



OFFICE OF THE PUBLIC AUDITOR
REPUBLIC OF PALAU

PERFORMANCE AUDIT REPORT

ON



NGATPANG STATE GOVERNMENT
REPUBLIC OF PALAU

PERIOD COVERED

OCTOBER 1, 2007 THROUGH SEPTEMBER 30, 2013

Performed by the Office of the Public Auditor

NGT08-13-P02*opa01

REPUBLIC OF PALAU



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Office of the Public Auditor

January 16, 2015
Serial#: opa15-008au

Honorable Francesca Otong
Acting Governor
Ngatpang State Government
Office of the Governor
Ngatpang, Republic of Palau

Subject: Final Report on the Performance Audit of Ngatpang State Government for the period from October 1, 2007 through September 30, 2013.

Dear Acting Governor Otong:

This report presents the results of our performance audit of Ngatpang State Government for the period from October 1, 2007 through September 30, 2013.

The Office of the Public Auditor (OPA) received your response to the draft audit report. Based on the additional supporting documents provided, the OPA has made, where appropriate, revisions to the draft audit report. The response (without the attachments) is published verbatim in the final report.

The OPA has established an audit recommendation tracking system to keep track of the status of recommendations issued in this report. Accordingly, the OPA will conduct follow up inspections on your responses and corrective action measures to assess their implementation and operation. On a semi-annual basis, June 30 and December 31 each year, the OPA will report the status of the recommendations to the Office of the President and Preciding Officers of the Olbiil Era Kelulau for their information and disposition.

If you have any questions regarding matters of audit findings and recommendations, the OPA will be available to discuss such matters at your request.

Sincerely,

Satruning Tewid
Public Auditor
Republic of Palau

Ngatpang State Government

Republic of Palau

Period from October 1, 2007 to September 30, 2013

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EXECUTIVE SUMMARY

Office of the Public Auditor

January 16, 2015

Honorable Francisca Otong
Acting Governor
Ngatpang State Government
Office of the Governor
Koror, Republic of Palau

Subject: Final Report on Performance Audit of Ngatpang State Government for the period from October 1, 2007 through September 30, 2013.

Dear Acting Governor Otong:

This report presents the results of the Office of the Public Auditor's (OPA) performance audit of Ngatpang State Government for the period from October 1, 2007 through September 30, 2013.

The objective of the audit is to determine whether (1) expenditures were incurred in accordance with national and state government laws and regulations, (2) cash receipts were properly deposited into the state treasury, (3) expenditures and cash receipts were supported by adequate documentation, (4) earmarked CIP grants were expended for purposes for which they were earmarked, and (5) the state has established proper internal controls to ensure that its properties are properly safeguarded and its transactions properly recorded.

As a result of our review, the Office of the Public Auditor found a number of problems and deficiencies noted below relating to the administration of Ngatpang State funds, which we believe should be brought to the attention of the State Government for appropriate corrective action. We also propose recommendations which, if implemented, we believe will correct these problems and deficiencies.

Finding 1: Unsupported Withdrawals

Ngatpang State Government closed and withdrew the remaining balance of its general operations checking account in the amount of \$3,261.11 from a local bank without any supporting documents to show where the balance was deposited or how it was used.

Recommendation

The OPA recommends that the Ngatpang State Treasury obtain and maintain bank records to support and show closure of bank accounts and the disposition of balances.

Finding 2: Unsupported Reimbursement

In fiscal year 2010, we noted two (2) checks totaling \$2,075 disbursed to the then Acting Governor purportedly as repayment for a loan made earlier by him to the State. The OPA found no supporting documents to substantiate these transactions.

Recommendation

The OPA recommends that all loan arrangements be documented in loan agreements specifying the terms and conditions of the loans, including repayment in order to protect the State's interests and to justify repayment of the loan.

Finding 3: Competitive Bidding

The State did not follow competitive bidding procedures when procuring milkfish feeds, an automobile, a boat engine, and supplies and materials for the renovation of the 2nd floor of the Legislative Chamber.

Recommendation

The OPA recommends that the Governor establish necessary controls to ensure that competitive bidding requirements are adhered to when procuring goods or services costing \$5,000 or more.

Finding 4: Open Fuel Charge Account

Ngatpang State operated an "open" fuel charge account to purchase fuel for the State without establishing the proper controls to safeguard the account and to ensure the integrity of fuel drawdowns.

Recommendation

The OPA recommends that in any "open" charge account arrangement for the purchase of goods the Governor establish the proper controls to safeguard the account from unauthorized use or other activities not serving the best interests of the State.

Finding 5: Loan

Ngatpang State obtained a \$10,000 loan from a local business to finance an aquaculture project ("Milkfish Farm") without obtaining prior approval from the Olbiil Era Kelulau ("OEK").

Recommendation

The OPA recommends that Ngatpang State obtains prior approval from the OEK prior to obtaining a loan to finance its projects or programs in accordance with Article XI, Section 4 of the Republic of Palau ("ROP") Constitution.

Finding 6: Audit Documentation

The OPA found that Ngatpang State in fiscal years 2008, 2009, and 2010 did not maintain adequate records to support its financial transactions including \$569,985 of deposits, \$74,542 of wire transfer expenditures, and \$13,025 of expenditures.

Recommendation

The OPA recommends that Ngatpang State establish and maintain an accounting system to record transactions, maintain supporting documents for the transactions, and conduct periodic reviews to ensure that the accounting system is operating as intended.

Finding 7: Deposit of Funds into State Treasury

The audit revealed that the State operated the Milkfish Farm and used \$9,558.63 of revenues from fish sales on credit to offset the Farm's obligations to the same vendors that purchased fish on credit.

Recommendation

The OPA recommends that the Governor comply with the Constitutions of the Republic of Palau and Ngatpang State and appropriation laws by depositing revenues into the State Treasury, having the funds appropriated by the State Legislature, and expending the funds as appropriated.

Finding 8: Fixed Assets

The State lacks a fixed asset accounting system to record the acquisition and disposal of its fixed assets, including donated equipment.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to establish a system to account for, monitor, and conduct periodic inventory of the State's fixed assets.

Finding 9: Liabilities

The State does not have a system in place to record and keep track of its obligations.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to establish an accounting system to account for and keep track of State's accounts payable and other obligations.

Finding 10: Bank Reconciliation

The State did not consistently perform bank reconciliations for its bank accounts.

Recommendation

The OPA recommends that the Governor instruct the State Treasurer to perform bank reconciliation on all state accounts to ensure the accuracy and balances of the accounts.

Finding 11: Check Issuance in Numerical Sequence

The OPA found that the State did not consistently issue checks in proper numerical sequence for a number of its checking accounts.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to issue checks in proper numerical sequence for all checking accounts.

Finding 12: Block Grants

Republic of Palau Law (“RPPL”) No. 8-40 earmarked \$35,000 of Ngatpang State block grants in fiscal year 2012 for the salaries and function of the Ngaimis to be administered by the Ministry of State (“MOS”). On November 26, 2012, \$22,298 was disbursed by the Ministry of Finance to the Ngaimis instead of to Ngatpang State Treasury.

Recommendation

The OPA recommends that the Ministry of Finance adheres to the Republic of Palau and Ngatpang State Constitutions by disbursing State block grants to Ngatpang State Treasury for appropriation and expenditure.

Finding 13: Accounts Receivable

The State lacked a record-keeping system to record and keeps track of its accounts receivable.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to establish a recordkeeping system to account for and keep track of the State’s accounts receivable.

Finding 14: Cash Receipts (Revenues)

The State has not established internal controls to ensure that cash receipts are issued to support revenue collections, reconciled to deposits, and deposited in a timely manner.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to issue cash receipts to support revenue collections, reconcile receipts to deposits, and ensure that cash receipts are deposited in a

timely manner.

Finding 15: Milkfish Farm Sales

The audit revealed that the Milkfish Farm sold fish both on credit and cash and issued invoices and receipts but failed to perform essential reconciliations to agree the total sales at the end of the day to the amount of cash and credit sales based on those invoices and receipts.

Recommendation

The OPA recommends that the Milkfish Farm management establish controls to ensure that milkfish sales are reconciled at the end of the day to agree total sales to the amount of cash and credit sales documented by invoices and receipts issued.

