

**OFFICE OF THE NATIONAL PUBLIC AUDITOR**  
**FEDERATED STATES OF MICRONESIA**

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**The Office of SBOC Violated the FPA and the FSM Budget Law**

**Report No. 2015-03**



**Haser H. Hainrick**  
**National Public Auditor**



# FEDERATED STATES OF MICRONESIA

## Office of The National Public Auditor

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December 16, 2014

Excellency Manny Mori, President  
Honorable Members of the FSM Congress  
Federated States of Micronesia

### **RE: Inspection of the Project Management Unit's FY-2014 Operations Budget**

We have completed our inspection of the Project Management Unit's (PMU) operation budget for fiscal year 2014. We conducted this inspection in response to a request from the Congress per Standing Committee Report No. 18-163. The Committee asked the National Public Auditor to look into the propriety of the use of un-appropriated sector funds from the prior fiscal year 2013 to finance the operations of the PMU during FY-2014.

Based on our inspection, we found that;

- SBOC authorized the use of Compact carry-over funds from FY-2013 for PMU's operations for the second and third quarters of FY-2014 based only on OIA's authorization yet without Congress appropriation as required. This action violated both the FPA and the FSM budget law.

We provided copies of this report to the Director of SBOC, Secretary of the Department of TC&I, and the Contracting Officer for PMU for their review and management response. They all agreed with the audit finding and recommendation. Their written responses are included in this final report.

Respectfully submitted,

A handwritten signature in blue ink, appearing to read "Haser Hainrick", is written over a blue ink scribble.

Haser Hainrick  
National Public Auditor

Xc: Director, Office of SBOC  
Secretary, Dept. Of TC&I  
Contracting Officer, PMU

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## **INTRODUCTION**

Among others, Standing Committee Report No. 18-163, which was adopted by the Committee on Transportations and Communications, stated in part that, “With the PMU funding, your committee is amazed that it (PMU) could continue to function for the remainder of FY-2014 without Congressional appropriation. Your committee would like the AG’s Office and the Office of the Public Auditor to look into the legality and use of the un-appropriated but used funding.” We conducted this inspection in response to the Committee’s request.

### **Background**

The Project Management Unit (PMU) at the National Government was the outcome of the National Steering Committee (NSC)<sup>1</sup> meeting in 2002. During the meeting, one of the decisions agreed upon was the creation of a PMU office at the National level to help facilitate the successful implementation and monitoring of the Infrastructure Development Program projects.

PMU was first contracted to GMP Hawaii Inc., in 2005<sup>2</sup>. It has the responsibility to facilitate the implementation of the Infrastructure Development Plan (IDP) for the Federated States of Micronesia. With approximately \$748 million predicted for infrastructure projects for the 20-year<sup>3</sup> IDP period, PMU’s role in the implementation of the IDP is extremely crucial.

PMU’s contract with GMP Hawaii Inc. expired on May 2007. During the Chief Executive Conference (CEC) in January 2008, the four state Governors and the President adopted a Resolution to relocate the PMU to the Office of the President. However, the Congress enacted a resolution that became Public Law 15-74. The law amended the FSM Code Title 2 Section 203 to place PMU under the Department of Transportation, Communication and Infrastructure (TC&I) at the FSM National Government effective March 2009. PMU remains there until now.

### FY-2014 PMU Operational Budget

PMU’s operational budget was funded by the compact infrastructure sector grant (Public Sector Infrastructure Program Management Unit Grant). In May 2013 however, the PMU through the Department of TC&I requested that the FY-2014 operational budget of \$1,250,909 be funded by the domestic revenue considering that the Compact Sector Grant would not be available before the beginning of Fiscal Year 2014. The FSM Congress initially appropriated \$312,727 or 25% of the total requested budget, which was enough for the first quarter budget only.

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<sup>1</sup> Created and formed by the President and the State Governors to oversee coordination and completion of the Infrastructure Development Plan (IDP)

<sup>2</sup> “Contract for Consulting Services between FSM National Government and GMP Hawaii, Inc. for Project Management Unit” executed 5/19/05 (Contract #CB0277).

