

Follow Up Audit Report No. FA 02-2019

Follow Up Audit Report on Lelu Town Government

A Report to the
Governor
and the
Legislature of
the State of Kosrae



Stoney S. Taulung
PUBLIC AUDITOR



GOVERNMENT OF KOSRAE
OFFICE OF THE PUBLIC AUDITOR
POST OFFICE BOX 847
KOSRAE, FEDERATED STATES OF MICRONESIA 96944
TELEPHONE: (691) 370-3766, FACSIMILE(691) 370-3443

December 30, 2019

The Honorable Governor, Carson Sigrah
The Honorable Speaker, Tulensa W. Palik
The Honorable Members, 12th Kosrae State Legislature
Kosrae State Government
Kosrae State, Federated States of Micronesia 96944

Re: Follow-Up Audit on Lelu Town Government

EXECUTIVE SUMMARY

We respectfully submit this Follow-Up Audit, FA 02-2019, related to PA 01-2018, a performance audit conducted on Lelu Town Government covering the period of FY 2017- February 28, 2018.

The objectives of the audit were to determine whether (1) Lelu Town Government cash balances are accurate and complete, 2) Lelu Town Government disbursements made during the period covered are valid, complete and accurate, and 3) Lelu Town Government cash receipts are complete, accurate, properly recorded and timely deposited. The status of each recommendation reviewed will be one of the following:

Implemented: Auditee fully implemented the recommendation, either as described in the report or in a manner that resolved the underlying issue.

In Progress: Auditee has specific plan to begin, or has begun, to implement and intends to fully implement the recommendation.

Partially Implemented: Auditee implemented the recommendation in part, but is not making efforts to fully implement.

Not Implemented: Auditee has not implemented the recommendation and indicates that it will not do so.

The follow up audit was performed in accordance with auditing standards generally acceptable in the United States of America and the standards applicable to performance audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. The audit was also

conducted pursuant to Title 10 Chapter 4 of the Kosrae State Code. Furthermore, Kosrae State Financial Management Regulation, Lelu Town Government Manual of Administration and Lelu Town Government charter were used as criteria for compliance.

With reference to the specific objectives, we concluded that most of the recommendations as stated in PA 01-2018 were properly implemented.

Finding 1 Status: Partially Implemented

Recommendation: We recommend compliance to the provisions of the Municipal Charter.

We also strongly recommend that the council pass a resolution to have an ordinance for financial management. Financial management rules and procedures that will include specific functions of the treasurer, books of accounts, preparation of bank reconciliation schedules, document filing system and retention period of disbursement documents such as disbursement voucher, vendor's receipts and invoices and other supporting documents.

Finding 2 Status: In Progress


Recommendation: That the executive and councils of LTG reorganize the existing procedure on the cash handling with the consideration of the internal control on the segregation of duties and reporting.

Finding 3 Status: In Progress

Recommendation: We recommend that Lelu Town Government to set up and maintain its books of accounts. Individual ledgers must be prepared to accommodate transactions on each type of assets, liabilities, revenues and expenditures especially with its classes to permit the preparation of its financial statements.

The Office of the Public Auditor provided draft copies of this Follow-up report with the Lelu Town Government for review and comment on December 27, 2019.

Respectfully submitted,


Stoney S. Taulung
Public Auditor

INTRODUCTION:

This audit was conducted by the Kosrae State Office of the Public Auditor (OPA) as requested by Lelu Councils as Resolution No. 10-61. Accordingly, we conducted a Performance Audit on Lelu Town Government operations and issued PA 01-2018.

In accordance with the Kosrae Public Auditor Office manual of operation, KOPA maintains an audit tracking system to monitor and follow-up on implementation and resolution of audit recommendations on significant findings and recommendations from its prior reports which period shall not exceed six (6) months. The Office will disclose in the ensuing report the status of uncorrected findings and recommendations.

A follow up is also needed because one important measure of the effectiveness of the internal audit function is its success in achieving a high implementation rate of recommendations made in audit reports.

