

OFFICE OF THE NATIONAL PUBLIC AUDITOR
FEDERATED STATES OF MICRONESIA

**INSPECTION OF THE
FSM EMBASSY IN WASHINGTON DC
FISCAL YEAR 2003 THROUGH 2006**

AUDIT NO. 2006-04 & 2006-05



**Haser H. Hainrick
National Public Auditor**



FEDERATED STATES OF MICRONESIA

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October 20, 2006

Honorable Members of the FSM Congress
His Excellency Joseph J. Urusemal, President
Federated States of Micronesia
Palikir, Pohnpei FM 96941

RE: Inspection of the FSM Embassy in Washington D.C.

We have completed our review of the FSM Embassy in Washington D.C. for fiscal years 2003, 2004, 2005 and the first three quarters of 2006. Our objectives were to determine whether FSM laws and regulations were complied with regarding 1) financial transactions, 2) the acquisition and use of a loan, 2) a renovation contract and 3) passport controls. We conducted our review in accordance with the Quality Standards for Inspections issued by the U.S. President's Council on Integrity and Efficiency and the Executive Council on Integrity and Efficiency.

Regarding the financial transactions, we found that most of the Embassy's expenditures were for direct operating costs, but expenditures lacked adequate documentation. The Embassy and Department of Finance & Administration (DOF&A) did not comply with FSM regulations and prudent business practices and we identified areas for possible cost savings. Regarding the Embassy's loan, we found that the Embassy and DOF&A did not follow FSM laws and regulations and that the loan proceeds were commingled in the operating account with all other sources of funds. Regarding the Embassy's renovation, we found that the Embassy did not comply with FSM laws and regulations or with the terms and conditions of the contract. Further, the Embassy overspent by \$14,799 on the \$200,000 allotted for the renovation work and the DOF&A has not properly recorded the renovation costs. Finally, regarding the handling of passports, we found that the Division of Immigration & Labor and the Embassy did not comply with FSM laws and regulations and did not adequately safeguard FSM passports.

In summary, we found that the Embassy did not comply with many FSM laws and regulations and that the corresponding FSM Departments in Palikir did not ensure compliance. The findings and recommendations are described in greater detail in the attachment to this letter.

Respectfully yours,

A handwritten signature in black ink, appearing to read "Haser Hainrick".

Haser Hainrick
National Public Auditor

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BACKGROUND

The FSM National Government has maintained an FSM Embassy in Washington D.C. (Embassy) since 1979 when the FSM Constitution was approved and ratified.

The functions and responsibilities of the Embassy are set forth in FSM Public Law 2-4, as amended. The Embassy represents the FSM Government before the U.S. Congress, departments and agencies of the U.S. Federal Government, other organizations, public and private, on all matters pertaining to the FSM. The Embassy assists public officials from the FSM, provides consular assistance to FSM citizens in the U.S., disseminates general information about the FSM, and promotes business opportunities in the FSM to domestic and international business organizations. Finally, the Embassy promotes and carries out the programs and policies of the FSM National Government as they are duly authorized.

The FSM laws and regulations govern all activities of the Embassy. The mode of operations is further guided by the Executive Branch's Manual of Administration, Presidential Orders and Directives, Secretarial Orders and Directives, the Embassy's own Manual of Administration signed by the President and the Embassy's Policy Memoranda signed by the Ambassador.

Table 1 below lists the funds provided to the Embassy by the FSM National Government by budget line item.

**Table 1 Schedule of Funding for the FSM Embassy in Washington D.C.
 For Fiscal Years 2003 through 2006 by Line Item**

BUDGET CATEGORIES	FY 03	FY 04	FY 05	FY 06	TOTAL
Number of Positions	4	4	4	4	4
Salaries & Benefits	\$174,380	\$174,380	\$174,380	\$176,212	699,352
Travel	103,920	33,378	40,000	23,500	200,798
Contractual Services	521,000	496,500	471,800	421,000	1,910,300
Other Current Expenses	50,850	40,000	40,000	40,000	170,850
Fixed Assets	25,400	1,000	6,000	0	32,400
Renovation	0	0	200,000	0	200,000
TOTAL	\$875,550	\$745,258	\$932,180	\$660,712	\$3,213,700

Source: The data is from the FSM National Government's Approved Budget Requests to the FSM Congress

SCOPE AND METHODOLOGY

The audit covers October 1, 2002 to June 30, 2006, which are fiscal years 2003 through 2005 and the first three quarters of 2006. The audit was conducted pursuant to the authority vested in the National Public Auditor as codified at Title 55 FSMC Chapter 5 of the FSM Code and it was

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conducted in accordance with the Quality Standards for Inspections issued by the PCIE and the ECIE¹.

The audit fieldwork was conducted at the Embassy, Department of Foreign Affairs (DOFA), Department of Finance & Administration (DOF&A), Division of Immigration & Labor (DI&L) and Department of Transportation, Communication & Infrastructure (TC&I). Audit procedures included analyzing data gathered on the Embassy's wire transfers, disbursements, loans, renovations and passport handling. We reviewed the Embassy's bank statements, checks, loan documents, contracts, control forms (purchase orders, travel authorizations, miscellaneous payment requests, etc.), invoices and receipts. We also observed the current condition of the major renovation performed on the Embassy building and the passport handling process. We also interviewed the Embassy staff to validate our analysis. The review included tests of records, transactions, and other procedures that were necessary under the circumstances. Finally, we summarized the results of our review procedures based on the review objectives.

On September 6, 2006, at the end of our review in Washington DC, we presented the draft findings to Embassy personnel. On September 20 and 21, we presented the draft findings to officials at DOFA, DOF&A, TC&I and DI&L. They generally agreed with our findings and we included their comments in the report as appropriate. In addition, the Deputy Secretary of the DOFA, Secretary of DOF&A, Acting Secretary of TC&I and Chief of DI&L provided their written comments, which are attached.

PRIOR AUDIT COVERAGE

This review represents the third undertaken by the Office of the National Public Auditor (ONPA) on the Embassy's operations. The two previous audits covered fiscal years 1992 through 1993 and fiscal years 1994 through 1997. However, this is the first review undertaken by the ONPA of the Embassy's passport handling procedures. A previous audit of the Passport Revolving Fund and the passport handling process at the DI&L was undertaken by ONPA covering fiscal years 1989 through 1994. Throughout this report, we identified findings that were previously reported.

FINDINGS AND RECOMMENDATIONS

**Finding 1 - Expenditures Not in
Compliance with FSM Requirements**

During the period October 2002 through June 2006 the FSM Embassy in Washington DC spent almost \$3,333,000 and wrote over 2,100 checks. We found that most of the Embassy's expenditures were for direct operating costs; however, most of the expenditures lacked adequate documentation. Of the 622 expenditures with more than minimal documentation, we found examples of non-compliance with FSM regulations and prudent business practices. We identified areas for possible cost savings.

¹ U.S. President's Council on Integrity & Ethics (PCIE) and the Executive Council on Integrity & Ethics (ECIE)

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Embassy's Expenditures

After piecing together the available documents, we found some information for most of the expenditures. To provide information on how the Embassy spent its funds, we reviewed the information available and categorized the expenditures into the five areas. As seen in Table 2 below, the largest expenditure of more than \$1,271,000 was used for direct business costs such as office equipment, supplies and communications. Almost \$558,000 was used for indirect Embassy operations such as utilities, bottled water and renovations. About \$709,000 was used for FSM personnel including take home pay and housing. We were unable to categorize about \$263,000 of the expenditures because they were reimbursement checks made to employees usually for items in multiple categories. Finally, we were unable to categorize about \$531,000 of the expenditures because there was not enough information. See Appendix I for a more detailed list of the Embassy's expenditures by fiscal year.

