

Audited Project Financial Statements

Project Number: 42439
Loan Numbers: 3060, 3061
Period covered: 8 May 2014 to 30 September 2015

Palau: Koror–Airai Sanitation Project

Prepared by Palau Public Utilities Corporation

For the Asian Development Bank
Date received by ADB: 26 August 2016

The audited project financial statements are documents owned by the borrower. The views expressed herein do not necessarily represent those of ADB's Board of Directors, Management, or staff. These documents are made publicly available in accordance with ADB's Public Communications Policy 2011 and as agreed between ADB and the borrower's executing agency.

**REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
FINANCED BY ADB LOAN NO. 3060-PAL AND 3061-PAL (SF)**

**STATEMENT OF PROJECT ACCOUNT,
ADDITIONAL INFORMATION AND
INDEPENDENT AUDITORS' REPORT**

YEAR ENDED SEPTEMBER 30, 2015

REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
FINANCED BY ADB LOAN NO. 3060-PAL AND 3061-PAL (SF)

Year Ended September 30, 2015
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INDEPENDENT AUDITORS' REPORT

His Excellency Tommy Remengesau, Jr.
President
Republic of Palau:

Report on the Financial Statements

We have audited the accompanying financial statements of the Republic of Palau Koror-Airai Sanitation Project (the "Project") financed by Asian Development Bank ("ADB") Loan No.'s 3060-PAL and 3061-PAL (SF), which comprise the statement of project account for the year ended September 30, 2015, and the related notes to the financial statements. The Project is administered by the Palau Public Utilities Corporation ("PPUC"), which is a component unit of the Republic of Palau.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the cash basis of accounting; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the statement of project account for the year ended September 30, 2015 in accordance with the cash basis of accounting.

Reporting Entity

As discussed in Note 1 to the financial statements, the financial statements referred to above presents only the activities of the Project and are not intended to present fairly the financial position and results of operations of the Republic of Palau or the Palau Public Utilities Corporation in conformity with accounting principles generally accepted in the United States of America.

Basis of Accounting

We draw attention to Note 2 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprises the Project's basic financial statements. The Other Supplementary Information listed in the accompanying table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The Other Supplementary Information is the responsibility of PPUC's management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements itself, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Other Supplementary Information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated August 25, 2016 on our consideration of the PPUC's internal control over financial reporting and on our tests of its compliance with provisions of the Project agreement with the ADB, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the Project's internal control over financial reporting and compliance.



August 25, 2016

REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
FINANCED BY ADB LOAN NO. 3060-PAL AND 3061-PAL (SF)

Statement of Project Account
Year Ended September 30, 2015

	<u>Loan 3060-PAL</u>	<u>Loan 3061-PAL (SF)</u>
Receipts:		
Loan proceeds - Direct	\$ <u>538,847</u>	\$ <u>448,051</u>
Disbursements:		
Consultants	<u>538,847</u>	<u>448,051</u>
Net change in cash	-	-
Cash at beginning of year	<u>-</u>	<u>-</u>
Cash at end of year	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to statement of project account.

REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
FINANCED BY ADB LOAN NO. 3060-PAL AND 3061-PAL (SF)

Notes to Statement of Project Account
September 30, 2015

(1) Organization

On March 28, 2014, the Republic of Palau (ROP) entered into two loan agreements with the Asian Development Bank (ADB) (Loan Nos. 3060-PAL and 3061-PAL (SF)) in the amounts of \$26,900,000 and Special Drawing Rights 1,258,000 (approximately \$1,767,000 at September 30, 2015), respectively, for the purpose of funding the Koror-Airai Sanitation Project (the Project). The objective of the Project is to provide effective, efficient, and sustainable sanitation services to Koror and Airai areas of the ROP which is expected to be completed by 2022. The Project includes sewage collection, treatment and disposal systems, and consulting services to manage and implement these activities. The Palau Public Utilities Corporation (PPUC), a component unit of the ROP, is responsible for carrying out the Project.

The loans have a principal repayment period of 20 years and a grace period as defined in the loan agreements. The accumulated drawn amount from these loans is \$986,898 as of September 30, 2015. For the year ended September 30, 2015, finance charges of \$56,454 were incurred and recorded by PPUC.