<sup>3</sup> Year 2004-2023

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FY-2014 Supplemental Budget

PMU requested for supplemental budget amounting to \$938,181 for the second, third and fourth quarters of FY-2014. However, Congress did not act on the request. Since PMU had unobligated funds from prior year (FY-2013) operational budget, it (PMU) decided to apply the allowable procedures<sup>4</sup> under the Fiscal Procedures Agreement (FPA) to be able to use the unobligated funds. PMU sent a letter to the Office of Statistics, Budget and Economic Management Overseas Development Assistance and Compact Management (SBOC) requesting the US Office of Insular Affairs (OIA) for the extension of the availability of the FY-2013 unused compact infrastructure sector grant. The request was approved by OIA.

Based on the OIA approval, SBOC extended the expiry of the compact infrastructure sector grant from September 2013 to June 2014 for PMU's operational budget without the required appropriation from the FSM Congress. The extension of the allotment allowed PMU to be able to finance the second and third quarter operations in FY-2014. To cover the budget shortfall for the last quarter of FY-2014, PMU requested a supplemental budget amounting to \$315,000, which Congress approved and appropriated under PL 18-75.

**Legal Framework**

The broader texts of the Compact unobligated carry-over funds and their applicable requirements are outlined at page 7 – 9. However, a summary of the requirements for Compact unobligated carry-over funds are presented below.

1. Article VI Section 1 (a) (1) of the FPA requires that Compact funds shall be used in accordance with the FSM laws and procedures for spending and accounting of funds.
2. The FSM Constitution gives the Congress the power of the purse....."Money may not be withdrawn from the General Fund or special funds except by law."
3. The operational budget from the General Fund shall commence its operation (by law) on October 1 (current fiscal year) and shall expire on September 30 (subsequent year). The extension of funds shall be subject to appropriation by the Congress.
4. All national budgets are approved along with the justification and condition of its activity in the appropriation law. Any other activities such as carry-over, re-allotment, or reprogram shall comply with the terms and condition of the budget, or grant award and the grantee applicable law. Title 55, Chapter 3, Section 315 (2) (b) requires that unobligated allotted funds will be available for re-allotment subsequent to further appropriation of unobligated funds by the State legislature or Congress.

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<sup>4</sup> Article VI Section 1(d) of the FPA , "The government of the Federated States of Micronesia shall obtain prior approval whenever any of the following is anticipated: (ii) the need to extend the period of funding availability".

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**Objective, Scope and Methodology**

Objective

The objective of the inspection was to determine whether the PMU’s operational budget for FY-2014 complied with the Fiscal Procedures Agreement (FPA) and the FSM budget laws and regulations.

Scope

The audit scope covered the PMU operational budget for FY-2014 as appropriated by the FSM Congress under Public Law 18-15, as amended. We conducted this inspection pursuant to Title 55 of the FSM Code, Chapter 5, which states in part:

*“The Public Auditor shall inspect and audit transactions, accounts, books and other financial records of every branch, department, office, agency, board, commission, bureau, and statutory authority of the National Government and of other public legal entities, including, but not limited to, States, subdivisions thereof, and nonprofit organizations receiving public funds from the National Government.”*

We conducted our inspection in accordance with the *Quality Standards for Inspections* issued by the U.S. Council of Inspectors General on Integrity and Efficiency (CIGIE). Accordingly, we included such tests of records, transactions, and other inspection procedures that were necessary to achieve our objective.

Methodology

We performed our inspection fieldwork at the Office of SBOC, the Office of PMU, Department of TC&I, and the National Treasury at the Department of Finance and Administration (DoF&A) main office in Palikir, Pohnpei.

The inspection procedures included the review of the appropriation law and advice of allotment relating to PMU’s FY-2014 operations budget. Since the budget was funded by compact infrastructure sector fund, we also reviewed the requirements of the Fiscal Procedures Agreement under the Compact agreement between the United States and the Federated States of Micronesia for the spending of Compact funds, as well as the applicable requirements of the FSM Constitution, the FSM Code, and the FMR. We further obtained and analyzed the budget, fund status, and line-item expenditure report for the PMU’s FY-2013 operations since carried over funds from previous year budget were used. Finally, we interviewed the key staff and officials at PMU, TC&I, SBOC, and DoF&A.

**Prior Audit Coverage**

This is the first inspection conducted by the ONPA relating to the PMU’s operational budget.

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**Conclusion**

Based on our inspection, we conclude that the use of the Compact carry-over funds from FY-2013 for PMU's operations for the second and third quarters of FY-2014 did not comply with the Fiscal Procedures Agreement or the related FSM budget laws and regulations.