Finding 16: Accounting System

The State's used two separate accounting systems to record financial activities. Thus the State's accounting system was maintained in a manner that did not track and was not compatible with the State's unified budget to facilitate monitoring of expenditures.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to design and implement an accounting system that tracks and is compatible with the State's unified budget to facilitate monitoring of expenditures. The OPA further recommends that this be the only accounting system used to record the State's financial activities.

Finding 17: Petty Cash

The State operated a Petty Cash Fund without essential policies and procedures governing its operation such as amount of the fund, method of replenishment, documentation requirements, petty cash limits on purchases, etc.

Recommendation

The OPA recommends that the Governor establish policies and procedures governing the operation of the Petty Cash Fund to include such policies as amount of the petty cash fund, method of replenishment, invoices/receipts requirements, limits on petty cash purchases, etc.

Finding 18: Personnel/Payroll

The audit revealed that the personnel system for Ngatpang State Milkfish Farm employees was inadequate. Specifically, the audit found that the employees had not filled out employment applications and were not employed pursuant to employment contracts, that no personnel action forms were completed for employees, etc.

Recommendation

The OPA recommends that the management of the Milkfish Farm establish a personnel system for its employees that would include such policies as employment applications, personnel contracts, and personnel actions for each employee.

Finding 19: Performance Reports

The audit revealed that the Ngatpang State Government failed to timely submit annual performance reports and thus did not comply with RPPL No. 6-11.

Recommendation

The OPA recommends that the Governor ensure that the State complies with the reporting requirements of RPPL No. 6-11 as amended by RPPL No. 7-7.

Finding 20: Local Noncompliance/Prior Year Findings

Ngatpang State failed to take corrective action to implement audit findings and recommendations contained in the Office of the Public Auditor's previous audit report.

Recommendation

The OPA recommends that the Governor comply with 5 PNCA §401 by taking affirmative action to implement audit findings and recommendations contained in the OPA's previous audit report.

Finally, Office of the Public Auditor would like to thank the staff and management of Ngatpang State Government for the professional courtesy and cooperation extended to us during the audit.

Sincerely,



Satrunino Tewid
Public Auditor

BACKGROUND

Ngatpang State is one of the sixteen (16) states of the Republic of Palau and is organized and structured under Article XI, Section 1 of the ROP Constitution and Article 1, Section 1 of the Constitution of Ngatpang State. The State Constitution was amended and adopted on May 28th, 2006. The major sections of the State Constitution relating to the establishment of the Office of the Governor, the Legislature, Ngaimis, and Ngatpang State Treasury are summarized below.

The Ngatpang State Legislature is a unicameral body with nine (9) members elected to four-year terms. The members are elected at large in a general or special election by the majority of the registered voters of Ngatpang State who vote in the election. No member of the State Legislature may hold any title of a chief in the State of Ngatpang. The presiding officers of Ngatpang State Legislature are the speaker, vice speaker, and floor leader.

The Ngaimis is a traditional council of chiefs composed of the ten (10) traditional chiefs of Ngatpang State. Rebelekuul is the head of State and is the first ranking chief of the Ngaimis. The members of the Ngaimis and their traditional titles appear below in the order of their traditional ranks.

- | | |
|--------------|------------------------------|
| 1. Rebelkuul | 6. Ucheldikes |
| 2. Rekemesik | 7. Rideb |
| 3. Secheuas | 8. Bedul |
| 4. Rubeang | 9. Madrasikos |
| 5. Rechiuang | 10. Madrainglai (Madraketom) |

All traditional powers of the State of Ngatpang are vested in Ngaimis.

The executive power in Ngatpang State is vested in the executive branch of Ngatpang State. The Governor is the chief executive of the State Government. The Governor is elected by the majority of the registered voters of Ngatpang State for a term of four (4) years and for not more than two (2) consecutive terms.

The Ngatpang State Constitution under Article XII, Section 1, states: "There shall be a state treasury into which all revenues derived from taxes or other sources shall be deposited. Funds may only be withdrawn from the state treasury pursuant to law." Similarly, Article XII, Section 1 of the Constitution of the Republic of Palau provides in pertinent part: "There shall be . . . a state treasury for each of the states. All revenues derived from taxes or other sources shall be deposited in the appropriate treasury. No funds shall be withdrawn from any treasury except by law."

The State Constitution requires that the salaries of the members of the State Legislature, Ngaimis, and the Governor be established by law; however, the salaries of the members of the State Legislature and the Governor may not be increased during their term in office.

On March 7, 2011, the former President of the Republic of Palau, the Honorable Johnson Toribiong, executed Administrative Order No. 290 appointing the Ministry of State ("MOS") as a custodian government for the State of Ngatpang, due to the absence of a legitimately elected State Government.

The MOS served in this capacity until the Palau Supreme Court reinstated its elected leadership in December 2012.

OBJECTIVE, SCOPE AND METHODOLOGY

The objective of the audit is to determine whether (1) expenditures were incurred in accordance with national and state government laws and regulations, (2) cash receipts were properly deposited into the state treasury, (3) expenditures and cash receipts were supported by adequate documentation, (4) earmarked CIP grants were expended for purposes for which they were earmarked, and (5) the state has established proper internal controls to ensure that its properties are properly safeguarded and its transactions properly recorded.

The audit covered the period from October 1, 2007 through September 30, 2013. 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 OPA conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The Public Auditing Act of 1985 expressly empowers the Office of the Public Auditor to 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 the audit objective, the OPA reviewed accounting records and other documents maintained at the office of Ngatpang State, including budgetary laws, other relevant laws and regulations, and records of the milkfish operations. The OPA also conducted on-site inspection of the State's fixed assets and projects. In performing the review, the OPA also conducted expenditures testing of the State's accounting system and procedures to assess the adequacy of the State's system of internal controls. In addition, the OPA examined relevant sections of the ROP's Unified Budget Acts and other applicable laws and regulations, interviewed appropriate state officials and reviewed relevant accounting records maintained at the Bureau of National Treasury.

PRIOR AUDIT COVERAGE

The most recent audit of the State was completed for fiscal year 2004 by the Office of the Public Auditor. Since then, there have not been any audits conducted by the OPA or private accounting firms covering the operations of the state.

FINDINGS

Finding 1: Unsupported Withdrawals

When closing a bank account and transferring the balance to another State account, documentation should be retained to support and evidence the transfer of funds.

In fiscal year 2009, the Ngatpang State Government closed its Bank of Hawaii general operations checking account and withdrew the remaining balance of \$3,261.11 without any supporting documents to show the account(s) into which the money was deposited or how it was used.

Ngatpang State Government did not ensure that proper supporting documents were maintained and filed to support the closure of the account, the transfer of funds, or how the money was used.

Question costs of \$3,261.11 exist as a result of this condition.

Recommendation

We recommend that the Ngatpang State Treasury obtain and maintain bank documents in its files to support the closure of bank accounts and transfer of balances to another account. In addition, we recommend that the Attorney General or the Interim Special Prosecutor investigate the closure of the above account and the disposition of the balance therefrom for possible legal action.

***Auditee's Response:** A. Resolution No. 1-09-35 authorizes Acting Speaker Siles Ngiraremiang and Acting Governor Takemura Erungel to close Accounts in Bank of Hawaii and bring the money to Bank of Guam. Bank of Guam new Account opened on April 3, 2009. Attached herewith supporting documents are: Resolution No. 1-09-35; Closing Bank Statement of April 17, 2009 for BOH Account No. 0037-038121 in the amount of \$190.99; a Bank of Guam Statement as of April 30, 2009 showing a deposit amount of \$3,452.10, the total of both closed accounts in BOH on April 17, 2009.*

B. Ngatpang State Government has prepared an Accounting, Audit and Financial Management Policy to implement for FY 2015 and the years to follow for the consistency of the activities and office documentation to follow:

1. Transfer and Closure

- a. The Ngatpang State Government will keep all funds available in a bank defined as local. "Local" is defined as having a physical presence for customer service within service area (Palau).*
- b. The Ngatpang State Treasurer/Controller will obtain and maintain in files all documents to support activities in Ngatpang State Government bank accounts.*
- c. When closing a bank account for Ngatpang State Government, the Governor will obtain an approval from Ngatpang State Legislature through a resolution.*
- d. Ngatpang State treasurer/controller will ensure that all documentation for closure of an account is obtained, maintained and kept in file to show closure of bank accounts. This includes a resolution authorizing closure, bank statement that reflects the closure, and a deposit slip to show the transferring from one bank to another.*
- e. All bank statements from the closed bank accounts should be kept in file and the documentation from the new opened bank account.*

f. Attachment: (Letter of Request from Acting Governor to BOG)

OPA's Comments: The OPA needs the source or primary documents for the closure of Bank of Hawaii account and the opening of the Bank of Guam account into which the money was transferred. Notwithstanding, the OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies; however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 2: Unsupported Reimbursement

A sound system of internal controls dictates that disbursement of state funds should be evidenced by the proper supporting documents to justify expenditures, their recording and classification in the accounting system.

