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**MANAGEMENT CHALLENGES
FOR INSULAR AREA GOVERNMENTS
AN OPPORTUNITY FOR IMPROVEMENT**

Guam, U.S. Virgin Islands, American Samoa,
Commonwealth of the Northern Mariana Islands, and
Compact States [Republic of the Marshall Islands,
Federated States of Micronesia, and Republic of Palau]





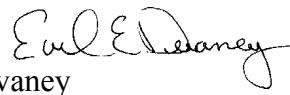
Mission: The mission of the Office of Inspector General (OIG) is to promote excellence in the programs, operations, and management of the Department of the Interior (DOI). We accomplish our mission in part by objectively and independently assessing major issues and risks that directly impact, or could impact, the DOI's ability to carry out its programs and operations and by timely advising the Secretary, bureau officials, and the Congress of actions that should be taken to correct any problems or deficiencies. In that respect, the value of our services is linked to identifying and focusing on the most important issues facing DOI.



United States Department of the Interior
Office of Inspector General
Washington, D.C. 20240

March 1, 2002

Memorandum

To: Secretary 
From: Earl E. Devaney
Inspector General
Subject: Management Challenges for Insular Area
Governments, An Opportunity for Improvements
(No. 2002-I-0017)

This report identifies what the Office of Inspector General (OIG) believes to be the major management challenges for the insular area governments. The report includes an assessment for each insular area government of its:

- h Overall Financial Management
- h Internal Audit Capabilities
- h Audit Resolution Issues
- h Areas for Improvement

Based on the results of audits performed by the OIG during the past 19 years (1983 to 2001), we believe that there exists unrealized opportunities for improvement in financial management, revenue enhancement, expenditure control, and program operations. However, some of these opportunities may require financial resources and/or technical expertise that may be beyond the current capacities of some of the insular area governments. In those cases the Office of Insular Affairs and other Federal grantor agencies should consider providing appropriate financial and/or technical assistance.

If you have any questions about this report, please do not hesitate to call me at (202) 208-5745.

- Review and, where appropriate, revise economic development laws and procedures to ensure that Federally-financed economic development loans are granted only to businesses that will enhance economic growth and have a reasonable financial ability to repay the loans.

Expenditure Control. To control expenditures, each of the Compact states should:

- Enforce the competitive procurement requirements contained in applicable Federal grant management regulations.

Program Operations. To improve general operations of Federally-funded programs, each of the Compact states should:

- Establish a comprehensive building maintenance program that has the staff and resources necessary to provide ongoing repair and maintenance to all Federally-financed facilities.

- Establish an effective governmentwide system to account for all Federally-financed property, including real property and equipment.

- Ensure that the Office of Public Auditor has the staff, other resources, and organizational independence necessary to function effectively in assessing government operations and developing recommendations for improvement.

- Establish a comprehensive audit followup system that can (1) track the level of resolution and implementation of audit recommendations made by local, Federal, and independent auditors and (2) enforce implementation by operating agencies of recommendations with which the Compact state's chief executive concurs.

principles, the Compacts of Free Association, the Single Audit Act of 1984 as amended, and Federal grant management requirements, each of the Compact states should:

- Evaluate the capabilities of its existing financial management systems and the long-term financial management needs of policy-makers and program personnel, and implement appropriate upgrades of the financial management systems to provide the ability to (1) effectively handle the volume of users and financial transactions projected to exist over the next 10 years and (2) provide user agencies with timely and accurate information on the status of their accounts.

- Implement procedural changes necessary to allow the Compact state’s independent auditors to perform and publish single audits on the state’s financial statements and Federal financial assistance within 9 months of the end of each fiscal year, as required by the Single Audit Act of 1984 as amended.

- Establish a governmentwide clearinghouse for information on Federal grants, including single audit and indirect cost rate information.

- Ensure that grant managers in all Compact state agencies receive ongoing training on the requirements for administration of Federal grants, with special emphasis on (1) the cost principles and the type and level of documentation necessary to show that grant expenditures are in compliance with applicable requirements and (2) the common rules for grant administration especially as related to financial management and reporting, procurement, and property management requirements.

Revenue Enhancement. To improve its ability to collect revenues, each of the Compact states should:

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Insular Area Governments

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education opportunities and as dependents of employed migrants. The data show that Compact migrants surveyed were working in jobs that required few skills and paid low wages, and most (over 50 percent) were living in poverty in all three U.S. island areas. According to GAO, the governments of Guam, Hawaii, and the Commonwealth of the Northern Mariana Islands identified significant Compact migration impact. The three U.S. areas have collectively reported at least \$371 million in costs to local governments for 1986 through 2000 that are associated with migrants from the Federated States of Micronesia, the Republic of the Marshall Islands, and the Republic of Palau, with Guam's estimate accounting for close to half of the total amount. All three U.S. island areas have shown that costs have been concentrated in the areas of health and education.

Areas for Improvement

Based on the results of audits performed by OIG during the past 19 years (fiscal years 1983 to 2001), we believe that the governments of Compact states should take the following actions in order to achieve greater levels of economy, efficiency, and effectiveness in the management of Federal source funds. These general recommendations distill the essence of hundreds of specific recommendations made in about 40 audit reports issued since October 1982. Some of these recommendations will require financial resources and technical expertise that may be beyond the current capacities of the Compact states. In those cases, the Office of Insular Affairs and other Federal grantor agencies should be approached about the possibility of providing appropriate financial and/or technical assistance.

Financial Management. To meet the financial management requirements of generally accepted accounting

Marshall Islands. This is evidenced by the fact that (1) per capita incomes have stagnated in the Federated States and fallen in the Marshall Islands; (2) Compact funds spent to support general government operations have maintained high government wages and a large level of public sector employment that has discouraged private sector growth; (3) Compact spending to create and improve infrastructure has not contributed to significant economic growth; (4) Compact-funded business ventures have generally failed. GAO further concluded that (1) while the Compact set out specific obligations for reporting and consulting regarding the use of Compact funds, the governments of the Federated States, the Marshall Islands, and the United States provided limited accountability over Compact expenditures and have not ensured that funds were spent effectively or efficiently; (2) the United States did not meet the Compact requirement to consult annually with both countries during the first 7 years of Compact assistance; (3) the Department of the Interior had devoted few resources to monitoring Compact assistance; and (4) disagreements between the Departments of State and the Interior limited monitoring, as did a Compact provision that guarantees funding to the two nations.

- The October 2001 report "Migration From Micronesian Nations Has Had Significant Impact on Guam, Hawaii, and the Commonwealth of the Northern Mariana Islands" (No. GAO-02-40) found that thousands of citizens from the Federated States of Micronesia, the Republic of the Marshall Islands, and the Republic of Palau have availed themselves of the migration rights provided under the Compacts. Almost 14,000 migrants were living in Guam and Hawaii in 1997 and the Commonwealth of the Northern Mariana Islands in 1998, according to Department of the Interior surveys. Guam had the most Compact migrants at 6,550, followed by Hawaii with 5,500 and the Commonwealth with 1,755. Compact migrants moved to U.S. island areas primarily for employment and

Guam

Overall Financial Management

The Government of Guam has been experiencing financial difficulties because of the downturn in the economies of most Asian countries during the late 1990s, which resulted in a reduction in tourist visitors and tourist-related income to the Government's General Fund. Hotel occupancy rates declined from an average of 85 percent in 1996 to only 61 percent in 1999. Although Guam's tourist arrivals had shown a slight increase during the first few months of 2001, the number of visitors were still not back to the peak levels of the mid-1990s. After the September 11th terrorist attacks, tourist arrivals declined significantly, with arrivals in October 2001 being reported at only 50 percent of October 2000 levels.