Background

We have conducted a follow-up work on certain audit report findings contained in Report No. PA 01-2018 Performance Audit on Lelu Town Government operation issued on October 30, 2018. The objectives of the follow up audit are to:

1. Identify audit report findings that require immediate management attention and any other findings for which follow up is considered necessary at this time, and inform the stakeholders about the follow-up review on those findings.
2. Identify and provide status information for each recommendation reviewed. The status of each recommendation reviewed will be one of the following:
 - **Implemented:** Auditee fully implemented the recommendation, either as described in the report or in a manner that resolved the underlying issue.
 - **In Progress:** Auditee has specific plans to begin, or has begun, to implement and intends to fully implement the recommendation.
 - **Partially Implemented:** Auditee implemented the recommendation in part, but is not making efforts to fully implement it.
 - **Not Implemented:** Auditee has not implemented the recommendation and indicates that it will not do so.

Scope

Our Follow up audit covered the results and findings in the Report No. PA 01-2018 Performance Audit on Lelu Town Government operation issued in October 30, 2018. However, the gathering,

reviewing and testing of relevant information and documentations included previous and subsequent period for analytical purposes. We conducted the audit and inspection pursuant to Kosrae State Code Title 10, section 4 which stated in part:

- “(a) The Public Auditor shall inspect and audit personally, or by his duly authorized assistants, all account, books, and other financial records of the State Government, to include but not be limited to, every branch, department, office, political subdivision, board, commission, agency, other public legal entity (owned, or partially owned by the state), whether they receive public funds or not, and nonprofit organizations that received public funds from the State Government;
- (b) Inspect and audit personally, or by his duly authorized assistants, the fiscal books, records and accounts of all allottees and other custodians of public funds, making independent verification of all assets, liabilities, revenues, expenditures and obligations of the State Government, entities owned in whole or part by the State Government, and agencies of the State Government;
- (c) Inspect and audit personally, or by his duly authorized assistant, the fiscal books, records, and other financial records associated with any project, program and activity receiving funding in whole or in part from public funds of the State Government, including the records of any contractor performing public work on a cost-reimbursement-type contract in order to verify the cost charged to the public contractor;
- (d) Inspect and audit personally or by his duly authorized assistants, the books, records, accounts, and other financial records associated with business sales that may be used for sales assessment for tax collection purposes”

AUDIT METHODOLOGY

The audit was conducted in accordance with generally accepted government auditing standard (GAGAS). Those standards requires that we plan and perform the audit to obtain, 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.

In planning our examination, we obtained sufficient understanding of the internal controls that is material to the audit objectives to plan the engagement and design the audit procedures. Based on this assessment, we reviewed documents and records relevant to the Project.

We considered compliance to state laws and regulations to be able to render an opinion to our audit objectives. Our procedures were also designed to identify weaknesses on internal controls that are material to the expression of an opinion to our audit objectives.

Audit procedures included, but were not limited to, interviews of Lelu Town Government employees and stakeholders. We also review transaction process and documentation. In

addition, we performed assessment on the implementation of previous audit. The audit criteria used to develop the required audit tests were based on previous audit report issued.

CONCLUSION

We concluded that based on the audit objectives:

- (1) Most of the recommendations and commitments on the previous audit were properly implemented.

Follow-Up Report on Prior Audit Findings Status of Findings

FINDINGS AND RECOMMENDATIONS

Finding Number 1: Lelu Town Government disbursement does not comply with the LTG financial management regulations and Manual of Administration resulting to questionable transactions.

Condition: Our examination was applied to all disbursements made by the Municipality for the period covered and noted the following findings:

- a. Checks issued files are incomplete for the covered period. Forty-eight percent (48%) or 10 pcs out of 21 pcs of void checks does not have original copy on file.
- b. Thirty-three percent (33%) of the total amount of disbursements aggregating to \$25,093.55 were completely unsupported by the required disbursement documents.
- c. Included in the unsupported check voucher are 3 checks drawn in the name of the Mayor amounting to \$1,000 per check (\$3,000) apparently should be classified as cash advance to purchase supplies in Pohnpei during his travel. The treasurer confirms that there is no liquidation for this amount up to the time of the audit.