Table 2 Embassy Expenditures from October 2002 to June 2006

	Expenditures	Percentage of expenditures	Number of checks	Percentage checks
Direct business	\$1,271,834	38%	728	35%
Indirect operating	557,630	17%	285	13%
FSM personnel	709,374	21%	468	22%
Reimbursement checks made to employees usually for items in multiple categorizes	263,500	8%	331	16%
Not enough information to categorize	530,655	16%	291	14%
Total	\$3,332,993	100%	2,103	100%

Note: the expenditures in this table include funds advanced from FSM, loans, and transfer among Embassy accounts.

Inadequate Documentation

The Embassy had various types of documentation for its expenditures. As seen in Table 3 below, over 70 percent of the transactions had only minimal information for the expenditure and did not meet FSM requirements for adequate documentation. Most of these expenditures were supported by information in the check register, check stubs or check copies. However, some of these expenditures were referred to only in the bank statements and had no other information even the payee's name. See Appendix II for type of documentation available for each fiscal year.

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**Table 3 Schedule of the Documentation Available for the Embassy
 For the Period October 2002 through June 2006**

Type of Information	ONPA's Conclusion	Amount of Checks	Percentage of Total Amount	Number of Checks	Percentage of Number of Checks
Minimal information available: Expenditure information obtained through check register, check stub, check copy or bank statement	Expenditure documentation is inadequate	\$2,302,310	69.1%	1,481	70.4%
Additional information available: Expenditure information obtained through documents such as travel document, purchase order, FSM payroll calculation, invoice or receipts, miscellaneous pay request form	Enough information is available to test compliance with FSM requirements	\$1,030,682	30.9%	622	29.6%
Total		\$3,332,992	100%	2,103	100%

Non Compliance with FSM Requirements

We tested the 622 remaining transactions that had additional information to determine if FSM funds were appropriately spent. The effect of non-compliance with FSM requirements as demonstrated below is lack of assurance of appropriate expenditures or evidence of inappropriate expenditures.

The following examples of non-compliance resulted in the FSM lacking assurance that funds were appropriately spent.

- Of the 622 expenditures with additional documentation, we found 222 expenditures lacked sufficient documentation because a receipt or FSM form was not attached. Combining these 222 with the 1,481 previously identified expenditures with minimal documentation means that 81 percent (1,703 of 2,103) of the expenditures lacked sufficient documentation. This finding was identified in a prior audit report.
- 59 expenditures were not properly authorized -- the Miscellaneous Payment Request form was not signed.
- 19 expenditures were authorized by the same employee who received the payment -- no separation of duties.

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- 3 expenditures lacked supporting documentations for representation fund expenditures. Specifically, a restaurant receipt was provided but there was no note identifying the person attending or the reason for the meeting. This finding was also identified in a prior audit report.

The following examples of non-compliance resulted in the inappropriate spending of FSM funds.

- Of the 622 expenditures with additional documentation, we found 16 expenditures that reimbursed the Ambassador for residential expenses; even though regulations state that only Justices of the Supreme Court will have their residential expenses paid by the FSM. Officials from the DOF&A said that it is the practice to pay these expenses (e.g. utilities and lawn mowing) as well as other expenses (such as a clothing allowance and children's school tuition) for Permanent Representative, Ambassadors or General Consuls.
- 19 expenditures reimbursed employees for commuting to and from work, even though the regulations state that the employees should pay expenses that are personal in nature.
- 1 expenditure paid \$1,340 for parking tickets, even though Embassy policy states that tickets for automobile offenses are the responsibility of the driver.
- 9 expenditures for medical expenses were inappropriately paid from funds budgeted for the operation activities of the Embassy.

The Embassy and DOF&A did not comply with FSM's monthly reporting requirements. These procedures were designed to assure that the Embassy complied with FSM requirements.

- We found that the Embassy did not submit to DOF&A Monthly Operating Fund Reports with the required support such as receipted duplicate deposit slips, duplicate checks with supporting documents, a copy of the check register and a copy of all purchase orders, job orders or contracts issued against the operating fund account.
- The Embassy did not submit a Monthly Imprested Fund Report or Replenishment Requests to DOF&A.
- The DOF&A replenished the Embassy's funds even though the required documents were not submitted.

Prudent Business Practices

Although not specifically required by FSM laws or regulations, the Embassy did not follow prudent business practices in some of its expenditures. For example,

- The Embassy did not pay a reasonable price for luggage. Specifically, a check was written to a local luggage store for over \$630 for a computer carrying case. There is no indication of who made the purchase or why such an expensive case was needed.
- The Embassy did not pay its bills in a timely manner. Of the 622 expenditures we reviewed 69 (11 percent) included a late fee and 22 (3.5 percent) included a notice to discontinue service if the payment is not received promptly.
- The Embassy does not have insurance to cover a major FSM asset. We found that the Embassy building with value of more than \$1.3 million has not been insured since the summer of 2005. The Ambassador said the insurance company dropped the coverage for several reasons including the policy infractions noted in an unannounced visit by insurance company staff as follows:

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- although the policy stated that no cooking was allowed in the building, cooking appliances that used a lot of energy and could cause an electrical overload had recently been used.
- a fire hazard was discovered. Specifically an unused decorative gas fireplace in the reception area was turned on allowing small amounts of gas to enter the building.
- although notice to repair decorative trim on the building's front façade (a hazardous condition) the work was not done in over two years.
- The Embassy's bookkeeper was not adequately supervised allowing unusual occurrences. For example, the bookkeeper received over \$19,000 for web site maintenance while he was already employed by the Embassy as the "accountant/driver".
- The Embassy did not have adequate control over purchases. It routinely allowed employees to purchase items for the Embassy and get reimbursed. Specifically, during the period reviewed, expenditures of \$61,814 were made through reimbursements. Routinely reimbursing employees for purchases is also hardship on the employees if they are not reimbursed in a timely manner. There is no documentation that shows the items purchased through reimbursements were approved in advance of the purchase or that the items were reasonably priced.
 - A contract employee was reimbursed \$450 for the purchase of rubber mats for the Embassy car.
 - Another employee was reimbursed twice within a month for the same computer repair work.

Possible Cost Savings

During our review we identified several areas in which the FSM could save costs at the Embassy.

- The FSM should consider selling the Embassy building and moving into rental space. An analysis of the potential benefits and costs should be done to make an informed decision. The benefit cost analysis should consider the following items:
 - The Embassy building was purchased in the 1990 for about \$1.3 million. Since that time the value of houses in the DC area has increased and the FSM could make a profit if the property was sold.
 - Currently the Embassy building is not insured thus putting value of this FSM asset at risk. According to the Ambassador, insuring the building as it currently is (without doing needed repairs) will cost substantially more than in the past.
 - According to the Ambassador, the building needs additional costly renovation work to obtain insurance as a reasonable rate. This work would include such items as updating the electrical wiring, plumbing pipes and possibly reinforcing the structural supports for the office space above the garage.
- The FSM should consider housing all the staff in the main building or requiring the legal consultant to pay for his own office expenses. Currently, a legal consultant under FSM contract uses the office space above the garage while four FSM employees occupy the 4-story Embassy building. If the consultant moved into space in the main building, the Embassy could potentially save \$150 to 300 a month for cost of heating and air

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conditioning the "rear" building. Alternatively, the legal consultant could be required to pay for the office expenses such as office space, electrical bills and phone service that are currently paid by the Embassy.

- The FSM should consider reducing the cleaning schedule for the Embassy. The current contract for cleaning of the Embassy building costs \$1,800 a month. Since the building houses only a few employees, the cleaning service may not be needed on a daily basis. If the cleaning schedule were reduced the costs may also be reduced.
- The FSM should consider reducing the number of phone lines in the Embassy building. The Embassy currently has 15 phone lines. We were told that 4 to 6 of the phone lines are designated for specific purposes (e.g. security alarm, DSL line, Fax line) and are not available for general phone calls. However, 10 undesignated phone lines for 4 staff seem excessive.

