

Office of the National Public Auditor

Federated States of Micronesia

Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01



Haser Hainrick
National Public Auditor



FEDERATED STATES OF MICRONESIA

Office of The National Public Auditor

P.O. Box PS-05, Palikir, Pohnpei FSM 96941

Tel: (691) 320-2862/2863; Fax: (691) 320-5482;

CID Hot Line: (691) 320-6768; E-mail: FSMOPA@mail.fm

June 16, 2006,

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

RE: Inspection of FEMA expenditures for Chuuk State

We have completed our inspection of the U.S. Federal Emergency Management Agency (FEMA) expenditures for Chuuk State for fiscal years 2004 and 2005. Our objectives were to determine whether FEMA expenditures in Chuuk were properly authorized and approved prior to the processing of payment checks and whether payment checks were addressed to the right payees. We conducted our inspection in accordance with the *Quality Standards for Inspections* issued by the U.S. President's Council on Integrity and Efficiency.

We found weaknesses of the internal controls in the expenditure of FEMA funds which could contribute to the appearance of misuse of these funds. The internal control weakness of writing checks to a government official instead of to the government entity allowed commingling of funds and led to other internal control weaknesses when new officials were elected into office. In addition, lack of adequate compliance with existing procedures and the absence of procedures, allowed various errors including making expenditures without proper authorization and missing documentation for expenditures.

In conclusion, of the vouchers we reviewed, we found that some of FEMA expenditures in Chuuk were not properly authorized and approved prior to the processing of payment checks, and some of the payment checks were improperly addressed to the person holding the office. This review excluded 22 of the 115 vouchers because they could not be found. 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", written over a horizontal line.

Haser Hainrick
National Public Auditor

Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01

BACKGROUND

The U.S. Federal Emergency Management Agency (FEMA) allocated \$4.96 million to the Federated States of Micronesia (FSM) for the State of Chuuk to recover from damage done by three typhoons: Chata'an in July 2002, Pongsona in January 2003 and Lupit in December 2003. The FEMA funds were meant to assist Chuuk State and local governments respond to and recover from the disasters created by the typhoons. See Table 1 for the breakdown of FEMA funds provided for each typhoon.

Table 1: Schedule of FEMA Funds Allocated to Chuuk for Three Typhoons

Description	US FEMA Funds
Chata'an typhoon public assistance projects	\$1,675,595
Chata'an typhoon sub-grantee administration	32,075
Chata'an typhoon hazard mitigation projects	1,195,278
Pongsona typhoon public assistance projects	1,967,982
Pongsona typhoon sub-grantee administration	44,500
Lupit typhoon public assistance projects	46,523
Total	\$4,961,952

The terms of the assistance from FEMA are described in the "Master Agreement For Requests For Direct Federal Assistant" document. In this Agreement FEMA is the grantor, the FSM Government is the grantee, and the Chuuk State Government is the sub-grantee. The FSM Disaster Control Office is the authorized representative of the FSM Government for the Agreement. After the FSM Government declared a disaster and requested assistance, FEMA determined the amount of funds to provide for public assistance projects including debris removal, implementation of emergency protective measures and permanent restoration of infrastructure. FEMA also determined the amount of funds to provide to the sub-grantee for administration of the public assistance projects. In addition, FEMA encouraged protection from future damage by providing assistance for hazard mitigation measures during the recovery process. FEMA and the Chuuk State Government agreed upon the scope and estimated costs of these hazard mitigation measures before the work began.

Responsibility for use of FEMA funds is shared among several National and State agencies. The FSM Department of Finance and Administration (DoF&A) initially receives the funds from FEMA. To obtain reimbursement from the DoF&A, the Chuuk Department of Administrative Services must provide documentation for the local and State government expenditures. After reviewing and verifying the request and supporting documentation, DoF&A reimburses the approved expenditures.

While Chuuk Department of Administrative Services reimburses the vendors and local governments, it deducts the related taxes. Specifically, the Department splits reimbursement payments into two vouchers, one for the vendor and the other for the state for taxes withheld.

Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01

In August 2005, FSM Disaster Office personnel were sent to Chuuk to review and reconcile FEMA accounts and review the status of FEMA project funds. The staff submitted a trip report detailing their findings resulting from the work performed in Chuuk. However, we did not rely on their findings because they could not provide any documentation to support their findings.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of this inspection were to determine whether FEMA expenditures in Chuuk were properly authorized and approved prior to processing of payment checks, and whether payment checks were addressed to the right payees. To meet these objectives, we obtained funds status and detailed expenditure reports, including related documents, from the DoF&A in Palikir and from the Department of Administrative Services, in Chuuk State.

We inspected supporting documentation for disbursement checks for selected FEMA vouchers that were available. We selected 115 vouchers of \$1,000 or more for review as follows: 89 vouchers involved Public Assistance expenditures, all 7 vouchers involved mitigation projects and all 19 involved grantee administrative expenditures. We inspected supporting documentation for vouchers, carbons of checks written and entries in the general and subsidiary ledgers.

We discussed these matters with officials at Chuuk Department of Administrative Services. In addition, we discussed the status of mitigation projects with the Chuuk Disaster Control Office which oversees these projects and verifies that the projects meet the technical specifications. We obtained documents from the DoF&A which shows the funds received from FEMA and the funds distributed to Chuuk. We obtained an understanding of the FEMA process in FSM from the FSM Disaster Control Office which is the authorized representative of the FSM Government. In addition we obtained a trip report detailing findings resulting from their work in Chuuk. We examined the FEMA accounts in light of the trip report submitted by the FSM Disaster Office staff. Since they could not provide supporting documentation for their findings, we inspected documentation to determine whether we could identify similar findings as those listed in their trip report.

FINDINGS AND RECOMMENDATIONS

We found internal controls weaknesses in the disbursement of FEMA funds which could contribute to the appearance of misuse of these funds. The absence of procedures related to consistent filing of adequate support documentation resulted in missing documentation for airline expenditures and entire vouchers. Lack of adequate compliance with exiting procedures resulted in various errors including an unprocessed stale check, an overpayment of \$1,000, and expenditures made without proper authorization. In addition, the lack of a policy regarding addressing checks to a government official allowed possible commingling of funds and led to other internal control weaknesses when new officials were elected into office.

**Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01**

**Lack of Internal Controls Procedures
Caused Incomplete and Missing Documentation**

We found several situations in which lack of procedures regarding controls over voucher folders and instructions on how documentation should be filed caused voucher documentation to be missing or incomplete. The FSM National Government Records Retention Policy requires that documentation of accounting records should be maintained for six years.

- Over 18 percent of the vouchers we requested (22 of 115) could not be found. These vouchers accounted for over 40 percent of the dollar value of the sampled vouchers (\$444,491 of \$1,088,069). We were therefore unable to review the propriety of these vouchers because the required documentation was missing.
- Almost 20 percent of the travel vouchers we inspected (3 of 16) had no supporting documentation for the cost of the airline ticket. Although we were able to find the travel agent's bill for the remaining voucher, they were not filed consistently. Some of the documentation was filed with the travel advance, some with the travel claim voucher, and some with the voucher for the state taxes paid on the travel. The lack of procedures resulted in three airline tickets totaling \$4,635 not having the required documentation.

We recommend that the Director of the Department of Administrative Services ensure that all checks have vouchers with supporting documents that establish the expense that has occurred before disbursement of checks. In addition, the Director should establish inventory control procedures for voucher storage which would identify the location of vouchers.

Auditee's Response:

Agreed

Beginning FY2006, travel documents are filed according to the sequential numbering of vouchers. Retrieval of documents is now easier since only the Travel Authorization personnel have access to Travel Authorization files. Documents being taken out from the Travel Authorization office are logged in/out to account for the movement of these documents.

**Internal Control Procedures
Were Not Followed**

We found several situations in which procedures have not been followed causing a voided check to be listed as paid, a voucher to be overpaid, and vouchers to be paid without proper authorization.

- Procedures were not followed causing 30 percent (28 of 93) of the vouchers we reviewed to be paid without proper authorization. See table 2 on page 4 for type and number of documents not authorized. Further, 7 of the 28 vouchers were paid although two of the documents

Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01

lacked proper authorization. These 28 checks totaling \$145,700 has been paid to vendors without the approval of the Director of Administrative Services or his designee.

