U.S. Department of the Interior
Office of Inspector General

American Samoa Government Building, Pago Pago

American Samoa: Top Leadership Commitment Needed to Break the Cycle of Fiscal Crisis

Report No. P-IN-AMS-0117-2003 September 2005

United States Department of the Interior

Office of Inspector General
Western Region
Federal Building
2800 Cottage Way, Suite E-2712
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7430
September 19, 2005

Mr. David B. Cohen
Deputy Assistant Secretary
for Insular Affairs
Office of Insular Affairs
U.S. Department of the Interior
1849 C Street, NW
Washington, D.C. 20240

Honorable Togiola T.A. Tulafono
Governor
American Samoa Government
Pago Pago, American Samoa 96799

Dear Deputy Assistant Secretary Cohen and Governor Togiola:

The enclosed report *American Samoa: Top Leadership Commitment Needed to Break the Cycle of Fiscal Crisis,* Report No. P-IN-AMS-0117-2003, presents the results of our audit of the American Samoa Government's 2001 Fiscal Reform Plan. Our audit objective was to determine whether the American Samoa Government (ASG) implemented the 2001 Reform Plan and related agreements. Our scope and methodology are detailed in Appendix 1 of the report.

Based on the July 12, 2005 response from the Deputy Assistant Secretary for Insular Affairs, we consider recommendations to the Office of Insular Affairs (OIA) to be resolved and implemented. The response stated that OIA had recently designated ASG as a "high-risk" grantee under 43 CFR 12.52, was aggressively monitoring the progress of the reform plan, and had increased reporting requirements and restricted access to funds. OIA also is developing a plan that identifies the actions ASG must complete to remove the high-risk designation. The April 22, 2005 response from the Governor of American Samoa, however, disagreed with our recommendations and concluded, "This ASG has already accomplished Fiscal Reform, and has taken the steps recommended in this audit." We noted that this conclusion was counter to the Deputy Assistant Secretary's actions and his June 9, 2005 letter to the Governor specifying the conditions ASG must meet to remove the high-risk designation. Despite OIA taking decisive and aggressive actions to closely monitor and oversight ASG's progress in meeting the requirements of the Reform Plan and related agreements, we consider the recommendations addressed to the Governor to be unresolved and request a response to this report by October 21, 2005, that includes the information in Appendix 7.

The legislation, as amended, creating the Office of Inspector General requires semiannual reporting to Congress on all audit reports issued, actions taken to implement audit recommendations, and recommendations that have not been implemented. Accordingly, this report will be included in our next semiannual report.

We appreciate the cooperation shown by the ASG and OIA during our audit. If you have any questions regarding this report, please call me at (916) 978-5653.

Sincerely,

Michael P. Colombo
Regional Audit Manager

Enclosure

cc: Nikolao Pula, Director, Office of Insular Affairs
Keith Parsky, Audit Liaison Officer, Office of Insular Affairs

Executive Summary

American Samoa Fiscal Reform

Top Leadership Commitment and Adoption of Comprehensive Long-Range Plan Needed to Break the Cycle of Fiscal Crisis

For the past two decades, the ASG has faced significant financial crises, which have yet to be corrected by a series of fiscal reform efforts. ASG has not controlled expenditures, produced timely and accurate financial reports, or taken effective corrective actions on deficiencies identified by the Office of Inspector General (OIG), the Government Accountability Office (GAO), and independent public accountants. The most recent reform was the Interim Fiscal Year 2001 Reform Plan (2001 Reform Plan). However, without the commitment of top management in the ASG and the Department of the Interior's OIA and the adoption of best practices that are critical to the success of any financial reform, the plan will be the latest in this series of failed efforts.

The 2001 Reform Plan included only goals designed to eliminate a deficit in the short run and did not address long-term reform that would lead to lasting financial stability. However, long-term reform was addressed in the 1995 Immediate Term Financial Recovery Plan (1995 Recovery Plan), developed by OIA and ASG. This plan recognized that permanent fiscal recovery was based on a balanced budget that included all ASG entities and on a framework for long-term public sector reform, private sector development, and overall economic growth. The 1995 Recovery Plan advocated aggressive revenue enhancement and cost-cutting measures, while exploring options for restructured current operations, privatization, expanded economic development, and direct foreign investment. However, ASG failed to fully implement the 1995 Recovery Plan, and its fiscal situation continues to deteriorate. We believe that developing a comprehensive and long-range reform plan, using the 1995 Recovery Plan as a framework, is the essential first step toward true fiscal reform in American Samoa.

Successful implementation of any fiscal reform plan, however, depends on the commitment of OIA and ASG management to drive the transformation to achieve fiscal self-sufficiency. In a July 2003 report, GAO outlined key practices and steps that are essential to the success of any organization in transforming business cultures and practices. These key practices include a transformation process driven by top management, an implementation team dedicated to managing the transformation, implementation goals and timelines to build momentum and show progress from day one, and a communication strategy to create shared expectations and report progress to key stakeholders.

We believe that without an immediate course correction that embodies these key practices, the 2001 Reform Plan will fail to break ASG's cycle of fiscal crisis. Our recommendations focus on the need for (1) an active partnership between OIA and ASG to develop a comprehensive fiscal reform plan and adopt successful key practices and steps in achieving fiscal accountability and stability and (2) OIA to coordinate with other agencies providing federal financial assistance to resolve cross-cutting management control deficiencies and hold ASG accountable if agreed upon fiscal reform goals and milestones are not met.