During the period covered by our review, the Embassy had two bookkeepers. Since neither bookkeeper is currently employed by the Embassy, the causes of non-compliance cannot be specifically determined. However, we believe there are two main reasons for lack of compliance: lack of knowledge regarding procedures or an intent to cover up inappropriate expenditures. The FSM policies and procedures are written so that compliance ensures that the expenditures are appropriate. Therefore our recommendations are basically to train staff regarding the procedures and provide oversight to see work is properly done.

Recommendations

We recommend that DOF&A and the Embassy should:

- ensure that FSM laws and regulations are complied with.
- review the Embassy's operating and accounting manual and ensure that the policies and procedures are followed or obsolete sections are updated.
- discontinue the practice of reimbursing costs of a personal nature such as commuting costs and Ambassador's residential costs, since this practice does not comply with FSM laws and regulations.
- purchase adequate property insurance for the Embassy building, a major asset of the FSM.
- consider allowing the Embassy to use a credit card for purchases to reduce the number and amount of employee reimbursements. These purchases should be pre-approved within the Embassy.

We also recommend that:

- at least one Embassy staff is trained in documenting and maintaining transaction records and submitting required monthly reports and supporting documentation.
- DOF&A require appropriate reports and documentation before expenditures are reimbursed to the Embassy.
- the Embassy personnel structure ensures separation of financial duties and adequate oversight of the finances.

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- Embassy's operating environment is reviewed for possible cost savings such as those we identified above.

**Finding 2 - Loan Records Not Complete
and Funds Commingled**

Although the Embassy's records regarding the loans are not complete, we were able to piece together a history of the Embassy's line of credit. However, we could not identify expenditures from the loan because the funds were commingled in the operating account. We found that DOF&A and the Embassy did not follow FSM laws and regulations related to the loan and therefore, DOF&A was not aware that the Embassy established a line of credit.

Although the Embassy's records regarding the loans are not complete, we were able to piece together information on the Embassy's line of credit as follows: In July 2004, the Embassy opened an overdraft line of credit for \$70,000. This was increased by \$30,000 in August 2004. In February 2005, the Embassy added another 120,000 to the loan and also repaid \$100,000. The highest outstanding principal amount for the overdraft was \$200,000, but balance as of January 2006 was \$120,000. In July 2006, FSM Congress appropriated \$122,000 to repay the remaining principal and interest on the loan. Subsequently, the bank reimbursed \$1,230 for an overpayment of the loan.

The loan funds were commingled in the operating account. We traced these loan deposits into the Embassy's operating account. We cannot determine what the loan funds were used for because of the Embassy commingled funds from FSM advances, FSM payroll, imprested account, and loans.

DOF&A and the Embassy did not follow FSM laws and regulations related to the loan. Specifically the Financial Management Regulations (FMR) requires that all funds received by the Embassy should be deposited promptly into an approved operating fund account and the Secretary of DOF&A should be notified as to the nature and amount of the deposit. While the Embassy did deposit the loan funds in an operating account, it failed to report the information to the Secretary. The Accounting Policies and Procedures for Embassies and Liaison Offices requires the Embassy to maintain a cash journal to record all incoming cash regardless of the source of funding, and there were no cash journal available for review. The Accounting Policies and Procedures for Embassies and Liaison Offices also requires that banks send statements regarding Embassy accounts to DOF&A. Instead the bank sent the statements to the Embassy building in Washington DC and the Embassy did not forward them to DOF&A. Finally, although the Finance Office Procedure requires DOF&A to reconcile bank statements for all general fund accounts, the Embassy accounts that are part of the general fund were not reconciled.

ONPA is still working on the loan issue. ONPA's Compliance Investigation Division is reviewing some aspects of the loan. In addition, we have requested an opinion from the Attorney General regarding the legality of the loan and have requested loan statements from the banks.

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Due to the change in the staff in the Embassy, the causes of non-compliance cannot be specifically determined. However, we believe there are two main reasons for lack of compliance: lack of knowledge regarding procedures or an intent to cover up inappropriate activities. The current FSM policies and procedures are written so when they are followed DOF&A is aware of all sources of funds and related obligations. Therefore our recommendations are basically to train staff regarding the procedures and provide oversight to see work is properly done.

Recommendations:

We recommend that DOF&A review the Accounting Policies and Procedures for Embassies and Liaison Offices and update these requirements as needed. Further, the DOF&A should review the financial requirements with Embassies and Consulates personnel to ensure understanding and compliance.

Finding 3 – Embassy Renovation Not in Compliance with FSM and Contract Requirements

The Embassy's contract for major renovation of the Embassy building did not follow FSM laws and regulations and therefore FSM is not assured that the proper work was done for a reasonable price. For example, the Embassy did not obtain the required bids, the renovation contract was not properly reviewed and approved and the Embassy did not comply with the terms and conditions of the contract. Further, the Embassy overspent by \$14,799 on the \$200,000 allotted for the renovation work and the DOF&A has not properly recorded the renovation costs.

FSM regulations require that a Project Control Document (PCD) be completed before funds can be allocated for any public project. The PCD specifies the total project budget, funding source, detail, nature and type of expenditures to be made. In addition, it lists the responsible officials such as the allottee (Embassy), administrating agency and the Project Inspection Official. The Allottee certifies that the project will abide by the FSM regulations. The Budget Officer (Division of Budget) should approve the PCD when he is satisfied that the PCD is complete and that the project and expenditures described in the PCD are consistent with the line-item of the applicable laws. Otherwise he should disapprove the PCD and return it to the Allottee with a statement of his reasons.

The PCD for the renovation of the Embassy describes the work as being done in three phases. Phase 1 work includes replacing the roof of the Embassy, scraping and painting metal railings and wooden frames on the front side of Embassy building and sandblasting bricks. Phase 2 includes the same work as phase 1 for the backside of the Embassy building and to resurface the retaining wall, courtyard, and front steps. Phase 3 is for renovation work on the inside of the building, which includes painting, carpentry work, electrical and installation of new carpet on the four floors. The contract lists the cost as \$92,000 for inside work and \$75,900 for outside work. See the Exhibits for some photos of the renovation.

The Embassy renovation did not comply with national laws and regulations.

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- Although a PCD is required to be completed prior to issuance of allotments, the Embassy was allotted funds before the PCD was completed. Specifically, the funds were allotted on June 15, 2005 and the PCD was completed July 20, 2005.
- Although contracts for construction projects involving the obligation of \$20,000 or more of Government funds are required to have free and open bidding by sealed bids, the Embassy did not obtain bids for the project estimated to cost \$167,900.
- Although all contracts should be reviewed and approved by the Justice Department and TC&I to ensure that it complied with various laws and regulations, the Embassy did not obtain these reviews.
- A Project Inspection Official must certify all requests for payment on design, construction, or procurement contracts; however, the PCD form does not list a Project Inspection Official as required. Although identifying and obtaining acceptance of a Project Inspection Official is the responsibility of the Embassy, the review by the Budget Officer should have identified the lack of the Project Inspection Official and the PCD should have been denied.

- The terms and conditions of the contract were not complied with as follows:
 - The contract stated that work would be completed no later than September 2005; however, based on contractor invoices, the work continued into January 2006. In addition, in August 2006 the Ambassador stated that there is still more work to be done under the contract. Specifically, work needs to be completed on the roof.
 - The contract states that the contractor will be paid according to a fee schedule; however, the schedule is not attached to the contract.
 - The contract states that job orders are to be cut for each of the three phases of the work. However only \$83,728 of work had job orders forms attached. Although the contract required job orders, TC&I requires them for repairs, maintenance and construction projects that are less than \$5,000.
 - The contract states that the contractor is to submit an invoice for half of the total amount under each of the three phases of the work; however, only \$96,353 had invoices attached. In addition the invoices received were not signed and had no details of material costs and labor.

