

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



**Enhancing Safeguards, Strengthening Duty Segregation, and
Optimizing Revenue Collection in the FSM - Chuuk State
REPORT NO. 2025-02**

SURPRISE CASH COUNT





FEDERATED STATES OF MICRONESIA

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March 21, 2025

His Excellency President Wesley W. Simina
Honorable Speaker and Members of the 23rd Congress
Secretary, Department of Finance and Administration
Secretary, Department of Resources and Development
Acting Postmaster General, FSM Postal Services
Federated States of Micronesia

RE: Inspection of FSM Revenue Collection Offices in Chuuk State

We have completed the inspection of four approved FSM Government collection field offices in Chuuk State, focusing on the effectiveness of the collection process, facility security, and internal controls. This included the Division of Customs Tax and Administration and National Treasury at the Department of Finance, the Quarantine Facility under the Division of Agriculture at the Department of Resources and Development, and FSM Postal Services, Chuuk Branch. The inspection was conducted in accordance with the Council of the Inspector General on Integrity and Efficiency's Quality Standards for Inspection and Evaluation.

Our inspection identified the following issues regarding the accountability of FSM Government collected revenues in the specified approved collection field offices:

1. Lack of Sufficient Safeguards in Customs and Tax Administration (CTA) Revenue Collection Process.
2. Weaknesses in Collection Mechanisms Limits Potential Revenue Growth for Customs Tax and Administration and Quarantine Facilities.
3. Inadequate segregation of duties poses risk of errors and fraud.

This inspection report on the surprise cash count is part II of a four-part series covering inspections of approved FSM Government collection offices and agencies across all four FSM states.

Sincerely,

Haser H. Hainrick
National Public Auditor

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Abbreviations	Meaning
CIGIE	Council of the Inspectors General on Integrity and Efficiency
CTA	Division of Customs and Tax Administration
DoFA	Department of Finance and Administration
EFTPOS	Electronic Funds Transfer at Point of Sales
FMR	Financial Management Regulations
NPS	National Post Services
PMG	Postmaster General
QSIE	Quality Standard for Inspections and Evaluations
R&D	Department of Resources and Development

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1. INTRODUCTION

- 1.1. This engagement was initiated following a request from the then Acting Secretary of the Department of Finance and Administration to conduct surprise cash count audits at the Division of Treasury, including all field offices in the FSM states. Our office, the National Public Auditor, then decided to expand the review to include the other cash-handling entities because they had not previously undergone a surprise cash count.

This engagement review, originally focused on the Division of Treasury, has now been extended to include the Division of Customs Tax and Administration, Quarantine at the Division of Agriculture, Department of Resources and Development, and FSM Postal Services field offices in Chuuk State.

1.2. Background

Division of Treasury

The Division of Treasury is one of the core operating divisions within the Department of Finance and Administration. The division was established pursuant to Section 206 of the Financial Management Act 1979. Section 207 of the Act, PL 1-45, Subsection 5, which set out the key responsibilities of the FSM Treasurer, which was specified as the Secretary of Finance who then delegates these tasks to the Treasury Division Staff. The Treasury Division is legally tasked with managing, collecting, and protecting all revenues owed to and paid to the FSM Government. All public financial management activities for the FSM Government are centralized and processed out of the FSM Treasury Division. The division has a field office in each of the four FSM States.

Division of Customs Tax and Administration

The Division of Customs and Tax Administration (CTA) is another core operation division within the Department of Finance & Administration (DoFA), which was established pursuant to Title 54 of the FSM Code. CTA maintains its main office in Palikir, Pohnpei and has a field office in each of the four FSM States. Its primary responsibilities are to maximize collection of local revenues and maintain border control through its customs services.

Quarantine

FSM Quarantine Services are under the Agriculture Division within the Department of Resources and Development. The Quarantine Services were set forth by law as a means of preventing the introduction and further dissemination of injurious insects, pests, and diseases into and within the FSM (Title 22. Agriculture and Livestock, Chapter 4). All four FSM States has a Quarantine Service office.

FSM Postal Services

The FSM National Postal Services (NPS) was established in 1983 by Public Law No. 3-13(referred to as the National Postal Services Act) which is codified as Title 39 of the FSM Code. The establishing Act created the NPS as an independent agency of the FSM National Government. Its primary purpose is to provide and deliver postal operations and services as well as to sell stamps and other philatelic products within the FSM and throughout the world. It is headed by the Postmaster General. The main office is in Kolonia, Pohnpei and there are three post offices in the four (4) FSM States, each under the supervision of a State Postmaster who serves under the authority of the PMG.