Contents

Abbreviations

Art.	Article
ASG	American Samoa Government
CAFR	Comprehensive Annual Financial Report
CFR	Code of Federal Regulations
DM	Departmental Manual
DOI	Department of the Interior
Exec. Order	Executive Order
Fed. Reg.	Federal Register
FY	Fiscal Year
GAO	Government Accountability Office (United States)
Medical Center	American Samoa Medical Center Authority – Lyndon B. Johnson Tropical Medical Center
MOA	Memorandum of Agreement
MOU	Memorandum of Understanding
1995 Recovery Plan	Immediate Term Financial Recovery Plan Issued 1995
OIA	Office of Insular Affairs, Department of the Interior
OIG	Office of Inspector General, Department of the Interior
OMB	Office of Management and Budget
TOFR	Territorial Office of Fiscal Reform (ASG)
2001 Reform Plan	Interim Reform Plan for Fiscal Year 2001
U.S.	United States
U.S.C.	United States Code

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American Samoa: A History of Fiscal Crisis

American Samoa is a U.S. territory in the South Pacific Ocean about 2,300 miles southwest of Hawaii. Comprising a group of principally five volcanic islands and two coral atolls, the island area is about 76 square miles, with a population of about 58,000 people. OIA is responsible for carrying out the Secretary of the Interior's responsibilities in U.S.-affiliated insular areas. OIA's strategies to accomplish economic self-sufficiency for the insular areas center on improving insular government financial management practices and increasing both economic development and federal responsiveness to the unique needs of island communities striving for self-sufficiency.

In recent years, U.S. Congressional and OIA concerns about American Samoa have focused on its fiscal situation, which cannot be improved without American Samoa overcoming significant obstacles. First, opportunities for expanded economic development are restrained by American Samoa's remote location, limited transportation, and devastating hurricanes. American Samoa's primary industry is tuna fishing and processing. Two tuna canneries and the associated retail and service enterprises employ about two-thirds of the work force. The remaining one-third is employed by ASG. Tourism is developing, but has not yet become a major industry that significantly contributes to the economy.

Second, American Samoa does not generate sufficient local revenues to fund its general government operations. To help make up its annual revenue shortfall, ASG depends on grants from the United States, including an operations grant administered by OIA. In fiscal year 2003, this grant totaled about \$23 million: \$15.2 million to the primary government and \$7.7 million to the American Samoa Medical Center Authority – Lyndon B. Johnson Tropical Medical Center, the only healthcare center available in American Samoa.

A third and critical obstacle to American Samoa's financial well being is an ineffectual financial management system. The system's deficiencies are significant and longstanding and have been well documented by our office, GAO,[1] and independent

[1] See Appendix 1, pages 17 and 18, for a discussion of OIG and GAO audits.

public accountants. The deficiencies center primarily on ASG's failure to make the following improvements:

- Reduce budget deficits through increased revenue collections and controlled expenditures,

- Generate timely and accurate financial reports that can be used to make informed decisions, and

- Correct significant internal control weaknesses that increase the risk of fraud, waste, and mismanagement.

ASG's inability to correct these deficiencies has resulted in continued general fund deficits, which have contributed to the government's cycle of fiscal crises. From 1980 to 1991, ASG operated at a deficit in its general fund for all but two fiscal years. As shown in Figure 1, this trend continued through the 1990s, with general fund deficits occurring from 1994 to 2001.

