



OFFICE OF THE FSM NATIONAL PUBLIC AUDITOR

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ONPA RELEASES AUDIT REPORT OF FSM DEPARTMENT OF FINANCE AND ADMINISTRATION, DIVISION OF CUSTOMS AND TAX ADMINISTRATION

The Office of the National Public Auditor (ONPA) announces the release of Audit Report No. 2012-01, Audit of the FSM Department Of Finance And Administration, Division Of Customs And Tax Administration. A digital copy of the report is available for public review online at www.fsmopa.fm and printed copies are available at the ONPA's offices in Palikir, Pohnpei and Weno, Chuuk. The audit was conducted in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States.

The Division of Customs and Tax Administration (CTA), within the Department of Finance & Administration (DFA), 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 states of Pohnpei, Chuuk, Yap and Kosrae. Its primary responsibilities are to maximize collection of local revenues and maintain border control through its customs services.

The Assistant Secretary of DFA for CTA is responsible for directing the general operations of the CTA main office and its field offices in the four FSM States. A Deputy Assistant Secretary, under the supervision of the Assistant Secretary, manages each field office. In total, approximately 44 full-time positions are authorized for the CTA main office and the four field offices, one in each respective FSM State. CTA Division structure is comprised of two main functions: *Customs* and *Tax* Administration:

Customs Administration includes inspection at ports of entry for sea and air, assessment of tax filing, and collection of taxes on goods and merchandise imported into the FSM by sea and air and prevention of prohibited goods of merchandise imported into the FSM.

The audit scope covered fiscal years 2008, 2009 and 2010 and the report states that according to CTA records, during this period of time total local tax revenues were approximately \$74 million. Of this amount, approximately 90% came from collection of the Business Gross Revenue Tax (BGRT), Wage & Salary Tax (Income), Import Tax, with the remainder being collected for miscellaneous fees. Of the 90%, each of the 3 categories was approximately equal.

The objective of the audit was to determine:

1. If management is adequately monitoring the controls to ensure payments collected by the Field Offices are properly receipted and remitted to the DNT.
2. If management is adequately monitoring controls that require business owners accurately and timely report BGR Tax and Wage & Salary Tax.
3. If management is adequately monitoring whether SADs on Import Taxes are properly assessed, verified and collected. And
4. If programs exist to promote ethical behavior in support of the FSM tax system.

Based on the audit testing, the auditors concluded that the CTA main office does not monitor adequately the field offices in carrying out their key activities of enhancing and enforcing tax collection throughout the FSM. Consequently, the following control weaknesses were found:

- Poor internal control over the system of manual cash receipts continues to put cash at risk of loss or theft. Instances of alleged theft by CTA employees have occurred.
- The tax rolls (list of active businesses) are incomplete and as a result, compliance and tax revenue collection is diminished. Unpaid or unreported taxes by businesses in Pohnpei are not followed-up and the auditors estimate that 40%, or more, of businesses in Pohnpei are not reporting taxes due. In Chuuk, they were followed up only when visited by a special task force.
- The accuracy of payment of import taxes is not verified by CTA and the inspection of freight containers is hap-hazard, not formalized and seldom performed.
- CTA employees are not trained in the proper handling of potentially unethical situations including how to maintain independence with local businesses. In the absence of a CTA Code of Ethics, independence with local businesses is not specifically required.

Ultimately, the practices of CTA are lax especially in Pohnpei and Chuuk, and do not assure the citizens of the FSM that the tax and revenue laws are being uniformly enforced or complied with throughout the FSM.

The audit report discusses the findings in detail and numerous, detail recommendations were made. However, the CTA management response indicates a lack of ownership of the field office operations, which, until corrected, holds little hope of progress.

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