The accompanying statement of project account is prepared for the year ended September 30, 2015 and includes only the activities of the Project.

(2) Summary of Significant Accounting Principles

Basis of Accounting

The Project uses the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The cash basis differs from accounting principles generally accepted in the United States of America primarily because receipts (revenues) are recognized when received rather than when earned and disbursements (expenses) are recognized when paid rather than when the obligation is incurred. Commitments are recorded separately from the accounting records and are not recorded in these financial statements. Payments for project expenditures have been made using the Direct Payments method following ADB's withdrawal application method.

Foreign Currencies

Transactions involving foreign currencies have been recorded in United States dollars using the rates of exchange ruling on the date of the transaction. No foreign currency adjustment was recorded for the year ended September 30, 2015.

(3) Compliance with Debt Covenants

PPUC is of the opinion that compliance with the applicable debt covenants has occurred.

REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
FINANCED BY ADB LOAN NO. 3060-PAL AND 3061-PAL (SF)

Cumulative Statement of Project Account
Period from Inception (May 8, 2014) through September 30, 2015

	<u>Cumulative</u>
Receipts:	
Loan proceeds - Direct	\$ <u>986,898</u>
Disbursements:	
Consultants	<u>986,898</u>
Net change in cash	-
Cash at beginning of period	<u>-</u>
Cash at end of period	<u>\$ -</u>

See Accompanying Independent Auditors' Report.

**REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
FINANCED BY ADB LOAN NO. 3060-PAL AND 3061-PAL (SF)**

Withdrawal Applications Submitted to Asian Development Bank
Period from Inception (May 8, 2014) through September 30, 2015

<u>W.A. No.</u>	<u>Application Date</u>	<u>Application Details</u>	<u>Direct Payment</u>
1	28-Oct-2014	Consultant's services - advance payment	\$ 400,000
2	2-Mar-2015	Consultant's services - Oct2014 to Dec2014	139,960
3	8-May-2015	Consultant's services - Jan2015 to Mar2015	114,147
4	12-Aug-2015	Consultant's services - Apr2015 to Jun2015	<u>332,791</u>
			<u>\$ 986,898</u>

See Accompanying Independent Auditors' Report.

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

His Excellency Tommy Remengesau, Jr.
President
Republic of Palau:

We have audited, 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, the financial statements of the Republic of Palau Koror-Airai Sanitation Project (the "Project") financed by Asian Development Bank ("ADB") Loan No.'s 3060-PAL and 3061-PAL (SF), which comprise the statement of project account for the year ended September 30, 2015, and the related notes to the financial statements, and have issued our report thereon dated August 25, 2016. The Project is administered by the Palau Public Utilities Corporation ("PPUC"), which is a component unit of the Republic of Palau.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Project's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Project's internal control. Accordingly, we do not express an opinion on the effectiveness of the Project's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a deficiency in internal control, described in the accompanying Schedule of Findings and Responses as item 2015-001 that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Project's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

PPUC's Response to Finding

PPUC's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Responses. PPUC's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Deloitte + Touche LLP".

August 25, 2016

REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
FINANCED BY ADB LOAN NO. 3060-PAL AND 3061-PAL (SF)

Schedule of Findings and Responses
Year Ended September 30, 2015

Finding No. 2015-001
Area: Record Maintenance

Criteria:

PPUC shall maintain, or cause to be maintained, records and accounts adequate to identify the items of expenditures financed out of the proceeds of the loans, to disclose the use thereof in the Project, to record the progress of the Project, and to reflect, in accordance with consistently maintained accounting principles, its operations and financial condition.

Condition:

PPUC maintained a schedule of Project expenditures and ADB loan withdrawals. However, they are not separately recorded in the general ledger. The Project expenditures and ADB Loans were recorded thru a proposed audit adjustment.

Cause:

Reconciliation and review between the Project accounts and general ledger accounts was not timely performed.

Effect:

Failure to maintain timely posting of transactions could result in a misstatement of the financial statements.

Recommendation:

PPUC should timely recognize Project expenditures and loan withdrawals in the general ledger.

Auditee Response and Corrective Action Plan: PPUC concurs with the findings and will implement the recommendation as stated.