In the review of State accounts in fiscal year 2010, we noted that two (2) checks totaling \$2,075, No. 1501 for \$1,000 and No. 1036 for \$1,075, were disbursed to then Acting Governor without proper supporting documents. The payments were purportedly for reimbursement to the Acting Governor purportedly for personal funds that he lent to the State in 2009 to purchase milkfish feed because the State had insufficient funds. The State, however, failed to provide supporting documents to evidence the receipt of the loan proceeds, the State account into which the money was deposited, or any loan agreement or other legal instrument that memorialized the terms and conditions of the transaction. The only supporting document provided was a withdrawal slip for a savings account, which purportedly was the Acting Governor's account. The withdrawal slip, dated December 23, 2009, was in the amount of \$2,075.

Thus, the State failed to ensure that loans were properly documented to support subsequent repayment of the loans.

As a result, we were unable to substantiate that the State was the recipient of or benefited from this loan from the Acting Governor.

Recommendation

We recommend that the Governor direct the State Treasurer to be more stringent in disbursing State funds by ensuring that disbursements contain the proper supporting documents. In this instance, documents such as a receipt, deposit slip, and a loan agreement should have been obtained and filed to support subsequent repayment of the purported loan.

Auditee's Response: *We noted that there was no proper process and proper supporting documents such as resolution to authorize this loan, and no agreement between Governor Takemura and the Ngatpang State Government. I have directed the NSG Accountant to be more stringent in disbursing Ngatpang State funds and to make sure that proper supporting documentation is properly filed and kept especially loan agreement and payment.*

- A. *Ngatpang State Government has prepared an Accounting, Audit and Financial Management Policy to comply with ROP law & Ngatpang State law to make sure that an approval to finance state projects is obtained:*
- B. *Ngatpang State Loan Agreement:*
 - 1. *In the case of borrowing money to finances state project, Ngatpang State will enter into an agreement, after approval from Olbiil Era Kelulau and Ngatpang State Legislature.*
 - 2. *Loan agreement should be approved by Ngatpang State Legislature and the Olbiil Era Kelulau.*
 - 3. *Loan agreement should include approval from NSL through a Resolution*
 - 4. *Loan agreement should include loan payment, interest, etc.*
 - 5. *All other supporting documents such as receipts, deposit slips should be filed and maintained to support the repayment of the purported loan.*
- C. *Ngatpang State Treasurer/Controller will ensure that all loan documents are maintained, filed and kept to support the transactions.*

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 3: Competitive Bidding

40 PNCA § 625 (b) requires that any procurement by a State Government of \$5,000 or more must be subject to competitive bidding.

The State did not follow competitive bidding procedures when procuring milkfish feeds, an automobile, a boat engine, and supplies and materials for the renovation of the 2nd floor of the Legislative Chamber.

This condition was caused by a lack of adequate controls to ensure compliance with the ROP Procurement Law and Regulations.

Due to lack of competitive bidding, the OPA questions \$260,382.43 and \$83,103.94 of procurements conducted during the period from fiscal years 2008 to 2011 and fiscal years 2012 to 2013, respectively. Furthermore, as a result of the lack competitive bidding, we were unable to assure ourselves that the State obtained the lowest prices or best quality products for the monies it paid for the goods and services.

Recommendation

We recommend that the Governor direct the State Treasury to comply with the ROP's Procurement Law and Regulations by ensuring that State procurements greater than or equal to \$5,000 are subject to competitive bidding.

Auditee's Response: *Ngatpang State was trying to comply with the procurement law and its regulations. Ngatpang State was advised by the Director of Bureau of Marine Resource of the National Government that milkfish fries can only be ordered in Taiwan due to the fact that Taiwan has not been found with pathogen. We admit that we did not bid as this was the only place we could order fish fries from. The Procedures as to bidding from outside of Palau was not known to us. We will comply with ROP procurement Act.*

- A. The Ngatpang State Government in FY 2011 and FY 2012 was under the caretaker of the Ministry of State. Boat engine for the Ngatpang State Marine Sanctuary, and the Pajero, the Service car for the Interim Governor or the Caretaker was purchased under the Ministry of State. We were told that competitive bidding for the National Government is \$10,000.00. Both Boat engine and the Pajero, bought at different time were below \$10,000.00.*
- B. Supplies and materials for the renovation of the Legislature Chamber is not a one invoice. We did not bid it because we were only charging on materials and the Ngatpang State carpenter and other employees will do the renovation. Due to the closure of Ngatpang State Government and the freezing of its bank accounts, the supplies and materials for the renovation was accumulated until a new operational account was opened under the Ministry of State.*
- C. In FY 2014, a Procurement Officer has already been appointed and is in charge of any procurement and disbursement activities and to make sure that any or program procuring \$5,000.00 and over are going through competitive bidding process to follow Procurement Process law.*
- D. The State Government of Ngatpang has directed the NSG Accountant to make sure to comply with the procurement law on competitive bidding before any disbursement is made.*
- E. Ngatpang State Government is already complying with ROP RPPL No. 3-54 Section 25 for FY 2014.*

OPA's Comments: Ngatpang State should have consulted the Procurement Officer for the purchase of goods and services, not the Director of Bureau of Marine Resources, when it encountered the problem with the procurement of milkfish fries.

- A. Although at the time the MOS was serving as caretaker for the State Government, the funds in question were Ngatpang State block grants and therefore were subject to the competitive bidding threshold of \$5,000 or greater. Therefore, the boat engine and Pajero vehicle should have been let out to competitive bidding in accordance with the ROP Procurement Law and Regulations.*
- B. The procurement of supplies and materials for the Legislative chamber was undertaken over a period of time. Collectively, the total of the procurement exceeded \$5,000 and therefore should have been let out to competitive bidding. The labor, however, was performed in-house and therefore the costs involved were not subject to the bidding requirements, even if the total of those costs equaled or exceeded \$5,000.*

Finding 4: Open Fuel Charge Account

The use of an “open” fuel charge account should contain the proper controls to ensure that fuel requisitions are properly authorized and justified as to official purpose, that the person and equipment receiving the fuel are properly identified, and that the person receiving fuel signs the invoices. In addition, certification of funds availability should be executed prior to the opening of the account.

During the audit the OPA found that the Ngatpang State operated an “open” fuel charge account to purchase fuel for the State. Because the State did not use a “Fuel Requisition” form or impose other control measures, we found numerous problems with the charge account including lack of approval for obtaining fuel, no justification as to official purpose, no identification of equipment or persons getting fuel, etc. In addition, there was no evidence of certification of funds availability prior to the operation of the account.

This condition was apparently caused by the State’s failure to establish and enforce controls over the use of the open fuel charge account.

The effect of this failure is that fuel may have been charged to the State’s open fuel charge account for unofficial purposes. In addition, without the necessary controls in place, the account may be readily abused without timely detection.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to implement and enforce the use of “Fuel Requisition” forms. Every fuel purchase should be accompanied by a Fuel Requisition form approved by an authorized official such as the Governor and include the official purpose for which the purchase is being made. The Fuel Requisition form should identify the equipment by license plate number and the person receiving the fuel; that person should be required to sign the invoice. In addition, the Governor should direct the State Treasurer to be more diligent in reviewing charge account billings to ensure that only those charges properly authorized, justified, and documented are processed and paid. Moreover, the Governor should consider alternative methods of obtaining fuel on credit; an “open” charge account is vulnerable to manipulation and abuse and increases the cost of operations. Before creating any credit account for fuel or other goods, the Governor should require that a purchase requisition be processed showing the proposed amount of the line of credit and certification of funds availability for this amount.

