

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



**STRONGER INTERNAL CONTROLS NEEDED AT THE DEPARTMENT
OF TRANSPORTATION, COMMUNICATION & INFRASTRUCTURE
TO PREVENT LOSS OF FUNDS ON DELAYED & INCOMPLETE
PUBLIC PROJECTS**

**Inspection Of Certain CFSM Road Projects in Kitti, Pohnpei State
under Public Laws 20-141 and 21-53**

Report No. 2022-05



FEDERATED STATES OF MICRONESIA

Office of The National Public Auditor

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September 26, 2022

His Excellency President David W. Panuelo
Honorable Members of the 22nd Congress
Secretary, Department of TC&I
Secretary, Department of Finance and Administration
Federated States of Micronesia

RE: INSPECTION OF CFSM KITTI ROAD PROJECTS (SALAPWUK & MWOAKOT) UNDER PUBLIC LAW 20-141 AND PUBLIC LAW 21-53

We have completed our inspection of the CFSM Kitti Road Projects (Salapwuk & Mwoakot) under Public Laws 20-141 and 21-53. The overall appropriation for both projects was \$150,000.000.

This inspection was conducted based on a request by the Mayor of Kitti Municipal Government (KMG) Pohnpei State, due to concerns of the FSM Department of Transportation, Communication, & Infrastructure (DTC&I) and the FSM Department of Finance and Administration (DoFA) releasing funding to the Contractor when both projects were not completed.

We concluded the following based on our inspection findings:

- There were ineffective and insufficient controls in relation to inspection reports or certifications used for the release of funds to contractors;
- There was non-compliance to the key terms and conditions of the construction contract agreement; and
- There were existing gaps in the process of evaluating bids and selecting the contractor at the FSM Department of Transportation, Communication and Infrastructure (DTC&I).

Overall, we identified a great need for improvement at the DTC&I whose officials are key players in the administration of public projects appropriated by the FSM Congress. There are also capacity needs to ensure adequate officials are available to handle the increasing projects and they are performing their work for the best interest of the Government and the people.

We have referred some of the issues to our Compliance Investigation Division (CID) for further review and evaluation.

Sincerely,

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

Haser H. Hainrick
National Public Auditor

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Abbreviations

\$	US Dollar
CFSM	Congress of the Federated States of Micronesia
DoFA	Department of Finance and Administration
DTC&I	Department of Transportation, Communication & Infrastructure
FMR	Financial Management Regulation
FSM	Federated States of Micronesia
KMG	Kitti Municipal Government
ONPA	Office of the National Public Auditor (FSM)
PCD	Project Control Document
PIO	Project Inspection Official
PL	Public Law
SOPs	Standard Operating Procedures

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1.0 INTRODUCTION

1.1. Reason for the Assignment

This inspection was first initiated by a request for an investigation that was made by the Mayor of Kitti Municipal Government (KMG) within Pohnpei state. The request was pertaining to two (2) public projects funded by the Congress of the FSM (CFSM projects). These were road projects for Salapwuk & Mwoakot. The Mayor for KMG raised concerns as to why the FSM Department of Transportation, Communication & Infrastructure (DTC&I) and the FSM Department of Finance and Administration (DoFA) released funding to the Contractor when both projects were not even half completed.

1.2. Background

Public Laws (PL) 20-141 and 21-53 were passed by the Congress of the Federated States of Micronesia (CFSM) to appropriate funds from the General Fund for road improvement and paving for Mwoakot and Salapwuk areas under the Pohnpei state At-Large Congressional election district.

Brief details of the two (2) projects are provided below:

Salapwuk road project

The FSM Congress appropriated \$50,000.00 to improve Rakuh to Utinpil secondary road in Salapwuk, Kitti as per PL20-141 section 4(1)(j). The intention of this project included contractual services to provide proper road improvements from the existing road at Kepingil, Salapwuk further up to Rakuh and Utinpil communities. The project will provide convenient transport of goods back and forth and with less vehicle maintenance cost after completion of the project. The awarded contractor for the Salapwuk Road project was a locally owned construction company. The approved estimated duration of the project was 45 days from the date in which the contractor signed the notice to proceed which was on June 2021.

Mwoakot road project

For the second project, the FSM Congress had appropriated \$100,000.00 to build a new paved road on the existing road in Mwoakot, Kitti as per PL21-53 section 4(10) (p). This road was intended to enable the passing of vehicles and people access to and from the community. The awarded contractor for the Mwoakot Road Project was the same locally owned construction company that was awarded the contract for the first road project above for Salapwuk. The approved contract duration of the project was 90 days from the date in which the contractor signed the notice to proceed which was on December of 2020.

1.3. Process for Administering Public Projects funded by the CFSM (referred to as CFSM Projects):

- i) Congress of the FSM:
 - ✓ Appropriates funding for the public projects
- ii) Allottee
 - ✓ Prepares Project Control Document (PCD) **to** specify and describe purpose of the projects;
- iii) Department of Finance, Budget Office:

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- ✓ Reviews the completed and signed PCD for approval if the information is sufficient in line with the appropriation law;
 - ✓ Issues Advice of Allotment for the approved PCD based on the approved budget.
- iv) Department of TC & I, Division of Infrastructure:
- ✓ Announces the project to interested bidders and requests for proposals;
 - ✓ Conducts bidding process and awarding of the contract to the selected bidder;
 - ✓ Administers the formalization of the Construction Contract Agreement;
 - ✓ Carries out inspection on the progress of the project and certifies payment requests made by the contractor(s).
- v) Department of Finance and Administration, Division of National Treasury:
- ✓ Issues payments if all attached documents are certified by the Project Inspection Officials (PIO) after due investigation and if the amount so requested is properly due and owing under the obligating contract

1.4. Expenditure Reports

The expenditure reports were obtained from DoFA and the details are summarized below for each of the two (2) projects:

1.4.1. Salapwuk Road Project:

The contract amount for the Salapwuk Road Project was \$49,600. Out of this amount, 10% of the project amount was for mobilization and another 10% for retention fees. The total amount expended for the project was \$37,200.00.

