, Low-Cost Housing Program has payable to Emergency Housing Revolving Loan Fund of \$25,000. In accordance with GASB No. 38, account balances for interfund activities were eliminated for financial statement reporting purposes

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(5) Capital Assets

A schedule of changes in capital assets for the fiscal years ended September 30, 2007 and 2006 is shown below:

Capital assets activity for the fiscal year ended September 30, 2007:

	Balance 9/30/06	Additions	Disposal	Balance 9/30/07
Residential units	\$ 213,431	\$ -	\$ -	\$ 213,431
Furniture, fixtures, and equipment	38,441	2,179	-	40,620
Vehicles	27,795	-	-	27,795
	279,667	2,179	-	281,846
Accumulated depreciation	(244,186)	(9,485)	-	(253,671)
	<u>\$ 35,481</u>	<u>\$ (7,306)</u>	<u>\$ -</u>	<u>\$ 28,175</u>

Capital assets activity for the fiscal year ended September 30, 2006:

	Balance 9/30/05	Additions	Disposal	Balance 9/30/06
Residential units	\$ 213,431	\$ -	\$ -	\$ 213,431
Furniture, fixtures, and equipment	38,441	-	-	38,441
Vehicles	27,795	-	-	27,795
	279,667	-	-	279,667
Accumulated depreciation	(230,954)	(13,232)	-	(244,186)
	<u>\$ 48,713</u>	<u>\$ (13,232)</u>	<u>\$ -</u>	<u>\$ 35,481</u>

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(5) Capital Assets, Continued

The residential units are constructed on properties leased from the Trust Territory Government, which properties were transferred to Palau Public Land Authority in accordance with U.S. Department of the Interior Secretarial Order No. 2969. The properties were subsequently transferred to the Koror Municipal Public Lands Authority through quitclaim deeds dated May 14, 1980 and February 16, 1983. Upon termination of the lease agreement (December 31, 2006), all improvements on the properties shall become the properties of the lessor or its successor.

(6) Employees Retirement Plan

The Authority contributes to the Palau Civil Service Pension Trust Fund (the Fund), a defined benefit, cost-sharing, multi-employer pension plan established and administered by the Republic of Palau. The Fund issues a stand-alone financial report which is available at its office site.

The Fund provides retirement, security and other benefits to employees, and their spouses and dependents, of the Republic of Palau State Governments and Republic of Palau agencies, funds and public corporations, which are paid monthly and are two percent (2%) of each member's average monthly salary. Normal benefits are the credited total service up to a maximum of thirty years total service. Generally, benefits vest after three years of credited service. Members, who retire at or after age 60, or with 30 years of vesting service, are entitled to retirement benefits. Republic of Palau Public Law 2-26 is the authority under which benefit provisions and contributions rates are established. Member contribution rates are established by Republic of Palau Public Law 2-26 at six percent (6%) of total payroll and are matched dollar for dollar by the employer. The Authority contributed \$3,482 and \$3,180 for fiscal years 2007 and 2006, respectively.

Under the provisions of the Republic of Palau Public Law 2-26, the Fund's Board of Trustees adopted a Trust Fund Operation which has the force and effect of law, and which sets forth the procedures for the administration and coverage of the Plan. Amendments to the Plan are subject to the requirements of Title 6 of the Palau National Code.

The Fund utilizes the actuarial cost method termed "level aggregate cost method" with actuarial assumptions used to compute the pension benefit obligation. The following is the statement of actuarial assumptions for the year October 1, 2004 to September 30, 2005 of the ROP Civil Service Pension Plan:

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(6) Employees Retirement Plan, Continued

Actuarial Cost Method: Normal costs are calculated under the level aggregate method.
Investment Income: 8.5% per year
Expenses: : \$300,000 each year
Salary Increase: : 3% per year
Mortality : 1984 Unisex Pension Mortality Table
Disabled Mortality : PBGC Mortality Table for Disabled Persons Receiving
Social Security
Retirement Age : Earlier of age 60 or 30 Years of Total Service

The pension benefit obligation, which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefits, adjusted for the affects of projected salary increases and any step-rate benefits, estimated to be payable in the future as a result of employment service to date. The measure is intended to assist users to evaluate the Fund's funding status on a going-concern basis, and evaluate progress made in accumulating adequate assets to pay benefits when due.