- According to the Ambassador, the contract was amended to add work outside of the original scope; however, no amended contract was provided.
- The Embassy overspent the budget appropriation for the renovation by \$14,799.
- As of July 2006, the Embassy renovation account at the DOF&A reflects a balance of \$128,646, which underreports the cost of the renovation by \$86,154. The actual cost for renovation was \$214,799.
- Although asset valued at \$150,000 or more and having a useful life of more than one year should be capitalized, the DOF&A has recorded the cost of the renovation as an expenditure. According to DOF&A officials, the expenditure is capitalized when closeout document is received from the Project Inspection Official. However, no Project Inspection Official was designated for this renovation.

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ONPA's Compliance Investigation Division is also reviewing aspects of the renovation and is seeking an independent assessment.

Due to the change in the staff in the Embassy, the causes of non-compliance cannot be specifically determined. However, we believe there are two main reasons for lack of compliance: lack of knowledge regarding procedures or an intent to cover up inappropriate activities. The current FSM policies and procedures are written so when they are followed FSM is ensured that contract work at the Embassy was suitable at a reasonable price. Therefore our recommendations are basically to train staff regarding the procedures and provide oversight to see work is properly done.

Recommendations:

We recommend that the PCD form be modified to require the budget officer's signature indicating that the form was approved or denied. Although the Division of Budget is required to review the PCD and determined that it is complete and that the project and expenditures described in the PCD are consistent with applicable laws, there is no space on the form for his signature. We believe that requiring a signature would ensure a more meticulous review before an official would give his approval. This approval should ensure a Project Inspection Official (TC&I inspectors or independent contractor) was designated to coordinate the design, construction, and procurement for the project.

In commenting on our draft findings TC&I officials commented that a renovation project done on the Guam Consulate Office 2 or 3 years ago worked well because DOFA designated TC&I to coordinate the design, construction, and procurement of the project.

**Finding 4 - Passport Handling Practices
Not in Compliance with FSM Requirements**

The DI&L and the Embassy passport handling practices are not in compliance with FSM requirements resulting in FSM Passports being inadequately safeguarded. FSM laws and regulations require that the Embassy assists FSM citizens residing on the U.S. mainland with renewing or extending their FSM passports by forwarding passport applications and related material (i.e. expired passports, renewed passport picture, money order, and birth certificate) to DI&L. This authority does not mention handling (i.e. touching, distributing) valid and specimen² passport booklets. However, we found that the Embassy handled renewed, lost, and specimen² passports. For example, DI&L has sent renewed passports to the Embassy for distribution to FSM citizens residing on the U.S. mainland. According to DI&L officials, renewed passports are sent to the Embassy for distribution when the applications are forwarded from the Embassy. In addition, the Embassy also received lost passports from the U.S. State Department to be forwarded to DI&L and specimen passports from the passport printer.

² Specimen passports are sample passports provided to other governments so they can identify genuine FSM passports.

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We found that the Embassy could not track the receipt and distribution of the passports they handled for distribution. For example, although the Embassy said that they logged passports in the incoming and outgoing mail logbooks, incoming entries for 441 workdays or 46% of the days reviewed were missing. Therefore our review of received passports is limited to those listed in the available logbooks. Although 22 passports were recorded in the incoming logbooks, we could only identify 12 passports in the outgoing logbook. The Embassy personnel could not explain the lack of entries in the outgoing logbooks.

Although, on February 6, 2006, the Ambassador issued internal procedures to improve passport security measures at the Embassy, the procedures are not fully implemented. Specifically, the passports were not recorded in a separate logbook or stored in a safe as required by the new procedures.

ONPA's Compliance Investigation Division is also reviewing the handling of specimen passports.

Although DI&L admitted that it did not follow FSM regulations when it sent passports to the Embassy for distribution, no specific reason was given. We believe that current FSM laws and regulations were written so when they are followed FSM would be ensured that the passports are being safeguarded. Therefore our recommendations are basically to train staff regarding the regulations and provide oversight to see work is properly done.

Recommendation:

We recommend that the DI&L discontinue sending all types of passports to the Embassy to comply with the passport regulations. The DI&L should also ensure that specimen passports are not sent to the Embassy from the passport printer. An amendment of the passport regulations to include allowing the embassies and consulates to distribute passports should only be considered when the Embassy has in place reasonable security precautions such as a proper recording system, an adequate safe and trained staff with adequate segregated duties.

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Appendix I

**Detailed Schedule of the Embassy's Expenditures
 For Fiscal Years 2003 To 2005 and the First Three Quarters of Fiscal Year 2006⁴**

		FY 03	FY 04	FY 05	FY 06	Grand Total
Direct Business	Bookkeeper/Driver	26,400	19,800	8,800	1,100	56,100
	Cable TV & Internet	1,168	1,804	1,246	1,767	5,986
	Cell Phone	18,020	17,514	16,978	10,420	62,932
	Computer Lease	5,594	8,180	5,701		19,475
	Delivery Service	3,493	1,341	251	127	5,213
	Email & Website Hosting	1,590	1,260	1,050	630	4,530
	Legal Services	200,000	140,000	230,000	149,000	719,000
	Network Upgrade				6,381	6,381
	Office Supplies	5,905	750	949	458	8,061
	Phone Service	14,983	6,758	9,220	3,895	34,856
	Phone System Leased	3,652	3,029	3,795	1,487	11,963
	Photo Copy Machine Lease	5,110	3,880	5,705	3,987	18,682
	Postage	600		41	328	969
	Postal Meter Equipment Lease	2,591	2,078	3,015	1,346	9,030
	Receptionist	15,600	13,686	2,520		31,806
	Representation Fund	18,628	29,416	800	2,879	51,722
	Subscriptions	790	854		840	2,485
	Travel	84,755	44,814	33,455	33,925	196,950
	Website Maintenance	25,696				25,696
Direct Business Total		434,575	295,163	323,527	218,570	1,271,834
Indirect Operating	Auto Repairs & Maintenance	129	409	2,549		3,087
	Car Rental			1,331	522	1,852
	Car Loan		3,266	73,303	8,167	84,736
	Cleaning Service	23,050	20,325	23,000	14,400	80,775
	Drinking Water	746	748	746	284	2,525
	Electricity	5,374	3,836	9,744	5,206	24,161
	Heating Gas	4,837	5,011	3,928	3,746	17,521
	Limo Service	17,130		705	600	18,435
	Pest Control	759	640	2,774	285	4,458
	Property Insurance	15,825	16,800	4,285		36,910
	Renovation			158,300	56,500	214,800
	Transfer to another account		10,000	35,807	20,630	66,437
	Water & Sewer Service	674	749	366	144	1,933
Indirect Operating Total		68,524	61,785	316,836	110,484	557,630
Personnel	Housing	98,330	84,766	112,838	91,520	387,454
	Personnel	53,592	48,063	116,099	96,501	314,254
	Storage	3,332	3,084	1,250		7,666
Personnel Total		155,254	135,913	230,186	188,021	709,374
Misc Reimburse Total		123,951	47,012	61,972	30,566	263,500
Unknown Total		450,495	8,959	56,284	14,917	530,655
Grand Total		1,232,799	548,831	988,805	562,557	3,332,992

⁴ The expenditures in this table includes funds advanced from FSM, loans, and transfer among Embassy accounts.