Table 2: Number and Percentage of Documents Not Authorized by Type of Document

Type of Documentation Not Authorized	Document Not Authorized	
	Number	Percentage
Accounts Payable Vouchers	8	9%
Purchase Orders	19	20%
Purchase Requisitions	8	9%
Total payments made without proper authorization	28	30%

- Procedures were not followed several times causing a voided check, almost 2 years old, to still be listed in the computer system as paid. The department staff did not comply with procedure that requires a voided check to be forwarded to the reconciliation section for processing. After one year, government checks become stale and can no longer be cashed. The reconciliation section should have processed the check when it became stale. Because the procedures were not followed a voided check for \$22,191 had not been removed from the computer system and the account balance was understated.
- Because processing and reviewing procedures were not followed, an overpayment of \$1,000 was made on a \$5,000 contract. Specifically the vendor was paid the entire contract amount of \$5,000, instead of using Chuuk Treasury's normal practice of withholding five percent (\$250) for taxes. In addition, the State was paid \$1,000 for taxes, instead of the \$250 it should have received. Because procedures were not followed, an overpayment of \$250 was made to the vendor and \$750 was made to the State.

We recommend that the Director of Administrative Services ensure that all internal control procedures are followed.

Auditee's Response:

Agreed

Although not a single set of documents (Accounts Payable Voucher, Purchase Order, and Purchase Requisition) has been processed without authorization, still, there was negligence on our part in missing authorization for some documents. However, beginning FY2006, a thorough review is now being done for all vouchers due for payment. All pertinent documents are properly approved before checks are printed and supporting documents are double checked by the payable section before the vouchers are filed.

The voided check remaining with the cashier was an error and is an isolated case. All voided checks are forwarded to the reconciliation department for corresponding adjustment in the computer system. We will implement a constant and periodic checking with the cashier to ensure that all voided checks are properly handled and accounted for.

Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01

The overpayment to vendors and to the Chuuk Treasury was due to miscalculation of the staff doing the processing of these documents. This error is an isolated case. Every payment being processed is being doubled checked to make sure we have the accurate computation of amounts due to vendor and the applicable withholding taxes. Our staff are required to carefully check every detail of the expenditures before they are processed into payable vouchers.

Checks Payable to Office Holders
Create Appearance of Misuse of Funds

Checks were made payable in the name of the official in office giving the appearance of misuse of FEMA funds. While we did not count the number of times we found checks payable to office holders, this appeared to be a common practice. Most of the time, the name of the office holder was followed by his title (e.g. John Doe, Mayor), but other times it just listed the name of the office holder (e.g. John Doe). Most checks to office holders were to mayors, but we did see several that were written to officials in the state government such as the director of a department.

Prudent business practice requires that checks should be written to the entity that is to receive the funds. For example, payments for goods received at the hardware store are made payable to the store, not to the president of the company. Similarly, checks to a state or municipality should be made payable to that entity not to the governor or mayor.

The Department of Administrative Services does not have a policy regarding who should be the payee on checks to government offices and municipalities. In addition, councilmen of some municipalities have requested the checks be made payable to the mayor because the municipality lacked a bank account and believed it would be difficult to cash the check quickly without a bank account.

There are several results of making a check payable to a government official. First, it leads to the appearance of inappropriate use of funds. Second, since the check could be intended for the official's personal use and not the office he/she represents, it is harder to prevent and/or identify when funds are actually misappropriated by government officials. Third, the official could commingle government and personal funds by depositing the check into the official's personal account.

We recommend that the Director of the Department of Administrative Services establish a policy that checks to municipalities and state government offices should be made payable to the entity and not the official currently in charge of the office. If the municipalities have concerns about this policy, the Director should suggest that municipalities discuss the check cashing issue with the local banks. One of these banks told us that they will cash a check drawn from their bank even if the municipality does not have a bank account.

Auditee's Response

Agreed

**Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01**

We are in the process of reviewing this practice of writing an individual's name (mostly mayors or officials of the municipalities) as payee to the check intended for municipalities' expenditures to minimize or eradicate the likelihood for abuse or misuse of funds. We may no longer give an exception to municipalities without bank accounts. If some municipalities could establish bank accounts for their respective municipalities, there is no reason why other municipalities cannot do the same.