Table 1: Total Expenditure Report

Check Date	Amount	Purpose
6/25/2021	\$4,960.00	Mobilization
7/06/2021	\$17,380.00	Clearing of road in Rakuh to Utinpil
7/26/2021	\$14,860.00	Per memo, the project was 75% completed.
Total	\$37,200.00	

Source: DoFA’s Fundware system report generated on April 14, 2022

1.4.2. Mwoakot Road Project:

The contract amount for the Mwoakot Road Project was \$100,000.00. Out of this amount, 10% of the project amount was for mobilization and another 10% for retention fee. The total amount expended for the project was \$80,000.00.

Table 2: Total Expenditure Report

Check Date	Amount	Purpose
12/17/2020	\$10,000	Mobilization
12/23/2020	\$10,000	20% work completed.
01/14/2021	\$10,000	30% work completed
01/21/2021	\$30,000	Projected completed as per Job Order, C210064.
02/26/2021	\$20,000	50% work completed per memo from Secretary of TC&I and MS request.

Source: DoFA’s Fundware system report generated on April 6, 2022

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2.0 OBJECTIVES, SCOPE, METHODOLOGY

2.1 Objectives:

To determine whether the Salapwuk and Mwoakot road projects were administered in accordance with applicable laws and regulations.

- a) Determine the effectiveness and sufficiency of the controls in relation to inspection reports used for the release of funds.
- b) Determine compliance to the key terms and conditions of the construction contract agreement; and
- c) Determine if there is a gap in the process of evaluating bids and selecting the contractor;

2.2 Scope:

The inspection covered the implementation of CFSM public projects for Pohnpei state; namely the Kitti Municipal Road projects for Salapwuk and Mwoakot that were appropriated under PL20-141 and PL21-53.

2.3 Methodology

We conducted this Inspection in accordance with the quality standards for inspections and evaluations issued by the Council of the Inspectors General on Integrity and Efficiency (CIGIE). Those standards require that we plan and perform the inspection to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our inspection objectives.

To achieve our objectives listed in Section 2 above, the inspection team:

- a) Reviewed and assessed all information and records pertaining to the scope of the inspection;
- b) Assessed whether the administration of the two road projects complied with applicable laws and regulations;
- c) Carried out site inspection; and
- d) Interviewed Key Personnel

3.0 AUDIT MANDATE

We conducted this inspection pursuant to the authority vested in the National Public Auditor as codified under Chapter 5, Title 55 of the FSM Code which states in part as the following:

“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 non-profit organizations receiving public funds from the National Government”

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4.0 PRIOR AUDIT COVERAGE

This is the first inspection of the CFSM Pohnpei public projects for Mwoakot and Salapwuk (Rakuh to Utinpil) under PL20-141 and PL21-53; however, the [last CFSM audit report](#) that included projects for Pohnpei state was issued by the ONPA in February 2015.

5.0 COMMENDATION

We commend the current administration of the Kitti Municipal Government (KMG) for stepping forward to raise concerns over the incomplete public projects at Mwoakot and Salapwuk, that were funded by the FSM National Government. We encourage this practice as it promotes a culture of accountability that we all have a role to play in ensuring the effective and proper spending of government funds to benefit the citizens and members of the public.

We also commend the Secretaries of the DTC&I and DoFA for positively responding to our recommendations and who have communicated their commitment to implement the recommendations and make the necessary improvement in their relevant processes.

6.0 CONCLUSION

We concluded the following based on our inspection of the implementation of CFSM public projects for Salapwuk (Rakuh to Utinpil) and Mwoakot Road Projects:

- a) There were ineffective and insufficient controls in relation to inspection reports or certifications used for the release of funds to contractors.
- b) There was non-compliance to the key terms and conditions of the construction contract agreement; and
- c) There were existing gaps in the process of evaluating bids and selecting the contractor at the FSM Department of Transportation, Communication and Infrastructure (DTC&I);

The result of this inspection relating to the findings and recommendations are discussed in detail in the following pages.

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7.0 FINDINGS AND RECOMMENDATIONS

7.1. Finding 1: Insufficient and Misleading Certification of Project Status by the Inspection Officials for the Mwoakot Road Project

Criteria

Section 10.2.4 (Disbursement) of the FSM Financial Management Regulation (FMR), requires:

- (1) Funds shall be disbursed only to satisfy obligations legally incurred and due under these regulations. Any request for payment under design, constructions, procurement, or independent consulting contract must be certified by the Project Inspection Official before payment is made;*
- (2) such certification shall signify that it is the Project Official's best judgement, after due investigation, that the amount so requested is properly due and owing under the obligating contract and these regulations; and*
- (3) The Budget Officer may develop and require use of more detailed certification form in appropriate circumstances.*

In addition, the Project Control Document (PCD) states *"the Project Inspection Official designated in the PCD shall provide project management and oversight so as to ensure the adequate accountability of funds expended and completion of the project."*

Condition

The total amount appropriated for Mwoakot Road Project was \$100,000.00. The project has started and not yet closed out. There were already 5 payments made. Four (4) of which were paid for construction services and one (1) payment was for mobilization. The Total amount expended based on the disbursement record and [Table 3](#) below was \$80,000.00. \$20,000.00 of the fund remained, in which \$10,000.00 was for construction and the other \$10,000.00 for retention fee.

