

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



**Compliance Issues Found Within the Monitoring, Reporting, and
Recording of Dormant Accounts
REPORT NO. 2025-03**





FEDERATED STATES OF MICRONESIA

Office of The National Public Auditor

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April 04, 2025

His Excellency President Wesley W. Simina
Honorable Members of the 23rd Congress
Commissioner, FSM Banking Board
Chairman, FSM Banking Board
Secretary, Department of Finance and Administration
Federated States of Micronesia
Palikir, Pohnpei FM 96941

RE: Inspection of Dormant Accounts

We have completed our inspection on Dormant Accounts. The inspection primarily focused on the effectiveness of monitoring, recording, and reporting dormant accounts specifically at the FSM Banking Board and Department of Finance and Administration from FY 2021 to December 2024. The inspection was conducted in accordance with the *Council of the Inspectors General on Integrity and Efficiency's Quality Standards for Inspection and Evaluation*.

Based on our inspection, we found the following issues pertaining to how the FSM Banking Board and Department of Finance and Administration monitors, records, and reports dormant accounts according to regulatory requirements:

1. Dormant Account Funds Deposited into the General Fund Instead of a Custodial Interest-bearing Account.
2. Insufficient and Improper Record-Keeping by the Department of Finance & Administration for Dormant Accounts.
3. Limited Enforcement of Banking Laws and Regulations by the Banking Board due to the lack of adequate internal controls.

We have also discussed the findings and recommendations with the Department of Finance and Administration and the FSM Banking Board. The team also requested formal management responses, which are included in this final report.

Respectfully submitted,

Hasef H. Hainrick
National Public Auditor

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Abbreviations

Abbreviation	Meaning
CIGIE	Council of the Inspectors General on Integrity and Efficiency
DoFA	Department of Finance and Administration
FSMC	Federated States of Micronesia Code
FSMDB	Federated States of Micronesia Development Bank
FSM	Federated States of Micronesia
FY	Fiscal Year
ONPA	Office of the National Public Auditor
PL	Public Law
QSIE	Quality Standards for Inspections and Evaluations
SOPs	Standard Operating Procedures

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1. INTRODUCTION

1.1. Reason for this Assignment

As per Section 3.6 of the Dormant Account Regulation, an audit of custodial accounts must be conducted as part of the Department of Finance's general audit. The Commissioner of the Banking Board made an inquiry with the Office of the National Public Auditor (ONPA) regarding the transfer of dormant accounts from commercial banks to the Department of Finance & Administration, in accordance with the relevant laws and regulations. The FSM has two licensed commercial banks, the Bank of FSM and the Bank of Guam, with branches across the four states. The review did not include FSMDB or other credit unions as they are not part of the statutory requirements for the FSM Banking Board.

1.2. Background

Process of how dormant accounts are transferred into the custodial interest-bearing account at the FSM through the Department of Finance and Administration (DoFA).

Title 29 of the FSM Code – Commercial Banking, Section 106, FSM Bank Act reads:

§ 106. Banking Practices—Dormant and Inactive Accounts

In the event there has been no activity of deposits or withdrawals in a savings account and no contact has been made with the account holder of such savings account for at least ten years, the account shall be deemed a “dormant account” and the bank in which such account is kept shall act to close the dormant account in accordance with the procedures set forth below in this section.

In the event there has been no activity of deposits or withdrawals in a checking account and no contact have been made with the account holder of such checking account for at least two years, the account shall be deemed a “dormant account” and the bank in which such account is kept shall act to close the dormant account in accordance with the procedures set forth below in this section.

Bank actions in crediting interest payments to an account or assessing service charges against an account shall not count as activity for the purposes of determining dormancy.

Dormant accounts shall be identified annually by each bank during the month of June. Any dormant account with a balance of \$25 or less is not subject to the procedures required by this section.

Upon identification of a dormant account, the bank shall send written notice to the depositor at the depositor's last known address, informing the depositor that the depositor's account will be closed, and the funds therein transferred to the Secretary of Finance if the depositor does not claim the funds in the dormant account by December 31 of that calendar year. The notice shall be sent no later than October 1 of that calendar year.