Operationally, the Government has had significant problems in several areas of interest to OIG. Perhaps most significantly, a new Oracle-based financial management system that was supposed to have brought the Government of Guam into the "new millennium" has not operated properly and the Government has had to commit several million dollars in funds to have further work done on the system, although millions of dollars had already been spent on initial development of the system. As a result, the Government has not been able to produce a comprehensive operating budget for the current fiscal year and has had to fall back on its old accounting system in order to provide even a modicum of accountability over revenues and expenditures. Further, the semi-autonomous Guam Power Authority and Guam Waterworks Authority both disclosed, during legislative hearings in late February 2001, that they had delinquent accounts receivable accounts valued at several million dollars, including thousands of dollars owed by prominent

Government of Guam officials and employees. Additionally, in early March 2001, the failure of a sewage pumping station resulted in the discharge of raw sewage into the bay where the majority of Guam's luxury hotels and resorts are located, resulting in the beaches being closed because of the presence of harmful bacteria.

Recent Audit Findings

OIG audits of Government of Guam operations during fiscal years 1999, 2000, and 2001 disclosed evidence of continued inadequate accounting for Federal funds, noncompliance with competitive procurement laws, and ineffective operations at Guam's main economic development agency.

A multi-segment audit of the Guam Department of Education disclosed that the Department (1) paid substitute teachers at least \$21,000 for hours not worked, hours worked on nonschool days, and hours that were not adequately supported by required documents (No. 99-I-13); (2) did not ensure that Federally funded travel costs totaling at least \$47,000 were adequately supported (No. 99-I-255); (3) did not adequately control program income of about \$32,000 or adequately account for and support expenditures totaling about \$2 million for a Federally funded after-school program (No. 99-I-455); and (4) did not use about \$5.4 million received under a contract with the U.S. Department of Defense for educational purposes as was required by the contract (No. 00-I-172).

A multi-segment audit of the Guam Economic Development Authority found that (1) the Authority issued economic development loans totaling almost \$7 million without ensuring that the proposed projects would enhance Guam's economy or that the borrowers had the ability to repay the loans and did not take effective collection action on delinquent loans totaling almost \$4 million (No. 01-I-417); (2) the Authority

health care and monitoring of islanders exposed to radioactive fallout. GAO also reported that, in gathering and verifying data on the cost of U.S. assistance provided to the Compact states, it found inaccuracies and inconsistencies with the data being used by Interior to supervise and monitor federal assistance programs. For example, Interior had a number of errors in the budget data it reported annually to Congress on direct payments to the Islands; there were significant inconsistencies in Interior's data on the assistance provided by other agencies to the Islands and the data the agencies reported to GAO; Interior had not used the annual single audit information available from the Compact states to corroborate its figures; and Interior's ability to accurately report on assistance provided was called into question.

- The September 2000 report "U.S. Funds to Two Micronesian Nations Had Little Impact on Economic Development" (No. NSIAD-00-216) concluded that (1) Compact funds were used for general government operations, capital projects such as building roads or investing in businesses, making debt payments, and improving targeted sectors such as energy and communications; (2) while the Federated States concentrated much of its spending on supporting government activities, the Marshall Islands emphasized capital spending; (3) although the two countries have made some progress in achieving economic self-sufficiency, as measured by their governments' lower reliance on U.S. funding, both countries remain highly dependent on U.S. assistance, which still provides more than half of total government revenues in each country; (4) although the amount of Compact funding has decreased since 1987 as required by the terms of the Compact, both countries have received other U.S. funding through their use of U.S. federal services and programs. The report also concluded that Compact expenditures to date have led to little improvement in economic development in the Federated States and the

**** Crosscutting Issues ****

GAO Audits on Compact States

Because the Compacts of Free Association between the United States and both the Republic of the Marshall Islands and the Federated States of Micronesia are currently under renegotiation, the U.S. Congress requested that GAO perform a series of audits on the Compact states. As of October 2001, GAO had issued three reports on the Compact states, as follows:

- The May 2000 report "Better Accountability Needed Over U.S. Assistance to Micronesia and the Marshall Islands" (No. RCED-00-67) concluded that (1) during fiscal years 1986 to 1999, the United States had provided more than \$2.6 billion in financial and other assistance, of which more than \$1.5 billion was provided to the Federated States and over \$1.1 billion was provided to Marshall Islands; (2) the Department of the Interior had provided the majority of the assistance, about \$2 billion, through quarterly payments to be used for such purposes as capital construction projects, energy production, communication capabilities, and current account costs, such as those for payroll, maintenance, and other governmental activities; (3) the remaining half billion dollars was provided by 19 federal agencies in the form of grants, loans, equipment, and technical assistance, such as weather forecasting support and airport training activities; (4) prior to the Compact, the United States provided about \$250 million in funding and assistance to what is now the Marshall Islands for the effects of the U.S. nuclear weapons testing program that took place in the Marshall Islands during the 1940s and 1950s; (5) the Departments of Defense, Energy, and Interior provided direct payments to the Marshall Islands' governments and individuals, rehabilitation and resettlement services, and

issued tax exemptions to tourist-oriented businesses without ensuring that the resulting benefits to the Guam economy would be commensurate with the more than \$61 million in potential tax revenues foregone over the life of the exemption certificates (No. 01-I-419); and (3) Government of Guam agencies lost or will lose as much as \$65 million as a result of not requesting and/or following the financial advice available from the Authority (No. 2002-I-016).

Audits are currently underway on the management of Federal grants by the Department of Mental Health and Substance Abuse (Assignment No. N-IN-GUA-002-00-M) and the management of water operations by the Guam Waterworks Authority (Assignment No. N-IN-GUA-001-01-R).

The most recently published single audit report is for fiscal year 1999, and it has a qualified opinion because (1) tax-related records and data could not be accessed to verify revenues and outstanding receivables, (2) information on the general fixed assets account group was incomplete, (3) fixed assets of the Guam Community College were not included, (4) information on the general long-term debt account group was incomplete, (5) financial information on the Pension Trust Fund, the Guam Housing and Urban Renewal Authority, the Guam Council on the Art and Humanities, the Guam Port Authority, the Guam Department of Education, the Supreme Court of Guam, the Guam Legislature, and the Guam Visitor's Bureau were not included, and (6) audited financial statements of the Guam Memorial Hospital Authority and the Guam Preservation Trust Fund were not included. The single audit also reported Federal financial assistance of \$169.6 million (Interior - \$9 million) with questioned costs of \$15.7 million (Interior - \$3.1 million). The financial statements indicated that the General Fund had an accumulated deficit of \$108.9 million as of September 30, 1999. The Government of Guam had to request a 6-month extension of the deadline for

completion of the fiscal year 1999 single audit because it was unable to prepare financial statements as a result of the failure of its new Oracle-based financial management system.

