

Audited Project Financial Statements

Project Number: 42439
Loan Numbers: 3060, 3061
Period covered: 1 October 2015 to 30 September 2016

Palau: Koror–Airai Sanitation Project

Prepared by Palau Public Utilities Corporation

For the Asian Development Bank
Date received by ADB: 3 July 2017

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

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

YEARS ENDED SEPTEMBER 30, 2016 and 2015

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

Years Ended September 30, 2016 and 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 statements of project account for the years ended September 30, 2016 and 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 audits. 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 statements of project account for the years ended September 30, 2016 and 2015 in accordance with the cash basis of accounting.

Use of Loan Proceeds

The loan proceeds have been used in all material respects in accordance with the conditions of the loan agreements and for purposes of the Project.

Compliance with Financial Covenants

PPUC complies with the financial covenants of the loan agreements as reflected in the accompanying statements of project account, except for compliance with the paragraph 14, Schedule 5 of the Loan Agreement No. 3061-PAL (SF), which states that “PPUC shall ensure that the Project is implemented on a full cost recovery basis and towards achieving this objective, shall ensure tariffs are set such that the total revenue from billed services for water and sewage are projected to be \$5.8 million by end of FY2014-2015”. Actual billed services for water and sewage totaled \$5.5 million at the end of FY2014-2015. Management informed us that PPUC’s achievement of a full cost recovery is now extended to FY2017-2018. Our opinion is not modified with respect to this matter.

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 June 30, 2017 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.

Deloitte & Touche LLP

June 30, 2017

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

Statements of Project Account
Years Ended September 30, 2016 and 2015

	2016	
	Loan 3060-PAL	Loan 3061-PAL (SF)
Receipts:		
Loan proceeds - Direct	\$ 1,078,794	\$ 831,435
Disbursements:		
Consultants	1,078,794	831,435
Net change in cash	-	-
Cash at beginning of year	-	-
Cash at end of year	\$ -	\$ -
	2015	
	Loan 3060-PAL	Loan 3061-PAL (SF)
Receipts:		
Loan proceeds - Direct	\$ 538,847	\$ 448,051
Disbursements:		
Consultants	538,847	448,051
Net change in cash	-	-
Cash at beginning of year	-	-
Cash at end of year	\$ -	\$ -

See accompanying notes to statements of project account.

REPUBLIC OF PALAU
KOROR-AIRAI SANITATION PROJECT
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Notes to Statements of Project Account
September 30, 2016 and 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 \$1,759,000 at September 30, 2016), 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 \$1,910,229 and \$986,898 as of September 30, 2016 and 2015, respectively. For the years ended September 30, 2016 and 2015, finance charges of \$78,872 and \$56,454, respectively, were incurred and recorded by PPUC.

The accompanying statements of project account is prepared for the years ended September 30, 2016 and 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 years ended September 30, 2016 and 2015.

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, 2016

	<u>Cumulative</u>
Receipts:	
Loan proceeds - Direct	\$ <u>1,910,229</u>
Disbursements:	
Consultants	<u>1,910,229</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, 2016

<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	332,791
5	16-Nov-2015	Consultant's services - Jul2015 to Sept2015	398,516
6	25-Mar-2016	Consultant's services - Oct2015 to Dec2015	150,315
7	31-May-2016	Consultant's services - Jan2016 to Mar2016	118,584
8	17-Aug-2016	Consultant's services - Apr2016 to Jun2016	177,044
		Capitalized financing charges as of Sept2016	<u>78,872</u>
			<u>\$ 1,910,229</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, 2016, and the related notes to the financial statements, and have issued our report thereon dated June 30, 2017. 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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*.

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.



June 30, 2017

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

Unresolved Prior Year Findings
Year Ended September 30, 2016

There are no prior year findings unresolved as of September 30, 2016.