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**FINDINGS AND RECOMMENDATIONS**

**Finding 1: SBOC’s Allotment of PMU’s FY-2013 Carry-Over Funds to Supplement Its (PMU) FY-2014 Operational Budget Did Not Comply with the FPA and FSM Budget Law**

Article VI Section 1 (a) (1) of the FPA provides that the FSM shall spend and account for Compact funds in accordance with its laws and procedures.

The Constitution gives the FSM Congress the power to appropriate all public funds on behalf of the National Government. It states, in part, “*Money may not be withdrawn from the General fund or special funds except by law.*”

Title 55, Chapter 3, Section 315 of the FSM Code requires that unobligated allotted Compact funds will be available for re-allotment subsequent to.....further appropriation, of unobligated funds, by the State Legislature or Congress.

Of the total \$1,074,249 (Table 1) actual allotment to PMU for its FY-2014 operational budget, Congress appropriated only \$627,727<sup>5</sup> (58%). To cover its budget shortfall, PMU requested through the Office of SBOC and OIA approved the extension for the availability of its lapsed but unobligated FY-2013 Compact sector funds to cover its second and third quarters operational budget for FY-2014. The Office of SBOC allotted the carry-over funds and PMU started availing them for its operational budget. However, this authority to allot and to spend the carry-over sector funds from FY-2013 took place, based only on the OIA approval, but without the appropriation by Congress as required.

As a result, the allotment of unobligated carry-over funds amounting to \$446,522 was effected but outside of the legal authority allowed by law. Consequently, PMU spent \$196,883 above its legal budget in FY-2014. (See table 1 below for details)

**Table 1.**

<b>Description</b>	<b>Amount</b>
A. Total PMU FY-2014 Budget Appropriated by Congress	\$ 627,727
B. Less: Total Allotment	1,074,249
<b>Total Un-appropriated Allotment (A - B)</b>	<b>\$ 446,522</b>
C. Less: Total Actual Expenditures	824,610
<b>Total Over-Expended Budget (A - C)</b>	<b>&lt;\$ 196,883&gt;</b>

<sup>5</sup> \$627,727 was a combined total of \$312,727 (PL 18-15 dated 9/30/13) funded by Domestic Revenue and \$315,000 (PL 18-75 dated 7/25/14) funded by Compact Fund



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**Cause and Recommendation**

Both the Office of SBOC and the PMU did not follow the applicable provisions of the FPA and the FSM Budget Law. For instance,

- The FPA provides that “*the FSM shall spend and account for Compact funds in accordance with its laws and procedures.*”
- Title 55, Chapter 3, Section 315 of the FSM Code requires that unobligated allotted Compact funds will be available for re-allotment subsequent to.....further appropriation, of unobligated funds, by the (State Legislature or) Congress.

We recommend that the Director of SBOC and the Manager of the PMU should observe the requirements of the FPA and the applicable FSM budget law at all times prior to issuing advice of allotment and spending of Compact funds.

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## **APPENDIX A – LEGAL FRAMEWORK**

The use of funds from Compact Sector Grant and Domestic Revenue should comply with the FSM laws, regulations and agreement. These include the Fiscal Procedures Agreement (FPA), the Financial Management Regulation (FMR), the FSM Code, and the FSM Constitution.

### **1) Use of Compact Funds**

- a) In addition to its spending requirements, Article VI Section 1.(a).(1) of the FPA<sup>6</sup> also requires that the Compact funds shall be used in accordance with the FSM laws and procedures for spending and accounting of funds.
- b) The FSM Code Title 55, Chapter 3, supports “the right of the FSM States and the National Government to appropriate and expend Compact funds in accordance with their own respective laws, plans, policies and prerogatives”.

### **2) Appropriation of Operations Budget**

- a) The FSM law requires that all operation budgets of the National Government shall be subject to appropriation.
- b) The Constitution gives Congress the power of the purse, the ability to tax and to appropriate public money for the national government. The power to appropriate funds gives Congress a powerful influence over all the activities of the government. Article XII, Section 1 of FSM Constitution states, in part, that all “*public money raised or received by the national government shall be deposited in a General Fund or special funds within the National Treasury. Furthermore, it states in part, “money may not be withdrawn from the General Fund or special funds except by law.”*
- c) Title 55 FSMC, Chapter 1, Section 102.3 defines “Appropriation” as a law enacted by Congress<sup>7</sup>, which authorizes the National Government to incur obligations and to make payments out of the National Treasury in accordance with the law.