***Auditee’s Response:** A. Ngatpang State in FY 2014 has already started using Fuel Requisition Forms, even the forms have been improved to comply with recommendations.*

B. Ngatpang State has prepared an Accounting, Audit and Financial Management Policy to implement for FY 2014-2015 for the consistency of the activities and Office documentation to follow:

- 1. Fuel Requisition Forms shall be used in order to receive fuel.*
- 2. Justification for official use and purpose shall be obtained from Procurement Officer*
- 3. Identification of the equipment (Name of equipment or vehicle, plate number, etc.)*
- 4. Identify the person receiving fuel (name of recipient). Person receiving fuel should sign the invoice.*

5. *Requisition should be approved by the Budget Officer or Accountant for availability of funds or Budget.*
6. *Fuel Requisition Form needs to be approved by an authorized official. (e.g. Governor)*
- C. *The Accountant has been directed to implement and enforce the controls and use of open fuel charge and Requisition Forms for open fuel charge account should comply with the policy stated herein. She is also directed to be more attentive in reviewing the charge account billings to ensure that only those that are properly authorized, justified, and documented are processed and paid.*
- D. *Moreover, the Governor shall mandate the requirement of purchase requisition be processed with the amount of the proposed line of credit and certification of funds availability for the purchase.*

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation. In particular, the controls over the "open" fuel charge account should be enforced and monitored to ensure it operates in accordance with management's established policies and procedures.

Finding 5: Loan

Article XI, Section 4 of the ROP Constitution states: "Subject to the approval of the Olbiil Era Kelulau, the state legislatures shall have the power to borrow money to finance public programs or to settle public debt." Article IV, Section 17(b) of the Ngatpang State Constitution similarly empowers the Legislature: "[t]o borrow money on credit of the State Government to finance public projects." A sound system of internal controls requires that relevant loan agreements and related documents should be filed and used to monitor the terms, conditions and activities of the loan such as interest rates and loan payments to ensure that the interests of the State are protected and the obligations of the State met.

The audit revealed that Ngatpang State obtained a \$10,000 loan from a local business to finance the Milkfish Farm Project without obtaining prior approval from the OEK. In addition, as noted under Finding 2, the State earlier borrowed money from the Acting Governor to finance the same project. With respect to the constitutional requirements set forth above, we were not provided documentation to show that the OEK or the State Legislature approved the loans or appropriated funds for the repayment of the loans. A closer review of the loans revealed that the State obtained them without any written loan agreement spelling out the terms and conditions of the loans such as the interest rate and repayment schedule and amounts. Such details are essential to monitor the loans and their repayment and to protect the interests of the State.

This condition was apparently caused by lack of awareness by State officials of the requirements of the ROP and State Constitutions governing the authority of the State to use debt financing to fund State projects. In addition, the State did not ensure that the loans were memorialized in written loan agreements.

As a result, Ngatpang State may have violated the ROP and Ngatpang State Constitutions by obtaining loans without prior approval of the OEK and the State legislature. In addition, without loan agreements, the State lacked written contracts spelling out its rights and obligations under the loans.

Recommendation

We recommend that Ngatpang State seek and receive approval from the OEK and the State Legislature prior to obtaining loans to finance public projects or programs. In addition, when obtaining a loan, the State should enter into a loan agreement spelling out its rights and obligations arising from the loan. Moreover, elected and appointed State officials should become familiar with the ROP and Ngatpang State Constitutions and laws to ensure that State operations are administered in accordance with their requirements.

***Auditee's Response:** A. Ngatpang State Government, under the administration of the then Acting Governor Takemura Erungel obtained this loan for the purpose of Ngatpang State Milkfish Project. Unfortunately this State official may have not been aware of the requirements of the Republic of Palau and the State of Ngatpang's constitution that obtaining a loan requires an approval from the Olbiil Era Kelulau and the Ngatpang State Legislature.*

B. As Ngatpang State has also violated the same in Finding No. 2, Ngatpang State will comply and has lined up for improvement a policy when obtaining a loan to fund the State's project. (Refer to Finding 2).

a. Ngatpang State Government has prepared an Accounting, Audit and Financial Management Policy to comply with ROP law & Ngatpang State law to make sure that an approval to finance state projects is obtained:

b. Ngatpang State Loan Agreement:

c. Loan agreement should be approved by Ngatpang State Legislature and the Olbiil Era Kelulau.

d. Loan agreement should include approval from NSL through a Resolution

e. Loan agreement should include loan payment, interest, etc.

f. All other supporting documents such as receipts, deposit slips should be filed and maintained to support the repayment of the purported loan.

g. Ngatpang State Treasurer/Comptroller will ensure that all loan documents are maintained, filled and kept to support the transactions.

C. Ngatpang State will make sure to obtain an approval from Ngatpang State Legislature and the Olbiil Era Kelulau when obtaining a loan to finance Ngatpang State Project or its Programs.

OPA Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 6: Audit Documentation

A sound system of internal controls dictates that all records and documentation that support financial transactions of the State be maintained and retained to enhance accountability and transparency in the use of public resources. In addition, the Public Auditing Act, 40 PNCA§ 280(a), requires that "all agencies shall enter into their public records sufficient information for a proper audit, and shall make the same available to the Public Auditor at his request".

During the audit, the OPA found that the State did not maintain adequate records and documents to support financial transactions in fiscal years 2008, 2009, and 2010. Records to support revenues and expenditures, cash, and other financial transactions were not maintained or filed. We found the following revenues (deposits) and expenditures lacked adequate supporting documents:

<i>Description</i>	<i>Amount</i>
Undocumented Deposits	\$ 569,985.20
Undocumented Wire Transfer Expenses	\$ 74,542.44
Undocumented Expenditures	\$ 13,025.40

Total Undocumented Financial Transactions: \$ 657,553.04

It appears that the State failed to monitor financial operations to ensure that proper records were maintained and filed to support revenues, expenditures, and other financial transactions.

As a result of the lack of documentation, we were unable to substantiate \$657, 553.04 of revenues and expenditures or to conduct audit procedures to substantiate cash balances at fiscal year's end. Moreover, the inability of the State to produce the records and documents to enable the OPA to conduct a proper audit violates 40 PNCA § 280(a). Finally, the lack of records, documents and accounting systems to keep track of revenues, expenditures, and other financial transactions negates the authority of the State Budget to establish and regulate levels of expenditures.

Recommendation

We recommend that Ngatpang State establish and maintain an accounting system with proper documentation to support the recording and classification of revenues, expenditures, cash, and other financial transactions of the State. As part of the accounting system, records should be maintained and filed in an orderly fashion to facilitate use by the State and, pursuant to 40 PNCA § 280(a), audits by the Office of the Public Auditor. In addition, a sound recordkeeping system is the foundation upon which the State budget is enacted to regulate and control levels of expenditures.

Auditee's Response: *A. A Policy for internal controls is in place to ensure that all records and documentation that supports financial transactions are retained and maintained. For FY 2014, Ngatpang State has established an accounting system with records to support the recording and classification of revenues, expenditures, cash and other financial transactions.*

B. Sometime in 2009 Ngatpang State through Acting Governor Takemura Erungel wrote and requested the Office of the Auditor to audit Ngatpang State Government after the termination of Ms. Marissa Lunaria, the then Ngatpang State Accountant. Ngatpang State Government regrets for hiring Ms. Lunaria when it found out that she did sabotage our accounting records, deleting all transactions in the system, confusing us in the way checks are written not in numerical sequence.

C. Ngatpang State Government has now an internal control system that all documentation be obtained, filed, and kept to enhance accountability and transparency of Ngatpang State funds.

- 1. All cash/check received through grants and other funding should be received, receipted, and deposited.*

2. *All wire transfers are to be documented, recorded and filed. The Treasurer/Accountant should maintain all records whether received or withdrawn.*
3. *Cash received are to be deposited in Ngatpang Treasury Account.*
4. *Ngatpang State will maintain and keep in files records and documentations of all transactions whether revenues, expenditures, cash, etc.*
5. *Ngatpang State Government has already started to document all transactions with classifications of revenues, expenditures, cash, and all other financial transactions for FY 2014.*

OPA Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 7: Deposit of Funds into State Treasury

As cited above, both the ROP and Ngatpang State Constitution require a state treasury into which all revenues from taxes or any other source must be deposited. Both Constitutions further mandate that funds may be withdrawn from the state treasury only when and as appropriated by the State Legislature.