Recommendation: We recommend compliance to the provisions of the Municipal Charter.

We also strongly recommend that the council pass a resolution to have an ordinance for financial management. Financial management rules and procedures that will include specific functions of the treasurer, books of accounts, preparation of bank reconciliation schedules,

document filing system and retention period of disbursement documents such as disbursement voucher, vendor's receipts and invoices and other supporting documents.

The municipality should ensure that all supporting documents for disbursements are verified and approved prior to payment. Pre-numbered voucher should indicate clear and detailed purpose of disbursement with the certification of what budget or appropriation to be charge with. Voucher numbers therein should be the basis of filing along with all supporting documents. By so doing, a systematic filing of disbursement documents can be easily achieved. Approval of check vouchers should be delegated to the Treasurer and/or Mayor and/or a representative of the council and should in accordance with proper internal control system.

STATUS: Partially Implemented

Based on interview and inquiries with the management and key staff of Lelu Town Government, they have implemented QuickBooks to sufficient accounting records. The said program provides voucher system however, the auditors were advised that LTG is now using request for payment form to save cost of supplies. It was also discussed that restitution of questionable transaction amounted to \$3,000.00 has not been settled pending for legal advice from the municipal legal consultant.

Finding Number 2: Weak Internal Control on Cash Transactions.

2.1 No Segregation of Duties

2.1a Collection

Condition: During our examination, we have noted that the municipality has no formal control procedures over collections. Review of the internal controls over cash receipts, we noted that the Mayor is responsible for the collection and deposit of funds and subsequently updating the cash receipts journal. These collections are from ordinances imposing taxes and all other revenues or reimbursements collected based on fines, fees, licenses, interests, rents or government services. And we noted in most cases that these collections are being paid in cash which is vulnerable to misappropriation.

The auditors noted and verified that the collection process is basically conducted by the mayor office. The mayor's secretary receives collection and prepares receipts for collection while mayor keep the money, do the deposit, keep the receipt stubs, deposit slips and bank statement All the documents for cash transactions were kept by the Mayor and submit it to the treasurer for recording but not in the regular manner.

In addition, no cash book is being maintained to record amounts collected. Schedule of deposits showing the receipts used to match with the validated deposit slip amount are not being prepared. Further, there are no review procedures to check if funds collected were properly and timely deposited.

2.1b Disbursement

Condition: Disbursement and approval function are not segregated from recording function. The Mayor/staff handles the preparation of check disbursement and at the same time performs the recording in the disbursement journal. Only Individual ledger was being maintained by the treasurer. Yet, the Mayor is one of the authorized signatories for the checks, approving officer at the same for purchasing activities.

2.2 No procedural control on Checks and Cash Items

Condition: During fieldwork the auditor observe and confirm that blank check stock and cash collection was being maintained by the Mayor in his desk drawer with no locks and sometimes at Mayor' house. In addition, no physical inventories of blank check stock periodically conducted by persons independent of the cash disbursement function.

2.3 No procedural control on detail accounting of Cash and Cash Item

Condition: Lelu Town Government does not have procedures to ensure that collections and disbursements are accurately and promptly recorded. No periodic checking and review is being made for cash transactions. Hence, LTG did not performed Bank Reconciliation for the period covered.