**Policy of Allowing Checks to Office Holders
Created Inaccurate Documentation**

We found documentation for two Accounts Payable Vouchers that did not support the name listed on the checks. Specifically, the voucher showed the name of the former mayor of the municipality and the check was made payable to the newly elected mayor. This usually occurred because 20 percent of funds for a FEMA project were reserved until the project was completed. Therefore, a check for 80 percent of the project costs was made payable to the mayor in office at that time. However, when the remaining 20 percent payment was to be made, a new mayor was in office and the check was written to the new mayor. All the documentation for the entire project (100 percent) contained the former mayor's name even though the 20 percent payment was made when the former mayor was replaced by a newly elected mayor. Further, on the vouchers we reviewed, there is no statement on the documentation that the check was made payable to the newly elected mayor. Therefore, the Accounts Payable Voucher did not support the name on the check. The effect is two checks totaling \$7,036 were made payable to the newly elected mayor without proper documentation.

Our previous recommendation—that checks to municipalities and state government offices should be made payable to the entity and not the official currently in charge of the office—should eliminate this documentation problem.

Auditee's Response:

Agreed

With the establishment of municipalities' bank accounts, the problem of issuing checks to office holders will be eliminated.

**Policy of Allowing Checks to Office Holders
Identified ADP System Weakness**

Because of a computer system internal control weakness, the computer system allowed a one time override of the payee for a check. This override caused a new person's name to be written as payee but did not record this name into the computer record. The computer system and printout reflected only the original payee's name as the check's recipient. In one case we found, the name of the former mayor of the municipality listed in the computer system and the name of the newly elected mayor on the actual check.

Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01

The result of this type of error is that the reliability of the computer system is suspect and the risk of fraud is heightened. Whenever basic information such as payee is found to be incorrect, the reliability of the entire computer system comes into question. Further, this lack of internal control could easily be used to misappropriate funds by changing the payee after the voucher is processed for payment. The computer system would not detect any problem and only an examination of the actual check (or check carbon) would identify the problem.

We understand that within the year, a new computer system will be installed. We recommend that the Director of the Department of Administrative Services ensure that the new system does not allow the payee of a check to be overwritten.

Auditee's Response:

Agreed

The existing computer system will be replaced in the beginning of FY2007. The unexplained computer errors in our current system will no longer be experienced in the new system (according to the new system specialist), as potential errors in check processing will be identified by the computer system before a check is printed. Likewise, supervisory approval will be required before any changes are made in the permanent file of the vendors.

**Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01**

PUBLIC AUDITOR'S COMMENTS

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

In conformity with general practice, we provided a copy of the draft inspection report to the Chuuk Director of Administrative Services for his review and comment. He agreed with our findings. His comments are included in the findings and recommendation section of the report.

In addition to providing copies of this report to the President and Members of the Congress, we also sent copies of this report to the Secretary of the DoF&A. 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 or hhainrick@fsmpublicauditor.fm. Contact points for our Office may be found on the last page of this report. The Office of the National Public Auditor (ONPA) staff who made major contributions to this report are listed on the last page.



Haser H. Hainrick
National Public Auditor

June 16, 2006

**Office of the FSM Public Auditor
Inspection of FEMA Expenditures for Chuuk
ONPA 2006-01**

ONPA CONTACT AND STAFF ACKNOWLEDGEMENT

ONPA CONTACT

Haser H. Hainrick, 691-320-2862
E-mail: HHainrick@FSMPublicAuditor.fm

ACKNOWLEDGEMENTS

In addition to the contact name above, the following
staffs made key contributions to this report:

Ann Walker, Audit Supervisor
Moses Russel, Auditor-In-Charge
Yolanda Leben, Staff Auditor
Keller Phillip, Staff Auditor

ONPA's Mission

To enhance governance, accountability and performance in
the public sector through the delivery of independent
assurance and investigative services.

**Obtaining Copies of ONPA
Audit Reports**

The fastest and easiest way to obtain copies of ONPA
documents at no cost is through the ONPA Web site:
<http://www.fsmpublicauditor.fm>.

Order By Mail or Phone

Office of the National Public Auditor
P.O. Box PS-05
Palikir, Pohnpei FM 96941

To order by Phone: (691) 320-2862/2863

Hotline:

Website:
<http://www.fsmpublicauditor.fm/hotline.htm>
691-320-6768