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All the above entities are tasked with the collection of funds as part of their respective mandates.

2. OBJECTIVES, SCOPE, METHODOLOGY

2.1. Objectives

The objectives of this inspection were to determine and assess the following:

1. Ensure accurate cash counts, timely deposits, secure collections, and compliance with cash handling procedures, with all transactions properly documented.
2. Evaluate the safeguards and effectiveness of operational infrastructure to improve revenue collection.

2.2. Scope

The inspection began on September 02, 2024, and fieldwork ended on September 27, 2024. The team conducted surprise cash counts and reviewed relevant internal controls surrounding the process of revenue collection. Below are the dates and inspection activities done on the respective division and agencies in Chuuk:

Field Offices	Date	Activity
Treasury	Sept 16-19, 2024	Interviews, Cash Count & Observations
CTA	Sept 16-19, 2024	Interviews, Cash Count & Observations
Post Office Services	Sept 20, 2024	Interviews, Cash Count & Observations
Quarantine Services	Sept 20, 25 and 27, 2024	Observations at the Airport

2.3. Methodology

We conducted this inspection in accordance with the Council of the Inspector General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation*. 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 objectives.

The team conducted interviews, observations, and cash counts at the National Field offices and agencies, including CTA, National Treasury, the Post Office, and Quarantine. The team also conducted interviews, reviews and analysis of relevant internal controls surrounding the cash collection process.

3. Legal Mandates/Standards

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 nonprofit organizations receiving public funds from the National Government".

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4. PRIOR AUDIT COVERAGE

This surprise cash count inspection is part II of a four-part series examining approved FSM Government collection offices and agencies across all four FSM states. The first report in the series, Report No. 2024-08, was released by ONPA on September 30, 2024.

The surprise cash count inspection part I was conducted at Pohnpei State at the following FSM National collection offices and agency:

- National Division of Treasury
- CTA Field Office
- CTA, Post Office
- CTA, Pohnpei Airport
- Quarantine Facility, Pohnpei Airport
- FSM Postal Services, Kolonia

5. CONCLUSION

In conclusion, this inspection revealed significant weaknesses in the Customs Tax and Administration revenue process, including insufficient security measures that undermine the integrity of collections. Ineffective collection mechanisms in both CTA and Quarantine Divisions further limit potential revenue growth, respectively. Additionally, the lack of proper segregation of duties exposes the operations to risks of errors and fraud. Addressing these issues is crucial to enhancing revenue generation and strengthening financial controls.

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6. FINDINGS AND RECOMMENDATIONS

6.1 Finding No.1: Lack of Sufficient Safeguards in Customs and Tax Administration (CTA) Revenue Collection Process

Criteria:

Pursuant to Section 4.4.3, Provision of safe custody facilities, of the Financial Management Regulations, states that:

1. *It is the responsibility of the Head of Department to ensure that adequate safe custody facilities are provided to officers working within the Department that is accountable for any cash.*
2. *It is the responsibility of the Head of Department to ensure that all due precautions are taken to prevent loss or theft of all cash collected for the FSM Government.*

Conditions:

During our visits to the division field offices, we observed the following:

1. The commonly used storage for securing the collection is a zippered bank bag, which everyone has their own and can easily always carry with him/her during the shift. At the end of the day, all collections are stored in a small secure safe box located in the office of the Field Manager.
2. Moreover, specifically at the CTA Post Office, the team noted the lack of secure storage for collections, resulting in the officer carrying the collected funds in a bag whenever leaving the workstation, such as when going out for lunch or assisting customers at the gate, thereby putting the funds at risk.
3. We also observed the absence of Electronic Funds Transfer at Point of Sale (EFTPOS), which offers several benefits including the following:
 - a. It allows customers to pay with debit or with credit cards, making purchases easier without cash limitations.
 - b. Payments are processed electronically and deposited into your account, often within a day or two, speeding up cash flow compared to handling checks or other payment methods.
 - c. EFTPOS reduces the need to handle cash, lowering the risk of theft or loss for both employees and the business. Electronic transactions are also more secure and traceable, helping prevent fraud.
 - d. It also automatically generates transaction records, making bookkeeping easier and reducing time spent on manual cash handling and reconciliation.
 - e. EFTPOS minimizes the risk of human error in handling payments, ensuring transactions are recorded accurately and reducing discrepancies.