Like other CFSM projects, funds were disbursed based on the inspection reports submitted to support payment requests.

We also made site inspections with the KMG officials and DTC&I officials. Various attempts were made to interview and carry out a site inspection with the Contractor; however, were unsuccessful.

Based on our review of disbursement records, physical inspection of the project site, and the inspection reports we noted the following:

- a) 80% of the funding was already expended; however, less than half of the required project work was done. A senior official of DTC&I claimed that the contractor had already purchased the materials to complete the project. However, no work has been done since.
- b) Insufficient supporting documents for the inspection reports. The report would only provide the percentage of work completed with no justification or supporting documents;

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- c) The actual project status reported was not in line with the actual condition of the road project upon the site verification by the inspection team;
- d) Project scope, inspection reports and contract documents did not include the work carried out on another road in Mwoakot, as claimed by DTC&I.
- e) Second payment processing request was made based on the first inspection report used for the first payment request. Refer to the [Table 3](#) below for the details as indicated in Footnotes 1&2. This was not captured by Finance when processing the payments.
- f) Inspection reports were prepared by two designated PIOs, who were not coordinating when it comes to the reporting of the project status.
- g) As also noted during our review of the inspection reports as shown in the table below (Table 3), the third inspection report stated that the project was **successfully completed as per work** scope; however, inspection report for the fourth payment indicated that the project was **50% completed**; and
- h) Contractor’s budget breakdown of the project cost/schedule of bid price indicated the number of aggregates or materials needed for the project. There was no documentation or inspection of whether the number of materials specified in the budget breakdown was purchased and used.

Table 3: Amount disbursed for mobilization & contractual services for Mwoakot Road Project

Date of Inspection	Inspection Report/Payment Request Date	Purpose of Request	Amount Requested
N/A	N/A	Mobilization	\$10,000.00
Dec 21,2020 ¹	Dec 21, 2020	10% of work completion	\$10,000.00
Dec 21,2020 ²	Jan 11,2021	32.22% of work completion	\$10,000.00
Jan 5,2021	Jan 15, 2021	Successfully completed as per work scope	\$30,000.00
No inspection report attached	Feb 18,2021	50% of work completion	\$20,000.00
Total			\$80,000.00

Source: Disbursement records obtained from DoFA.

¹ Date of inspection was the same for the next payment request in footnote 2.

² Date of inspection was the same for the payment request in footnote 1.

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Effects:

As a result of false information provided for payment processing:

- Majority (80%) of the funds were expended and the project remained incomplete;
- Mwoakot Road project was delayed for over a year from the agreed completion date and work scope was not met, when the contractor submitted his request for time extension;
- Government did not collect the Liquidated Damage of \$66,802 from the contractor, being for delayed number of days from the agreed completion date; and
- The people and community who should be benefitting from the project were not satisfied with the condition of the road resulting in the complaint raised to ONPA, hence our inspection.

Therefore, we are referring this matter for further evaluation by our Compliance Investigation Division (CID).

Causes:

- FMR only states that projects are to be certified based on the best judgement of project inspection officials, without clearly specifying the required information and support documents to accompany the certification to make it eligible.
- Absence of internal policies and standard operating procedures in place to guide the administration of the infrastructure projects that are administered by the DTC&I.
- Project was assigned to two inspection officials who both issued either misleading or incomplete inspection reports as summarized in [Table 3](#) above.
- DTC&I did not have effective controls and procedures in place to mitigate conflict of interests with contractors. This is critical as most people are related in a small nation like FSM. During our inspection, we were informed of close family relations between the contractor and a senior official who was responsible for supervising the projects and inspection officials. We also noted that TC&I officials responsible for the monitoring of the projects were aware of the Mwoakot project delay and failure and claimed to have communicated with the contractor several times; however, there were no progressive actions taken by both TC&I and the contractor until the KMG and respective traditional chiefs started raising concerns in late 2021.
- There is no payment schedule tailored to the project scope that should reflect the details of work (such as in work phases if applicable) together with the percentage (%) that the completed work represents.
- Funding was claimed by the TC&I to have been used for road improvement at another site in Mwoakot; which our inspection team could not verify due to absence of documentation. We also made attempts to interview the contractor and to confirm this information; however, all attempts were not successful.

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- There was lack of effective review on the sufficiency and accuracy of the certification (by DTC&I) for payment requests.
- DTC&I Management stated that they did not have enough manpower to handle the increasing CFSM projects that they are expected to manage and provide oversight on.

Recommendations:

We recommend the Secretary of DoFA to:

- (1) Revise the FMR to specify the requirements that should be met during the certification process by the project inspection officials to support the payment request made to Finance; and
- (2) Return payment requests that are supported by questionable certifications submitted by the project officials.

We recommend the Secretary of DTC&I management to:

- (3) Develop, create awareness and implement policies and standard operating procedures (SOP) for the department that should include, among others:
 - a. A standard inspection requirement/checklist to guide the Inspection official for inspecting projects and certifying the payment requests;
 - b. A requirement for proper inspection reports that should be documented in a designed template;
 - c. A requirement for sufficient evidence (photos that are clearly dated, if applicable) to support the certification by the project official;
 - d. A checklist for inspection and certification of projects to be verified by the supervisors prior to signing the payment requests;
 - e. A requirement for proper and complete documentation and filing (records management); and
 - f. Guidance for those that are reviewing and approving the certifications submitted by the project officials.
- (4) Immediately document a Policy on Conflict of Interest that should contain guidelines on mitigation or managing any identified conflicting interests that have been disclosed by officials of the department that handle bid evaluations and selection, contracts, projects and other key processes.
- (5) Ensure that every project has a payment schedule prior to issuing the "Notice to Proceed." This should be part of the internal policy and SOP being recommended above. The payment schedule should be tailored to the project scope that should reflect the details of work (such as in work phases if applicable) together with the percentage (%) that the completed work represents. This recommended payment schedule to be used by the contractor when requesting for payments. Similarly, DTC&I and DoFA can use it for verification of payment requests submitted by the contractors.
- (6) Ensure that the contractor complete the project in accordance with the approved contract.