Internal Audit Capabilities

The Office of Public Auditor was established by Guam public law. Until 1999, the position was filled by having a special commission submit possible candidates (either an attorney or a Certified Public Accountant) to the Governor. The Governor appointed an individual from this list with confirmation by the Legislature. The term of office was 6 years and, if the individual wished to remain in office beyond the initial term, he had to be popularly elected for another 6-year term. However, in 1999, the Guam Legislature amended the Public Auditor law to make the Public Auditor position an elected office and to reduce the qualification requirements by allowing an individual with 5 or more years of experience in budget formulation and/or execution to hold office. The current Public Auditor was elected to office in November 2000 and took office in January 2001. Based on the revised law, the office is now funded at a specified percentage of General Fund appropriations. As of February 2002, the office had a staff of 9 (the Public Auditor, 7 audit staff, 1 support staff), or an increase of 4 employees since 1999.

Audit Resolution Issues

The lack of adequate audit resolution and implementation of recommendations by the Government of Guam contributed to the existence of long-standing financial management deficiencies. OIG's experience has been that, although the Government may implement recommendations that address the specific deficiencies and transactions noted in audit reports, it often does not implement recommendations that call for substantive, systemic changes in operating policies and

Senate and the House. The term of office is 6 years and the individual may be reappointed to a second 6-year term. The office is funded by annual General Fund appropriations and unused funds may be carried over to the next year. As of March 2001, the office had a staff of 9 (the Public Auditor, 5 auditors, 1 investigator, and 2 support staff), or a decrease of 2 employee since 1998.

**** Republic of Palau ****

Overall Financial Management

The Republic of Palau did not have adequate control over Federal funds provided for capital improvement projects. An OIG audit in fiscal year 2000 concluded that Palau did not effectively manage construction projects funded by the Trust Territory of the Pacific Islands and the Compact of Free Association and, as a result, (1) Compact funds totaling almost \$6.5 million were not effectively used for badly-needed capital improvement projects and (2) Trust Territory-funded projects valued at more than \$48 million remained uncompleted for periods ranging from 5 to 25 years (No. 00-I-537).

The most recent published single audit report is for fiscal year 1999, and it included a qualified opinion because (1) the general fixed assets account group was not updated and (2) financial statements of the Palau District Housing Authority and the Palau National Communications Corporation were not included. The single audit also reported Federal financial assistance of \$31.5 million (Interior - \$25.2 million) with questioned costs of about \$30,000 (Interior - \$30,000). The financial statements indicated that the General Fund had an accumulated deficit of \$18.7 million as of September 30, 1999.

Internal Audit Capabilities

The position of Public Auditor was created by Palau's Constitution, and the Office of Public Auditor was established by the Public Auditing Act of 1985. The position is filled by appointment (the candidate must be a Certified Public Accountant) by the President with confirmation by both the

procedures to ensure that similar problems do not occur in the future. As a result, our audit reports often disclose problems that are identical or at least similar to ones that had been disclosed by prior audit reports. For example:

- Reports issued in 1990 (No. 90-78), 1993 (No. 93-I-706), 1994 (No. 94-I-980), 1995 (No. 95-I-1202), and 2000 (No. 00-I-172) disclosed internal control and compliance deficiencies that resulted in Federal funds awarded to the Government of Guam not being properly accounted for or used in accordance with grant or contract requirements.

- Reports issued in 1984 (No. N-TG-GUA-16-84B), 1989 (No. 89-70), and 1998 (No. 98-I-570) presented information on ineffective administrative and collection enforcement practices by the Guam Department of Revenue and Taxation that resulted in lost gross receipts tax revenues that totaled as much as \$2 million in 1998.

- Reports issued in 1991 (Nos. 91-I-372 and 91-I-563) and 1997 (No. 97-I-1051) concluded that Government of Guam agencies did not have adequate personnel management practices, which resulted in excessive personnel service costs that ranged from \$1.9 million in 1991 to \$3.6 million in 1997.

- Reports issued in 1993 (No. 94-I-37), 1997 (No. 97-I-241), and 1998 (No. 98-I-14) concluded that Government of Guam agencies did not comply with competitive procurement requirements for purchases and contracts totaling as much as \$24 million.

Areas for Improvement

Based on the results of audits performed by OIG during the past 19 years (fiscal years 1983 to 2001), we believe that the Government of Guam should take the following actions in

order to achieve greater levels of economy, efficiency, and effectiveness in its financial management and program operations. These general recommendations distill the essence of hundreds of specific recommendations made in about 115 audit reports issued since October 1982. Some of these recommendations will require financial resources and technical expertise that may be beyond the current capacities of the Government of Guam. In those cases, the Office of Insular Affairs and other Federal grantor agencies should be approached about the possibility of providing appropriate financial and/or technical assistance.

Financial Management. To meet the financial management requirements of generally accepted accounting principles, the Insular Areas Act of 1982, the Single Audit Act of 1984 as amended, Federal grant management requirements, and appropriate local laws and regulations, the Governments of Guam should:

- Evaluate the capabilities of its existing financial management systems and the long-term financial management needs of policy-makers and program personnel, and implement appropriate upgrades of its financial management systems to provide the ability to (1) effectively handle the volume of users and financial transactions projected to exist over the next 10 years and (2) provide user agencies with timely and accurate information on the status of their accounts.

- Ensure that users of the financial management systems in all operating agencies receive ongoing training on the capabilities and use of the systems.

- Implement procedural changes necessary to allow (1) the central accounting department to produce comprehensive annual financial reports within 120 days of the end of each

requirements) by the President with confirmation by the Congress. The nominal term of office is 6 years, but the individual continues in office until replaced by another Presidential appointee. The office is funded by annual General Fund appropriations and, as of March 2001, had a staff of 9 (the Acting Public Auditor, 6 auditors, 1 investigator, and 1 support staff), or a decrease of 8 employees since 1998. The position of Public Auditor has been vacant since early 1999. As of March 2001, each of the four states of the Federated States had small audit offices with staffs of 7 (the State Auditor, 5 auditors, and 1 support staff) in Pohnpei, 2 (the State Auditor and 1 support staff) in Kosrae, 2 (the State Auditor and 1 support staff) in Yap, and 1 (support staff only) in Chuuk.

***** Federated States of Micronesia *****

Overall Financial Management

The Federated States of Micronesia also did not have effective controls over Federally-funded loan programs. An OIG audit in fiscal year 1999 concluded that the Pohnpei Local Office of the Rural Development Loan Program, which was funded by the U.S. Department of Agriculture and jointly operated by Agriculture and the Federated States, did not ensure that recipients of home loans totaling more than \$700,000 used the loans for houses that met program requirements and/or would be used for noncommercial, personal residency purposes (No. 99-I-953).

The most recent published single audit report is for fiscal year 1999, and it included a qualified opinion because (1) fixed assets, receivables, amounts due to and from other governments, and revenues of the governmental fund types could not be verified; (2) there were questions about the propriety and disclosure of accounts payable for the Health Insurance Fund; and (3) financial statements of the National Fisheries Corporations were not included. The single audit also reported Federal financial assistance of \$99.3 million (Interior - \$90 million) with questioned costs of \$68,000 (Interior - \$58,000). The financial statements indicated that the General Fund did not have an accumulated deficit as of September 30, 1999.

Internal Audit Capabilities

The position of Public Auditor was created by the Federated States' Constitution, and the Office of Public Auditor was established by the National Public Auditor Act. The position is filled by appointment (no specific qualification

fiscal year, as required by the Insular Areas Act of 1982, and (2) the Government's independent auditors to perform and publish single audits on the Government's financial statements and Federal financial assistance within 9 months of the end of each fiscal year, as required by the Single Audit Act of 1984 as amended.