Between November 1 and November 15 and between December 1 and December 15 of each year, each bank shall publish a “Notice of Inactive Bank Accounts”, which shall contain:

(a) the names, in alphabetical order, and last known addresses of depositors of dormant accounts; and

(b) a statement that, if not claimed, such funds shall be transferred to the Secretary of Finance during the month of January of the following year. The Notice of Inactive Bank Accounts shall

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be published in a newspaper of general circulation or by other means as determined by the Banking Board.

During the month of January of the calendar year immediately following the notification and publication required by subsections (4) and (5) of this section, each bank shall transfer to the Secretary of Finance, for the account of the depositor, the full balance of each dormant account, provided however, that the bank may deduct costs of notice and publication in a manner to be determined by the Banking Board in regulations.

Except as provided for in this section, no bank shall assess any fee against any bank account for reasons of inactivity.

In the event that a bank holds, for three years or more, any funds for which the owner or payor cannot be determined by the bank or for which the owner or payor cannot be located by the bank, the bank shall transfer such funds to the Secretary of Finance for the account of the owner or payor, in the event such owner or payor is determined or located at a later date.

Upon receiving sums of money pursuant to this section, the Secretary of Finance shall furnish the transferring bank with a receipt for such transferred funds and shall deposit such sums into a custodial interest-bearing account separate and apart from the General Fund of the FSM National Government. Interest earned on funds deposited with the Secretary of Finance pursuant to this section shall be deemed the property of the FSM National Government and shall not be paid to the owner of the funds.

The Secretary of Finance shall be responsible for maintaining accurate records of funds received pursuant to this section in accordance with any regulations adopted by the Banking Board.

At any time within 20 years of the date of transfer of funds to the Secretary of Finance pursuant to this section, such funds may be claimed by their rightful owner or owners by furnishing proof of his, her or their right to such funds, which proof is deemed satisfactory to the Secretary of Finance.

All funds transferred to the Secretary of Finance pursuant to this section shall escheat to the National Government of the Federated States of Micronesia 20 years following the date of such transfer.

Each bank shall hold the FSM National Government harmless for any liability incurred due to the handling of an account by the bank. The FSM National Government shall not be liable for any transaction on an account made by any bank, including the transfer of the balance of the account to the Secretary of Finance pursuant to this section. The FSM National Government shall not be liable for damages or penalties for any payment to a claimant of funds deposited pursuant to this section.

The bank shall not be liable for any mishandling of an account by the Secretary of Finance.

The Banking Board shall adopt such rules and regulations as may be necessary to implement the provisions of this section.

2. OBJECTIVES, SCOPE, METHODOLOGY

2.1. Objectives

The objectives of this inspection were to determine:

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1. Whether DoFA is effectively managing the transfer of dormant and inactive accounts from licensed commercial banks as required by the Dormant Account Regulations per Title 29 of the FSM Code, Section 106 of the FSM Bank Act.
2. Whether the FSM Banking Board is effectively monitoring compliance with licensed commercial banks in accordance with Title 29 of the FSM Code, Section 106 of the FSM Bank Act including other requirements as outlined by the Dormant Accounts Regulations.

2.2. Scope

The Inspection covered all dormant or inactive accounts from licensed commercial banks during FY 2021 – December 2024. It also included an assessment of the FSM Banking Board’s ability to monitor and ensure compliance with legal and regulatory requirements for all banks operating in the FSM.

2.3. Methodology

We conducted this Inspection in accordance with the Council of the Inspectors General on Integrity and Efficiency’s Quality Standards for Inspection and Evaluation. Those standards required that we plan and perform the inspection to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusion based on our objectives.

Fieldwork was conducted at the DoFA and the FSM Banking Board. Our inspection focused mainly on the compliance requirements surrounding dormant or inactive accounts as set forth by Title 29, Section 106 of the FSM Bank Act as well as with the Dormant Account Regulations established by the FSM Banking Board.