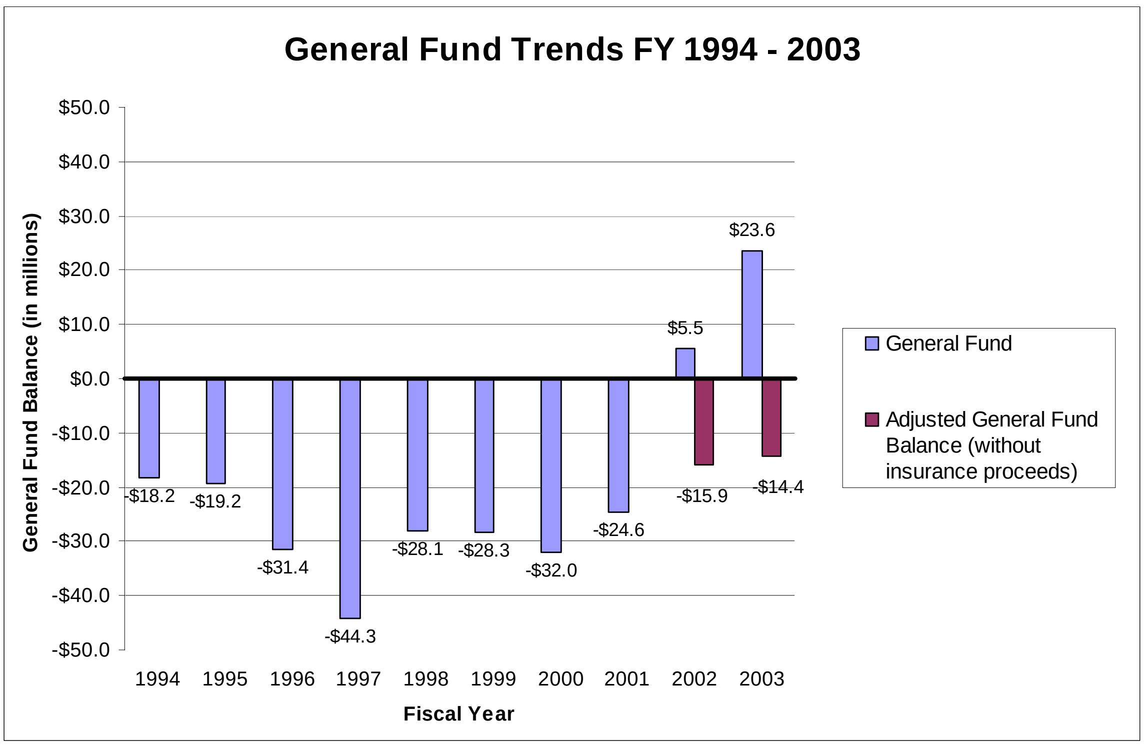

Figure 1

Although ASG recorded general fund surpluses in fiscal years 2002 and 2003, it is important to note that the surpluses were due to $38 million[2] in long-awaited insurance settlement proceeds for hurricane damage that occurred in 1991. Without these proceeds, ASG would have reported a general fund deficit of about $15.9 million and $14.4 million in fiscal years 2002 and 2003, respectively.

Over the years, OIA has worked with ASG in attempting numerous fiscal reform efforts. None of these efforts have succeeded. Progress has been hindered because top OIA and ASG leaders have not fully committed to correcting the longstanding deficiencies in ASG's financial management system. As a result, ASG operates in a constant state of fiscal crisis and moves from one failed fiscal reform effort to another. The chronology of failed fiscal reform efforts since 1988 is described in Appendix 2.

ASG's latest fiscal reform effort, the 2001 Reform Plan, was precipitated by ASG's inability to pay outstanding debts, thereby initiating another round of reform. In 1999, Congress responded to ASG's financial distress by authorizing an $18.6 million loan ($14.3 million to liquidate outstanding debt and $4.3 million for fiscal reform). As conditions of the loan, ASG took the following actions:

- Agreed to pay off the $18.6 million loan with proceeds from the Master Settlement Agreement[3] and signed a Memorandum of Understanding (MOU) with the Secretary of the Interior in November 2000. The MOU described procedures ASG must follow in discharging its debts and implementing fiscal reforms.

- Developed the 2001 Reform Plan and signed a Memorandum of Agreement (MOA) with the Deputy Assistant Secretary of the Interior for Insular Affairs in August 2002 to implement the plan. Under the MOU and MOA, release of the $18.6 million loan was contingent on ASG's taking the following actions:

    - Liquidating the outstanding debt of $14.3 million.

[2] ASG received the $38 million in two installments: $21.4 million in fiscal year 2002 and $16.4 million in fiscal year 2003.

[3] In November 1998, four of the nation's largest tobacco companies negotiated and signed an agreement, known as the Master Settlement Agreement, with the attorneys general of 46 states, the District of Columbia, and 5 U.S. territories. Under the agreement, the tobacco companies make annual payments in perpetuity as reimbursement for health care costs related to tobacco use. ASG assigned these payments to the Department of the Interior.

- Instituting a series of revenue enhancements, expenditure savings measures, and collection improvements, beginning in fiscal year 2001 and continuing in fiscal year 2002, to yield a balanced budget for fiscal year 2003 and beyond.

- Enacting fiscal reform policies and procedures to develop realistic and adequate budgets and respond to revenue shortfalls or budget overruns in a timely and responsible manner.

- Completing all audits required by the Single Audit Act of 1984.

We conducted our audit from October 2003 to September 2004 to determine whether ASG actually implemented the 2001 Reform Plan. The scope and methodology of our audit are detailed in Appendix 1. It should be noted that in September 2003, ASG submitted revisions to the 2001 Reform Plan. OIA did not accept these revisions because they did not include baseline financial data, explanations for changes from the approved 2001 Reform Plan, or timetables for completing fiscal reforms. OIA did accept revisions submitted in July 2004, which compared projected and actual revenues, included expenditure and collection improvements, and provided an action plan and milestones for fiscal reform activities.

Results of Audit:

Top Management Commitment and Comprehensive Plan Needed to Realize True Fiscal Reform

The 2001 Reform Plan was designed primarily to solve ASG's short-term fiscal crisis and noticeably lacked two components essential to correcting long-standing financial management deficiencies and creating lasting fiscal reform. The first component is a comprehensive plan that addresses the correction of long-standing financial deficiencies and encompasses the full range of ASG operations. No matter how well designed, however, such planning will not succeed without the second component; that is, the commitment of top management in both OIA and ASG to achieving long-term fiscal solvency for American Samoa and its citizens. A strong, dedicated, and active partnership between OIA and ASG will ultimately be the requisite factor in breaking the cycle of fiscal crisis and failed reforms.

Comprehensive Planning

The 2001 Reform Plan addressed only short-term goals and did not include the full range of government operations. The plan, for example, did not require participation and coordination from key ASG officials, such as those in the Treasury, Tax, and Procurement Offices, and the Medical Center. As shown in the following examples, inclusion of the Medical Center and the Treasury Office was essential to long-term fiscal reform.