- Ensure that annual executive budgets are prepared and submitted for legislative consideration and approval within the deadlines specified in local laws.

- Enforce existing prohibitions against making or authorizing expenditures or obligations in excess of the amount of any appropriation or allotment.

- Establish a governmentwide clearinghouse for information on Federal grants, including single audit and indirect cost rate information.

- Ensure that grant managers in all Government agencies receive ongoing training on the requirements for administration of Federal grants, with special emphasis on (1) the cost principles and the type and level of documentation necessary to show that grant expenditures are in compliance with applicable requirements and (2) the common rules for grant administration especially as related to financial management and reporting, procurement, and property management requirements.

Revenue Enhancement. To improve its ability to generate and collect revenues, the Government of Guam should:

- Computerize the tax administration functions and vigorously enforce the laws and regulations related to income taxes and existing local taxes to ensure that (1) potential

taxpayers are identified and assessed taxes on a fair and equitable basis and (2) all taxes owed to the Government are properly accounted for and collected.

- Ensure that all agencies that generate accounts receivable have procedures to (1) maintain accurate and up-to-date records on the amounts owed to the Government and (2) aggressively enforce collection of such amounts.

- Implement and enforce internal controls, including the providing of an adequate level of supervisory oversight, within all agencies that make collections on behalf of the Government.

- Review and, where appropriate, revise economic development laws to ensure that (1) tax exemptions and/or rebates are provided only to industries and firms that would not otherwise establish in Guam without such incentives, (2) cost-benefit analyses are performed on a periodic basis to ensure that the benefits of economic development programs are commensurate with the tax revenues foregone, (3) economic development beneficiaries comply with employment and other requirements intended to provide economic benefits to the Guam economy, and (4) economic development loans are granted only to businesses that will enhance economic growth and have a reasonable financial ability to repay the loans.

- Ensure that all agencies that rent Government-owned property to private entities charge rental rates that are commensurate with market conditions and enforce collection of lease rental receivables.

Expenditure Control. To control expenditures and provide operating agencies with the resources necessary to

of the government were not included. The single audit also reported Federal financial assistance of \$106.5 million (Interior - \$70.5million) with questioned costs of \$2.8 million (Interior - \$2.3 million). The financial statements indicated that the General Fund did not have an accumulated deficit as of September 30, 1999.

Internal Audit Capabilities

The position of Auditor General was created by the Marshall Islands' Constitution, and the Auditor General's duties and responsibilities are defined by the Auditor General Act of 1986. The position is filled by appointment (no specific qualification requirements) by the President with confirmation by the Legislature. The term of office is permanent until the individual reaches the age of 72, resigns, or is removed for cause. The office is funded by annual General Fund appropriations, usually at a level of 0.5 percent of total appropriations, and, as of March 2001, had a staff of 5 (the Auditor General, 4 auditors, and no support staff), or a decrease of 2 employee since 1998.

Compact States

**** Republic of the Marshall Islands ****

Overall Financial Management

The Republic of the Marshall Islands did not have effective controls over Compact funds, including a Compact-funded loan program. An OIG audit in fiscal year 1999 concluded that the Marshall Islands Development Bank (1) had used Compact funds totaling about \$13.7 million to issue commercial loans without adequate assurance that the loans were for purposes that conformed to approved economic development plans and that the borrowers had the capability to repay the loans, (2) did not enforce collection on additional Compact-funded loans totaling about \$4.1 million that were delinquent, and (3) did not adequately account for outstanding Trust Territory loans totaling about \$380,000 (No. 99-I-952). Additionally, an October 2000 news article reported that a former President of the Marshall Islands had allowed the Bank of New York (the Marshall Islands' custodian for Compact funds) to use Compact funds to pay \$270,000 against a \$400,000 personal loan that the former President had with the Bank of Guam. This matter was referred to the OIG investigators on Guam.

The most recent published single audit report is for fiscal year 1999, and it included a qualified opinion because (1) minutes of board of directors' meetings of the government-owned Majuro Resort, Inc. and Air Marshall Islands, Inc. were not available for review, (2) the general fixed assets account group was not updated, (3) there were inadequacies in the accounting records and internal controls over financial reporting for all governmental fund types and a component unit of the government, and (4) financial statements of a component unit

carry out their operational responsibilities, the Government of Guam should:

- Enforce the competitive procurement requirements contained in local laws and regulations and, where appropriate, in Federal grant management regulations.
- Ensure that the central procurement department and other authorized purchasing agencies fully document competitive procurement actions taken or provide justification as to why competitive procurement procedures were not used.
- Review and, where appropriate, revise existing procurement and vendor payment policies and procedures to ensure that agencies receive required goods and services and vendors are paid for such goods and services in a timely manner.
- Review and, where appropriate, revise space leasing policies and procedures to ensure that commercial space is not leased unless suitable Government-owned property is not available and, in such cases, that rental rates paid are commensurate with existing market conditions.
- Require that operating agencies control travel costs in accordance with existing travel regulations.

Program Operations. To improve general program operations, the Government of Guam should:

- Provide operating agencies with qualified staff, adequate training, and other resources necessary for them to carry out their legally mandated responsibilities efficiently and effectively.

- Review and, where appropriate, revise existing personnel policies and procedures to (1) consolidate multiple pay schedules, (2) streamline the personnel recruitment process, and (3) ensure that career service positions are not filled by political appointments that destroy the credibility of the personnel merit system.

- Establish a comprehensive building maintenance program that has the staff and resources necessary to provide ongoing repair and maintenance to all Government-owned facilities.

- Establish an effective governmentwide system to account for all Government-owned property, including real property and equipment.

- Ensure that the Office of Public Auditor has the staff, other resources, and organizational independence necessary to function effectively in assessing government operations and developing recommendations for improvement.

- Establish a comprehensive audit followup system that can (1) track the level of resolution and implementation of audit recommendations made by local, Federal, and independent auditors and (2) enforce implementation by operating agencies of recommendations with which the Government's chief executive concurs.

Program Operations. To improve general program operations, the Commonwealth of the Northern Mariana Islands should:

- Establish a comprehensive building maintenance program that has the staff and resources necessary to provide ongoing repair and maintenance to all Commonwealth-owned facilities.

- Establish an effective governmentwide system to account for all Commonwealth-owned property, including real property and equipment.

- Ensure that the Office of Public Auditor continues to have the staff, other resources, and organizational independence necessary to function effectively in assessing government operations and developing recommendations for improvement.

- Establish a comprehensive audit followup system that can (1) track the level of resolution and implementation of audit recommendations made by local, Federal, and independent auditors and (2) enforce implementation by operating agencies of recommendations with which the Government's chief executive concurs.

- Computerize the tax administration functions and vigorously enforce the laws and regulations related to income taxes and existing local taxes to ensure that (1) potential taxpayers are identified and assessed taxes on a fair and equitable basis and (2) all taxes owed to the Commonwealth are properly accounted for and collected.

- Ensure that all agencies that generate accounts receivable have procedures to (1) maintain accurate and up-to-date records on the amounts owed to the Commonwealth and (2) aggressively enforce collection of such amounts.