The audit revealed that the State operated an aquaculture project (“Milkfish Farm”) and used \$9,558.63 of revenues to offset obligations to vendors with whom the Farm was doing business. The revenues stemmed from the sale of fish on credit to two (2) local businesses in 2012 and 2013, which were subsequently applied to offset obligations to these businesses. Pursuant to the constitutional requirements, the revenues should have been recorded in the State’s accounting records and then authorized and appropriated to pay the obligations.

It appears the State may not be aware of the constitutional requirements governing the deposit and appropriation of state funds.

As a result, Ngatpang State violated its Constitution and that of the ROP by bypassing the deposit of Milkfish Farm revenues into the State Treasury and, instead, using the proceeds from the sale of fish to offset its obligations. In addition, the revenues may not have been authorized and appropriated by the State Legislature. Moreover, the Milkfish Farm may not have recorded these sales as revenues in its accounting system.

Recommendations

We recommend that the Governor comply with the Ngatpang State and ROP Constitutions by depositing revenues from Milkfish Farm sales and other sources into the State Treasury. In addition, we recommend that all revenues be authorized and appropriated by the State Legislature before expenditure. If and when the State opts to use Milkfish Farm revenues to fund its operations, it should coordinate the process with the Milkfish Farm management to ensure that all relevant transactions including revenues and sales are properly recorded.

Auditee's Response: A. Ngatpang State Legislature passed a Resolution No. 1-10-45 authorizing the opening of an account for Ngatpang State Aquaculture Milk Fish Project. In the same manner, authorized the Ngatpang State Marine Resources Authority through NSPL No. 0602-13-01, and NSPL 3010-13-08 to transact business with the revenues collected verses expenses.

B. The Office of the Governor has already requested the NSMRA to make sure the Executive Director understands and transmits all revenues collected to the Ngatpang State Finance Department for verification, noted, and deposited, and to be properly recorded.

C. The Office of the Governor has taken the initial step to recommend to the NSMRA to submit their proposed budget for appropriation and authorization.

OPA's Comments: The Governor, the Legislature, and the Ngatpang State Marine Resources Authority ("NSMRA") need to collectively discuss and determine which Ngatpang State statute governs the operations of the Milkfish Farm and, accordingly, the Farm should operate pursuant to that law. If the Milkfish Farm is operating as Ngatpang State entity, revenues from sales of milkfish and other products should be deposited into the State Treasury and expenditures authorized and appropriated by the Legislature for purposes it deems appropriate. Clearly, the Legislature could decide that the revenue generated by the Milkfish Farm should be appropriated for the Farm's operations. If the Milkfish Farm is determined to be legally separate from the State, the Farm's revenues should be deposited into the Milkfish Farm account and used as the Farm management determines.

Finding 8: Fixed Assets

The State should establish a fixed asset accounting system to account for, monitor, and safeguard its fixed assets. A detailed fixed asset accounting system is essential to properly account for the acquisition and disposition of fixed assets. Policies and procedures are essential to identify State properties, to safeguard them against unauthorized use and to conduct periodic physical inventory.

The State lacks a fixed asset accounting system to account for the acquisition and disposal of fixed assets, including donated equipment. In addition, it lacks policies and procedures governing periodic inventory of fixed assets to determine their years of service, location and condition. Because of the absence of a fixed asset accounting system, the OPA was unable to determine whether State properties and equipment were properly accounted for and safeguarded.

The failure of the State to establish a fixed asset accounting system has resulted in the State's inability to effectively control and monitor its properties and equipment. Information such as equipment cost, years of service, location, and condition is not readily available for the State Government's decision making.

Recommendation

The OPA recommends that the Governor direct the State Treasurer to establish a system to account for fixed assets. The fixed asset accounting system should include the following:

- Procedures to record fixed asset acquisitions, which would include recording the acquisition date, description, cost, vendor, etc.;

- Procedures to record disposal of fixed assets; and
- Procedures to identify, monitor, and conduct annual inventory of fixed assets to determine their condition and location.

Auditee's Response: *A. We need to improve our Fixed Asset system and have come up with a policy to comply with FY 2015.*

B. Ngatpang State has prepared an Accounting, Audit and a Financial Management policy to improve our Fixed Asset System in the coming FY 2015 to follow:

Fixed Asset Policy

- 1. Custodian Officer will be the recipient of all the fixed assets or supplies/materials for inventory, use the log book to assign inventory number and assign person in charge to account the asset. To follow the procedure to identify, monitor and conduct annual inventory of fixed assets to determine their condition and location.*
- 2. Finance Officer will record fixed asset and do the list based on the Itemized Budget for reconciliation purposes and for future inventory. To follow the procedure to record fixed asset acquisitions, which includes the acquisition date, description, cost, vendor and etc.;*
- 3. Every month needs to print the list and do the inventory per department for monitoring purposes.*
- 4. Needs to do the Physical Inventory every quarter.*
- 5. Annual Inventory will be tagging and surveying some broken item for Balance Sheet and Auditing purposes. To follow the procedure to record disposal of fixed assets.*

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 9: Liabilities

A sound system of internal controls dictates that the State establishes a system to account for and keep track of its obligations.

During the audit we found that the State does not have a system in place to record and keep track of its obligations. Even though the State provided a list of obligations as of the end of the most recent fiscal year audited (September 30, 2013), the State had not implemented an accounts payable system to record and keeps track of its payables. As a result, the State had to rely on its vendors to provide a statement of its accounts. For example, according to the Treasurer, there were no accounts payable as of September 30, 2012, but we found \$6,824 of payments in fiscal year 2013 made on invoices dated before September 30, 2012.

It appears the State has no system to account for and keep track of its obligations.

As a result, the State is unable to effectively keep track of its obligations. The lack of an accounting system also affects the availability, timeliness, and accuracy of information for decision-making purposes. Moreover, financial statements prepared based on an inadequate accounting system are susceptible to misstatements.

Recommendation

We recommend that the Governor direct the State Finance office to establish a system to account for, monitor, and reconcile the State's obligations. All credit purchases and payments on account should be properly recorded and reconciled. Such a system would enable the State to maintain timely and accurate information on State obligations for decision-making purposes. In addition, the system would facilitate reconciliation of State records with vendor statements to ensure accuracy of obligations.

***Auditee's Response:** A. Ngatpang State was trying to pay invoices on a monthly basis and not to accumulate accounts payables at year end.*

B. The Governor has directed the Accountant/Controller to establish a system to account for and to keep track, to monitor and to reconcile the State's obligations. Ngatpang State will comply with all requirements on liabilities.

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 10: Bank Reconciliation

Effective cash management requires that monthly bank reconciliation be performed to reliably and accurately account for and monitor the State's cash activity. In addition, records should be maintained for all state accounts, both active and inactive, to evidence closure of accounts and disposition of balances therefrom.

The audit showed that Ngatpang State Government did not consistently perform monthly bank reconciliations for its accounts. Timely, *i.e.* monthly, reconciliation is especially critical to ensure the accuracy of bank account balances when, as here, the State maintained six (6) separate checking accounts. In addition, the State did not provide the OPA with records for Acct. #0037-038121, which was closed in April 2009; thus we were unable to determine the balance upon closure and the disposition of the balance, if any.

It appears that the State was not diligent in performing monthly bank reconciliation on any of its checking accounts.

As a result, in the absence of bank reconciliation, neither the OPA nor the State could assure the balances of State's checking accounts. In addition, we were unable to determine whether Account #0037-038121 contained a cash balance upon closure and, if so, the disposition of the balance.

Recommendation

We recommend that the Governor direct the State Treasurer to perform monthly bank reconciliations on all State checking accounts. In addition, the Governor should reevaluate the need to operate six (6) checking accounts and consider consolidating unnecessary accounts to reduce costs and workload.