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- (7) Issue relevant disciplinary actions to officials of the department that are not performing their work as expected.
- (8) Request additional budget to the FSM Congress to be used for recruiting additional employees to handle the increasing CFSM projects.

7.2. Finding 2: Breach of Certain Provisions of the Construction Contracts Were Not Addressed Including Uncollected Liquidated Damage of \$66,802

Criteria:

The construction contract for both projects (Mwoakot and Salapwuk -Rakuh to Utinpil) road projects stated “For Good and Valuable Consideration, the parties agree to fully and faithfully perform the terms and conditions set out in the contracts.

Condition:

Based on our assessment of compliance with the terms and conditions of the construction contract for both Mwoakot and Salapwuk Road Projects, we noted issues of non-compliance. [Table 4](#) below shows the provisions that the contractor did not comply with.

Table 4: Provisions in the Construction Contract that were not met by the Contractor

(The details of the provisions and terms & conditions of the contract are in [Appendix A](#))

Summary of the Provisions and Terms & Condition of the Construction Contract (Details are in Appendix A)	Our Findings for both the Mwoakot & Salapwuk (Rakuh to Utinpil) Road Projects
1) General Provision #8: Daily Contractor’s Report The contractor shall fill out a daily report to submit to contracting officer within 7 days of the end of the day being reported.	Based on our review of documents obtained from Finance and TC&I and our inquiry with TC&I official, there was no evidence of daily reports for both projects

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Provisions and Terms & Condition of the Construction Contract (Details are in Appendix A)	Our Findings for both the Mwoakot & Salapwuk (Rakuh to Utinpil) Road Projects																													
<p>2) General Provision #20: Liquidated Damage for Untimely Completion</p> <p>Failure to complete the project within the completion date would damage the contractee. Such damages are liquidated and will be incurred for each calendar day that project is not completed and accepted within the stated time. The amount of said liquidated damage shall be equal to one tenth of one percent (0.10%) of the total Contract Price which is indicated on the fact Sheet.</p>	<p>Our assessment below shows that there were liquidated damages that should have been compensated by the contractor to the National government. DTC&I did not invoice the contractor for this during the past over 1 year:</p>																													
	<table border="1"> <thead> <tr> <th>Description</th> <th>Mwoakot</th> <th>Salapwuk</th> </tr> </thead> <tbody> <tr> <td>Liquidation damage per day</td> <td>\$100 per day</td> <td>\$49 per day</td> </tr> <tr> <td>Date contractor accepted the Notice to Proceed</td> <td>December 15,2020</td> <td>June 25, 2020</td> </tr> <tr> <td>Agreed Commencement date</td> <td>Before or on December 25, 2020.</td> <td>Within 7 days of acknowledgment (June 25 to July 1, 2020)</td> </tr> <tr> <td>Agreed completed date</td> <td>March 25, 2021</td> <td>On or before August 14, 2020</td> </tr> <tr> <td>Agreed project days</td> <td>90 calendar days</td> <td>45 days</td> </tr> <tr> <td>Number of project delay days as of April 4, 2022 (date Contractor's request for extension of time)</td> <td>375 days</td> <td>598 days</td> </tr> <tr> <td>Amount of liquidated damage that was not collected</td> <td><u>\$37,500.00</u></td> <td><u>\$29,302.00</u></td> </tr> <tr> <td>Current state of the project</td> <td>Remained open and incomplete with some issues found.</td> <td>Remained open and was delayed with some additional work carried out in early 2022.</td> </tr> </tbody> </table>	Description	Mwoakot	Salapwuk	Liquidation damage per day	\$100 per day	\$49 per day	Date contractor accepted the Notice to Proceed	December 15,2020	June 25, 2020	Agreed Commencement date	Before or on December 25, 2020.	Within 7 days of acknowledgment (June 25 to July 1, 2020)	Agreed completed date	March 25, 2021	On or before August 14, 2020	Agreed project days	90 calendar days	45 days	Number of project delay days as of April 4, 2022 (date Contractor's request for extension of time)	375 days	598 days	Amount of liquidated damage that was not collected	<u>\$37,500.00</u>	<u>\$29,302.00</u>	Current state of the project	Remained open and incomplete with some issues found.	Remained open and was delayed with some additional work carried out in early 2022.		
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<p>Summary of the Provisions and Terms & Condition of the Construction Contract (Details are in Appendix A)</p>	<p>Our Findings for the Mwoakot Road Project</p>	<p>Our Findings for the Salapwuk (Rakuh to Utinpil) Road Projects</p>
<p>3) General Condition of the Construction Contract Article 8: Time #8.1 Progress and Completion: (8.1a) the contractor shall begin the work on the date of commencement as defined in paragraph 8b. He shall carry the work with adequate force and shall achieve substantial completion within the contract time.</p>	<p>Per the construction contract for Mwoakot Road Project, the project should be completed within 90 days. However, the project was 375 days overdue as of April 4, 2022. (Date Contractor’s request for extension of time was received at DTC&I)</p>	<p>Per the construction contract for Salapwuk Road Project, the project should be completed within 45 days. However, the project was 598 days overdue as of April 4,2022. (Date Contractor’s request for extension of time was received at DTC&I)</p>
<p>4) General Condition of the Construction Contract Article 8: Time #8.2a Delay and Extension of Time If the Contractor is delayed at any, then the contract Time shall be extended by Change Order for such reasonable time as the Contracting Officer may determine.</p>	<p>The road project was delayed more than a year. During those days delayed there was no change order for any extension. Just recently on April 4, 2022 a request for change order to extend the completion date was submitted for both Mwoakot and Salapwuk Road Project. The request for change order took place after our inspection queries were raised. The change order was recently approved for the Mwoakot Road Project on June 24,2022 to extend the project completion date to August 31,2022.</p>	<p>The road project was delayed more than a year. During those days delayed there was no change order for any extension. Just recently on April 2022 (after the commencement of our ONPA inspection) a request for change order to extend the completion date was submitted for both Mwoakot and Salapwuk Road Project. The change order to extend the completion date of the project to May 31, 2022 was approved by the Department of Justice on July 04, 2022. Note: The approval of the Change Order was made after the proposed extension date.</p>
<p>5) Construction Contract Attachment D: Scope of Work</p>	<p>Per the initial change order dated February 23, 2021 for Mwoakot Road Project, the scope of work should be concrete paving of road 850’x14x2”. Per our site inspection carried out on April 19,2022. We noted</p>	<p>The scope of work for Salapwuk Road Project as follows:</p> <ul style="list-style-type: none"> i. The contractor shall do clearing and grubbing 18’wide x 800ft. Remove tree trumps and roots. ii. Excavate for earth swale along two sides of the road where applicable.