- The fiscal condition of the Medical Center is directly tied to the overall financial health of ASG. For the past 6 years, the Medical Center has experienced an average operating loss of $2.2 million a year, despite an annual Departmental operating grant of $7.7 million. Consequently, by February 2004, the financial condition of the Medical Center had deteriorated to the point that ASG itself provided a $5 million bailout loan and required the Medical Center to develop and submit a fiscal reform plan.

- The 2001 Plan actually omitted ongoing and planned fiscal reforms within the Treasury Office to facilitate reliable and timely financial reporting. These planned reforms included major upgrades to the financial management information system, development of new standard operating procedures, and re-assessment of Treasury staff levels.

We believe that developing a comprehensive fiscal reform plan, using the 1995 Recovery Plan as a framework, is the essential first step toward true fiscal reform. As differentiated from the 2001 Reform Plan, the 1995 Recovery Plan focused on short- **and** long-term fiscal reforms for the **entire** government, including the Medical Center, by (1) balancing the budget in the immediate term while simultaneously establishing a framework for long-term public-sector reform, private-sector development, and overall economic growth; (2) ensuring that revenues collected for services were consistent with the cost of providing those services over time; (3) outlining long-term, aggressive revenue-enhancing and cost-saving measures; (4) outsourcing activities best handled outside the government; and (5) recommending options for restructuring current operations, as well as opportunities for privatization, economic development, and direct foreign investment.

During the course of our audit, we briefed top ASG officials, the Director of OIA, and members of the Director's staff on the results of our audit. ASG initiated corrective actions by submitting an action plan to OIA. The action plan included planned and ongoing fiscal reforms for the entire ASG operations, including the American Samoa Power Authority and the Medical Center and also incorporated elements from the 1995 Recovery Plan, such as reducing payroll, increasing hospital and user fees, and outsourcing functions. The action plan, however, did not include clear benchmarks for measuring financial performance. In addressing reduced payroll, for example, the action plan simply stated, "review in detail many of the government offices to determine whether they can be reduced in size." Continued efforts are therefore needed by OIA and ASG to develop a comprehensive fiscal reform plan with clear financial benchmarks and details.

Commitment of Key OIA and ASG Managers

Development of a comprehensive fiscal reform plan alone will not ensure success. Successful implementation of fiscal reform ultimately depends on the commitment and participation of key OIA and ASG managers to drive the transformation of achieving fiscal self-sufficiency. To ensure true reform and break the cycle of fiscal crisis, OIA and ASG should apply the key practices outlined by GAO in its July 2003 report[4].

At a minimum, these practices should include the following:

- The Deputy Assistant Secretary for Insular Affairs and the Governor of the American Samoa Government must drive the transformation.

- A dedicated, high-performing implementation team should manage the transformation process.

- A performance management system should be used to define responsibility and assure accountability for change.

- The implementation plan should include goals, timelines, and regular progress reports.

- A communications strategy should be developed to report progress to key stakeholders and employees.

GAO identified its key practices by looking at a variety of organizations that had undergone major change and successfully transformed their business cultures and practices. (See Appendix 3 for the full text of these practices.)

Implementation of such a comprehensive fiscal reform plan would span several years and require considerable effort, commitment, and resources. However, application of these key practices is essential to ensure transparency, accountability, integrity, and continuity in bridging political changes over the years. We compared four key practices with OIA and ASG's performance and found that these practices were not applied in developing and implementing the 2001 Reform Plan (see Table 1).

[4] GAO: *Results-Oriented Cultures – Implementation Steps to Assist Mergers and Organizational Transformations*, GAO-03-669, July 2003.

Table 1 Comparison of Selected GAO Key Practices and OIA/ASG Performance	
GAO Key Practice	**OIA/ASG Performance**
Ensure top leadership drives the transformation.	OIA and ASG top leadership did not drive the fiscal reform process. Top leaders must articulate a succinct and compelling reason for change, demonstrate conviction for the change, and report on early successes. The manager of ASG's Territorial Office of Fiscal Reform (TOFR) was responsible for developing and managing the fiscal reform process. OIA top management officials were not actively involved in the fiscal reform process.
Dedicate an implementation team to manage the process.	OIA and ASG did not establish a dedicated high-performing implementation team to manage the implementation process. The "team" consisted of the manager of TOFR, who managed the process only on a part-time basis because he was assigned other responsibilities within ASG. OIA staff was not an integral part of the implementation team and participated on an ad hoc basis because they were assigned other responsibilities within OIA.
Set implementation goals and a timeline to build momentum and show progress from day one. Goals and timelines are essential because the process could take years to complete.	OIA and ASG did not develop a comprehensive implementation plan that included all short- and long-term goals for ASG and component units and a timeline for accomplishing the goals.
Establish a communication strategy to create shared expectations and report related progress.	OIA and ASG did not make public the final reform goals or report related progress to key stakeholders, such as ASG senior officials and employees, American Samoa citizens, Department of the Interior senior officials, and Congress.