Inspection procedures included researching the enabling law of the FSM Banking Board to document and understand their functions and operations. The focus of the inspection was on Dormant Accounts being transferred from the commercial banks located in the FSM to DoFA. We interviewed relevant officials at the FSM Banking Board and DoFA to better understand the processes and obtain relevant information and records pertaining to the transfer of dormant or inactive accounts within the FSM to DoFA. Additionally, the team reconciled and verified transactions related to the transfer of dormant or inactive accounts to the Secretary of DoFA, based on selected samples. We also reviewed claims associated with these accounts to ensure they were processed in accordance with relevant regulations. Finally, the team assessed for compliance with applicable laws and regulations concerning dormant and inactive accounts.

3. Legal Mandates/Standards

3.1 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 nonprofit organizations receiving public funds from the National Government”.

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4. PRIOR AUDIT COVERAGE

This is the first engagement conducted by ONPA on matters relating to Dormant Accounts.

5. CONCLUSION

Based on our inspection, the team concluded that the FSM Banking Board and the Department of Finance & Administration are not effectively monitoring, recording, and reporting dormant accounts, as outlined in the following findings:

1. Dormant Account Funds Deposited into the General Fund Instead of a Custodial Interest – Bearing Account.
2. Insufficient and Improper Record-Keeping by the Department of Finance & Administration for Dormant Accounts.
3. Limited Enforcement of Banking Laws and Regulations by the Banking Board due to the lack of adequate internal controls.

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6. FINDINGS AND RECOMMENDATIONS

6.1 Finding No.1: Dormant Account Funds Deposited into the General Fund Instead of a Custodial Interest-Bearing Account

Criteria:

Pursuant to Section 106 of Public Law 13-56, it states that Upon receiving sums of money pursuant to this section, the Secretary of Finance shall furnish the transferring bank with a receipt for such transferred funds and shall deposit such sums into a custodial interest-bearing account separately and apart from the General Fund of the FSM National Government.

Section 3.4 of the Dormant Account Regulations also requires *that the funds shall be deposited into a custodial interest-bearing account.*

Condition:

Funds transferred to the Department of Finance are being deposited into the General Fund of the FSM National Government, instead of the required separate custodial interest-bearing account, as mandated by Section 106 of PL 13-56 and Section 3.4 of the Dormant Account Regulations. As a result, the inspection team was unable to reconcile the total amount of dormant funds that have been escheated to the Secretary of DoFA throughout the years. This non-compliance raises concerns about the proper handling and safeguarding of dormant account funds. Staff from DoFA also confirmed to the inspection team their lack of awareness and knowledge of the relevant laws and regulations pertaining to Dormant Accounts.

Effect(s):

1. Dormant funds being deposited into the General Fund may have missed the opportunity to accrue interest from investments, leading to a loss of potential income that could have benefited the FSM National Government.
2. The lack of familiarity with the FSM Bank Act and its Dormant Account Regulations among key DoFA officials, due to the absence of Standard Operating Procedures (SOPs), increases the risk of non-compliance. Additionally, the absence of clear procedures may lead to inconsistent practices, reduced accountability and ultimately, undermining the department's ability to manage dormant accounts effectively and transparently.

Cause(s):

1. DoFA's failure to establish a required custodial interest-bearing account resulted in dormant funds being deposited into the General Fund.
2. Staff within DoFA, responsible for managing dormant accounts, are unfamiliar with the FSM Bank Act and its Dormant Account Regulations due to the lack of SOPs with respect to managing dormant accounts from commercial banks operating in the FSM.

Recommendation(s):

1. We recommend that the Secretary of DoFA should establish a custodial interest-bearing account separate from the General Fund as required by law. This will ensure that they fully understand their legal requirements and properly implement the necessary procedures for managing dormant account funds.

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2. We also recommend that the Secretary of DoFA should develop and implement Standard Operating Procedures (SOPs) for managing dormant accounts, in alignment with the FSM Bank Act and its Dormant Account Regulations. These SOPs should provide clear guidance on the responsibilities of key officials and outline the processes for managing dormant accounts from commercial banks operating in the FSM. Additionally, DoFA should provide training to all relevant staff to ensure they are familiar with these procedures and the legal requirements for managing dormant accounts effectively.