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Appendix II

**Schedule of the Number of Expenditures by
 Type of Documentation by Fiscal Year**

	FY 03	FY 04	FY 05	FY 06	Grand Total
<u>Minimal Information</u>					
Check register	559	275	84	9	927
Check stub		1	23	105	129
Check copy	142	24	30	2	198
Bank statement	210	1	10	6	227
Total	911	301	147	122	1,481
<u>Additional Information</u>					
Travel doc		2	8	5	15
Purchase order	2				2
FSM Nat Gov't stub	33	22	51	32	138
Invoice/ Letter	6	39	123	100	268
Misc pay request	2	37	77	14	130
Receipts	20	13	18	18	69
Total	63	113	277	169	622
Grand Total	974	414	424	291	2,103

Note: Expenditures are listed next to the best type of documentation available. For example if an expenditure has a receipt and a check stub, the expenditure would be listed next to receipt and not check stub.

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Appendix III

Response from the Chief, DI&L



FSM IMMIGRATION & LABOR

Department of Justice

P.O. Box PS-157, Palikir, Pohnpei FM 96941 Phone: (691) 320-5844/2605 Fax: (691) 320-7250 Email: ImHq@mail.fm.Mesiel@mail.

September 25, 2006

MEMORANDUM

TO: FSM Public Auditor
FROM: Chief of Immigration & Labor
SUBJECT: **Comments on Routine Passport Handling**

Thank you for the opportunity extended to us to comment on the routine passport handling at our FSM Embassy in Washington D.C.

I must agree with you that we do not have in place policy procedures that specifically address approved and issued passports that subsequently are transmitted to our oversea offices for dissemination to our FSM citizens living abroad. While the assistance rendered had proven to be worthwhile, it is incumbent upon us to institute the necessary regulatory guidelines that would assist us in the proper handling of these documents, as noted.

The Department of Foreign Affairs is in a better position to provide the proper administrative protocol in the management of their respective oversea offices, especially the assistance extended to our citizens when applying for FSM passport. The oversea offices are the only means of access we have in reaching our citizens, except for those that we have direct contact with, which also has its own disadvantages.

We are at a critical stage now in upgrading our passports to MRP ICAO International Standard and we must put in place the appropriate tools to ensure security and accountability of our passports. The internal procedures issued on 2/6/2006 stated in your letter, although I have not seen it, is a positive move forward to provide the required security issues and I am confident that it can be improved.

I would recommend that we establish a similar passport control logging system at all our oversea offices similar to what we have at the home office.

Thank you and please let me know if we can be of assistance.


Mohner A. Esiel
Chief of Immigration & Labor

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Appendix IV

Response from the Acting Secretary, TC&I



Office of the Secretary

Federated States of Micronesia
Department of Transportation, Communication & Infrastructure
Palikir, Pohnpei State FM 96941

October 2, 2006

MEMORANDUM

TO: FSM Public Auditor
FROM: Acting Secretary
SUBJECT: Your Inspection Report of the FSM Embassy in Washington DC

Thank you for giving us the opportunity to review and make comments on the subject report. Although there were several findings in the report, we can only commend on the renovation project of the embassy building.

1. The department is fully aware that it is its responsibility to assist the other departments, offices and agencies including embassies of the National Government in implementing construction contracts/projects under those departments/offices when requested. We were not aware of the project or the appropriation because we were not informed.
2. The Division of Infrastructure could have assisted the embassy in preparing the contract documents and inspection of the project which could have saved some money. As mentioned in the report, the department administered the contract for the Consulate General's residence in Guam and it worked out well. One person was assigned to the project and the travel expenditures were not more than \$10,000.00. Perhaps, in this case the DC Embassy could have hired a local engineer (DC resident) on a part-time basis to monitor the project to minimize the cost as opposed to TC & I doing the inspection.

The department stands ready to assist the Washington DC Embassy and other FSM embassies and offices overseas in implementing any type of renovation work to their offices and/or staff residences abroad.

Thank you,

Weener Hadley

Tel. No. (691) 320-2865/2381/5829

Fax No: (691) 320-5853

E-mail: Transad@mail.fm

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Appendix V

Response from the Secretary, DOF&A



Secretary of Finance
&
Administration

GOVERNMENT OF THE
FEDERATED STATES OF MICRONESIA
Department of Finance and Administration

P.O. Box PS 158
Palikir, Pohnpei FM 96941
Tel: (691) 320-2640 Fax: (691) 320-2380
E-mail: fsmsofa@mail.fm

October 6, 2006

Mr. Haser H. Hainrick
Public Auditor
FSM National Government
Palikir, Pohnpei State, FM 96941



Dear Mr. Hainrick:

We appreciate very much the opportunity given to us to review and comment on the draft Inspection Report concerning the FSM Embassy in Washington, D. C. financial related activities. In summary, we agree with the findings and recommendations cited in the Report.

The Department of Finance and Administration is taking appropriate measures to ensure that public funds appropriated for the operations and programs of all our missions abroad are disbursed in accordance with the provisions of relevant laws and regulations of the FSM National Government. We also plan to increase monitoring by periodic on-site visit to our missions abroad to ensure financial compliance.

Again, thank you for the opportunity to review and comment on the Report.

Sincerely,

A handwritten signature in black ink, appearing to read "Nick L. Andon".

Nick L. Andon
Secretary

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Appendix VI

Response from the Deputy Secretary, DOFA



DEPARTMENT OF FOREIGN AFFAIRS
of the
FEDERATED STATES OF MICRONESIA
P.O. Box P.S. 123
Palikir, Pohnpei FM 96941
Telephone: (691) 320-2641/2613 Fax: (691) 320-2933

17 October 2006

The Honorable Haser Hainrick
National Public Auditor
Office of the National Public Auditor
FSM National Government
Palikir, Pohnpei FM 96941



Dear Mr. Hainrick *Haser*

We sincerely appreciate the opportunity so kindly extended to us to provide comments on the draft Audit Report. The audit provides a useful basis upon which to formulate measures aimed at improving the financial management and operation of the FSM Embassy in Washington DC.

While noting the Report's caveat in some instances about the insufficiency if not absence of documentation upon which to make conclusive determination of its findings, in itself a serious deficiency, it is not our intention to obliterate the overall message of the Report that corrective measures is the order of business of the day. Thus, the task of formulating and implementing corrective measures must be undertaken - immediately, comprehensively, firmly, and steadily. While the Department of Foreign Affairs and the Embassy in particular will do their part in the rehabilitative process, we also acknowledge the critical roles that various departments and offices of the National Government can - and should - play in this endeavor. For this task to succeed, it is imperative that we all work together in a collaborative spirit and with collective resolve.

If our responses to the findings are wanting, it is because the thrust of our efforts is on seeking concrete and measurable improvement. Guided by this priority, we are pleased to report that we have made an early headstart in the rehabilitative process. In particular, these measures have already taken place:

1) As of this writing, resulting from the coordinated efforts between the Departments of Foreign Affairs and of Finance & Administration, as well as the Embassy itself, an official of the Department of Finance and Administration is already on site in Washington and will remain for about one month to train Embassy staff in the relevant laws, financial regulations, and procedures. Part of her assignment is also to follow-through on the recommendations of the Audit Report with a view to implementing them where necessary and appropriate;

2) We've met with officials of the HSBC Bank, where the Embassy does its banking, to ensure proper safeguards of the government accounts maintained at the HSBC Bank

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by the Embassy. We've also discussed with the Finance representative not only internal controls but also improvement in reporting features of expenditures;

3) While it is unreasonable to expect immediate wholesale improvement in the management and operation of the Embassy with its current one-man staff, every effort is being made by the Department of Foreign Affairs and Department of Finance & Administration/Personnel Division to expedite the hiring of the regular staff of the Mission so that, with them on board, the rehabilitative task can be pursued headlong with greater force and impact.

4) Concurring completely with the Audit Report about the grave situation of the Embassy not being insured, we have removed the materials from the Embassy premises that increased the risks of hazard and fire, hence the rate of insurance premium, and have begun seeking advice and consulting with insurance agents to compare insurance rates and services. We will engage the services of a professional assessor to determine the value of the building after the renovation work. Whatever the case is, the property must be insured at the earliest opportunity.