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Summary of the Provisions and Terms & Condition of the Construction Contract (Details are in Appendix A)	Our Findings for the Mwoakot Road Project	Our Findings for the Salapwuk (Rakuh to Utinpil) Road Projects
	<p>that the scope of work was not met. The only work done was an excavation of 300 feet in length and with coral fills. There is no concrete paving done; however, corals started to washed away by rain as observed and seen on site.</p> <p>Refer to Appendix A for inspection pictures.</p>	<p>iii. Coral fill shall be 14feet wide x800feet x1'thick minimum and compacted by road roller and other mechanical means of compaction. Length of roadway is approximately 800ft.</p> <p>iv. Provide box culvert 3'high X 5'wide 18'width at the stream.</p> <p>v. Riprap with coral rock at wing wall.</p> <p>Based on our inspection of the project, we noted that the scope of work was not met. The total length of the road measured by the team was 810 feet. The width of the road varies, some part was 14', 13',12', & 10'. The coral filling was not even 1 foot. The coral filing is less than 3 inches and the soil is already showing on the surface. Refer to Appendix B for inspection Pictures</p>

Effects:

Following are the results of non-compliance to the terms and conditions of the construction contract:

- i. Breach of Construction Contracts;
- ii. Loss of public funds as penalty fines (liquidated damages of about \$\$66,802) were not collected due to change orders approved over 1 year later from the agreed completion date;
- iii. Projects were delayed more than a year;
- iv. No impact to the people who are the recipients of these public projects as they were not happy; resulting in the complaint that initiated this inspection by ONPA.

Therefore, we are referring this matter for further evaluation by our Compliance Investigation Division (CID).

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Causes:

- i. Inadequate monitoring of projects to ensure compliance with the terms and conditions of the construction contract, including the scope of work; and
- ii. Lack of policies and procedures in place to guide the process in administering the CFSM Projects.

Recommendations:

Management of DTC&I should:

- (1) Consider liaising with the Department of Justice to review the existing clauses in the construction contract agreement template to ensure that the terms and conditions are realistic and customized to the local environment and economy before it is signed.
 - For example, review whether the 0.10% of project cost as liquidation damage per day is realistic when project delay is highly likely going to be experienced with limited skilled labor and equipment on island on top of the rainy climate which is always a root cause for most infrastructure project delays.
 - If practical, the construction contract agreement could also specify how the liquidated damage be calculated if the project is delayed past the agreed completion date and the DOJ approved the change order before the liquidated damage was recovered (as seen for the 2 subject projects);
- (2) Develop, create awareness on and implement policies and standard operating procedures (SOPs) to guide the processes of administering CFSM Projects as well as all other processes of the department; and
- (3) Ensure that procedures are designed in collaboration with the DoFA to enforce contractual obligations such as the collection of liquidated damage owed by the Contractor to the FSM National Government for delayed projects.

(Note: in this case the FSM National Government lost out about \$66,802 being \$37,500 for the Mwoakot project and \$29,302 for the Salapwuk project. This was calculated based on days of delay from the agreed completion date to the date when the contractor's request for time extension was received by the DTC&I on April 4, 2022).

- (4) Take necessary actions to improve and implement effective controls that can provide incentives for the contractors to treat Government public projects with efficiency and quality. This can include blacklisting non-performing contractors for a relevant period, before considering them for any new public projects. (We note that it will not be realistic to blacklist nonperforming contractors indefinitely due to limited vendors on island for infrastructure projects).
- (5) Make a monthly review of the Contractors Blacklist recommended above and consider it to be part of the Department's standard operating procedures.

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7.3. Finding 3: Lack of Segregation of Duties in the Processes of Procurement and Independent Inspections of the Road Projects

Criteria:

According to leading practice as set in the Standards for Internal Control in the Federal Government (September 2014 version)³:

- Paragraph 10.12: 10.12 Management considers segregation of duties in designing control activity responsibilities so that incompatible duties are segregated and, where such segregation is not practical, designs alternative control activities to address the risk.
- Paragraph 10.13: Segregation of duties helps prevent fraud, waste, and abuse in the internal control system. Management considers the need to separate control activities related to authority, custody, and accounting of operations to achieve adequate segregation of duties. Segregation of duties can address the risk of management override. Management override circumvents existing control activities and increases fraud risk.
- Paragraph 10.14 of the standards states: "If segregation of duties is not practical within an operational process because of limited personnel or other factors, management designs alternative control activities to address the risk of fraud, waste, or abuse in the operational process."