The failure to apply these key, or similar, practices to ensure a hands-on commitment to fiscal reform has resulted in the failure of all previous reform efforts (see Appendix 2). With regard to the 1995 Recovery Plan, OIA stated in its fiscal year 2004 budget justification that after the November 1996 gubernatorial election in American Samoa, a new Governor took office and pledged to take the necessary steps to return the government to fiscal health and stability. That pledge was never carried out, however, and ASG's financial situation remains poor. Thus, we believe that ASG's failure to fully achieve the goals of the 2001 Reform Plan is witness to the necessity of a committed, hands-on approach by top OIA and ASG leaders.

Key Shortcomings in Implementing 2001 Reform Plan

The 2001 Reform Plan set only short-term goals to address ASG's immediate fiscal crisis. In addition to providing for the immediate liquidation of ASG debts that were outstanding as of April 1999, its goals included enhancing revenue and controlling expenditures to balance the budget and completing seriously delinquent financial statements by fiscal year 2003. Although ASG liquidated its outstanding debt with the $14.3 million[5] in debt relief provided by Congress and reported a balanced budget for 2003, it did not meet expenditure targets, enact procedures for developing realistic budgets, or meet deadlines for financial statements or single audit reports.

Expenditure Targets and Budget Overruns

The 2001 Reform Plan projected a $12 million savings for fiscal year 2003 through a combination of $10.9 million in enhanced revenues and $1.1 million in reduced expenditures. According to ASG's unaudited general fund revenue and expenditure report, ASG met revenue targets but did not control expenditures, which in fiscal year 2003 were $5.7 million more than in fiscal year 2001. Fiscal year 2004 expenditures were expected to be $9.2 million more than those for fiscal year 2001.

Expenditures increased, in part, because ASG continued its practice of not developing realistic budgets and not enforcing the budgetary controls stipulated in ASG law, which prohibits expenditures beyond funds appropriated or allotted to government departments. As shown on Table 2, expenditures of governmental departments from fiscal years 1998 through 2003 exceeded appropriations by $25.1 million.

[5] As of December 2001, ASG's TOFR had drawn down the entire $14.3 million designated by Congress for debt liquidation. TOFR developed alternative procedures to validate the debt prior to payment because ASG's accounting records were unreliable. The ASG independent certified public accountant had disclaimed an opinion on the fiscal year 1998, 1999, and 2000 general purpose financial statements because of significant internal control failures related to (1) preventing or detecting misstatements of accounting information, (2) the lack of review and approval of transactions, and (3) inadequate management oversight. We reviewed TOFR's procedures and determined they were adequate.

Table 2 Expenditures Exceeding Appropriations		
Fiscal Year	**No. of Departments**	**Budget Overruns (millions)**
1998	35	$ 8.6
1999	28	3.7
2000	27	2.6
2001	26	5.1
2002	15	1.1
2003	22	4.0
Total		$25.1

Source: ASG's (1) Comprehensive Annual Financial Report (CAFR) for fiscal years 1998, 1999, and 2000, issued February 2004; (2) CAFR for fiscal year 2001, issued June 2004; and (3) quarterly reports for 2002 and 2003

A primary goal of the revenue enhancements and expenditure saving measures was to balance the budget and eliminate the general fund deficit, which has been a continuing problem (see Figure 1). Although ASG ostensibly achieved this goal in fiscal year 2003 by reporting a $23.6 million surplus, the surplus was the result of $38 million in hurricane insurance settlements received in fiscal years 2002 and 2003 for damages incurred in 1991. Without these settlements, ASG would have reported a continuing general fund deficit of about $15.9 million and $14.4 million in fiscal years 2002 and 2003, respectively.

CAFRs and Single Audit Reports

ASG also did not complete its CAFRs and single audit reports for fiscal years 2002 and 2003, and the CAFRs and single audits completed for fiscal years 1998 through 2000 were issued with disclaimed opinions because of significant findings, questioned costs, and internal control failures. Although the requirements[6] for completing the requisite reports are incorporated in the annual ASG operations grant, OIA has not enforced them, with the result that ASG has not complied with these requirements for several years. As shown in Table 3, ASG failed to meet any of the deadlines agreed to in the 2001 Reform Plan.

[6] Under the Single Audit Act of 1984, as amended, entities expending $300,000 or more annually in federal awards must complete a single audit within 9 months of fiscal year end. Under the Omnibus Territories Act of 1982, the Governor of American Samoa is required to produce the CAFR within 4 months of fiscal year end.

Table 3 Submission of CAFRs and Single Audit Reports (as of September 2004)				
Fiscal Year Ending September 30	**Due Date: CAFR/ Single Audit**	**Agreed-on Date in 2001 Reform Plan**	**Date Issued**	
			CAFR	**Single Audit**
1998	1/1999 6/1999	12/2002	2/2004	8/2003
1999	1/2000 6/2000	12/2002	2/2004	8/2003
2000	1/2001 6/2001	5/2003	2/2004	8/2003
2001	1/2002 6/2002	5/2003	6/2004	6/2004
2002	1/2003 6/2003	9/2003	Not Issued	Not Issued
2003	1/2004 6/2004	6/2004	Not Issued	Not Issued

The CAFR and single audit report completed for fiscal year 2001 were issued with a qualified opinion because the independent public accountants were unable to satisfy themselves as to the (1) accuracy of the beginning general fund balance; (2) amount of compensated absences, claims, and other liabilities; (3) amount due to and from other funds; (4) amounts due from other governments and advances from grantors; (5) physical existence and cost of fixed assets; (6) financial position and activity of the American Samoa Telecommunication Authority and Medical Center; and (7) amounts due from other governments and advances from grantors of the American Samoa Community College. Until these weaknesses are corrected, neither OIA nor ASG can ever ensure fiscal accountability and stability, and the likelihood of fraud, waste, and mismanagement will increase.