Maintaining an effective internal management system for the Embassy is – must necessarily be – an ongoing task. We therefore applaud the recommendation by the Audit Report for a follow-up on the audit in the next six to nine months. More than just applauding, we strongly urge that a more periodic review of our financial management be institutionalized, as we believe this is critical to the need for improvement.

While we are prepared to do all that we can do to improve the financial management of the Embassy, we beg to make the following observations and clarifications:

Sources of Authority and Governance

It is true that the FSM has been maintaining an office in Washington since the creation of the constitutional government in 1979.¹ However, ten years later in 1989, what was then known as the "FSM Representative Office" was elevated to the status of a full-fledged "FSM Embassy." This was when the FSM and US, desiring to conduct their relations in accordance with the Vienna Convention on Diplomatic Relations of 1963 (VCDR), agreed to amend relevant provision of the Compact.

The clarification is made here for more than just a penchant for historic accuracy. It is necessary to correct the omission of the VCDR as a source of authority for the Embassy or the basis for its conduct. The omission results in the failure to shed light on the reality of the unique environment within which our overseas missions operate and the reality of the constant tug-of-war in which they struggle to maintain an appropriate zone of balance between the requirements of our domestic laws and regulations on the one hand and, on the other, the norms and standards of the diplomatic community – in cases where the two are not in neat fit. True, our allegiance must be to our own national laws and regulations.

¹ While the office could technically be traced to the Liaison Office during the Trust Territory, tracing its historic evolution is not necessary for the present purpose. Its subsequent elevation of status as a full-fledge Embassy, however, is important in appreciating, among other things, the authorities or the norms or standards to which it is expected to conform.

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At the same time, lest we have forgotten, our petition for and acceptance of membership in the international community and, in this particular case our accession to the VCDR, conveys the consent of the FSM Government to abide by the "rules of the game" of the diplomatic community as well – unless we decide to exit from it or sit on the periphery. In acceding to the VCDR, is it not then safe to say that the Vienna Convention has been incorporated into our legal system and become part and parcel of our "supreme law of the land" and a basis for the conduct of the Nation's diplomacy? As such, would it not be safe to further say that our complying with the terms and conditions of the VCDR would be our complying with domestic laws and regulations? Do we have no obligation to conform at least to the minimum norms and practices of the diplomatic community?

It is important to highlight the "international character" of the overseas missions and the instruments by which they are to be governed. Unlike most domestic based offices, the overseas missions exist and operate in a diplomatic milieu in which they have to work and make decisions that would almost inevitably seek to accommodate both domestic and external factors. As intermediaries between their own sending government and their host governments, they constantly struggle to maintain a balance – and their success depends on striking a comfortable balance between domestic requirements and certain "rules of the road" of the diplomatic community which, through the sovereign act of accession, we have also adopted to be our own.

The above paragraph is a summarized restatement of the classic dilemma of diplomats and diplomatic missions in the conduct and operation of their offices. We believe it appropriate for the Audit Report to at least make note of it.

See ONPA note 1

2) Embassy Responsibilities and Mission Statement

The Audit Report makes note of the responsibilities of the Embassy. One of them is to "represent the FSM Government before the US Congress, departments and agencies of the US Federal Government, other organizations, public and private ..." The issue here relates to the responsibility of the Embassy where *private* organizations, particularly commercial enterprises, are concerned. We believe this is the Embassy's annually recycled "mission statement" in its budget proposals.

While there is an increasing call or expectation on the government to assist in the development of the private sector (i.e., one of the six agreed-upon funding sectors of the Amended Compact), one of the concerns here is that this is essentially a vacuous statement of ideal as far as the Embassy in DC is concerned. Lacking support both material and properly trained human resources over the years, the Embassy has never been in a position to undertake this task in a significant way.

Furthermore, the mission statement needs to be thoroughly examined, or the Embassy will run the risk of engaging in commercial activities. The present formulation of the mission statement should not be taken lightly, as it could inadvertently drag the Embassy into murky legal issues, including liability. But most importantly, it raises expectations that we are not in a position to meet.

3) Handling of Passports

In its discussion of the need for internal measures to safeguard the issuance, renewal, and passports, the Report keeps referring to the "passport *handling* process". In particular, it

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See ONPA note 2

states that "FSM laws and regulations specify that FSM foreign offices ... [sic] are not allowed to *handle* passports."

First of all, the term *handling* or *handle* does very little to clarify what it is that the overseas missions are prohibited from doing. In the context in which the term is employed in the Report, *handling* or *handle* could mean anything - from making the passport application forms readily available to our citizens residing abroad; notarizing the applications (an authority that has been delegated to several staff of our overseas offices) even if they are to be sent by the applicants themselves; forwarding passports to our citizens; returning expired, destroyed or lost passports to the Passport Office; assisting in informing the diplomatic community through diplomatic circulars about lost, stolen, or revoked passports, which is a standard diplomatic function; etc. In short, *handling* is an all-inclusive term that creates ambiguity where precision in the delineation of responsibilities is clearly preferable.

Second, to the best of our knowledge, the issuance and renewal of passports is a normal consular function of embassies and consulates but it is one that apparently has not found its fitness for resolution in our system. We recommend that the relevant laws and regulations be reviewed with a view to updating them where necessary. In many countries with which we are familiar, including the US, passports are issued or renewed by foreign ministries or departments of foreign affairs, while the *enforcement* aspects of the immigration laws and passport regulations is delegated to the legal authorities, such as ministries of justice or departments of homeland security.

The third point that we would like to underscore here is the rationale for the common practice, as we understand it, to vest the authority in foreign ministries or departments to issue and renew passports. Passports are documents that are meant primarily for use outside one's country and come into play when citizens travel abroad. In other words, when an FSM passport is used beyond our national borders, its treatment or request for recognition becomes a *foreign affairs* matter between the FSM and foreign governments - hence the need for the Department of Foreign Affairs, through its satellite offices, to be engaged on behalf of our citizens.

Insofar as it is a request for admission or recognition of admissibility into a country, a passport is like a diplomatic note - and the request for the admission of the citizens of the FSM into other countries is part of the function of the Department of Foreign Affairs as the mouthpiece of the government to foreign governments. To exclude the embassies and consulates from the so-called passport *handling* process would be tantamount to a thorough override of one of the fundamental consular functions of the Department of Foreign Affairs.

In recognition of the consular role of the Department of Foreign Affairs and its overseas missions, we recall that the authority was extended to the Embassy to renew passports for a period of not to exceed six (6) months. We were subsequently advised by the DI&L that this authority was recently overridden when the law lengthening the duration of the passports from five (5) to ten (10) years went into effect. In our view, the delegation of this authority to extend the validity of a passport, albeit in a limited manner, is an acknowledgment of the shared function and responsibility between the Department of Justice and the Department of Foreign Affairs in this very important field of governmental authority.

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The fourth and final point that should be made on this subject is that laws and regulations must be established to cater to the real needs of the living rather than to serve merely as decorative pieces or museum displays. Accordingly, discussions relating to the functions of the overseas offices in the so-called passport handling process must take into full consideration the unabated out-migration trends of our citizens especially to the US and its territories and possession, and the increasingly enforced adherence to the requirement for the FSM citizens to possess a passport as a condition not only to enter the US but also to seek employment.