- Implement and enforce internal controls, including the providing of an adequate level of supervisory oversight, within all agencies that make collections on behalf of the Commonwealth.

Expenditure Control. To control expenditures and provide operating agencies with the resources necessary to carry out their operational responsibilities, the Commonwealth of the Northern Mariana Islands should:

- Enforce the competitive procurement requirements contained in local laws and regulations and, where appropriate, in Federal grant management regulations.

- Ensure that the central procurement department and other authorized purchasing agencies fully document competitive procurement actions taken or provide justification as to why competitive procurement procedures were not used.

- Require that operating agencies control travel costs in accordance with existing travel regulations.

U.S. Virgin Islands

Overall Financial Management

The Government of the U.S. Virgin Islands continues to face severe financial difficulties. A September 1998 audit report (No. 98-I-670) disclosed that the Government had about \$588 million in outstanding operating-related debt and made unauthorized loans of about \$120 million from its Special and Other Funds bank account, which includes Federal grant funds, to cover General Fund payroll expenses. Since the issuance of that report, the Government continued to suffer severe cash flow problems, which resulted in the accumulation of debt totaling close to \$1 billion, including amounts owed for income tax refunds, payments to vendors, negotiated salary increases to employees, FEMA disaster assistance loans, accumulated operating deficits, and ever-increasing outstanding bonds. In November 1999, the Government issued over \$300 million in bonds, which was used to pay long-outstanding operating-related expenses, including the overdue income tax refunds, payments to vendors, and negotiated employee raises. However, the Government pledged a portion of future gross receipts tax revenues to pay the bonds, meaning that this important source of revenue is no longer available to pay future operating expenses. The U.S. Virgin Islands suffered a significant drop in tourist arrivals in the months immediately following the September 11, 2001 terrorist attacks, and the ultimate financial impact of that tourist decline on Government revenues is still unknown.

In October 1999, the Governor of the U.S. Virgin Islands and the Secretary of the Interior entered into a Memorandum of Understanding (MOU) intended to provide the U.S. Virgin Islands with some financial relief in return for pledges of improved financial accountability on the part of the

Government of the U.S. Virgin Islands. The MOU contains 13 fiscal accountability and financial performance standards that require the Government to establish a 5-year financial recovery plan; reduce expenditures, including regular personnel costs and overtime; achieve a balanced budget by fiscal year 2003; prepare and issue comprehensive annual financial reports and single audit reports within legally-mandated timeframes; develop and implement a staff training program; and exert "all efforts" to reduce the Government's outstanding debt. The MOU also required the Government to provide the Department of the Interior with monthly (later changed to quarterly) progress reports. Progress reports submitted by the Government stated that the Government had met required expenditure reduction goals related to fiscal year 2000. However, pressure for salary increases from government employee unions and the lack of support from the Legislature to some of the Executive Branch's cost-cutting initiatives has resulted in subsequent increases in Government expenditures in fiscal years 2001 and 2002. A limited review by OIG of the Government's compliance with the MOU disclosed that 8 of 13 the fiscal accountability and financial performance standards contained in the MOU had not been "substantially achieved" as of October 2001 (Draft No. V-IN-VIS-0045-2001).

In December 2001, a joint Federal/Virgin Islands conference was held on St. Thomas, during which Federal and Virgin Islands government representatives developed an outline for a plan of action to achieve significant improvements in three key areas: financial management, procurement and property management, and human resources management. This conference was spearheaded by the U.S. Department of Education as part of a formal process to put the Virgin Islands Department of Education under a compliance agreement to meet Federal grant management requirements. However, the plan of action developed during the conference involves

over the next 10 years and (2) provide user agencies with timely and accurate information on the status of their accounts.

- Ensure that users of the financial management systems in all operating agencies receive ongoing training on the capabilities and use of the systems.

- Implement procedural changes necessary to allow (1) the central accounting department to produce comprehensive annual financial reports within 120 days of the end of each fiscal year, as required by the Insular Areas Act of 1982, and (2) the Commonwealth's independent auditors to perform and publish single audits on the Commonwealth's financial statements and Federal financial assistance within 9 months of the end of each fiscal year, as required by the Single Audit Act of 1984 as amended.

- Approve, on an annual basis, governmentwide budgets that limit expenditures and transfer authorizations to the most current and realistic revenue projections available.

- Ensure that grant managers in all Commonwealth agencies receive ongoing training on the requirements for administration of Federal grants, with special emphasis on (1) the cost principles and the type and level of documentation necessary to show that grant expenditures are in compliance with applicable requirements and (2) the common rules for grant administration especially as related to financial management and reporting, procurement, and property management requirements.

Revenue Enhancement. To improve its ability to generate and collect revenues, the Commonwealth of the Northern Mariana Islands should:

improvement appropriations. As of March 2001, the office had a staff of 35 (the Public Auditor, 24 auditors, 5 investigators, 2 attorneys, and 3 support staff), or a decrease of 5 employees since 1998.

Areas for Improvement

Based on the results of audits performed by OIG during the past 19 years (fiscal years 1983 to 2001), we believe that the Commonwealth Government should take the following actions in order to achieve greater levels of economy, efficiency, and effectiveness in their financial management and program operations. These general recommendations distill the essence of hundreds of specific recommendations made in more than 40 audit reports issued since October 1982. Some of these recommendations will require financial resources and technical expertise that may be beyond the current capacities of some of the insular area governments. In those cases, the Office of Insular Affairs and other Federal grantor agencies should consider providing appropriate financial and/or technical assistance.

Financial Management. To meet the financial management requirements of generally accepted accounting principles, the Insular Areas Act of 1982, the Single Audit Act of 1984 as amended, Federal grant management requirements, and appropriate local laws and regulations, the Commonwealth of the Northern Mariana Islands should:

- Evaluate the capabilities of its existing financial management systems and the long-term financial management needs of policy-makers and program personnel, and implement appropriate upgrades of its financial management systems to provide the ability to (1) effectively handle the volume of users and financial transactions projected to exist

crosscutting systems and procedures that will have beneficial effects on governmentwide operations.

Recent Audit Findings

OIG audits of Government of the U.S. Virgin Islands operations during fiscal years 1999 through 2001 disclosed that the Government (1) did not effectively collect unemployment insurance taxes totaling more than \$18.5 million (No. 99-I-148), delinquent loans to members of the Government Employees Retirement System totaling about \$5.3 million (No. 99-I-261), real property taxes totaling at least \$15.4 million (No. 99-I-379), and excise taxes totaling more than \$1 million (No. 01-I-291); (2) did not implement policies and procedures to restrict the hiring of political appointees to positions that, by law, should be part of the personnel merit system and did not ensure that the number of Government employees was reduced to the levels required by an early retirement law (No. 99-I-365); (3) did not effectively manage, account for, and use Federal grants totaling about \$25 million from the Federal Transit Administration (No. 99-I-701), the Department of Justice Child Support Program, (No. 99-I-921), the Department of Education (No. 99-I-956), the Department of Health and Human Services (No. 99-I-957), the Department of the Interior (No. 00-I-216), the Department of Housing and Urban Development (No. 00-I-625), and the Environmental Protection Agency (No. 00-I-696); (4) did not ensure that the Virgin Islands Lottery properly accounted for and expended funds totaling more than \$1.3 million (No. 01-I-290); (5) did not ensure that the Virgin Islands Port Authority properly accounted for and collected lease rental and parking lot fees totaling about \$1.2 million (No. 01-I-303); and (6) did not ensure that the Virgin Islands Department of Education paid payroll charges of \$120,000 from the correct accounts (No. 01-I-330). Audit reports issued since September 30, 2001, also disclosed

weaknesses in the financial and operational activities of the Virgin Islands Fire Service (No. 2002-I-001), the Joint Partnership Training Act program of the Virgin Islands Department of Labor (No. 2002-I-002), the Virgin Islands Housing Finance Authority (No. 2002-I-009), and the Virgin Islands Police Department (No. 2002-I-010).