We also identified ASG's failure to meet the short-term goals of the 2001 Reform Plan in our March 2002 report *Management Challenges for Insular Area Governments – An Opportunity for Improvement*, OIG No. 2002-I-0017 (Appendix 1), which included recommendations that ASG enforce existing prohibitions against overspending, implement the procedural changes necessary to produce reliable and timely financial statements and single audit reports, and follow up on past audit recommendations to stabilize its financial system. Although ASG is currently revising the 2001 Reform Plan in concert with OIA, the chances of success for this revised plan are uncertain. What is certain is that the need for federal assistance to ASG will continue and that active OIA participation in financial governance is imperative to correct ASG's long-standing financial deficiencies.

OIA's Role

OIA has historically seen its role as providing technical assistance to and advising ASG. However, the history of failed fiscal reform efforts and ASG's failure to fully implement the 2001 Reform Plan point to the need for a new approach.

Based upon the authority set forth in 48 U.S.C §1661(c) and the delegation of responsibilities described in Executive Order 10264, which has been acknowledged in ensuing Secretary's Orders and Departmental Manual Provisions,[7] the Secretary continues to have full authority and ability to take a proactive role in the administration of American Samoa. The Samoan Constitution, approved by the Secretary in 1967, provides for an elected Governor who is given "general supervision and control of all executive departments, agencies and instrumentalities of the Government of American Samoa."[8] Even though the Secretary approved self-governance subject to Departmental oversight, the ultimate responsibility for civil, judicial, and military power in American Samoa remains with the President of the United States, acting through the Secretary, until Congress provides further for the civil government of American Samoa. Stated differently, with few exceptions, the Secretary has plenary

[7] All civil, judicial, and military power to govern the Territory of American Samoa is vested in the President of the United States "and shall be exercised in such manner as the President of the United States shall direct." *See* 48 U.S.C. §1661(c). Since 1951, the President has delegated his authority with regard to American Samoa to the Secretary of the Interior. *See* Exec. Order No. 10264, 16 Fed. Reg. 6417 (June 29, 1951): Secretary's Order No. 3009, §5, DOI (Sept. 13, 1977), *as amended by* Secretary's Order No. 3009, Amendment No. 1, DOI (Nov. 3, 1977) *and as further amended by* Secretary's Order No. 3009, Amendment No. 2, DOI (June 27, 1978); *see also* 575 DM 1.2(B) and 575 DM 3.3(B).
[8] American Samoa Constitution, art. IV, §7.

authority over most affairs in American Samoa, except where otherwise limited by statute[9] or Executive Order.[10]

OIA recently implemented an important initiative—the competitive allocation system—to improve fiscal performance in the insular areas. Under this system, OIA allocates $28 million in mandatory capital improvement funding to insular areas based on established competitive criteria that include demonstrated ability to (1) exercise prudent financial practices, (2) select and administer high priority projects, and (3) meet federal grant requirements. OIA also recently created the position of Accountability and Insular Policy Specialist to promote accountability for federal grants in the insular areas. We believe these kinds of initiatives, together with collaboration with other federal agencies and ASG, are the key to OIA fulfilling its responsibility to improve the financial management practices of ASG. OIA must assume leadership in coordinating efforts to correct single audit cross-cutting issues among federal agencies, such as the Departments of Agriculture, Education, Health and Human Services, Housing and Urban Development, Labor, and Transportation, which also provide financial assistance to ASG.

In a recent audit, GAO[11] cited the need for exactly this kind of improved coordination among federal agencies to ensure accountability over federal grants awarded to ASG. GAO concluded that while federal agencies relied on single audit reports to assess the accountability for funds awarded to ASG, they were slow to respond when ASG failed to complete these reports. GAO also noted that incidents of theft and fraud within ASG did not prompt agencies to increase their monitoring or their efforts to enforce the requirements of the Single Audit Act.

We identified the Department of Education, however, as one federal agency that did take action. In September 2003, the Department designated ASG a "high-risk grantee" under 34 CFR 80.12 because of major accountability problems stemming from ASG's inability to provide timely and complete single audits. The Department of Education imposed sanctions that included limiting draw downs to 50 percent of funds awarded until ASG submitted documentation to substantiate expenditures and

[9] The only governing matter which Congress has withdrawn from the Secretary is the ability to amend the Samoan Constitution. *See* (48 U.S.C. §1662a).
[10] For example, Exec. Order No. 8766, 6 Fed. Reg. 2741 (June 3, 1941) authorizes the Governor of American Samoa to regulate immigration in American Samoa.
[11] *American Samoa – Accountability for Key Federal Grants Needs Improvement* – GAO-05-51, December 2004.

progress on the grant and requiring ASG to submit detailed quarterly reports for Department of Education programs; certify and attest, under penalty of federal law, to the accuracy and completeness of the reports; and adopt transparent budgeting and expenditure reporting that was available to the general public.

Recommendations

We recommend that the Governor of American Samoa and Deputy Assistant Secretary, OIA:

1. Actively partner to develop a comprehensive fiscal reform plan using the 1995 Recovery Plan as the framework. The plan should include fiscal reforms for the entire government, with clear benchmarks for measuring performance, to ensure permanent financial stability.