According to the Project Control Document (PCD), the projects inspection official (PIO) from the Department of Transportation, Communication and Infrastructure (DTC&I) designated in the PCD shall provide project management oversight to ensure adequate accountability of funds expended and completion of the project.

Condition:

Based on our review of the bidding documents and contract documents we noted that there is no separation of duties for those involved in the two (2) processes below:

- Procurement process for evaluating and selecting the contractor for the project; and
- Independent inspection and certification of the project status before payments can be released.

We noted the PIO designated in the PCD for Salapwuk and Mwoakot Road Projects were also involved in the evaluation and selection process for the contractor.

In addition to the PIOs involvement in the bidding process, he/she monitors and reports on the status of the project. Funds were disbursed by the Department of Finance and Administration (DoFA) based on the inspection and certification made by the PIO.

Effects:

³ <https://www.gao.gov/assets/gao-14-704g.pdf>

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There is high risk of selecting contractors that are not competent to deliver project results on time; as seen for the 2 projects discussed in this report which resulted in incomplete projects for over 1 year.

When segregation of duties is not implemented it increases the risk of undetected collusion between government officials and the contractor; which may eventually lead to financial loss and no or low positive impact on the community or recipients of the public projects.

Therefore, we are referring this matter for further evaluation by our Compliance Investigation Division (CID).

Causes:

- i. Based on our meeting with DTC&I officials, there is currently no team within DTC&I that is responsible specifically for the evaluation of bids and selection of contractors, due to limited resources in the department. Therefore, project managers (who were normally involved in the evaluation and selection of the contractor during the bidding process), were also assigned the project inspection official/PIO roles.
- ii. The FSM FMR version (2019) did not require representative from other Departments that should be involved in the evaluation of bids for project costs that were equal to or less than \$100,000.
(Note: The current FMR version (2021) was revised to require that representatives from Department of Finance and Department of Justice should be part of the evaluation panel when the project cost is \$100,000 or more).

Recommendations:

Secretary of DTC&I should:

- (1) Implement proper segregation of duties when administering high risk processes (such as open bidding and independent inspections/certifications) of public projects to avoid the possibility or reduce the likelihood of wrong decisions and possible undetected collusion occurring. This can be implemented by:
 - a. Ensuring that the assigned PIO (as documented in the PCD) is not part of the bidding panel; and
 - b. Including the state of municipal governments to also take part in the independent inspection of projects, alongside the DTC&I officials; for projects being implemented within their jurisdiction (such as for the 2 projects discussed in this report which could have also been co-inspected by someone in the Kitti Municipal government).

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- (2) Develop and create awareness on an internal policy (in addition to the FMR) to address and ensure that segregation of duties is always maintained for identified high-risk processes within the department.

7.4. Finding 4: Lack of Compliance to the Provisions of the FMR for the Procurement Process for Sealed Bids

Criteria:

The purpose of the FSM Financial Management Regulation (FMR) is to implement the provisions, as amended, of the Financial Management Act of 1979, and other laws of the FSM relating to the government management through the establishment of National Government-wide standard and procedures necessary to provide adequate degree of fiscal control and accountability over funds appropriated by the Congress of FSM, allotted to the FSM National Government or entrusted to the management of the FSM National Government.

Condition:

Below are the provisions of the FSM FMR Version 2019 (applicable version of the FMR for the 2 projects) pertaining to the procurement process that were not fully complied with:

6.2.2 Call for Sealed Bids: (2) *Bidding documents will include bidding instructions, bidding form's and contractor's qualification statement. Usually contractor's will be requested to provide additional information that will include, but not limited to:*

- a) *Copy of Company Business License;*
- b) *Company's financial statements (more than one year may be requested);*
- c) *List of past completed projects;*
- d) *List of current on-going projects;*
- e) *List of subcontractors and their scope and nature of work to be performed;*
- f) *List of equipment;*
- g) *Intention to bid as a citizen bidder (including additional information);*
- h) *Certification from CTA and FSM Social Security that the Company is up to date with furnishing returns and payment of social security and tax liabilities; and*
- i) *Cost summary and detailed breakdown of the bid amount.*

6.2.7 Sealed Bids: (1) *When submitting bids, the prospective contractor must submit the following information:*

- a) *completed bid form that includes the following:*
 - i) *project name;*
 - ii) *contract name, address and contract details;*
 - iii) *declaration that the bid is genuine and can be carried out and has not taken part in any act of collusion to limit free and open competition;*
 - iv) *Lump sum price;*
- b) *In addition to the completed bid form, the contractor must also provide additional information as detail in subpart 6.2.2(2) and any other information requested by the CO.*

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Based on the documents obtained from DoFA and TC&I, there were only two bidders for the Salapwuk (Rakuh to Utinpil) road project. One of the bidders did not submit the required documents for the bid. The only document in file for the bidder was the project cost estimate; however, the selection panel still included the bidder in their evaluation.

6.2.9 Bid and Proposal Opening: *(1) Bids and proposals shall be opened publicly, immediately following the deadline for submission advised in the call for sealed bids, in the presence of all bidders who attended and the bidding panel, and at the same time and place for the opening of bids as stated in the call for sealed bid.*

(5) All bids and proposals should be opened in the presence of the full bidding panel. In any case where representatives from the Department of Finance and Department of Justice are unable to attend, another representative from each respective department must be selected to attend the bid opening.