The Government has made significant progress to achieve compliance with the requirements of the Single Audit Act of 1984, as amended in 1996. The most recent published single audit report is for fiscal year 1999, the fiscal year 2000 report is due in January 2002, and the Government is on a Federally-mandated timetable to produce future single audit reports in a timely manner. Additionally, the Government has agreed to Federal grantor agency demands that agreed-upon procedures reviews be performed for fiscal years 1996 and 1997. However, the single audits show that financial management deficiencies continue to exist. Specifically, the fiscal year 1999 single audit report included a qualified opinion because (1) the general fixed assets account group was omitted, (2) current financial information on the Housing Finance Authority and Housing Authority was not included, (3) the Government Employee Retirement System auditors issued a qualified opinion due to their inability to verify cash and outstanding loan balances, (4) financial records were not maintained to verify accounts receivables, inventories, and fixed assets of Government-owned hospitals, and (5) landfill closure and postclosure costs were not included in the general long-term debt account group. The single audit also reported Federal financial assistance of \$163.3 million (Interior - \$3.3 million) with questioned costs of \$17.8 million (Interior - \$0). The financial statements indicated that the General Fund had an accumulated deficit of \$345.2 million as of September 30, 1999.

the Department of the Interior) concluded that the Ports Authority (1) did not adequately analyze or justify contract change orders, (2) entered into an unauthorized, noncompetitive contract for construction management services, and (3) improperly used Saipan harbor project funds for a project on the nearby island of Rota (Draft No. N-IN-NMI-003-00-R). These deficiencies led to a delay of more than 6 years in the completion of the project, which contributed to questioned costs totaling \$11.9 million.

The most recent published single audit report is for fiscal year 1999, and it included a qualified opinion because (1) the general fixed assets account group was not updated, (2) there were inadequacies in the accounting records and internal controls for all governmental fund types and a component unit of the government, and (3) financial statements of other component units of the government were not included. The single audit also reported Federal financial assistance of \$45.9 million (Interior - \$19.1 million) with questioned costs of about \$146,000 (Interior - \$146,000). The financial statements indicated that the General Fund had an accumulated deficit of \$39.9 million as of September 30, 1999.

Internal Audit Capabilities

The position of Public Auditor was created by the Commonwealth's Constitution, and the Office of Public Auditor was established by the Commonwealth Auditing Act. The position is filled by appointment by the Governor with confirmation by the Legislature. The term of office is 6 years and the individual may be reappointed for a second 6-year term. The Office is guaranteed a minimum \$500,000 annual budget but, in accordance with the Commonwealth Auditing Act, generally receives a budget of 1 percent of the total amount of annual Commonwealth operating and capital

Commonwealth of the Northern Mariana Islands

Overall Financial Management

Like Guam, the Commonwealth of the Northern Mariana Islands has had severe financial difficulties because of a downturn in its tourism-based economy. The Commonwealth suffered a more drastic drop in visitor arrivals than did Guam as a result of the Asian economic recession, with hotel occupancy rates declining from almost 86 percent in 1996 to only 58 percent in 1999. Additionally, a recent resurgence in visitors had not been to the same extent as experienced in Guam and the decline in tourist arrivals was exacerbated by the September 11th terrorist attacks. However, based on press reports, it appears that the Commonwealth Government has tried to take the steps necessary to cut operating expenditures. This is most critical for the Commonwealth because the Northern Mariana Islands do not receive the same level of Federal financial assistance as do either Guam or American Samoa. OIG audits on the Commonwealth Government's operations during fiscal year 1999 disclosed that (1) the Public School System did not use competitive procurement requirements to make purchases totaling more than \$500,000 that were funded by Federal grants and could not locate equipment valued at almost \$200,000 that was purchased with Federal grant funds (No. 99-I-147) and (2) the Office of the Governor made expenditures from the Governor's discretionary fund that exceeded legislative appropriations by almost \$6.5 million and improperly reprogrammed appropriated funds totaling more than \$400,000 (No. 99-I-356). A more recent audit of the Commonwealth Ports Authority's \$50 million project to upgrade the Saipan harbor facilities (which included \$23.5 million provided by

Internal Audit Capabilities

The position of Inspector General and the Bureau of Audit and Control were created by Virgin Islands public law. The position is filled by appointment (no specific qualification requirements other than training, character, and experience) by the Governor with confirmation by the Legislature. The term of office is 6 years and the individual may be reappointed for additional 6-year terms. Legislation passed by the Virgin Islands Legislature in December 1999 revised the law establishing the Bureau to create the Virgin Islands Office of Inspector General as an independent agency under the Executive Branch for administrative purposes. The amended legislation also gave the new organization investigative authority. The office is funded by annual General Fund appropriations and, as of February 2002, had a staff of 11 (the Inspector General and acting Deputy Inspector General, 1 legal counsel, 3 auditors, 2 investigators, 1 prosecutor¹, and 2 support staff), or a decrease of 4 employees since 1995. The office's budget also includes positions (currently vacant) for 2 audit managers, 4 auditors, 1 investigator, and 1 support staff. The Inspector General is in the process of trying to fill these vacant positions. The Virgin Islands Inspector General and the Virgin Islands Attorney General have formed a Government Fraud and Corruption Task Force to identify, investigate, and prosecute individuals involved in public corruption. The Task Force has identified and filed charges against several Government officials (including a former Governor, an acting Commissioner of Health, the director of an off-shore tourism office, and other Government employees) on various cases of fraudulent activities. Most of these individuals were required to make restitution as part of

¹The prosecutor is funded by and supports the Government Fraud and Corruption Task Force.

plea-bargain agreements with the Virgin Islands Attorney General and therefore were not formally prosecuted.

Audit Resolution Issues

The lack of adequate audit resolution and implementation of recommendations by the Government of the U.S. Virgin Islands contributed to the existence of long-standing financial management deficiencies. OIG's experience has been that, although the Government may implement recommendations that address the specific deficiencies and transactions noted in audit reports, it often does not implement recommendations that call for substantive, systemic changes in operating policies and procedures to ensure that similar problems do not occur in the future. As a result, our audit reports often disclose problems that are identical or at least similar to ones that had been disclosed by prior audit reports. For example:

- Reports issued in 1987 (No. V-TG-VIS-10-86), 1988 (No. 88-102), 1993 (No. 93-I-1382), and 1998 (No. 98-I-670) presented information regarding problems with the financial management system of the Government of the U.S. Virgin Islands that prevented the system from providing user agencies with accurate, current, complete, and reliable information on the status of their Federal grant and local appropriation accounts.