The Fund's October 1, 2005 actuarial valuation determined the unfunded pension benefit obligation as follows:

Present value of accrued benefits, 10/1/2005	
Active participants	\$ 33,893,000
Inactive participants with vested deferred benefits	1,565,000
Participants in pay status	<u>47,711,000</u>
Total pension benefit obligation	83,169,000
Market value of assets	<u>41,965,000</u>
Unfunded benefit obligation	<u>\$ 41,204,000</u>
Funded Ratio as of 10/1/2005 (ratio of assets to liabilities)	<u>50.46%</u>

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(7) Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. The Authority has elected to be self-insured for the risks of loss to which it is exposed.

(8) Commitments and Contingencies

Litigation

The Authority is subject to various claims and other legal actions in the normal course of business. Palau District Housing Authority consults their legal counsel and the Office of the Attorney General of the Republic of Palau whenever there is a potential or asserted claim, and relies on the advice of counsel for direction and for establishing reserves for potential unfavorable outcomes.

The Authority has initiated several foreclosure actions now pending in the Trial Division of the Supreme Court of Palau (the Court) against seven (7) borrowers who have defaulted on rehabilitation loans whose principal and interest balance approximate \$93,000 as of September 30, 2007. The Authority intends to take the following courses of action with respect to these matters: (1) renegotiate the loan; (2) pursue the claim in Court to recover the amount through judgments for monetary awards; or (3) pursue the claim in court to recover the amount through judgments for foreclosure on mortgaged properties.

Commitments

The Authority's operations are conducted from premises under a lease agreement expiring on December 04, 2007. The future minimum rental payment for the year ending September 30, 2008 is \$1,700.

Contingencies

The Authority entered a thirty (30) year lease agreement with Koror State Government that expired on December 31, 2006. The Authority constructed seven low-cost housing units on the property that was funded by the U.S. Department Housing Urban Development under the Section 8 Housing Federal grant program. The lease has not been renewed because another party is claiming ownership of the property. Currently, the Authority is still paying the lease to Koror State Government every six months but is essentially on month-to-month lease arrangement pursuant to the lease provisions.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Combined Financial Statements
September 30, 2007 and 2006

(8) Commitments and Contingencies, Continued

Contingencies, Continued

The Authority is waiting for the Court's judgment and decision on the true owner of the property. If the lease is not renewed, the building and improvements would become the property of the Koror State Government or the other party claiming the ownership title. The ultimate outcome is uncertain and no provisions have been made to the accompanying financial statements as a result of this contingency.

(9) Reclassifications

Certain reclassifications have been made to the prior year's financial statements to conform to the current year presentation. These reclassifications had no effect on previously reported results of operations or retained earnings.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

**INDEPENDENT AUDITOR'S REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE**

Year Ended September 30, 2007

J. Scott Magliari
COMPANY

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**INDEPENDENT AUDITOR'S 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**

To the Board of Directors
Palau District Housing Authority

I have audited the financial statements of Palau District Housing Authority (the Authority) as of and for the year ended September 30, 2007, and have issued my report thereon dated November 30, 2007. I conducted my 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 my audit, I considered the Authority's internal control over financial reporting as a basis for designing my auditing procedures for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, I do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

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 Authority'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 Authority's financial statements that is more than inconsequential will not be prevented or detected by the Authority's internal control.

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 Authority's internal control.

My consideration of 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 internal control that might be significant deficiencies or material weaknesses. I did not identify any deficiencies in internal control over financial reporting that I consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, I 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 my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board of Directors, federal awarding agencies and the cognizant audit and other federal agencies. However, this report is a matter of public record and its distribution is not limited.

J. Scott Maglian & Company
Koror, Republic of Palau
November 30, 2007

J. Scott Magliari
COMPANY

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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH
REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH
OMB CIRCULAR A-133 AND ON THE SCHEDULE
OF EXPENDITURES OF FEDERAL AWARDS**

To the Board of Directors
Palau District Housing Authority

Compliance

I have audited the compliance of Palau District Housing Authority (the Authority) with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended September 30, 2007. The Authority's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Authority's management. My responsibility is to express an opinion on the Authority's compliance based on my audit.

I conducted my audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that I plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Authority's compliance with those requirements and performing such other procedures as I considered necessary in the circumstances. I believe that my audit provides a reasonable basis for my opinion. My audit does not provide a legal determination of the Authority's compliance with those requirements.

In my opinion, the Authority complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2007.

Internal Control Over Compliance


The management of the Authority is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing my audit, I considered the Authority's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine my auditing procedures for the purpose of expressing my opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, I do not express an opinion on the effectiveness of the Authority's internal control over compliance.