6.2 Finding No. 2: Insufficient and Improper Record-Keeping by the Department of Finance & Administration for Dormant Accounts

Criteria:

According to PL 13-56 Section 106, it states that *the Secretary of Finance shall be responsible for maintaining accurate records of funds received pursuant to this section in accordance with any regulations adopted by the Banking Board.*

Part 3. Transfer to Secretary of Finance, Section 3.5 of the Dormant Regulations also requires that *there shall be a database in the Department of Finance and Administration for administering the custodial account. The database shall include the following information:*

- i. The name, identification number, bank of transfer and dormant bank account number of each sub account.*
- ii. The balance at transfer, the date of transfer, and the date of escheat of each sub account.*
- iii. A record of all payments made out of the account to individual sub account holders.*
- iv. A record of all payments made out of the account to the General Fund.*
- v. A record of all interest payments made into the account.*
- vi. A record of all service charges paid out of the account.*

Condition:

Contrary to PL 13-56 and Section 3.5 of the Dormant Account Regulations, the Department of Finance and Administration (DoFA) has not established the required database for managing custodial accounts. Instead, DoFA relies on spreadsheets to store dormant account information. This approach does not meet the legal and regulatory requirements, which specify that a database must be maintained to record critical information such as sub-account details, transfer dates, escheatment dates, payments, interest, and service charges. The use of spreadsheets raises concerns about accuracy, completeness, and security of dormant account records, as well as challenges in managing and retrieving information efficiently. The inspection team also had to wait over long periods of time for DoFA to provide any information on dormant accounts. Furthermore, the records were insufficient and not properly documented as required. For example, the team could not verify the following information mandated by Section 3.5 of the Dormant Account Regulations:

- o A record of all payments made from the account to individual sub-account holders.*
- o A record of all payments made from the account to the General Fund.*
- o A record of all interest payments deposited into the account.*
- o A record of all service charges deducted from the account.*

Effect(s):

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1. There is a direct non-compliance with PL 13-56 and the Dormant Account Regulations by DoFA.
2. Without a centralized database, there is a higher risk of incomplete, outdated, or inconsistent records for dormant accounts. This can lead to errors in financial reporting, making it difficult to accurately assess the status of these accounts.
3. Lack of proper tracking of dormant accounts may increase the risk of fraudulent activity, misappropriation, or mismanagement of funds, as there would be no systematic oversight or audit trail for these accounts.

Cause(s):

) DoFA has not yet established a database for managing dormant accounts, as required by PL 13-56 and Section 3.5 of the Dormant Account Regulations.

Recommendation(s):

We recommend that the Secretary of DoFA establish a comprehensive database for managing dormant accounts, in compliance with PL 13-56 and Section 3.5 of the Dormant Account Regulations. This database should be designed to accurately track and manage all dormant accounts, ensuring that required information is properly recorded, easily accessible, and regularly updated. Additionally, transitioning from spreadsheets to a database will improve data accuracy, security, and efficiency, ensuring compliance and enhancing the department's ability to manage dormant accounts effectively.

6.3 Finding No. 3: Limited Enforcement of Banking Laws and Regulations by the Banking Board due to the lack of adequate internal controls

Criteria:

PL No. 13-56, Section 601 requires that all domestic banks and, to the extent of and with respect to business done at any branches established in the Federated States of Micronesia, all foreign banks doing business in the Federated States of Micronesia shall be regulated and supervised by the Banking Board in such manner as to secure the safe and sound conduct of such business, to prevent unsound practices, and to maintain the public confidence in such business and protect the public interest and the interests of depositors. In determining if a Bank is carrying on its business in a prudent manner, the Banking Board will have regard to internal controls, risk management and accounting systems.

PL No. 13-56, Section 605 also states that the Banking Commissioner may request from the banks special reports. The Banking Commissioner may, from time to time, by notice in writing, require any domestic or foreign bank to submit such reports and returns as he may require for the purposes of the administration and enforcement of the provisions of this title and any regulations made thereunder. During the first five years of operations in the Federated States of Micronesia by any domestic bank, the Banking Commissioner shall call for special reports of its condition not less frequently than each calendar quarter.