Auditee's Response: *A. Ngatpang State encountered a situation where all documents for CIP files, check copies, receipt books, and even the transaction in the Quick Books were sabotaged.*

B. Unfortunately Ngatpang State was not aware that the State accountant then, Marissa Lunaria, has already destroyed all files. The then Acting Governor Erungel after terminating her, found out what has been done to the files and records of Ngatpang State Government. He requested the Office of the Public Auditor to perform an audit, but Public Auditor could not finalize because lot of records were missing, check copies on this CIP account were missing, no bank statements found, no bank reconciliation found.

C. The Office of the Governor has written to Bank of Hawaii requesting for the bank statements missing in our files but have not received any reply.

D. The State's accountant/controller is currently performing monthly bank reconciliations for all the accounts under Ngatpang State Government.

E. From FY 2011-to present all bank statements are reconciled.

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation. In addition, periodic reviews should be conducted over the State's accounting system and records to ensure their proper maintenance and safeguarding.

Finding 11: Check Issuance in Numerical Sequence

To facilitate control and accountability over disbursement of funds, the State should issue checks in proper numerical sequence.

During our review, we found the State was operating several checking accounts in which checks were not issued in numerical sequence.

We were unable to determine why the State did not issue its checks in numerical sequence.

This failure to issue checks in numerical sequence added to the State's difficulties in performing bank reconciliations and keeping track of the sequence of check issuance.

Recommendation

We recommend that the Governor instruct the State Treasurer to issue checks in numerical sequence.

Auditee's Response: A. This is one of the problems the State saw during Marissa's time. Lot of checks were written, obtained signatures from the signatories but not received by the vendors.
B. As of present time, the accountant/controller is complying as the Governor has instructed the Accountant to issue checks in numerical order from FY 2011 to present all checks are in numerical sequence.

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 12: Block Grants

RPPL No. 8-40, Section 8 (State Block Grants), Subsection (12) states in part: "Until such time that Ngatpang State has validly elected and installed the officials of its executive and legislative branches of government, of the amount appropriated herein to Ngatpang State, the Ministry of State shall expend and account for the amount necessary to maintain state government operations. Of the amount appropriated herein to Ngatpang State government, thirty-five thousand (\$35,000) shall be expended or obligated for salary and functions of the Ngaimis and shall be disbursed by the Ministry of State in accordance with the laws and Constitution of Ngatpang State and the Republic of Palau." Moreover, as noted above, both the ROP and Ngatpang State Constitutions require that all revenues derived from taxes or other sources must be deposited into the State Treasury and that all expenditures be made as appropriated by the State Legislature.

The audit found that National Treasury Check No. 334487 was issued on November 26, 2012 in the amount of \$22,297.87, payable to the first and/or second ranking chief of the Ngaimis. The check was deposited on November 27, 2012 into the account of the Ngaimis at a private bank, contrary to State law. In response to the OPA's inquiry dated December 11, 2013 regarding this check, the chiefs stated that the funds were still in the account with the principal and interest intact. Attachments to their response, including bank statements for the Ngaimis account, verified this assertion. The bank statements showed a balance in the account of \$22,353.08 as of October 3, 2013. It appears no expenditures were made from the account during the period up to October 3, 2013. Be that as it may, the funds should have been disbursed to Ngatpang State, deposited into Ngatpang State Treasury, and disbursed by the State Treasury to the Ngaimis pursuant to the ROP and Ngatpang State Constitutions. In addition, the disbursement of the \$22,297.87 block grant to the Ngaimis should have been executed at the direction of the Ministry of State, not Finance, in accordance with the mandate of RPPL No. 8-40, quoted above.

This condition was caused by the apparent unfamiliarity by State and National Treasury officials with the legal restrictions imposed by the ROP and Ngatpang State Constitutions and the mandates of RPPL No. 8-40.

As a result, the Ministry of Finance may have disbursed a significant portion of the Ngatpang State block grant to the Ngaimis contrary to the ROP and Ngatpang State Constitutions and RPPL No. 8-40.

In addition, maintaining a bank account outside of the State Treasury and depositing money from the State's block grant into that account may have violated the ROP and Ngatpang State Constitutions.

Recommendation

We recommend that the ROP Ministry of Finance disburse block grants in accordance with the Constitution of the Republic of Palau, those of the individual states, and other requirements imposed by law. In addition, the Governor should pursue legal action to recover the money that was illegally disbursed to the Ngaimis.

***Auditee's Response:** A. The Office of the governor has written to High chief Rebelkuul Felix Osilek requesting him to comply with the Ngatpang State Constitution and to release the amount of \$22,297.87 to Ngatpang State Government as it should be deposited into the State Treasury and to be expended by law.*

B. The Office of the Governor will seek legal action if this transaction does not materialize by October 7, 2014.

OPA's Comments: The OPA has learned that the State has taken action to recover the \$22,297.87 since the issuance of the Draft Report and the State's response.

Finding 13: Accounts Receivable

A sound system of internal control dictates that a recordkeeping system be established to account for and keep track of the State's accounts receivable. In addition, policies and procedures are essential to ensure that a process is in place to follow up on outstanding accounts to ensure their collection.

The audit revealed that, according to the State's accounting records, a total of \$8,245.08 in accounts receivable remained as of September 30, 2013. A further review showed that \$2,148 of the receivables related to employee salary advances dating back to 2011. The balance, \$6,097, is receivables for Milkfish sales on credit to various individuals and businesses. In addition, we found that the State has no policies and procedures in place to follow up on delinquent accounts for collection.

This condition is caused by a lack of policies and procedures for following up on outstanding accounts to ensure collection.

The uncertainty surrounding the collection of outstanding accounts means that the State's accounts receivable may be overstated. Moreover, without robust policies and procedures in place, these receivables and others that may follow in the normal course of business may continue to be delinquent, which could result in their collection becoming harder or contested over time.

Recommendation

We recommend that in addition to maintaining an accounts receivable system, the State establish policies and procedures for following up on outstanding accounts to ensure collection. The policies and procedures should be established for both the State and Milkfish operations.

Auditee's Response: A. Ngatpang State Government has prepared an Accounting, Audit and Financial Management Policy to establish an accounting system to track all receivables and for the collection of delinquent accounts to follows:

e. COLLECTIONS ON DELINQUENT ACCOUNTS (Accounts Receivables)

1. The accountant/controller will ensure that an account receivable system is in place to track all unpaid accounts.
2. Statements of unpaid accounts will be sent periodically
3. Ngatpang State Government may utilize outside collection agency if all past efforts to collect money due have been exhausted.
4. Ngatpang State Government has discretionary authority to submit delinquent debt (over 120 days) to a collection agency.

f. WRITE-OFF DELINQUENT DEBTS/CHARGES (Accounts Receivables)

1. Records must indicate that all efforts to obtain payment have been exhausted before decision is made to write off any debt.
2. The request for approval of a write-off must include a narrative of actions taken to collect and the rationale for the debt being considered uncollectable.

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 14: Cash Receipts/Revenues

A proper system of internal controls dictates the issuance of cash receipts to account for and support revenue collection, revenue classification by source on financial statements, and reconciliation of cash receipts to deposits.

The OPA's testing of cash receipts/revenues found that cash receipts were not consistently issued and reconciled to deposits. In addition, cash receipts were not filed with the corresponding bank-validated deposit slip to evidence revenue collections and their deposit. Moreover, there were no records of cash receipts for fiscal year 2008 to 2010 to facilitate a review.

This condition is caused by a lack of effort by the State to establish a system of cash receipts to document revenue collections and their deposit.

As a result, \$1,116,557 of collections tested during the period from 2008 to 2013 lacked cash receipts. Hence, we were unable to substantiate total revenue collections, their classifications and deposit during this period due to the lack of or inadequate cash receipts and related deposit tickets.

Recommendation

We recommend that the Governor instruct the State Treasurer to issue cash receipts to evidence all revenue collections, including Milkfish operations. In addition, cash receipts should be reconciled to collections on a daily basis, and should be reconciled to deposits when a deposit is made. Finally, cash receipts are essential documents to enable the State to classify revenues by source in its accounting system and on financial statements.