2. Apply the best practices in Appendix 3 that have been identified as critical for implementing major change and transforming business cultures and practices.

We recommend that the Governor of American Samoa:

3. Ensure that the underlying financial system problems are corrected, including:

    a. Implementing procedural changes necessary to enable the Treasurer's office to produce timely CAFRs and single audits,

    b. Enforcing existing prohibitions against making or authorizing expenditures in excess of appropriations, and

    c. Establishing a comprehensive audit follow-up system and implementing agreed-upon recommendations.

We recommend that the Deputy Assistant Secretary for Insular Affairs:

4. Make greater use of existing authority as a means of ensuring that ASG strengthens management controls and practices and initiate appropriate and timely sanctions should ASG fail to meet agreed-on fiscal reform goals and milestones. These actions could include withholding grant monies, awarding grants with special protective conditions, and arranging for appropriate technical assistance.

5. Take the lead in coordinating efforts with other federal agencies that provide financial assistance to ASG to ensure accountability and resolve cross-cutting issues related to management controls.

OIA and Governor Responses and OIG's Reply

With respect to the recommendations addressed to OIA, the July 12, 2005 response from the Deputy Assistant Secretary for Insular Affairs (Appendix 4) was sufficient for us to consider recommendations 1, 2, 4, and 5 resolved and implemented. OIA's response agreed that top leadership commitment is necessary for the success of the partnership between the OIA and ASG to achieve fiscal reform and pledged continued commitment. The response stated that OIA is making considerable use of the tools available in order to keep the reform process moving forward and has recently designated ASG as a "high-risk" grantee under 43 CFR 12.52. The response also stated that OIA is aggressively monitoring the progress of the reform plan, has requested ASG to provide implementation steps for each measure that is not yet completed, increased reporting requirements, and restricted access to funds. In addition, OIA is determining if additional sanctions will help encourage completion of the actions necessary to remove the high-risk designation and bring ASG back into compliance with the MOA and fiscal reform plan. OIA is also developing a plan to identify the actions ASG must complete to remove the high-risk designation, which includes correction of the underlying financial system deficiencies. Further, OIA is coordinating closely with other federal agencies and expanding this coordination by convening a meeting of major federal grantors to discuss the administration of federal programs in American Samoa.

The April 22, 2005 response from the Governor of American Samoa (Appendix 5) disagreed with our recommendations and, in summary, stated:

> This ASG has already accomplished Fiscal Reform, and has taken the steps recommended in this audit... We continue to work to improve our services to the public and to improve our financial management. I, along with my entire administration, are committed to this goal.

The Governor's viewpoint, however, is counter to the Deputy Assistant Secretary's June 9, 2005 letter to the Governor (Appendix 6) that designated ASG as a "high-risk" grantee and determined that ASG was in not in compliance with the MOA and fiscal reform plan. The letter also specified the following conditions that ASG must meet to remove the high-risk designation:

- ASG shall have completed Single Audits by the statutory deadlines for the two most recent consecutive years, resulting in opinions that are not disclaimed and do not contain material qualifications.

- ASG shall have a balanced budget as confirmed by independent auditors for the two most recent consecutive years, without regard for nonrecurring windfalls, such as insurance settlements.

- ASG shall be in substantial compliance with the MOA and fiscal reform plan.

Therefore, despite OIA taking decisive and aggressive actions to closely monitor and oversight ASG's progress in meeting the requirements of the Reform Plan and related agreements, we are considering Recommendations 1, 2, and 3, addressed to the Governor, as unresolved. Appendix 7 describes the additional information that the Governor should provide in order to close out these recommendations. The status of all audit recommendations is shown in Appendix 7.

Appendix 1

Objective, Scope, Methodology, and Prior Audit Coverage

The objective of our audit was to determine whether ASG implemented the 2001 Reform Plan and related agreements. We conducted our audit from October 2003 to September 2004 in accordance with the *Government Auditing Standards*, issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances. To accomplish our objective, we:

- Evaluated the actions taken by OIA and ASG to develop and implement the 2001 Reform Plan.

- Obtained and reviewed the 2001 Reform Plan and related documents, financial and budgetary reports, internal and external audit reports, operations grant agreement, federal loan agreement, and other relevant documents.

- Interviewed officials from OIA Headquarters and ASG.

- Selected key performance standards from the 2001 Reform Plan and assessed ASG's progress in these areas, which included:

  - Completion of audited financial statements and single audits,

  - Implementation of revenue enhancing and cost-saving measures, and

  - Discharge of debts with federal loan proceeds.

- Reviewed GAO Report, *Results-Oriented Cultures – Implementation Steps to Assist Mergers and Organizational Transformations*, dated July 2003 (GAO-03-669) to identify best practices used by organizations that had successfully undergone major organizational change. We compared best practices identified by GAO with the practices used by ASG in developing and implementing its 2001 Reform Plan to identify practices ASG should adopt to ensure financial stability for the long term.

- Identified internal control weaknesses, which are discussed in the Results of Audit section of this report. Our recommendations, if implemented, should improve the internal controls in these areas.