Part 2 of the Dormant Account Regulations, Section 2.2. also states the following:

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b.) The notice shall contain the names, in alphabetical order, and last known addresses of depositors of dormant accounts; and a statement that, if not claimed, such funds shall be transferred to the Secretary of Finance during the month of January of the following year.

c.) The Notice of Inactive Accounts shall be published in a newspaper of general circulation and on the radio. The Notice shall also be posted at bank offices and post offices. The Notice shall be published in English and the local language.

d.) A record of the Notice and where and when it was published shall be maintained by the banks.

Condition:

The inspection team asked the FSM Banking Board how often they conduct bank examinations regarding the condition of the FSM banking system. According to the Bank Examiner, the most recent examination was completed in 2017. We attempted to obtain the report but were unable to due to confidentiality concerns as claimed by the FSM Banking Board

Another example of a direct compliance issue noted by the team was regarding the requirement of publishing dormant accounts. The team was able to obtain several dormant account publications from local newspapers, as mentioned above and required by law. However, these publications made by the banks did not fully comply with the relevant laws and regulations. For instance, we found that the names of the account holders were not in alphabetical order and that such publications are being prepared only in English by a certain bank and not in the local language as required. Additionally, we also noted that some supporting documents in the form of signature cards were also missing as required by the FSM Bank Act and its regulations.

The team also found that the FSM Banking Board lacks standard operating procedures (SOPs) for its operations and that they rely on the relevant laws and regulations. However, the Board is currently in the process of drafting their respective SOPs.

Potential Effect(s):

1. Without adequate internal controls for regular examinations and oversight, licensed commercial banks may fail to comply with laws and regulations, resulting in financial instability, legal issues, or unethical practices.

Cause(s):

1. The FSM Banking Board may lack sufficient staff or resources to regularly conduct bank examinations or ensure full compliance with all regulatory requirements, leading to delayed or incomplete examinations and enforcement.
2. The absence of established SOPs for the Board's operations can result in inconsistent practices, including in the preparation and review of reports and publications. Without clear guidelines, there may be confusion or oversight in complying with detailed regulatory requirements.

Recommendation(s):

We recommend that the Commissioner of the FSM Banking Board should:

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1. assess staffing levels to ensure sufficient and qualified personnel for comprehensive examinations and monitoring.
2. establish and document Standard Operating Procedures (SOPs) for the Banking Board's operations. These SOPs should outline clear guidelines for the preparation, review, and approval of reports and publications, ensuring consistency and compliance with regulatory requirements.

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7. MANAGEMENT RESPONSE

Department of Finance and Administration



Secretary of Finance
&
Administration

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

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January 8, 2025

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



RE: Management Response to Report No. 2025-02 relating to the Inspection on Dormant or Inactive Bank Accounts

Dear National Public Auditor Hainrick,

We appreciate the opportunity to respond to the inspection/audit report. The review was conducted in a timely manner, and we acknowledge the findings that the law was not being followed and that record keeping by the Department of Finance and Administration was inadequate. We will collaborate with the Banking Board to amend the law, as maintaining records for 20 years is burdensome for the Department, especially considering that the retention period for accounting records is 6 years.

We are currently in the process of implementing a new FMIS and have consulted with the supplier, FreeBalance, about setting up a sub-ledger to hold the required details. The following procedures will be implemented to comply with the law, with further explanations provided in the responses to your findings below:

Finding No. 1: Dormant Account Funds Deposited into the General Fund Instead of Custodial Interest-Bearing Account.

1. Funds from dormant accounts were initially placed into an interest-bearing savings account at the Bank of FSM. At some point, they were deposited directly to the general fund account. The exact date of this change is not known, but the savings account has accumulated interest for many years. Future deposits will be directed to the savings account again.

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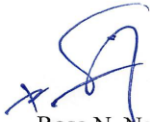
2. Standard Operating Procedures will be developed and staff will receive training as part of the FreeBalance implementation.

Finding No. 2: Insufficient and Improper Record-Keeping by the Department of Finance & Administration for Dormant Account.