Auditee's Response: *A. Ngatpang State Government has prepared an Accounting, Audit and Financial Management Policy to establish an accounting system to track all the State revenues:*

CASH RECEIPTS

1. *Ngatpang State Collection of Cash: an assigned staff from the billing and Collection Unit performs daily verification of collections, consolidate cash, prepare daily transmittal report to the Ngatpang State Treasury; receipts collection, prepare deposit slip, prepare daily cash transmittal reports and deposit funds on the next working day. The bank's stamped duplicate deposit slip is attached to the remittance documentation. The daily cash transmittal report and deposit receipt from the bank is then submitted to the Governor to note and submitted to the accountant to post and file.*
2. *All other cash/check received through grants and other funding, should be received, receipted, and deposited.*
3. *Wire transfers are to be documented, recorded, and filed. The controller/accountant should maintain all records whether received or withdrawn.*
4. *Cash received should be deposited in Ngatpang State Treasury Bank Account.*

Requirements for depositing Revenues and forms to be needed:

1. **Form: Deposit History Form** – *Gather all the receipts and prepare for reconciliation by date, receipt number in sequence, name of customer, purpose of payment and amount. With 3 signatures below; Prepare by: name of person preparing the deposit history, Deposit by: person who deposit the money and Noted by: Authorized person/or Governor for verification of the deposit.*
2. **Deposit Slip** – *Gather all the receipt and deposit the money based on the deposit history not more than a week collection.*
3. *Right after deposit forward all the copy to Finance Officer the same day for necessary reporting and posting to Accounting System.*
4. *Fill and prepare for Audit Reporting.*

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation.

Finding 15: Milkfish Farm Sales

To facilitate proper control over and accountability for the State’s Milkfish Farm sales, cash receipts and invoices should be reconciled to total sales at the end of the day. In addition, cash receipts should be issued in proper numerical sequence, reconciled to deposits and posted to the sales journal.

The audit revealed that internal controls and accounting over Milkfish sales were inadequate. Invoices for credit sales and cash receipts for cash sales were not reconciled to total sales at the end of daily operations. Cash receipts were not issued in proper numerical sequence and recorded, making reconciliation even more essential, and cash receipts were not consistently posted to the sales journal. Moreover, the OPA found no evidence that cash receipts were reconciled to actual collections and deposits. The chart below, listing invoices issued by the Milkfish Farm since its inception in March 2010 through September 30, 2013, shows that collections consistently were not posted to the sales journal.

Schedule of Aquaculture Farm Invoices

Beginning Series	Ending Series	Date Begin	Date End	Reconciled To Cash Receipts
0194	0260	4/5/2010	6/28/2010	Not posted to Sales Journal
0261	0314	7/4/2010	9/30/2010	Not posted to Sales Journal
0315	0350	10/4/2010	11/22/2010	Not posted to Sales Journal
0351	0400	11/22/2010	1/17/2011	Not posted to Sales Journal
0401	0450	1/17/2011	3/28/2011	Not posted to Sales Journal
0451	500	3/30/2011	5/15/2011	Not posted to Sales Journal
0501	0550	5/16/2011	6/18/2011	Not posted to Sales Journal
0551	600	6/18/2011	7/13/2011	Not posted to Sales Journal
601	650	7/14/2011	8/5/2011	Not posted to Sales Journal
0651	0700	8/8/2011	9/2/2011	Not posted to Sales Journal
0701	0750	9/2/2011	10/2/2011	Not posted to Sales Journal
0751	0800	10/2/2011	11/5/2011	Not posted to Sales Journal
0801	0850	11/7/2011	12/22/2011	Not posted to Sales Journal
0851	0900	12/22/2011	2/6/2012	Not posted to Sales Journal
0901	0950	1/20/2012	4/26/2012	Not posted to Sales Journal
0951	1000	4/30/2012	6/25/2012	Not posted to Sales Journal
1001	1050	6/23/2012	8/27/2012	Not posted to Sales Journal
1051	1150	8/27/2012	10/29/2012	Not posted to Sales Journal
1101	1150	10/30/2012	1/10/2013	Not posted to Sales Journal
1151	1200	1/10/2013	5/13/2013	Not posted to Sales Journal
1201	1230	5/13/2013	9/30/2013	Not posted to Sales Journal

This condition is caused by the failure by the State and the Milkfish Farm’s management to establish the essential controls to ensure that total sales were reconciled to invoices or receipts issued, that cash receipts were issued in proper numerical sequence, posted to the sales journal, and reconciled to collections and deposits.

As a result, we were unable to substantiate that all fish sales were accounted for and properly deposited. In addition, these conditions -- lack of reconciliation of sales, cash receipts not properly recorded, no reconciliation of cash receipts to deposits, etc. -- create an environment where fraud is likely to occur.

Recommendation

The OPA recommends that the Board of Directors of Ngatpang State Marine Resources Authority direct the Executive Director of the Milkfish Farm to obtain the proper expertise to advise and assist in establishing an accounting system and related controls and procedures for the operation of the Farm so that sales and related operations are properly documented and transactions accounted for.

***Auditee's Response:** To follow documents for reconciliation please extend until Friday. c/o Ma. Ellien Mangeron, State Accountant.*

Finding 16: Accounting System

A properly designed and operating accounting system is essential to record and account for the financial activities of the State, to keep track of budget versus expenditures, to provide accurate and timely information for decision making, and to comply with reporting obligations imposed by law and other mechanisms.

The audit of Ngatpang State Government for the six-year period ending September 30, 2013 revealed that the State was recording its financial activities into two (2) different QuickBooks Accounting Systems. This exposes the system to unnecessary risks of inaccuracies and errors caused by the recording of transactions in one system and not the other. In addition, the dual system unnecessarily increases costs of maintenance and the level of reconciliation required to ensure that the two systems agree, of which we did not see any evidence. Moreover, the format of the accounting system for classifying expenditures did not parallel the State Budget.

We were unable to determine the reasoning behind the State using the two (2) separate QuickBooks Accounting systems to record its financial transactions.

As a result, the State is unable to effectively monitor the level of expenditures for each budget activity to ensure that expenditures do not exceed the budget. In addition, without a reliable system to record and keep track of expenditures, the accuracy of financial reports to the legislature or other recipients becomes questionable.

Recommendation

We recommend that the Governor direct the State Treasurer to use only one (1) system to record the financial transactions of the State. In addition, the Governor should obtain expert advice on the format of the accounting system to ensure that the format, particularly for recording expenditures, parallels that of the State Budget.

***Auditee's Response:** A. Ngatpang State Government was under supervision of Interim Governor on FY 2011-12 and we received the direction to separate the Accounting System of State based on the letter communication attached:*

- 1. Office of the Public Auditor Serial#11-121 (Acting Public Auditor – Director of BDA)*
- 2. Bureau of Domestic Affairs Serial#BDA11-026 (Dir. of BDA to Office of the President)*

OPA's Comments: Neither communication from the Office of the Public Auditor (Serial # 11-121) or from the Bureau of Domestic Affairs directs the State to use dual accounting systems. On the contrary, both express concern that the State was not properly recording its financial transactions, *i.e.*, cash receipts and disbursements,

Finding 17: Petty Cash

A proper system of internal control dictates that the operation of a petty cash fund be governed by policies and procedures such as authorized limit of the petty cash fund, method of replenishment, documentation requirements, restrictions on purchases, etc.

The audit revealed that Ngatpang State operated its Petty Cash Fund without any policies and procedures to regulate its use. There were no policies and procedures on the authorized limit of the fund, method for replenishment, documentation requirements such as invoices or receipts, prohibited and allowable purchases, etc. In addition, there was no reconciliation at any time to determine if the total of invoices/receipts plus the balance of cash equaled the amount of petty cash.