Causes:

The practice of using small zipper bank bags, each being carried by individual officers during their shifts, has resulted from several underlying causes that negatively impact security, accountability, and operational efficiency within the CTA Division field office. Key contributing factors include the following:

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1. Without centralized procedures, officers manage their own collections, resulting in inconsistent practices and no secure system for consolidating cash on-site.
2. The absence of secure storage options, such as tamper-evident bags or lockable drawers, likely led to the use of insecure zipper bank bags for convenience.
3. The division may have prioritized convenience, allowing officers to use individual bank bags for collections during shifts, compromising secure and efficient cash management.
4. A lack of strategic planning or failure to recognize EFTPOS benefits may have delayed its adoption, missing the chance to improve revenue collection and customer convenience.

Effects:

1. The practice of using small zipper bank bags, each carried by individual officers during their shifts, has several potential negative effects:
 - a. Carrying cash in individual zipper bags without secure tracking or oversight exposes funds to theft or loss, especially during busy shifts when officers move between locations.
 - b. Zipper bags offer minimal security and lack features such as tamper-evident seals or dual control. This makes it easy for unauthorized individuals to access funds or for cash amounts to be altered before formal processing.
 - c. The process of combining and counting funds from multiple bags at the end of the day is time-consuming and inefficient, detracting from valuable staff time that could be allocated to core operational tasks.
2. The absence of EFTPOS has some negative effects which include the following:
 - a. Without EFTPOS, the office relies on cash transactions, which increases the risk of theft, loss, misappropriation, and mistakes during cash counts and reconciliations.
 - b. Cash transactions take extra time for counting, recording, and reconciling, which slows down processing and reduces efficiency, especially during peak collection times.
 - c. Handling and storing large amounts of cash on-site increases security risks, requiring extra resources for protection and posing safety concerns for staff.
 - d. EFTPOS automatically records transactions, ensuring better transparency and accountability. Without it, the office relies on manual records, which are more prone to errors and manipulation.

Recommendations:

We recommend the Secretary of the Department of Finance & Administration (DoFA) to develop and implement the following:

1. Create and enforce a uniform cash handling policy that consolidates cash collection and storage, following Financial Management Regulations. Officers will be required to safely secure funds at set intervals, reducing the risk of theft or loss.

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2. Invest in secure storage options, like tamper-evident cash bags or lockable cash drawers at each workstation, to prevent officers from carrying cash and ensure its security until end-of-day processing.
3. Provide thorough training for officers on secure cash handling, including the risks of carrying cash and the proper use of secure storage.
4. Speed up the adoption of Electronic Funds Transfer at Point of Sale (EFTPOS) systems to encourage digital payments, reduce cash handling, and improve payment transparency.

6.2 Finding No. 2: Weaknesses in Collection Mechanisms Limit Potential Revenue Growth for Customs Tax and Administration and Quarantine Divisions

Criteria:

According to Title 54 of the FSM Code, under Taxation and Customs, it states that *the primary function of the Authority is to maximize, over time, the collection of revenue lawfully owing to the FSM National Government and the States given the resources available to it. Without limiting the generality of the foregoing, the Authority has the following specific functions:*

1. *To take such measures as may be required to improve the standards of service provided to taxpayers with a view to improving efficiency and effectiveness in administration and maximizing revenue collection.*
2. *To take such measures as may be required or considered necessary to prevent tax evasion and fraud of any type.*

Also, pursuant to Section 4.4.3, Provision of safe custody facilities, of the Financial Management Regulations, states that:

1. *It is the responsibility of the Head of Department to ensure that adequate safe custody facilities are provided to officers working within the Department that is accountable for any cash.*

In addition, *Title 22, Agriculture and Livestock, §410 Inspection*, stated the following:

(1) All animals and plants or parts thereof, including seeds, fruits, vegetables, cuttings, etc., entering or transported within the Federated States of Micronesia are subject to inspection by agriculture quarantine inspectors and may be refused entry into or movement within the Federated States of Micronesia if they are known to be, or are suspected of being, infected or infested with disease or pests.

Conditions:

Based on our communications and observations conducted at the Chuuk International Airport, Quarantine and CTA Post Office, we found the following conditions per location:

1. CTA Field office in Chuuk State (Division of FSM DoFA)

Chuuk State's main entry point for incoming items (parcels, packages, baggage, goods) lacks functional scanning machines. The scanning machine at Chuuk Airport is reported to be non-functional. The absence of a functional scanning machine at a key entry point can severely impact tax

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revenue collection, as scanners are essential for accurately identifying the contents, values, and quantities of incoming goods.