As part of the implementation of the new Financial Management Information System (FMIS), any payments to or from dormant accounts will be recorded against the account holder to which they pertain. This database will maintain these records. We are planning to implement FreeBalance in the very near future, and no later than the start of FY26 (1 October 2025). In the meantime, we will continue to update the spreadsheet and use it as a monitoring tool.

Thank you for informing us about this issue. We will take the necessary actions to address it. We will continue to work with your office to uphold our fiduciary responsibilities at the highest standard and improve the accounting process for dormant accounts.

Sincerely



Rose N. Nakanaga
Secretary

cc: DOFA Treasury

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FSM Banking Board



FEDERATED STATES OF MICRONESIA
BANKING BOARD

Town Plaza Building, Suites 3 & 4
Tel: (691) 320-2015/2064 Fax: (691) 320-5433 E-Mail: fmnb@mail.fm

December 17, 2024

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

Dear National Public Auditor Hainrick:

Thank you for affording us the opportunity to meet with your Audit Team today to review, discuss and provide our comments or inputs on the draft Exit Inspection on Dormant Accounts document. Aside from the minor comments and inputs verbally provided, please see below what we believe to be of substance and worthy for your consideration as per each section of the Exit Inspection on Dormant Account document:

INTRODUCTION: (page 2)

We suggest deletion of the first sentence and be replaced with: "The Commissioner of the Banking Board inquired into audits of the Dormant Account in light of Section 3.6 of the Dormant Account Regulations." (This, in our opinion, best describes our intention and substance of our email in 2021. Citation of Section 3.6 of the Dormant Account Regulations can also be inserted under this section. Title 29 of FSMC (Bank Act) and Dormant Account Regulations do not grant authority to the Commissioner to engage the Public Auditor to audit the dormant account or custodial account at the Department of Finance and Administration. Rather, Section 3.6 of the Dormant Account Regulations allows for a copy of the audited report on the dormant account to be provided to the Commissioner and Board).

3. Legal Mandates/Standards (page 4)

We suggest that subsection 3.2 also be added or inserted under this Section to read: "Section 3.2 of the Dormant Account Regulations stipulates that the custodial account shall be audited as part of any general audit of the Department of Finance. The Department of Finance shall provide a copy of the audit to the Banking Board."

7.3 Findings No. 3: Limited Enforcement of Banking Laws and Regulations by the Banking Board (this section should be 6.3, instead)

Criteria:

1st paragraph: Comments: As discussed with your Team, the Banking Board has been producing consolidated Annual and Quarterly reports on the banking system as required. The banks are also required to file with our office annual reports March each year. These reports are reviewed and data and information therein are analyzed, verified and reconciled carefully with our internal data. Such are assessed against compliance standards or requirements, whether be financial soundness and safety or consumer compliance protection legal, regulatory and prudential standards. In other words,

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our office undertakes its due diligence review, analysis, monitoring, and reconciliation as required prior to producing our Annual Report.

As to Dormant or Custodial Account, please see our Annual Report posted on our website: www.bankingboard.gov.fm. We work with the Department of Finance and Administration to try to obtain information in their system for reconciliation with our internal figures (our office also receives a copy of the dormant account checks along with documents sent to Secretary of Finance and Administration by the banks). It is important to note our office takes no part in the transactions against the custodian account, i.e. claims). However, our Annual Report provide certain information on the dormant account, including the balance.

2nd paragraph: Comments: The Bank [redacted] designated or appointed [redacted] many years ago as its Agent for Service of Process for branch operations in the FSM as required under Section 408, not Section 501. Our office maintains constant communication (formal, email and verbal) with [redacted] and others at the Bank [redacted].