A *control deficiency* in the Authority's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the Authority's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the Authority's internal control.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the Authority's internal control.

My consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. I did not identify any deficiencies in internal control over compliance that I consider to be material weaknesses, as defined above.

This report is intended for the information and use of management, the Board of Directors, federal awarding agencies and the cognizant audit and other federal agencies. However, this report is a matter of public record and its distribution is not limited.


Koror, Republic of Palau
November 30, 2007

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Schedule of Expenditures of Federal Awards
Year Ended September 30, 2007

Grantor/Account Title	Grant/ Contract I.D.#	CFDA No.	Total Authorizations	Prior Years Expenses	FY2007 Expenses/ Revenues	Total Program Expenses	Excess (Deficit) Authorization over Program Expenses
<u>U.S. Department of Housing and Urban Development</u>							
Community Development Block Grant							
- Insular Area:							
Meyuns Elementary School	B-86-ST-70-0001	14.225	\$ 179,256	\$ 179,256	\$	\$ 179,256	\$ -
Home Rehabilitation Loan Program	B-88-ST-70-0001	14.225	165,510	165,510		165,510	-
Ibobang Dock	B-88-ST-70-0001	14.225	80,234	80,234		80,234	-
Ollie Community Center	B-89-ST-70-0001	14.225	120,000	120,000		120,000	-
Ngeremlengui Elementary School	B-89-ST-70-0001	14.225	180,000	180,000		180,000	-
Iyebukl Community Center	B-94-ST-70-0001	14.225	100,000	100,000		100,000	-
Peleliu Old Age Center	B-94-ST-70-0001	14.225	150,000	150,000		150,000	-
General Program Administration	B-94-ST-70-0001	14.225	47,500	47,500		47,500	-
Emergency Shelter Transitional Home	B-95-ST-70-0001	14.225	45,000	45,000		45,000	-
Palau High School Toilet Facility	B-95-ST-70-0001	14.225	50,000	50,000		50,000	-
Meyuns Community Center	B-95-ST-70-0001	14.225	70,000	70,000		70,000	-
Meyuns Parking			5,000	5,000		5,000	-
Peleliu Elementary School Cafeteria	B-95-ST-70-0001	14.225	120,000	120,000		120,000	-
General Program Administration	B-95-ST-70-0001	14.225	42,500	42,500		42,500	-
Rehabilitation Loan Administration	B-95-ST-70-0001	14.225	30,000	30,000		30,000	-
Rehabilitation Loan Program	B-96-ST-70-0001	14.225	180,000	180,000		180,000	-
Rehabilitation Loan Administration	B-96-ST-70-0001	14.225	33,000	33,000		33,000	-
General Program Administration	B-96-ST-70-0001	14.225	20,000	20,000		20,000	-
Ngerusar Community Center	B-97-ST-70-0001	14.225	106,000	106,000		106,000	-
Rehabilitation Loan Administration	B-97-ST-70-0001	14.225	20,000	20,000		20,000	-
General Program Administration	B-97-ST-70-0001	14.225	30,000	30,000		30,000	-
Melekeok State Gym	B-98-ST-70-0001	14.225	42,400	42,400		42,400	-
Rehabilitation Loan Administration	B-98-ST-70-0001	14.225	20,000	20,000		20,000	-
General Program Administration	B-98-ST-70-0001	14.225	15,600	15,600		15,600	-
			1,852,000	1,852,000		1,852,000	-
Emergency Shelter Grant	S-94-DC-70-0001	14.231	10,000	10,000		10,000	-
Emergency Shelter Grant	S-95-DC-70-0001	14.231	14,000	14,000		14,000	-
Emergency Shelter Grant	S-96-DC-70-0001	14.231	9,000	9,000		9,000	-
Emergency Shelter Grant	S-97-DC-70-0001	14.231	8,000	8,000		8,000	-
Emergency Shelter Grant	S-98-DC-70-0001	14.231	7,000	7,000		7,000	-
			\$ 1,900,000	\$ 1,900,000		\$ 1,900,000	\$ -
Section 8 Housing Assistance							
Payments Program	SF-78-192	14.856			-		
Total federal financial assistance					\$	-	

See accompanying notes to schedule of expenditures of federal awards.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2007

(1) Scope of Review

The Palau District Housing Authority (the Authority) is a component unit of the Republic of Palau. The Authority was established by Public Law 4-5-5 of the Palau District Legislature of the Trust Territory of the Pacific Islands and subsequently reorganized by Trust Territory Public Law 5-37. Upon emergence of the Republic of Palau Constitutional Government, the Authority was transferred to the Republic.