### **3) Allotment**

- a) Title 55 FSMC, Chapter 2, Section 215 defined "allotment" as “*the delegation of authority to a person to create legally enforceable financial obligations in accordance with applicable FSM State or National Law and the Compact, and its related agreement, within the limits specified in the National and State appropriation act*”.
- b) The President or his designee is authorized by law to issue an allotment advice.

### **4) Supplemental Budget**

- a) Supplemental Budget is a budget to fill in the gap between the "to date" of the previous authorization bill and some future date. These are additional funds provided to an agency or office to supplement its funding in order to keep the operation running.
- b) Like the Annual Budget, supplemental budget is subject to Congressional approval through appropriation law. It is an additional fund to the original budget thus; it adheres to the same reviewing procedures and requirements of the Annual Budget.

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<sup>6</sup> Article VI Section 1.(a).(1) of the FPA

<sup>7</sup> Article IX, Section 3 of the FSM Constitution explicitly defined the power of the Congress, which include the power to appropriate public funds.

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- c) Title 55, Chapter 1, Section 105 of the FSM Code specifies the procedure on supplemental or deficiency appropriations. It states that, “*The President shall transmit to Congress such proposed supplemental or deficiency appropriation as may be necessary on account of laws enacted after the transmission of the annual budget or which are otherwise in the public interest*”. It further states that the President shall accompany the proposals with a statement of the reasons for their omission from the annual budget.

5) Expiration of Operations Budget

- a) All budgets have beginning period and ending period or expiration date specified in the Budget Law. Chapter 3, Section 305 of Title 55 partly states that the allotment of funds shall specify the expiration date, provided by the appropriation laws of the respective State Legislature or Congress, upon which the previously allotted and unobligated funds should lapse. The operational budget from the General Fund shall commence its operation (by law) on October 1 (the current fiscal year) and shall expire on September 30 (the subsequent year). The extension of the funds shall be subject to appropriation by the Congress.

6) Unobligated funds and Carry-Over of Unused Funds

- a) All national budgets are approved along with the justification and condition of its activity in the appropriation law. Any other activities such as carry-over, re-allotment, or reprogram shall comply with the terms and condition of the budget, or grant award and the grantee applicable law. Title 55, Chapter 3, Section 315(2b) requires that unobligated allotted funds will be available for re allotment subsequent to further appropriation of unobligated funds by the State legislature or Congress.
- i. Alteration of approved budget should comply with the Compact Fund requirements in the FPA and the laws of the respective state. Public Law No. 13-63 affirmed the same concept when amending Title 55, Section 106(3) of the FSM Code, reiterating that the appropriation legislation covering Compact funds shall comply with the terms of the Compact and the Fiscal Procedure Agreement with respect to the receipt of Compact sector funds, and shall allow for reprogramming of funds to the extent permitted under the Compact and Chapter 3 of Title 55 of the FSM Code, and may require, as a condition to such reprogram, prior notice to Congress.

It further stated in part that appropriation or authorization of expenditure of funds shall be made by law.

- b) Article IV, Section 1 of the Fiscal Procedures Agreement (FPA) states that *unobligated funds shall carry over to the following Fiscal Year for reallocation to the applicable grant, unless otherwise provided in the Agreement or the Compact, as amended*. Title 55, Chapter 3, Section 315 of the FSM Code reaffirmed the same concept in its requirement that “*unobligated allotted funds will be available for re-allotment subsequent to;*
- *The determination by the State finance or Secretary of Finance of the total level of unobligated funds for each allotment; and*
  - *Further appropriation, of unobligated fund, by the State Legislature or Congress*

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- c) The act further require that the FSM Budget Officer shall allot all carry-over current account<sup>8</sup> program funds as current operations funds as specified by the State Governor or President, in accordance with applicable law. Furthermore, the FSM Budget Officer shall allot the carried-over compact funds for the operations of program account specified in appropriation laws.

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<sup>8</sup> Current Account – for each year of the Compact, those portions of the total grant assistance which are to be obligated for recurring operational activities including infrastructure maintenance as identified in the annual budget justifications submitted yearly to the Government of the United States.