3rd paragraph: Comments: Subsection 2(f) of Section 601 stipulates some of the general prudential standards for assessing whether a bank is conducting its banking business consistent with banking prudential standards. One of those areas is spelled out in Subsection 2(f), the internal controls, risk management and accounting system. Both banks, the domestic and the foreign branch operating in the FSM are under regulatory and supervisory purview of the FSM Banking Board and the US Banking authorities. This dual regulatory and supervisory approach has helped with instilling confidence and trust in the FSM banking system by the general public. There are certain standards or requirements imposed by the FSM Banking Board, especially in the areas of "soundness" and "safety" of banks that are more stringent than that imposed by the US banking regulatory/supervisory authorities. Our Office utilizes different approaches for assessing and monitoring the internal control, risk management and accounting system of regulated/supervised banks. For example, the banks are required to file monthly prudential returns or Call Report. Banks are also required to file their adopted policies in these respective areas, among many other areas. Over the course of off-site monitoring, analysis and on-site examinations, the Board and the Commissioner feel bank policies and performance in these areas are satisfactory. In other words, every year on-site examination is conducted by FDIC and our staff accompany or piggy-back to the FDIC Examination Team to conduct such examination on Capital Adequacy, Asset Quality, Management, Earning, Liquidity, and Sensitivity to Market (CAMELS). Internal control, risk management and accounting system are few elements that fall under CAMELS, particularly under the M. Overall, the banking system in the FSM is safe, sound and stable as we have been reporting.

4th paragraph: no comment here, except those relayed to the Team – not substantial in nature but rather inadvertent typos.

5th paragraph: Comments: This is a citation from the regulations and we concur. Please see our comments below under "Cause(s)" and "Recommendation(s)". If the implication here is for the Board to require the banks to file such notices, publication and radio announcement with the Board, there is a regulatory compliance cost the banks will incur and such expenses usually pass-on to the customers or general public. There is a need for a "balancing act" here so the banks are in compliance while the Banking Board has the flexibility to assess compliance using other sources of information, such K-Press. The banks also have sophisticated and reliable automated system in place that automatically tracks down, for example, what to be the dormant accounts. Our Office informed the banks in early November of the discrepancies or inconsistencies or noncompliance we found in the K-Press (dormant account holders not published in alphabetical order and the lacking of

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vernacular translations). We are of the belief this citation in the Exit Inspection on Dormant Account document can be deleted.

6th paragraph: Comments: We believe this is a citation from the regulations and we concur.

Conditions:

1st paragraph: Comments: We need more information or explanation gathered by your Team in respect to this statement that “we could not provide reasonable assurance that the Board is effectively monitoring, recording, and reporting on its mandates.” We believe this statement is too vague and specific example(s) is needed. For example, the specific task before us relates to Section 106 and Dormant Account Regulations. In other words, we believe it is deceiving to say this general statement when the specific task deals only with Section 106. We feel these sentences need to be fully explained and clarified with concrete examples. The “insufficient information” may relate to the 2017 On-Site Examination Report which is a confidential report in our opinion per requirement under Section 704 of the Bank Act or 29FSMC. Our Office sought legal opinion as to whether the 2017 On-Site Examination Report could be availed. Our request is still pending as of this communication. There are other areas the Board monitors, assesses, gathers information on and do reporting on. Since the final outcome of this audit undertaking will be made to the public, we highly encourage precautionary and discrete or specific language so to avoid any potential implications and perception that may give rise to misperception and misunderstanding, especially in the public. As the bank regulatory and supervisory arm, one of our primary objectives is to ensure public confidence and trust in our banking system. This is another reason why we do not divulge certain activities and/or reports or findings by our office. Rather we work with the banks to ensure our findings are resolved for protection of depositors, safety, soundness and stability of the banking system.

2nd paragraph: Comments: As this relates to the immediate 1st paragraph above, we agree the banks did not fully comply with the “alphabetical order and vernacular languages” in the K-Press. Our office immediately took action by way of formal communication served to the banks regarding the non-compliance. Again, we feel this citation in the Exit Inspection on Dormant Account document is no longer applicable or relevant.