Recommendation: That the executive and councils of LTG reorganize the existing procedure on the cash handling with the consideration of the internal control on the segregation of duties and reporting such as:

1. Schedule of deposits showing the cash receipts used must be prepared and filed in every deposit transaction along with the validated deposit slip. We also recommend that a person not connected with the collection and depositing process inspect on a regular basis to ensure that all collections have been properly and timely deposited.
2. Perform timely Bank Reconciliations (monthly) to ensure
 - a. Comparison of checks in appropriate detail with disbursement records.
 - b. Accounting for numerical sequence of cashed checks
 - c. Examination of signatures and endorsements on a test basis.
 - d. Comparison of book balances used in reconciliations with the general ledger
 - e. Comparison of deposit amounts and dates with cash receipt entries
 - f. Investigation of outstanding items
 - g. Footing of cash books.
3. Physical inventories of blank check stock periodically conducted by persons independent of the cash disbursement function, and reconciled to department records

STATUS: In progress

Review of updated transaction flow chart as provided by the current Mayor shows improvement on the internal control for disbursement. However, there is a need for further review on the verification function so as the reviewer or inspection function for collection and deposit should be done by a person not connected to the process of collection and deposit.

The current Mayor also mentions that bank reconciliation is regularly done however, there was no bank reconciliation report submitted or shown to the auditor.

Finding Number 3: Absence of books of accounts

Condition: Lelu Town Government only maintains cash disbursement journal to record payments made on various expenditures incurred and cash receipts journal to record collections arising from local revenues including funds received from revenue sharing. The Municipality does not maintain individual general ledgers to accommodate transactions involving its assets, liabilities, only fund balances, revenues and different types of expenses are being maintained. We noted also that some expenses are not properly classified to its nature.

Interview with the treasurer confirms that the recording and maintenance of books of accounts was not done regularly because of unavailability of documents which was usually kept by the mayor.

Recommendation: We recommend that Lelu Town Government to set up and maintain its books of accounts. Individual ledgers must be prepared to accommodate transactions on each type of assets, liabilities, revenues and expenditures especially with its classes to permit the preparation of its financial statements. Subsidiary ledgers must be maintained necessary in keeping track of individual vendors/contractors. By doing so, relevant and reliable financial information can be easily obtained which is useful for management's decision making.

STATUS: In progress

Lelu Town Government is now using Quickbook for fiscal transaction. The auditor receives copy of detailed ledger and sample of Profit and Loss Year-to-date Comparative Summary. As per review of the sample, there is a need to further update the chart of account, for general and subsidiary accounts and to establish beginning balance for its Real Accounts (Balance sheet accounts) and Nominal Accounts (Income Statement accounts) to maximize the benefit of using Quickbooks.

Public Auditor's Comments

We would like to extend our appreciation to Lelu Town Government Mayor and staff for their cooperation and assistance throughout the course of our follow up audit.

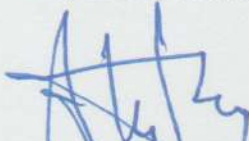
In compliance with the Generally Accepted Government Auditing Standards, a copy of the draft report was shared with the Mayor and Staff.

In addition to providing copies to the Mayor and his staff, we also extend copies to the following officials and agencies:

- 1 Governor, Kosrae State Government
- 2 Lt. Governor, Kosrae State Government
- 3 Speaker, 12th KSL and all members
- 4 Chief Clerk, Kosrae State Court
- 5 Attorney General, Kosrae State Government
- 6 V6AJ Radio

If there is any question or concern regarding this report, please feel free to contact the Office of the Public Auditor.

Respectfully Submitted,



Stoney S. Taulung
Public Auditor

ACKNOWLEDGEMENT AND OPA CONTACT

A Follow Up Audit on Lelu Town Government
Report No. FA02-2019

OPA CONTACT

Stoney S. Taulung, Public Auditor
ksauditor@mail.fm

ACKNOWLEDGEMENT

Emma Balagot, CPA, Audit Manager
Alice S. George, Auditor III
Elizabeth Jonah, Auditor II
Reed J. Floyd, Auditor I

OPA MISSION

To conduct effective and efficient Audits and
Investigations to ensure that Government
Resource are properly managed

OFFICE CONTACT

Government of Kosrae
Office of the Public Auditor
P.O Box 847
Kosrae, Federated States of Micronesia 96944

Tel. No. (691) 370-3766
Hotline No. (691) 370-3767
Website: www.ksaopa.fm