2. Quarantine Facility in Chuuk State (Division of the FSM Department of R&D)

According to the Assistant Secretary of the Division of Agriculture, Department of Resources and Development, the Quarantine Field Office is located at the State Agriculture Departments. In addition, the Quarantine Field Offices also has a facility at the airports where they assist passengers that need to declare local produces, they wish to take with them to their destinations.

The team visited the Chuuk International Airport and confirmed that there was a Quarantine facility however, the facility is not located in a convenient spot for travelers needing assistance because it is in the arrival baggage claim area, making it difficult for departing travelers to access when they require assistance.

During multiple visits at the Chuuk airport, the team noted that quarantine officers are occasionally present in the check-in area to assist passengers, but at other times, they may be hard to find or arrive late to their designated duty station. Since there is no visible office or counter near the airport entrance or check-in area, travelers, often at times, have to search for a quarantine officer and sometimes they proceed without receiving any assistance. Therefore, it is highly likely that there may be a lot of revenue collections as required by law not being collected as result. More importantly, any undeclared items may go unnoticed and unaccounted for resulting in non-compliance and the potential for any revenue to be collected as required by the relevant laws and regulations.

Causes:

1. Failure to prioritize and focus on the need for working scanning equipment in revenue collection at CTA Collection Points (Airport and Post Office).
2. Quarantine facility is hard to access, and quarantine officers are inconsistently present onsite at the Chuuk Airport.

Effects:

1. Without proper scanning due to the lack of inadequate measures such as the availability of such facilities, items may bypass detailed inspection, increasing the chances of undeclared or under-declared goods entering the State. This directly results in lost revenue from unpaid or underpaid taxes.
2. Scanning allows customs officials to detect restricted or high-value items that may be subject to additional taxes. Without these machines, such goods may enter without appropriate duties taxes.
3. Scanning machines streamline inspection process, allowing customs to process more goods with fewer delays. This efficiency can improve revenue collection by ensuring that all packages are assessed within a reasonable timeframe.

Recommendations:

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1. We recommend that the Secretary of DoFA should prioritize the maintenance and functionality of scanning equipment at all collection points, including the airport and post office, and ensure regular assessments and upgrades to support efficient and accurate revenue collection.
2. We recommend that the Secretary of R&D collaborate with Chuuk State Government to either relocate or renovate the existing Quarantine workstation, ensuring it is situated in a more accessible location to better assist travelers with item declarations and minimize the risk of potential confiscations.

6.3 Finding No. 3: Inadequate segregation of Duties poses risk of errors and fraud

Criteria:

According to the Green Book, *Standards for Internal Control in the Federal Government of September 2014*, which was developed by the Committee of Sponsoring Organizations (COSO), Section 10.13, states that:

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. In particular, segregation of duties can address the risk of management override. Management override circumvents existing control activities and increase fraud risk. Management addresses this risk through segregation of duties but cannot absolutely prevent it because of the risk of collusion, where two or more employees act together to commit fraud.

Additionally, Part of 1.4.26 of the FMR also states that internal control:

Means a process, implemented by the National Government, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- a. *Effectiveness and efficiency of operations.*
- b. *Reliability of reporting for internal and external use; and*
- c. *Compliance with applicable laws and regulations.*

Conditions:

During our visits to CTA Post Office from September 16-18, 2024, we observed that only one officer was responsible for all operations, including customer assistance, package release, and tax collection. This led to delays, increased workload, and potentially security vulnerabilities due to the lack of sufficient staffing and segregation of duties.

At the CTA field office, officers are responsible for collecting and retaining funds throughout the day, with cash counts conducted at day's end for processing and deposit. However, we observed and confirmed that there is no clear designation of responsibility for collections and processing, leading to a lack of segregation of duties. Multiple officers (more than two) are involved in handling collection without defined roles, which increases the risk of errors, mismanagement, and potential security issues.

Upon reviewing samples of daily cash count records, we observed that the same individual who prepared the document was also responsible for counting the collections. This raises more concerns about the segregation of duties.

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Causes:

1. There may be no policies for role segregation, which could lead to one person being assigned customer service, cash handling, and security tasks.
2. Limited supervisory oversight may have allowed a single officer to take on all duties, leading to security risks and inefficiencies.