Our review of the bid evaluation report shows that there were five (5) members of the selection panel for the Salapwuk (Rakuh to Utinpil) road Project. However, based on the abstract of bid, we noted only three witnesses during the opening of the bids. Two (2) of the witnesses were representative from the bidding companies and one (1) representative from the selection panel.

6.2.13 Award of Contract *(3) In deciding the 'lowest responsible bidder' for construction contracts, the bidding panel must consider and document following in awarding the the contract: (a) Ensure there is a declaration of no conflict of interest by participating panel members and if there is any doubt a replacement representative must be made.*

From our review of documents and inquiry with staff involved in the procurement process, we noted that members of the selection panel did not declare their independence before taking part.

Effects:

As a results, the expected outcomes of the projects were not fully met. In addition, issues of conflict interest can arise which can undermine and threaten the department's organization culture. It could result in fraud and reputational risk, a failure to act in the best interest of the government and poor governance.

Therefore, we are referring this matter for further evaluation by our Compliance Investigation Division (CID).

Causes:

There is no effective supervision and monitoring of the bidding process at the Department of TC&I as well as no internal policies and standard operating procedures (including templates and checklists) to guide the officials involved in the procurement process besides the general provisions of the FSM FMR.

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Recommendations:

Secretary of DTC&I should:

- (1) Develop internal policies and standard operating procedures / SOPs (that should include sample templates and checklists) as a reference tool to guide officials responsible for the procurement process in the national government; and
- (2) Develop and implement internal performance measurement procedures to ensure that the officials of the department are effectively performing their duties for the best interest of the FSM National government and for public service.
- (3) Issue relevant disciplinary measures to non-performing officials of the department.

8.0 APPNEDIX

Appendix A: Inspection Photos for the Mwoakot Road Project

Picture 1: Net was put in place to prevent the corals from washing away



Picture 2: No concrete paving in place



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Picture 3: Road conditions is bad



Picture 4: End of the Road Project



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Appendix B: Inspection Photos for Salapwuk (Rakuh to Utinpil) Road Project

Picture 1. Salapwuk (Rakuh to Utinpil) Road Project – 850 feet length



Picture 2. Coral filling is less than 3 inches.



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Picture 3: soil is showing on the surface indicating less coral filling



Picture 4: End of the Salapwuk Rakuh to Utinpil) Road



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9.0 MANAGEMENT RESPONSE

9.1. Department of Transportation, Communication & Infrastructure's Response



Government of the Federated States of Micronesia
Department of Transportation, Communication & Infrastructure
P.O. Box PS-2 Palikir, Pohnpei FM 96941

Office of the Secretary

September 19, 2022

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

Re: Management response to the CFSM Pohnpei Public Projects (Salapwuk & Mwakot Road Projects) under Public Law 20-141 and Public Law 21-53

Dear Mr. Hainrick:

Let me precede my response to the draft audit report by first extending our Department's appreciation for the audit. I must thank you and all your staff for all the painstaking work you all had to do, not only by reviewing paper work but also going out in the field with our staff to actually walk the projects and experience the challenges that our project managers face on a daily basis.

It has always been my intention to improve and strengthen the Department and therefore I do welcome the audit report to help us identify the weaknesses and challenges in our Division of Infrastructure so that we can all work together to strengthen it. In assuming the position of Secretary in December 2019, I had made a commitment to do my best to upgrade the capabilities of the staff and to equip them with the necessary tools to help make them more capable and efficient. At the end of my term as Secretary, I want to leave this Department in a better state than when I found it.

Having said that, we have reviewed the findings and recommendations in the draft report and have noted the weaknesses and challenges. We are also doing our own internal reviews to implement corrective measures to ensure that similar mistakes and challenges are not repeated. These corrective measures will include the recommendations you have outlined in the draft report.

Please find below the responses provided by our Division of Infrastructure in direct reference to your findings in the draft report:

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Finding No. 001 – Insufficient and misleading certification of project Status by the Inspection Officials for the Mwoakot Road project.

Management response: The finding regarding insufficient and misleading certification of project status by the inspection official for Mwoakot Road project is well noted. Furthermore, the management accepts the insufficient and misleading certification of project status by the inspection official and recommendations are well noted. We are looking at creating redundancies in our work process so that the work can be double checked to ensure accuracy of reports.

Finding No. 002 – Breach of certain provisions of the Construction Contracts were note addressed including uncollected liquidated damages cost of \$ 66,802.00.

Management Response: The finding regarding the question cost of \$ 66,802.00 due to lack of proper planning and oversight of certain contract provisions is well noted. The management notes the recommendations and appreciates if the issue can be further clarified given the fact that both contracts are still valid and a recent change order has been approved by the Department of Justice.

Finding No. 003 – Lack of Segregations of Duties in the processes of Procurement and Independent Inspections of the Road projects.

Management Response: The findings regarding the lack of segregation of duties in the processing and the procurement and independent Inspections or road projects is well noted. The management accepts the findings and recommendations and will further continue to improve the weaknesses as cited and notes the absence of records to support the transaction. The management also noted that DTC&I should institute more effective measures for the timely monitoring and coordination of project implementation and that documents are recorded properly. The management will also begin excluding the project managers from the selection panel on future bids or request for proposals to maintain impartiality between the selection process and the project manager.

Thank you again for your important work. We look forward to working with you and all other relevant departments to create a more transparent and progressive process of implementing public projects.