- Reports issued in 1985 (No. V-TG-VIS-11-84), 1990 (Nos. 90-80 and 90-103), 1997 (No. AC-03-36-97),² and 1998 (No. AC-01-36-98) presented information on ineffective billing and collection procedures at hospitals owned by the Government of the U.S. Virgin Islands that allowed hospital

Program Operations. To improve general program operations, the American Samoa Government should:

- Provide operating agencies with qualified staff, adequate training, and other resources necessary for them to carry out their legally mandated responsibilities efficiently and effectively.

- Establish a comprehensive building maintenance program that has the staff and resources necessary to provide ongoing repair and maintenance to all Government-owned facilities.

- Establish an effective governmentwide system to account for all Government-owned property, including real property and equipment.

- Ensure that the Office of Territorial Auditor has the staff, other resources, and organizational independence necessary to function effectively in assessing government operations and developing recommendations for improvement.

- Establish a comprehensive audit followup system that can (1) track the level of resolution and implementation of audit recommendations made by local, Federal, and independent auditors and (2) enforce implementation by operating agencies of recommendations with which the Government's chief executive concurs.

²Audit reports with numbers that begin with the letters "AC" were issued by the Virgin Islands Bureau of Audit and Control.

the loans are repaid and the proceeds are used as provided in the loan applications.

- Implement and enforce internal controls, including the providing of an adequate level of supervisory oversight, within all agencies that make collections on behalf of the Government.

Expenditure Control. To control expenditures and provide operating agencies with the resources necessary to carry out their operational responsibilities, the American Samoa Government should:

- Enforce the competitive procurement requirements contained in local laws and regulations and, where appropriate, in Federal grant management regulations.
- Ensure that the central procurement department and other authorized purchasing agencies fully document competitive procurement actions taken or provide justification as to why competitive procurement procedures were not used.
- Review and, where appropriate, revise existing procurement and vendor payment policies and procedures to ensure that agencies receive required goods and services and vendors are paid for such goods and services in a timely manner.
- Review and, where appropriate, revise space leasing policies and procedures to ensure that commercial space is not leased unless suitable Government-owned property is not available and, in such cases, that rental rates paid are commensurate with existing market conditions.
- Require that operating agencies control travel costs in accordance with existing travel regulations.

service charge receivables to increase from \$63.7 million in 1984 to \$174 million in 1997.

- Reports issued in 1984 (No. V-TG-VIS-08-84), 1990 (No. 90-67), 1994 (No. AC-02-30-94), and 1999 (No. 93-I-379) commented on ineffective collection procedures at the Virgin Islands Department of Finance that allowed real property tax receivables to increase from \$1.7 million in 1984 to \$15.4 million in 1998.

It is expected by Federal grantor agencies that the plan of action developed during the December 2001 conference (see the third paragraph under "Overall Financial Management") will correct some of the long-standing financial management, procurement and property management, and human resources management deficiencies which have plagued the Government.

Areas for Improvement

Based on the results of audits performed by OIG during the past 19 years (fiscal year 1983 to 2001), we believe that the Government of U.S. Virgin Islands should take the following actions in order to achieve greater levels of economy, efficiency, and effectiveness in its financial management and program operations. These general recommendations distill the essence of hundreds of specific recommendations made in almost 200 audit reports issued since October 1982. Some of these recommendations will require financial resources and technical expertise that may be beyond the current capacities of the Government of the U.S. Virgin Islands. In those cases, the Office of Insular Affairs and other Federal grantor agencies should be approached about the possibility of providing appropriate financial and/or technical assistance.

Financial Management. To meet the financial management requirements of generally accepted accounting principles, the Insular Areas Act of 1982, the Single Audit Act of 1984 as amended, Federal grant management requirements, and appropriate local laws and regulations, the Governments of the U.S. Virgin Islands should:

- Evaluate the capabilities of its existing financial management systems and the long-term financial management needs of policy-makers and program personnel, and implement appropriate upgrades of its financial management systems to provide the ability to (1) effectively handle the volume of users and financial transactions projected to exist over the next 10 years and (2) provide user agencies with timely and accurate information on the status of their accounts.

- Ensure that users of the financial management systems in all operating agencies receive ongoing training on the capabilities and use of the systems.

- Implement procedural changes necessary to allow (1) the central accounting department to produce comprehensive annual financial reports within 120 days of the end of each fiscal year, as required by the Insular Areas Act of 1982, and (2) the Government's independent auditors to perform and publish single audits on the Government's financial statements and Federal financial assistance within 9 months of the end of each fiscal year, as required by the Single Audit Act of 1984 as amended.

- Ensure that annual executive budgets are prepared and submitted for legislative consideration and approval within the deadlines specified in local laws.

- Enforce existing prohibitions against making or authorizing expenditures or obligations in excess of the amount of any appropriation or allotment.

- Establish a governmentwide clearinghouse for information on Federal grants, including single audit and indirect cost rate information.

- Ensure that grant managers in all Government agencies receive ongoing training on the requirements for administration of Federal grants, with special emphasis on (1) the cost principles and the type and level of documentation necessary to show that grant expenditures are in compliance with applicable requirements and (2) the common rules for grant administration especially as related to financial management and reporting, procurement, and property management requirements.

Revenue Enhancement. To improve its ability to generate and collect revenues, the American Samoa Government should:

- Computerize the tax administration functions and vigorously enforce the laws and regulations related to income taxes and existing local taxes to ensure that (1) potential taxpayers are identified and assessed taxes on a fair and equitable basis and (2) all taxes owed to the Government are properly accounted for and collected.

- Ensure that all agencies that generate accounts receivable have procedures to (1) maintain accurate and up-to-date records on the amounts owed to the Government and (2) aggressively enforce collection of such amounts.

- Ensure that the American Samoa Development Bank provides adequate analysis and control in issuing loans so that

Financial Management. To meet the financial management requirements of generally accepted accounting principles, the Insular Areas Act of 1982, the Single Audit Act of 1984 as amended, Federal grant management requirements, and appropriate local laws and regulations, the American Samoa Governments should:

- Evaluate the capabilities of its existing financial management systems and the long-term financial management needs of policy-makers and program personnel, and implement appropriate upgrades of its financial management systems to provide the ability to (1) effectively handle the volume of users and financial transactions projected to exist over the next 10 years and (2) provide user agencies with timely and accurate information on the status of their accounts.

- Ensure that users of the financial management systems in all operating agencies receive ongoing training on the capabilities and use of the systems.

- Implement procedural changes necessary to allow (1) the central accounting department to produce comprehensive annual financial reports within 120 days of the end of each fiscal year, as required by the Insular Areas Act of 1982, and (2) the Government's independent auditors to perform and publish single audits on the Government's financial statements and Federal financial assistance within 9 months of the end of each fiscal year, as required by the Single Audit Act of 1984 as amended.

- Ensure that annual executive budgets are prepared and submitted for legislative consideration and approval within the deadlines specified in local laws.

- Enforce existing prohibitions against making or authorizing expenditures or obligations in excess of the amount of any appropriation or allotment.

- Establish a governmentwide clearinghouse for information on Federal grants, including single audit and indirect cost rate information.

- Ensure that grant managers in all Government agencies receive ongoing training on the requirements for administration of Federal grants, with special emphasis on (1) the cost principles and the type and level of documentation necessary to show that grant expenditures are in compliance with applicable requirements and (2) the common rules for grant administration especially as related to financial management and reporting, procurement, and property management requirements.