The overwhelming majority of the consular needs of our citizens that bring them into contact with the Embassy in Washington relates, in one form or another, to problems of passport – i.e., for purpose of travel or to procure a visa to travel to other countries besides the US; secure employment; obtain drivers licenses or an additional source of identification; establish residence or eligibility for certain benefits; etc. Our overseas missions are expected to be pro-active in assisting our citizens. In the first place, the DC Embassy in particular is presently undermanned to effectively cater to the consular needs, in many different forms, of our citizens in a timely fashion. But what useful consular service would our diplomatic and consular officers provide to our citizens if, on top of the problem of staff shortage, their hands are tied tightly behind their backs by potentially outmoded legal strictures?

In saying this, we do not intend to downplay the critical importance of promulgating effective safeguard measures. Such safeguards should be formulated and put into place. In this regard, we are pleased to hear the DI&L noting that steps have already been taken to upgrade the security features of our passports to comply with ICAO international standards. The upgrade should help deter or minimize the misuse of our passports.

Just as important, we are not oblivious to the recent discovery about the misuse of our passports or passport specimen which should high-beam the need for greater internal safeguard and security controls. Mindful that this matter is still under investigation, we can only express our sincere hope that this incidence, grave though it is, will not be a basis for a thoroughgoing divesture of the consular responsibilities of the Embassy in the passport *handling* process, as this will undoubtedly be a disservice to our citizens. While we do recognize the need to improve and strengthen our internal safeguard measures, we should also make sure that our citizens who may stand in need of assistance do not inadvertently become the victims in the process. In this spirit, we stand ready to cooperate with the Department of Justice and DI & L to formulate such safety precautions and to undertake relevant training that may be provided.

In short, we acknowledge the existing laws and regulations relating to the issuance and renewal of passports. But we feel, as does the Audit Report, that there is now a need to review the existing system and to determine whether the carry-over from the Trust Territory days -- when there was not a Department of Foreign Affairs and when all authorities relating to the issuance of passports and the enforcement of the immigration laws and passport regulations were delegated to the Trust Territory Attorney General's Office. (Note that even during the TTPI, the renewal or revocation of a Trust Territory passport by the High Commissioner or his/her designee was still subject to the approval of the US Department of State).

Prudent Business Practices

A) We compliment the Report for calling attention to the problem of delinquency in the payment of bills. While there are many factors and sources contributing to this matter,

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the Embassy must not shirk its responsibility for this problem which it will do its utmost in preventing its recurrence.

But we would like to seize the opportunity to highlight the point that the potential consequence of this grave matter goes far beyond the relationship between the Embassy and the individual vendors. Track record of not paying bills on time contributes to a far larger "image problem" that in the long-run could raise concerns for the host countries of our overseas missions, including our donor countries and organizations. Preempting the stigma of truancy in the payment of legitimate obligations calls for the cooperation of all - from those tasked to write checks and send out bills to those charged with release or wire-transferring of funds to those responsible for determining the appropriate level of budget allocation.

B) We fully support the recommendation of the Audit Report to strengthen the Embassy's internal controls in making purchases for the Embassy - i.e., to obtain prior approval and to provide adequate supporting documents for the expenditure of funds. Equally, we applaud the Report in its effort to relieve the staff of the burden of using their salaries to make purchases especially when reimbursements are not made in a timely manner. This should also prevent the potential problem, as also cited in the Report, of presenting requests for reimbursement more than once.

C) If it can be brought to light in here, it is regrettable that the Audit Report overlook to note the consequences or impact of the practice of having the Embassy paying for the repatriation costs of human remains to the FSM without being fully reimbursed or not being reimbursed at all. We are pleased that this practice has ceased in the last two or three years, but we believed it left a great impact on the management of the Embassy's financial resources.

D) It would also have been appreciated if the audit looked into the problem of health insurance coverage for Embassy staff and excessive delays in getting reimbursed. There is the perennial problem that the FSM health insurance is not recognized anywhere on the US mainland, making the FSM insurance virtually useless for the Embassy staff and their dependents - unless one has expendable income or tons of cash stashed away that can be used to pay for medical services upfront.

This is a serious problem that has been overlooked by the Government. Embassy staff pay their premium on time through automatic deductions from their payroll. They are assessed an additional fee for non-residents. In light of the non-recognition of the FSM insurance on the US mainland and the excessive long delay for staff to be reimbursed from Pohnpei, in what ways can the Government come to the rescue of its own responsibility. The FSM Government should also deliver on its responsibilities and obligations.

See ONPA note 3

Possible Cost Savings

A) While we shall leave it to the FSM leadership to decide the wisdom of the recommendation to sell the Embassy and to move into rental space, we beg leave to offer some thoughts for all to ponder over:

f) Unlike now that the Embassy building is an investment, the FSM Government will have no title over the rental property. The rental funds will be money flushed down the drain without ownership;

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ii) With its recommendation to rent, the Report opaquely renders a decision as to the level and direction of the FSM Government's relations with the US Government in the foreseeable future by vagabonding in rented, possibly smaller spaces;

iii) The decision as to where to locate our "embassy on wheels" is not a unilateral decision. We cannot locate our office wherever we please to place it. We must first obtain the permission of the host state and the application process is cumbersome

iv) Renting has many potential problems, as we have already learned from the recent experience of one of our sister missions when enough funding was not made available and lease payment was not paid. Fortunately the impending eviction was averted at the last minute. Without a permanent home, our Embassy in DC would also run the inherent problems of moving around - i.e., disruption in the operation of the Embassy, financial costs of relocation. Of course, change of address and contact details could be made; but they are more than just a nuisance to ourselves and our citizens but also to the countries with which we deal, including perhaps the host country itself, and finally

v) The Report provides no basis of the assurance that renting in the long-run will be more economical, except perhaps if we decide to drastically reduce the size of our diplomatic presence in the US and rent a smaller room outside the designated zones for embassies - which will be a different matter altogether.

B) The Report's proposed relocation of the Legal Counsel to the main building from the carriage house as another possible cost-cutting measure could, using the higher cost estimates of the Report, result in a savings of approximately \$3,600 per annum for the FSM Government. This matter is under active discussion.

But at least for the purpose of historic accuracy, let it be pointed out that the idea of relocating the Legal Counsel on to the premises of the Embassy was conveyed in the form of the decision of two Secretaries of Foreign Affairs. In their judgment, it was in the best interest of the FSM Government to have full access to the Legal Counsel and to have him present on site especially during the renegotiation of the Compact to have his full attention and access. We believe there is still value to that access, taking into consideration that the Legal Counsel helps out in other useful functions of the Embassy not necessarily directly related to his Compact responsibilities.

See ONPA note 4

"Access" is a priceless commodity in Washington DC, as it is elsewhere. Thus, unless there are no other factors to be considered, the question is whether the savings of \$3,600 has greater value than the FSM Government's need for full access and ears of the Legal Counsel.

C) We also take note of the Report's other cost-saving recommendation relating to the reduction of cleaning services of the Embassy for lesser pay. In these hard times of reduced government resources, austerity should be the modus operandi. Yet, this recommendation seems to "tease" the Report's other observation about the increased value of the Embassy building after the renovation work and the need to safeguard it with property insurance coverage and, by implication, to maintain its upkeep and physical appearance at a satisfactory level.

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The upkeep of our embassy after some renovation work on it has just been done is no small matter. And thanks to the Audit Report for inviting attention to the issue, we would like to take the matter further where the Report left it off. For those of us who witnessed first-hand, literally speaking, the establishment of a rodent colony on the Embassy premises, apparently encouraged by careless disposal of food waste and other garbage from nearby restaurants and buildings, the need for rigorous or constant upkeep of the Embassy is an absolute necessity.

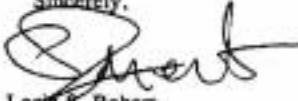
At least on two occasions as a result of the rodent problem, the local health authorities and alarmed neighbors came to the Embassy to inquire about the matter. Besides the embarrassment that the situation created, we also faced the risks of having the Embassy declared by the authorities as an unsanitary building. Accordingly, we urge that the recurrence of this serious problem should not be allowed after the Embassy building has just gotten a new face-lift. This kind of problem can also contribute conveniently to another form of "image problem" in this city where diplomatic missions are kept tidy, prim and proper.