The table below illustrates the breakdown of funds disbursed to the Petty Cash Fund from various State Accounts:

<i>Account Name</i>	<i>Fiscal Year (FY)</i>	<i>Total Petty Cash</i>
Ngatpang State Government* * State Operations Account under the Ministry of State as a custodial government	2011	-0-
	2012	-0-
	2013	<u>\$ 15,424.51</u>
	Total	\$ 15,424.51
Ngatpang State Government* * Original State Operation Account	2009	-0-
	2010	-0-
	2011	\$ 2,413.23
	2012	-0-
	2013	<u>-0-</u>
	Total	\$ 2,413.23
Ngatpang State Government* *Account for Aquaculture Farm	2010	\$ 354.72
	2011	\$ 4,092.95
	2012	\$ 3,278.67
	2013	<u>\$ 2,397.91</u>
	Total	\$ 10,124.25
Total Disbursements to Petty Cash Fund for the Six (6) year period ended September 30, 2013		<u>\$ 27,961.99</u>

In addition, the State did not use purchase requisition forms or similar documents to show which person or department was requesting petty cash and for what purpose, or to demonstrate official approval of the request. Moreover, because there were no restrictions on types of purchases, use of the fund was essentially at the discretion of the requestor. For example, we found purchases for food and drinks, supplies and materials, taxis, travel tax, tools and equipment, representation and contingency funds, and others for which there was no supporting documentation.

Moreover, on several occasions we noted that petty cash was issued to a State official and the official used his personal debit card to make purchases on behalf of the State. During the period from June to September 2013 the official charged a total of \$8,715 on his personal debit card for purchases for the State. And perhaps because of our inquiry into this matter, the State official on September 27, 2013 returned \$5,000 to the State Government, which was deposited into Ngatpang State account.

This condition is caused by the State's failure to establish policies and procedures governing the operation of its Petty Cash Fund.

As a result, petty cash activities were unregulated, which created an atmosphere of loose controls and undocumented petty cash expenditures.

Recommendation

We recommend that the Governor establish policies and procedures governing the operation of the Petty Cash Fund. The policies and procedures should include establishing a petty cash authorized limit, approved methods for replenishing the fund, restrictions on types of purchases, requirements for supporting documents such as invoices and receipts, and periodic reconciliation of the fund. In addition, all revenue collections should be deposited into the State Treasury and replenishment of the Petty Cash Fund should be done by check, not collections. Lastly, we recommend the Office of Attorney General or the Interim Special Prosecutor further investigate the activities of the Petty Cash Fund and take appropriate action for any misconduct involving the use of public funds.

***Auditee's Response:** A. Ngatpang State Government has prepared an Accounting, Audit and Financial Management Policy for Petty cash:*

A. PETTY CASH

1. *Petty cash is limited to \$100.00 only.*
2. *Receipts or itemized slips are required for every disbursement. The accountant and the controller/procurement officer will be responsible for verification of receipts and cash.*
3. *Petty cash should be used for emergency only. It is not intended for purchases that can be made with designated suppliers. Procedures should follow the Ministry of Finance Petty Cash Policies.*
4. *Whenever a petty cash is used, a pre-numbered "**Petty Cash Requisition Form**" slip must be filled out. A completed slip will include date, the amount taken and returned, the cash category and the total spent. When a staff receives cash, he/she will sign on the "Received By" line of the petty cash log. Items purchased should be listed on the log. The controller/accountant will be responsible for the reconciliation and replenishment of the petty cash account.*
5. *This is for both NSMRA-Aquaculture Farm Project and Office of the Governor.*

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation. The Petty Cash Fund policies and procedures, in particular, should be enforced and monitored to ensure compliance.

Finding 18: Personnel/Payroll

A sound system of internal control dictates that the State maintains personnel files for each employee. At a minimum, these files should contain personnel action form(s), employment contract, employee evaluations, and related documents.

The audit revealed that the payroll system for Ngatpang State Milkfish Farm employees was inadequate. The employees lacked personnel files containing personnel action forms, employment contracts, and such other personnel documents. As such, we were unable to determine the authorized rate of pay for the employees and found instances where mandatory withholdings including income taxes, social security, pension, and national health insurance were not deducted from employees' pay.

These conditions existed because the State and the Farm's management failed to establish a payroll system for Milkfish Farm employees. In addition, the State may have failed to deduct social security and income taxes from these employees' pay in fiscal year 2008 and 2009.

As a result, we were unable to determine if the pay levels for the Milkfish Farm employees were properly authorized. In addition, failure to deduct social security and income taxes from employees' pay is a violation of ROP laws.

Recommendation

We recommend that the Board of Directors of the Ngatpang State Marine Resources Authority direct the Manager to establish a personnel system for the Farm's employees. As part of the personnel system, each employee should have a personnel file which contains, at a minimum, personnel action form(s), an employment contract, pay increment documents, and documentation of other personnel actions as applicable. In addition, the Manager should ensure that all payroll withholdings required by law are properly and timely executed.

***Auditee's Response:** A. Compliance with this Audit finding will start on FY 2014 based on their contract with the Requisition of Executive Director and sign by an Authorized Personnel/Governor/Acting Governor. Ngatpang State Marine Resource Authority – Aquaculture Farm, the Executive Director assumed that there is no need to comply with the Personnel Action since they are getting paid from the local revenues account, not from the National Government.*

OPA's Comments: Regardless of the source of funding for payroll, whether local revenues or block grants, payroll expenditures must be substantiated, transparent, and accounted for.

Finding 19: Performance Report

RPPL No. 6-11, Section 371, requires each agency to submit to the President, the OEK, and the Public Auditor a performance report “for the programs and services it administers or provides” no later than April 1st of each year. RPPL No. 7-7 changed the deadline to April 15th of each year.

The audit revealed that the Governor failed to submit the required reports on time or submitted them after the due date as follows:

<i>Fiscal Year</i>	<i>Required Submission Date</i>	<i>State’s Report Date of Submission</i>
2008	04/15/08	No Report Submitted to OPA
2009	04/15/09	No Report Submitted to OPA
2010	04/15/10	No Report Submitted to OPA
2011	04/15/11	No Report Submitted to OPA
2012	04/15/12	4/11/13
2013	04/15/13	02/21/14

The failure to submit the reports and their late submissions may be due to the problems with the State’s accounting system noted above.

The State’s failure to submit performance reports and its submission of reports after the statutory deadline constitutes non-compliance with the RPPL Nos. 6-11 as amended by RPPL No.7-7.

Recommendation

The OPA recommends that the Governor of Ngatpang State comply with the reporting requirements of RPPL No. 6-11 and as amended by RPPL No.7-7.

Auditee’s Response:

- A. The Acting Governor of Ngatpang State Government understand that Ngatpang State should comply for RPPL No. 6-11 Section 371 (for submission of Performance Report every 30th of April for the Fiscal Year ended)*
- B. Ngatpang State was not aware that Performance Report should be sent to OPA. Ngatpang State will comply with RPPL No. 6-11 Section 371.*
- C. Attached letter of transmittal from Acting Governor Francesca Otong.*

OPA’s Comments: The Governor should obtain a copy of RPPL No. 6-11 and related amendment and become familiar with the requirements; in particular, the requirements on the report recipients and the deadline for submitting the report, which is April 15 of each year.

Finding 20: Local Noncompliance/Prior Year Finding(s)

Ngatpang State should comply with 40 PNCA § 2201 by implementing the recommendations contained in the OPA's previous audit report.

Ngatpang State took no affirmative action to address the prior audit's findings and to implement the report's corresponding recommendations:

- Competitive Bidding
- Representation Fund

The cause of this condition appears to be the State's failure to give audit reports the level of attention required to implement corrective action.

As a result, some of the findings contained in this report are repeated from the prior audit.

Recommendation

The OPA recommends that the Governor prioritize corrective actions to address audit findings and implement recommendations contained in the OPA's previous audit report.

Auditee's Response:

1. *Competitive Bidding*
 - a. *We already follow the Procurement process for FY 2014.*
 - b. *Please refer to Draft State Policy; **ACCOUNTING, AUDIT AND FINANCIAL MANAGEMENT POLICIES***
2. **Representation Fund**
 - a. *Beginning FY 2014 we have an Itemized budget and representation funds and expending are accordingly.*
3. *Ngatpang State Treasurer/Accountant strictly monitoring the expenditure based on the Itemized Budget.*

OPA's Comments: The OPA is encouraged to see that Ngatpang State has taken the initiative to strengthen and improve its internal controls by preparing an Accounting, Audit and Financial Management Policy, which it plans to implement in Fiscal Year 2015. These policies, however, require management and area supervisors to periodically monitor and review to ensure their proper execution and operation. The "Draft" State Policy needs to be finalized and adopted by the State, communicated with the appropriate personnel to ensure its proper implementation and operation.



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

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

(Closed on Legal Holidays)