Sincerely,



Carlson D. Apis

Cc-copy: Assistant Secretary, Division of Infrastructure

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September 22, 2022

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

Re: Management response to the CFSM Pohnpei Public Projects (Salapwuk & Mwakot Road Projects) under Public Law 20-141 and Public Law 21-53

Dear Mr. Hainrick:

Further to our letter of September 19, 2022 on the above referenced subject, I regret that we had inadvertently left out our response to Finding No. 004 in the draft Audit Report. Please find below our response on the specific issue:

Finding No. 004 – Lack of compliance to the provisions of the FMR for the procurement process for sealed bids. The management notes and accepts the findings and recommendations regarding the lack of Compliance to the provisions of sealed bids. The Department, however, wishes to point out that we have strengthened our procurement process by having the review panel include representatives from the Department of Finance and Administration and the Department of Justice. A confidentiality form has also been incorporated requiring all members to fill out prior to the evaluation of any project. Furthermore, while we have included project managers in the review panel in the past due to short staffing, we have noted the audit's recommendation of excluding project managers from involvement in the panel. For future review panels, we will no longer include the project managers.

Thank you again for your important work.

Sincerely,



Carlson D. Apis

Cc-copy: Assistant Secretary, Division of Infrastructure

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9.2. Department of Finance and Administration's Response



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) 320-2640/5852 Fax: (691) 320-7728
E-mail: fsmsofa@mail.fm

September 20, 2022

Haser Hainrick
FSM Public Auditor
Palikir, Pohnpei
FM 96941

Dear Mr. Hainrick:

I take this opportunity to express my appreciation to the National Public Auditor's Office for completing this year's audit report. We acknowledge the findings and recommendations from your office to assist with guidance and enhancement of our internal controls. Moreover, I am transmitting our management response to the "Inspection of Certain CFSM Road Projects in Kitti, Pohnpei State, Report No. 2022-05" to convey the Department of Finance & Administration's perspective.

Finding 1: Insufficient and Misleading Certification of Project Status by the Inspection Officials for Mwoakot Road Project

Management Response:

- DoFA concurs with this finding and wishes to adopt the recommendations laid out for implementation. A concise checklist will be created and used specifically for reviewing contracts. As for the inspection reports, DoFA has already started implementing/requiring proof of completion projects by ensuring images are provided to demonstrate a proof of actual work completed or progress made. Also as being recommended, DoFA will work with TC&I to improve their, inspection reports to ensure relevant supporting documents are provided to justify the percentage mention in the inspection reports towards incremental progress and/or require verification from local governments to ensure accuracy to prevent misleading inspection reports.

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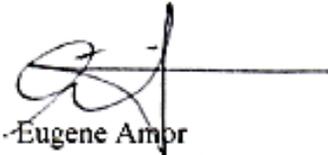
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To conclude, I wish to stress that Finance highly value your efforts in this audit to ensure proper implementation and execution of public projects to promote accountability of public funds. We will implement the recommendations to strengthen our internal controls and procedures. We look forward to working with TC&I when they address the findings especially their implementation of your audit recommendations as well.

With respect to other findings we concur with the findings and recommendation. As they are for TC&I, we will work with Secretary of TC&I to ensure practical solutions are put in place to improve their implementation.

Should you require further information or assistance, please let us know.

Thank you,



Eugene Amor
Secretary of Finance

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10.0 ONPA EVALUATION OF MANAGEMENT RESPONSE

The inspection team requested for management responses from the Secretary, Department of Transportation, Communication, and Infrastructure (DTC&I) and Secretary, Department of Finance and Administration (DoFA). Management of both departments' responses generally agreed with the findings and recommendations in this report; however, we would like to clarify a statement in the management response by the DTC&I pertaining to Finding 2 that is discussed below:

1. Finding 2: Breach of Certain Provisions of the Construction Contracts Were Not Addressed Including Uncollected Liquidated Damage of \$66,802.

1.1. Response by DTC&I

The finding regarding the question cost of \$66,802 due to lack of proper planning and oversight of certain contract provisions is well noted. The management notes the recommendation and appreciates if the issue can be further clarified given the fact that both contracts are still valid and a recent change order has been approved by the Department of Justice.

1.2. ONPA Evaluation:

We evaluated the management response and have amended the recommendation that we had initially made in the draft report to address the clarification in the management response as we were later made aware of the recently approved change order that was initiated way past the agreed completion date.

We have therefore made slight amendments in the final report and instead of recommending the DTC&I to initiate the recovery of the uncollected liquidated damage of \$66, 802, we have recommended that the DTC&I should design procedures to ensure that contractual obligations such as the liquidated damage are collected on time from contractors that fail to meet the agreed completion date. The FSM Government has lost out in terms of liquidated damage of about \$66,802 which cannot be collected now due to the change orders that were approved and certified by the Department of Finance and the Department of Justice.

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11.0 NATIONAL PUBLIC AUDITOR'S COMMENTS

We would like to thank the relevant staff of the Kitti Municipal government, the FSM Department of Finance and Administration and the Department of Transportation, Communication, and Infrastructure (TC&I) for their assistance and cooperation during the Inspection.

We have provided copies of the final inspection report to the President, Members of the 22nd FSM Congress and those charged with governance. 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 conducted the inspection and prepared this report.



Haser H. Hainrick
National Public Auditor

September 26, 2022

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12.0 ONPA CONTACT AND STAFF ACKNOWLEDGEMENTS

ONPA CONTACT Haser Hainrick, National Public Auditor
Email: hhainrick@fsmopa.fm

ACKNOWLEDGEMENTS In addition to the contact named above, the following staff
made key contributions to this report during the period
specified:

Miriam Naivalu, Audit Manager
Rosadelima Alfons, Team Leader
Trifonovitch Sound, Team Member
Brenda Carl, Team Member

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