Revenue Enhancement. To improve its ability to generate and collect revenues, the Government of the U.S. Virgin Islands should:

- Computerize the tax administration functions and vigorously enforce the laws and regulations related to income taxes and existing local taxes to ensure that (1) potential taxpayers are identified and assessed taxes on a fair and equitable basis and (2) all taxes owed to the Government are properly accounted for and collected.

- Ensure that all agencies that generate accounts receivable have procedures to (1) maintain accurate and up-to-date records on the amounts owed to the Government and (2) aggressively enforce collection of such amounts.

- Implement and enforce internal controls, including the providing of an adequate level of supervisory oversight,

within all agencies that make collections on behalf of the Government.

- Review and, where appropriate, revise economic development laws to ensure that (1) tax exemptions and/or rebates are provided only to industries and firms that would not otherwise establish in the U.S. Virgin Islands without such incentives, (2) cost-benefit analyses are performed on a periodic basis to ensure that the benefits of economic development programs are commensurate with the tax revenues foregone, (3) economic development beneficiaries comply with employment and other requirements intended to provide economic benefits to the U.S. Virgin Islands economy, and (4) economic development loans are granted only to businesses that will enhance economic growth and have a reasonable financial ability to repay the loans.

- Ensure that all agencies that rent Government-owned property to private entities charge rental rates that are commensurate with market conditions and enforce collection of lease rental receivables.

Expenditure Control. To control expenditures and provide operating agencies with the resources necessary to carry out their operational responsibilities, the Government of the U.S. Virgin Islands should:

- Enforce the competitive procurement requirements contained in local laws and regulations and, where appropriate, in Federal grant management regulations.

- Ensure that the central procurement department and other authorized purchasing agencies fully document competitive procurement actions taken or provide justification as to why competitive procurement procedures were not used.

result, our audit reports often disclose problems that are identical or at least similar to ones that had been disclosed by prior audit reports. For example:

- Reports issued in 1987 (No. S-TG-AMS-11-86), 1989 (No. 89-92), 1990 (No. 90-16), and 1994 (No. 94-I-651) concluded that the American Samoa Government did not follow established internal controls to prevent the obligation of funds in excess of appropriations, with the result that the Government's unreserved fund deficit increased from about \$2 million in 1988 to \$54 million in 1993.

- And reports issued in 1986 (No. S-TG-AMS-16-85), 1989 (No. S-TG-AMS-11-88), 1992 (GAO report), 1994 (No. 94-I-651), and 2002 (No. 2002-I-0003) concluded that the American Samoa Government was not effective in administering and collecting income taxes, which resulted in up to \$7 million in potential tax revenues not being collected.

Areas for Improvement

Based on the results of audits performed by OIG during the past 19 years (fiscal years 1983 to 2001), we believe that the American Samoa Government should take the following actions in order to achieve greater levels of economy, efficiency, and effectiveness in its financial management and program operations. These general recommendations distill the essence of hundreds of specific recommendations made in more than 60 audit reports issued since October 1982. Some of these recommendations will require financial resources and technical expertise that may be beyond the current capacities of some of the insular area governments. In those cases, the Office of Insular Affairs and other Federal grantor agencies should consider providing appropriate financial and/or technical assistance.

system of financial accounting and reporting was inadequate, (2) there were significant failures in the operation of computer systems, (3) there were significant weaknesses in the internal control structure related to general accounting and grant administration, and (4) there was a lack of appropriate management oversight, including a lack of review and approval of financial transactions. The single audit also reported Federal financial assistance of \$88.9 million (Interior - \$30.6 million) with questioned costs of \$4.4 million (Interior - \$500,000). The financial statements indicated that the General Fund had an accumulated deficit of \$31.4 million as of September 30, 1996.

Internal Audit Capabilities

The Office of Territorial Auditor was established by American Samoa public law. The position is filled by appointment (the candidate must be either a Certified Public Accountant or a Certified Internal Auditor) by the Governor with confirmation by both the Senate and the House. The term of office is 4 years and may be renewed. The office is funded by annual General Fund appropriations and, as of March 2001, had a staff of 4 (the acting Territorial Auditor, 2 auditors, and 1 support staff), or a decrease of 2 employees since 1998. The position of Territorial Auditor has been vacant since late 1998.

Audit Resolution Issues

The lack of adequate audit resolution and implementation of recommendations by the American Samoa Government contributed to the existence of long-standing financial management deficiencies. As in Guam, OIG's experience has been that the Government has had a very poor track record in implementing recommendations that call for substantive, systemic changes in operating policies and procedures. As a

- Review and, where appropriate, revise existing procurement and vendor payment policies and procedures to ensure that agencies receive required goods and services and vendors are paid for such goods and services in a timely manner.

- Review and, where appropriate, revise space leasing policies and procedures to ensure that commercial space is not leased unless suitable Government-owned property is not available and, in such cases, that rental rates paid are commensurate with existing market conditions.

- Require that operating agencies control travel costs in accordance with existing travel regulations.

Program Operations. To improve general program operations, the Government of the U.S. Virgin Islands should:

- Provide operating agencies with qualified staff, adequate training, and other resources necessary for them to carry out their legally mandated responsibilities efficiently and effectively.

- Review and, where appropriate, revise existing personnel policies and procedures to (1) consolidate multiple pay schedules, (2) streamline the personnel recruitment process, and (3) ensure that career service positions are not filled by political appointments that destroy the credibility of the personnel merit system.

- Establish a comprehensive building maintenance program that has the staff and resources necessary to provide ongoing repair and maintenance to all Government-owned facilities.

- Establish an effective governmentwide system to account for all Government-owned property, including real property and equipment.

- Ensure that the Office of Virgin Islands Inspector General has the staff, other resources, and organizational independence necessary to function effectively in assessing government operations and developing recommendations for improvement.

- Establish a comprehensive audit followup system that can (1) track the level of resolution and implementation of audit recommendations made by local, Federal, and independent auditors and (2) enforce implementation by operating agencies of recommendations with which the Government's chief executive concurs.

American Samoa

Overall Financial Management

The American Samoa Government continues to face financial management problems and receive operating subsidies of about \$23 million annually through Interior's Office of Insular Affairs. Even with these operating subsidies, the Government has had operating deficits in recent fiscal years. Primary among the causes of the recurring operating deficits is the inability or unwillingness of the American Samoa Government to control expenditures and collect all tax revenues due. For example, OIG audit reports issued in fiscal years 1998 and 2002 disclosed that (1) a legislative renovation project was allowed to expand from a \$78,000 roof repair project to a comprehensive \$1 million building renovation project without proper planning, construction oversight, or use of competitive procurement (No. 98-I-653) and (2) the American Samoa Tax Office was not effective in the administration and collection of income taxes (No. 2002-I-003). With regard to tax collections, we found that the Tax Office lost potential tax revenues of at least \$7.1 million because it did not have procedures to identify and pursue income tax nonfilers; did not have an effective system for selecting tax returns for audit; did not complete tax audits before expiration of the statute of limitations; did not take prompt action to collect identified delinquent taxes; did not adequately justify the abatement of taxes, penalties, and interest; and did not ensure that a new automated income tax system functioned properly. Similar problems had been disclosed by OIG, GAO, and the American Samoa Territorial Auditor in at least five reports issued since 1986.

The most recent published single audit report is for fiscal year 1996, and it included a disclaimer of opinion because (1) the