The purpose of the Authority is to develop and administer low cost housing and urban renewal projects and to assist in correcting housing conditions endangering the health, safety, and welfare of the people through low interest loans.

The accompanying Schedule of Expenditures of Federal Awards presents federal programs related to the U.S. Department of Housing and Urban Development (HUD), administered by the Authority. The U.S. Department of the Interior has been designated as the Authority's cognizant agency for the OMB Circular A-133 audit.

(2) Summary of Significant Accounting Policies

A. Basis of Accounting

For purposes of preparation of the accompanying Schedule of Expenditures of Federal Awards, certain accounting procedures were followed, which help illustrate the authorizations of expenses of the individual programs. All authorizations represent the total allotment or grant award received. All expenses and capital outlays are reported as expenses.

B. Indirect Cost Allocation

The Authority does not currently have an approved indirect cost allocation plan.

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2007

(2) Summary of Significant Accounting Policies, continued

C. Federal Programs

The following federal program was received in a direct capacity from HUD:

Section 8 Housing Assistance Payments Program CFDA # 14.856

The Authority administers a “Home Rehabilitation Loan Program” funded originally by sub-grants from the Republic of Palau under the HUD Community Development Block Grant – Insular Area (CFDA # 14.225). The total value of the Home Rehabilitation Loan Program’s loan portfolio, net of allowance for loan losses of \$78,000, amounted to \$1,457,967 as of September 30, 2007 and is included in the determination of a major program.

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COMPANY

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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE
WITH SPECIFIC REQUIREMENTS APPLICABLE TO
AFFIRMATIVE FAIR HOUSING AND NON-DISCRIMINATION**

To the Board of Directors
Palau District Housing Authority:

I have audited the financial statements of the Palau District Housing Authority ("the Authority"), a component unit of the Republic of Palau, as of and for the year ended September 30, 2007 and have issued my report thereon dated November 30, 2007.

I have applied procedures to test the Authority's compliance with the Affirmative Fair Housing and Non-Discrimination requirements applicable to its HUD assisted programs, for the year ended September 30, 2007.

My procedures were limited to the applicable compliance requirements described in the Consolidated Audit Guide for Audits of HUD Programs issued by the U.S. Department of Housing and Urban Development, Office of Inspector General. My procedures were substantially less in scope than an audit, the objective of which would be the expression of an opinion on the Authority's compliance with the Affirmative Fair Housing and Non-Discrimination requirements. Accordingly, I do not express such an opinion.

The results of my tests disclosed no instances of noncompliance with the Affirmative Fair Housing and Non-Discrimination requirements.

This report is intended for the information of the Board of Directors, management, and the Department of Housing and Urban Development. However, this report is a matter of public record and its distribution is not limited.

J. Scott Magliari & Company
Koror, Republic of Palau
November 30, 2007

PALAU DISTRICT HOUSING AUTHORITY
(A Component Unit of the Republic of Palau)

Schedule of Findings and Questioned Costs
September 30, 2007

Part I – Summary of Auditor’s Results

Audit of Financial Statements

1. The Independent Auditor’s Report on the financial statements of the Authority expressed an unqualified opinion.
2. There were no reportable conditions required to be disclosed by Government Auditing Standards issued by the Comptroller General of the United States of America.
3. There were no instances of noncompliance considered material, as defined by the Government Auditing Standards, in the financial statements.

Audit of Federal Awards

1. There were no reportable conditions required to be disclosed by OMB Circular No. A-133.
2. The Independent Auditor’s Report on compliance requirements applicable to major federal award programs for Authority expressed an unqualified opinion
3. The audit disclosed no audit findings, which the auditor is required to report under OMB Circular No. A-133, Section 510 (a).
4. The Authority’s one major program was Community Development Block Grant – Insular Area CFDA # 14.225.
5. A threshold of \$300,000 was used to distinguish between Type A and B programs as those terms defined in OMB Circular A-133.
6. The Authority qualifies as a low-risk auditee pursuant to OMB Circular A-133.

Part II – Findings on Financial Statements

There were no reportable findings noted concerning the audit of the financial statements.

Part III – Findings on Federal Awards

There were no reportable findings or questioned costs noted concerning federal awards.