Effects:

1. Without adequate segregation of duties, employees may have unchecked control over critical process, increasing the likelihood of fraud, or theft.
2. Lack of role separation can lead to errors going undetected, resulting in inaccurate financial reporting, misstatement, or undetected data entry mistakes.

Recommendations:

Here are several actionable recommendations to address the inadequate segregation of duties and reduce risks associate with errors, fraud, and inefficiencies:

1. We recommend the Secretary of DoFA to develop and implement policies and procedures to enforce role segregation, ensuring that customer service, cash handling, and security tasks are assigned to different individuals to strengthen internal controls and reduce risks.
2. We also recommend that the Secretary of DoFA improve supervisory oversight to ensure proper task distribution and prevent any single officer from handling multiple duties, thereby reducing security risks and inefficiencies. This can be achieved by implementing the following best practices:
 - a. Establish a dual-control process for cash handling, where two individuals are responsible for verifying and reconciling collections at the end of the day. Ensure that funds are counted and verified by two officers before deposit.
 - b. Conduct regular internal audits and random spot checks of cash handling and role assignments to ensure compliance with segregation and cash handling policies.
 - c. Provide training for all staff on the importance of duty segregation, secure cash handling, and internal controls, highlighting the security risks of assigning multiple responsibilities to one person.

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7. MANAGEMENT RESPONSE

7.1 Department of Resources and Development Management Response:



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January 29, 2024

Haser H. Hainrick
National Public Auditor
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Subject: Response to Finding No. 2 Regarding Quarantine Field Office in Chuuk

We would like to thank the ONPA team for their thorough review and acknowledge the findings regarding the Quarantine Field Office at Chuuk State International Airport.

We recognize the challenges posed by the current placement of the Quarantine workstation at Chuuk Airport. However, this matter falls outside the jurisdiction of FSM R&D and is at the discretion of the State to determine a more accessible location for travelers. We are committed to collaborating with Chuuk State to improve the services provided through our Quarantine Field Office for travelers.

Immediate Actions Taken:


1. We have begun assessing the premises during our annual State visit to Chuuk and observed passengers moving in and out with outbound agricultural goods for inspection.
2. Multiple directional signs have been installed on the airport walls and at the main check-in area to guide passengers to the declaration area.
3. We have secured a designated space in the main terminal through discussions with the Airport Manager and Director of Public Works and Transportation.
4. Quarantine Officers have been reminded to adhere to operational hours to ensure that travelers receive the necessary services.

Actions Moving Forward:

1. We will maintain open communication with the Chuuk State Government to ensure that our services to travelers remain uninterrupted.
2. As part of our ongoing initiatives, we will post directional signs to inform travelers about the location of our workstation at the Chuuk Airport.

We remain dedicated to providing essential quarantine services for both outbound and inbound travelers. The Division of Agriculture will continue to work closely with Chuuk State to identify future actions regarding the location of the Quarantine workstation at Chuuk Airport.

Sincerely,


Elina Akinaga
Secretary

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8. ONPA EVALUATION OF MANAGEMENT RESPONSE

As part of the inspection process, we requested exit conference meetings with the management of the FSM Department of Finance and the Department of Resources and Development to discuss the results of the cash count and internal control inspection. Both departments generally agreed with the findings and recommendations. However, R&D suggested involving Chuuk State Government in the recommendation for Finding 2, which the team evaluated and agreed to do so.

Despite multiple attempts in obtaining a formal management response from the FSM Department of Finance and Administration, we did not receive any written management response.

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9. NATIONAL PUBLIC AUDITOR COMMENTS

We extend our sincere gratitude to the Secretary of the Department of Finance and Administration and her team, including the field offices in Chuuk, as well as the Department of Resources and Development and its Quarantine field office in Chuuk. We also appreciate the cooperation of the Postmaster in Chuuk during this inspection.

Copies of the final inspection report have been shared with the President, Members of the 23rd FSM Congress and relevant governing authorities. Additional copies will be made available to 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 this inspection and prepared this report.



Haser H. Hainrick
National Public Auditor

March 21, 2025

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ONPA CONTACT AND STAFF ACKNOWLEDGEMENTS

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ACKNOWLEDGEMENTS In addition to the contact named above, the following staff played significant roles in contributing to this report during the period specified:

Isireli T. Vanigi, Audit Manager (9/6/2024 to 12/6/2024)
Brandon Rodriguez, Audit Supervisor
Joey A. Iwo, Auditor in Charge

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