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MANAGEMENT RESPONSE: Office of SBOC



THE FEDERATED STATES OF MICRONESIA  
OFFICE OF STATISTICS, BUDGET & ECONOMIC MANAGEMENT,  
OVERSEAS DEVELOPMENT ASSISTANCE AND COMPACT MANAGEMENT (S.B.O.C.)  
P.O. BOX PS 52, PALIKIR, POHNPEI FM 96941  
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December 12, 2014

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

*Handwritten signature and date:*  
12.15.2014



Subject: Comments for ONPA Audit on Inspection of the PMU Operational Budget for FY2014

Dear Mr. Hainrick:

Thank you for the opportunity to comment on the subject audit. We offer the following as our comments concerning the finding in the audit report.

Finding 1 – SBOC’s Allotment of PMU’s FY2013 Carry-Over Funds to Supplement Its (PMU) FY2014 Operational Budget Did Not Comply with the FPA and FSM Budget Law.

Comments: Prior to the audit, it was not clear to us especially to the budget staff that issuance of the allotment for PMU’s FY2013 carry-over funds, which was sourced from the infrastructure sector grants, would be conditioned only on the passage of a new appropriation law as you have pointed out in the audit. Instead, the understanding was that once the grant managers for the carry-over funds had approved the extension of the expired grant award for PMU’s operations, this would enable our office to issue the allotment. It had been the practice of the budget office over the years that as long as the terms of a grant are approved by the grant manager, SBOC can issue an allotment. In this case, the approval sought for PMU was to allow extension of an already approved grant award which had been approved earlier by an appropriation law. We were under the notion that issuance of the allotment for PMU would still be covered under our budget procedures. We now know this is a misreading of our budget procedures on our part and we will work toward correcting this.

As I have indicated in your other audit findings, we will endeavor to improve all aspects of handling allotments including ensuring our budget staffs are trained and new guidelines are in place to ensure strict adherence to the requirements of issuing allotments. We have started to make sure all grant awards whether they are new grant awards or grant award terms that have been approved for extension by the grant managers are endorsed by Congress before SBOC issues allotments.

We thank you for the opportunity to comment and for the recommendations for improving our processes.

Sincerely,

*Handwritten signature of Evelyn Adolph*  
Evelyn Adolph  
Director

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**MANAGEMENT RESPONSE: Office of PMU**



**FEDERATED STATES OF MICRONESIA  
Program Management Unit**

P. O. Box PS 4, Palikir, Pohnpei FM 96941  
Tel: (691) 320-2080 Fax: (691) 320-4532

December 8, 2014

To: National Public Auditor

From: Contracting Officer PMU

Through : Secretary D TC&I

Subject: Inspection of the PMU Operational Budget for FY 2014



I appreciate the opportunity to attend your exit conference on November 28th. The PMU has no objections to the findings in your inspection report dated November 25, 2014.

At the time we received the advice of allotment for the FY 13 carry over funds, neither our legal counsel or administrative staff took note of the lack of appropriation. Having never had the opportunity of using carry over funds, I was not aware of the proper procedure.

In the future I will make sure that all carry over funds are properly appropriated prior to expenditure by the PMU.

A handwritten signature in cursive script that reads "Bruce Howell".

Bruce Howell  
Contracting Officer

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**ONPA’S EVALUATION OF MANAGEMENT RESPONSE**

The Office of SBOC, the Department of TC&I, and the PMU all agreed with the audit finding and recommendation.

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**NATIONAL PUBLIC AUDITOR'S COMMENTS**

We would like to thank the management and staff at SBOC, TC&I, PMU, and DF&A for their assistance and cooperation during the course of the audit.

We have provided copies of the final audit report to the President and Members of the Congress for their use and information. Furthermore, we will make copies available to other interested parties upon request.

If there are any questions or concerns regarding this report, please do not hesitate to contact our Office. Contact information for the Office can be found on the last page of this report along with the National Public Auditor and staff that made major contributions to this report.



Haser Hainrick  
National Public Auditor

December 16, 2014



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**ONPA CONTACT AND STAFF ACKNOWLEDGEMENT**

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ONPA CONTACT:                   Haser H. Hainrick, National Public Auditor  
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ACKNOWLEDGEMENTS        In addition to the contact named above, the following staff made key contributions to this report:

Manuel San Jose CPA, CGAP, CIA, CISA, CRMA, Audit Manager  
Keller Phillip, Auditor-In-Charge  
Dane William, Staff Auditor  
Fidarina Akapito, Staff Auditor

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