Effect(s):

1. As the audit team was informed, our office also received a copy of the transferring dormancy funds and all supporting documents provided by the banks to the Secretary of Finance. Also, the Board monitors dormant accounts notices in major and widely general publications, such as K-Press as cited above. Section 106 and its regulations is usually taken into scoping for our on-site examination, a consumer protection compliance matter. Consumer protection compliance examination is usually once every five years, depending on our findings during the off-site monitoring and assessment. Our examination team also piggy-back to the FDIC Consumer Compliance Examination Team when consumer protection compliance examination is conducted.
2. Agreed partially with this statement. However, examinations are conducted on both banks and the Board can consider and adopt such examination reports taken by, for example, FDIC Examination Team. As stated above, our staff participate and piggy-back to the FDIC Team when on-site examinations are conducted. The statement in the draft Exit Report is rather vague and can give false information or impression to the general public. Banks are heavily regulated and supervised due to the high level or degree of risks.

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Cause(s):

1. We believe this statement is also vague and may result in false information/impression to others. It is our opinion the Board has effective and efficient monitoring systems and processes in place for tracking or monitoring and assessing compliance, safety, soundness and stability. The Board may not have the state-of-the art or the most effective and efficient systems and process in place, though, but the present systems and processes in place allow us to discharge our mandate to the level that is satisfactory, given the available resources and capacity.
2. We agree there should be another staff to help on consumer protection compliance aspects of our mandate. We agree with your independent view on this, thank you.

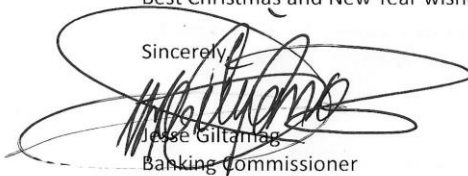
Recommendation(s):

1. In brief, examinations are recorded or documented and discussed with the bank. In fact, the findings and recommendations as the results of the examination are followed-up during next round of examination and during off-site monitoring. As to compliance check, the Board has already communicated to the bank on the discrepancies found in the K-Press regarding publishing of document accounts. Our office has compliance checks and templates for monitoring and assessing financial soundness, safety, stability and consumer protection compliance. Generally, we concur with this statement and recommendation.
2. We agree. Note: Staff capacity building is one of our priorities. Due to FDIC classes being full for the past three years, staff have not been able to attend FDIC Schools on financial soundness, safety, and consumer compliance protection. We have been communicating with FDIC (in person and via email) seeking classes slots for our staff. We are also exploring other avenues, such as banking schools (West Coast Banking School), virtual seminar and courses, i.e. IMF and others. Our proposed FY'26 budget proposal will include another examiner (new position) to focus solely on consumer compliance protection matters.

Again, I take this opportunity to thank you and your Team for affording us your independent review, particularly on areas where we can improve and develop.

Best Christmas and New Year wishes and greetings from all of us!

Sincerely,



Jesse Gilman
Banking Commissioner

Board Members, FSM Banking Board/Commission

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ONPA EVALUATION OF MANAGEMENT RESPONSE

We requested written management responses from the Department of Finance and Administration and the FSM Banking Board, and both offices have generally agreed with the findings and recommendations contained in the inspection report.

However, there were certain comments made in the management response from the FSM Banking Board that ONPA needs to provide further clarification on and would like to express our thanks and appreciation to them for pointing them out. The FSM Banking Board provided feedback on the introduction and details regarding the origin of the initial inspection request which we have addressed accordingly. Additionally, there was also a comment on the issue concerning the production of annual reports. ONPA would like to clarify that we are not questioning their production of annual reports, but rather other compliance requirements set forth by law and regulations for the banks.

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8. NATIONAL PUBLIC AUDITOR COMMENTS

We would like to thank the Banking Commissioner, staff, and leadership of the FSM Banking Board for their cooperation during the inspection. We also want to acknowledge the Secretary of the Department of Finance and Administration and her team for providing essential information related to the inspection.

We have provided copies of the final inspection report to the President and Members of the 23rd 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

April 4, 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 made key contributions to this report during the period specified:

Isireli T. Vaniqi, Audit Manager (former)
Brandon Rodriguez, Audit Supervisor
Christopher Delcampo, Team Leader
Ariel C. Perman, Team Member

ONPA MISSION We conduct quality audits and investigations to improve good governance and to prevent and deter fraud, waste and abuse for the stakeholders' benefit.

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