Set aside for the time being the disappointing result of the renovation work of the Embassy and the manner in which the renovation money was managed or spent which have understandably angered a good many of us. The fact remains that: *i)* some significant amount of money has been spent on the building, and we should not make the situation worse by reducing the cleaning services and maintenance of the Embassy; *ii)* the Embassy is a public facility that should bear semblance of neatness and dignity, and *iii)* the Chancery is part of our country's soil in the heart of Washington DC and therefore a showcase for the FSM to all its visitors.

See ONPA note 5

In short, the Embassy building should be adequately maintained, both interior and exterior. The building that stands on 1725 N Street NW is not just a house, it is a soil of the FSM. It should be kept and maintained in a dignified manner so that we all can be proud to say it is our own.

In concluding our response, we hope that the comments and observations that we make will contribute meaningfully to the efforts aimed at improving the management and operation of the Embassy in Washington. Thank you again for the opportunity to comment.

Sincerely,

Lorin S. Robert
Deputy Secretary

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Appendix VII

Auditor's Response to DOFA's Comments

Note 1: Page 3 of the comments suggests we incorrectly included the responsibility of the Embassy toward private organizations from a mission statement in the budget proposal. Note that the responsibilities of the Embassy provided in the report are statutory requirements established through FSM Public Law 2-4, as amended.

Note 2: Page 4 of the comments suggests that our term of "handling" passports is not clear. We changed the sentence in the final report to highlight the information originally located in the footnote which deals with authority the Embassy has with the FSM passports. Specifically, the Embassy assists FSM citizens residing on the U.S. mainland with renewing or extending their FSM passports by forwarding passport applications and related material (i.e. expired passports, renewed passport picture, money order, and birth certificate) to DI&L. This authority does not mention handling (i.e. touching, distributing) the actual passport booklets. If the FSM government decides to amend current regulations to allow the Embassy to receive renewed, lost and specimen passports, DOFA and the Embassy needs to establish adequate controls over passports. Without adequate controls the passports are not safeguarded against fraud, waste and abuse.

Note 3: Contrary to the comments on page 6, ONPA did not recommend selling the embassy building. We recommended that an analysis of the benefits and cost of maintaining the embassy in the current building be performed. We agree with DOFA that intangible aspect of keeping the embassy building should be included in the benefit cost analysis. We recommended this analysis to identify the real cost of maintaining the Embassy building. For example, although some interior cosmetic work, primarily painting and carpeting, has been done on the building, the Ambassador stated that more work needs to be done. The work needed, upgrading the electrical wiring and plumbing, is expensive especially in a building over a hundred years old. We believe that the FSM government should have full information to make a decision and be aware of the real cost of maintaining a 100 year old building as the Embassy.

Note 4: The comments on page 7 acknowledge that there are active discussions underway to consider moving the legal counsel into the main building. However, contrary to comments made in the third paragraph of the section, we believe moving the legal counsel into the main building with the Embassy staff could actually improve "access."

Note 5: We agree with the statement on page 8 of the comments that the embassy building should be adequately maintained, both interior and exterior. The goal of our suggestion was to reduce the cost of the cleaning services. While we don't have the prices of other cleaning services for comparison, spending about \$90 a day (\$1,800 a month divided by 20 working days) seems excessive to clean after 4 people worked in the building.

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Description

Exhibit I – Front, Main Building

Exhibit 1-- View of the Embassy's front façade.

During renovation, the decorative blocks on the windows and under the eaves were repaired and repainted. The red bricks were sandblasted.

Exhibit 1



Exhibit 2-- View of the Embassy's front façade.

During renovation, the light fixture was installed, and the red bricks were sandblasted. The security bars were installed before the renovation.

Exhibit 2



Exhibit 3-- View of the Embassy's front walkway.

During renovation, the previous walkway was replaced with slate tiles.

Exhibit 3



Exhibit 4-- View of the Embassy's front steps.

During renovation, the red bricks were also added to enclose the small front lawn area.

Exhibit 4



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Description

Exhibit II – First Floor, Main Building

Exhibit 5

Exhibit 5-- View of the first floor reception area.

According to Embassy officials the loss of the property insurance resulted in part from the property insurers citing a gas leakage from the fireplace during one of their spot checks.



Exhibit 6

Exhibit 6-- View of the first floor hallway.

Although painted about 2 months ago during the renovation, the wall shows stains have developed from leaking pipes to the water heater in the closet behind the door.



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Description

Exhibit III – Fourth Floor, Main Building

Exhibit 7-- View of the fourth floor bathroom door.

During the renovation, the bathroom was painted but the doorknob was not adequately replaced. An employee was accidentally locked in the bathroom and used his cell phone to call the secretary to get out.

Exhibit 7



Exhibit 8-- View of the fourth floor ceiling in Deputy Chief of Mission's office.

During the renovation, the office was painted, but areas of the ceiling appear to have only the primer paint applied.

Exhibit 8



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Description

Exhibit IV – Rooftop, Main Building

Exhibit 9

Exhibit 9-- View of the air conditioner on the roof.

During the renovation, the roof had new roof paper and tar applied.



Exhibit 10

Exhibit 10-- View of the air conditioner on the roof.

During the renovation, a water drainage pipe connected to the centralized air conditioner was not connected to the gutter. Instead, the pipe scattered water throughout the roof.



Exhibit 11

Exhibit 11-- View of the second air conditioner on shed roof in courtyard.

Note: that the electrical wiring and panel box are corroding.



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Description

Exhibit V – Courtyard

Exhibit 12-- View of courtyard from the third story fire escape.

During renovation, the courtyard was paved with slate tiles. Note the puddle of water in the center that indicates that the drainage is clogged.

Exhibit 12



Exhibit 13-- View of steps leading to the basement entrance from the courtyard.

Note the moss-covered steps. During our fieldwork, this area of the courtyard did not dry out.

Exhibit 13



Exhibit 14-- View of steps leading to the basement entrance from the courtyard.

Gutter from the roof of the main building is drained outside the back entrance of the basement.

Exhibit 14



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Description

Exhibit VI – Garage

Exhibit 15-- View of column in the garage that supports the offices above.

Note that the support beam has temporary reinforcements, which may need to be replaced.

Exhibit 15



Exhibit 16 & 17-- View of the back wall of the garage.

Note the cracks in the cinder blocks.
Exhibit 17 is a close-up of this area.

Exhibit 16



Exhibit 17



Exhibit 18 -- View of the main office space above the garage.

This is the office space used by the legal consultant.

Exhibit 18



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NATIONAL PUBLIC AUDITOR'S COMMENTS

We wish to thank the staff at the Embassy, DOFA, DOF&A, DI&L and TC&I for their assistance and cooperation during the review.

The ONPA will perform a follow-up review within the next 6-9 months to ensure that the Embassy has taken corrective measures to address all findings and recommendations provided in this report.

In conformity with general practice, we presented our draft findings to officials from DOFA, DOF&A, DI&L and TC&I. They generally agreed with our findings and provided written comments, which are attached.

In addition to providing copies of this report to the President and Members of the FSM Congress, we also sent copies of this report to the Secretary of the DOFA, DOF&A, TC&I and Department of Justice. We will make copies available to other interested parties upon request.

If you or your staff have any questions regarding this report, please contact me at 691-320-2862/2863 or hhainrick@fsmpublicauditor.fm. Contact points for our Office may be found on the last page of this report. The ONPA staff who made major contributions to this report are listed on the last page.



Haser H. Hainrick
National Public Auditor

October 20, 2006

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ONPA CONTACT AND STAFF ACKNOWLEDGEMENT

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