- Reviewed the Department of the Interior's Report on Performance and Accountability for fiscal year 2003, including information required by the Federal Manager's Financial Integrity Act, and OIA's annual assurance statements on management controls. We found that OIA identified the need for insular area governments to increase self-sufficiency by improving financial management practices, increasing economic development, and increasing federal responsiveness to the unique needs of the island communities.

- Reviewed the following prior audit coverage related to or applicable to ASG:

  - June 2004, *Single Audit Report In Accordance with OMB Circular A-133 for FY 2001*. The independent public accountant issued a qualified opinion on ASG's financial statements and single audit for fiscal year 2001 because they were unable to satisfy themselves as to the following: (1) accuracy of the beginning general fund balance, (2) amount of compensated absences, claims, and other liabilities, (3) amounts due to/from other funds, (4) amounts due from other governments and advances from grantors, (5) physical existence and cost of fixed assets, (6) financial position and activity of the American Samoa Telecommunication Authority and Medical Center, and (7) amounts due from other governments and advances from grantors of the American Samoa Community College.

  - September 2003, *Report on Grants Administered by the Office of Insular Affairs* (OIG No. 2003-I-0071). The report focused on the need for OIA to improve monitoring of grants to Insular Area governments. The weaknesses in grant oversight contributed to project delays and waste of federal monies intended to improve Insular Area governments.

  - August 2003, *Single Audit Report In Accordance with OMB Circular A-133 for FYs 1998 to 2000*. The independent public accountant disclaimed an opinion on

ASG's financial statements and single audits for fiscal years 1998, 1999, and 2000. The disclaimer was issued as a result of significant findings, questioned costs, and deficiencies in the internal control structure.

- July 2003, *Results-Oriented Cultures: Implementation Steps to Assist Mergers and Organizational Transformations* (GAO-03-669). The report identified key practices that were consistently found at the center of successful organizational transformations.

- March 2002, *Management Challenges for Insular Area Governments – An Opportunity for Improvement* (OIG No. 2002-I-0017). The report identified ASG's financial management problems as a major management challenge and cited opportunities for improvement in financial management, revenue enhancement, expenditure control, and program operations.

- November 2001, *Assessment and Collection of Taxes* (OIG No. 2002-I-0003). The report stated that ASG was not effective in administering and collecting income taxes, which resulted in at least $7.1 million in potential tax revenues not being collected from fiscal years 1997 to 1999.

- April 1992, *Inadequate Management and Oversight Contribute to Financial Problems* (GAO/NSIAD-92-64). The report stated that ASG's financial condition had deteriorated rapidly from fiscal years 1986 to 1991, tax revenues were difficult to predict, collection efforts were inadequate, and poor financial management practices had resulted in excess expenditures. In addition, OIA had not enforced conditions of the operations grant.

We did not evaluate whether the $4.3 million authorized to implement fiscal reform was used appropriately because we considered OIA's coverage of this area to be sufficient. The MOA outlined authorized fiscal reform expenditures. We found that OIA reviewed supporting documents and concluded that ASG substantially used the $4.3 million as intended. ASG hired additional accounting staff, awarded a contract to an independent public accounting firm to perform financial statements and single audits, and upgraded the Treasury's financial systems. OIA is following up on some minor items that may not have been justified under the MOA.

Appendix 2

Chronology of ASG Fiscal Reform Efforts

Fiscal Reform Effort

1988

To address rising budget deficits, ASG developed, but failed to implement, a fiscal recovery plan. Result:

- Overruns of $4.7 million in fiscal year 1989 because of unbudgeted government pay raises and hiring.
- A deficit of $17.6 million by fiscal year 1990 (up from a deficit of about $500,000 in fiscal year 1987).

1990

ASG developed, but failed to implement, a fiscal recovery plan. The resulting deficit spending forced ASG to:

- Borrow $5 million from its Employees' Retirement Fund.
- Temporarily place government employees on a 36-hour workweek.
- Overdraw its checking account by about $1.6 million.

1995

ASG, as part of a Joint Working Group of OIA and contractor staff, developed a Recovery Plan, based on a 1992 GAO report of ASG's financial problems. The plan was not fully implemented because top management did not follow through. Result:

- ASG could not pay outstanding debts, including amounts owed to off-island medical providers.

In 1997, Congress authorized OIA to withhold $2 million in capital improvement funding until the plan had been substantially implemented. As of September 2004, OIA had not released the $2 million.

Appendix 3

GAO Key Practices and Implementation Steps

Practice	Implementation Step
Ensure top leadership drives the transformation	• Define and articulate a distinct and compelling reason for change • Balance continued delivery of services with transformation activities
Establish a coherent mission and integrated strategic goals to guide the transformation	• Adopt leading practices for results-oriented strategic planning and reporting
Focus on a key set of principles and priorities at the outset of the transformation	• Embed core values in every aspect of the organization to reinforce the new culture
Set implementation goals and a timeline to build momentum and show progress from day one	• Make public implementation goals and timeline • Seek and monitor employee attitudes and take appropriate follow-up actions • Attract and retain key talent
Dedicate an implementation team to manage the transformation process	• Establish networks to support implementation team • Select high-performing team members
Use the performance management system to define responsibility and ensure accountability for change	• Adopt leading practices to implement effective performance management systems with adequate safeguards
Establish a communication strategy to create shared expectations and report related progress	• Communicate early and often to build trust • Ensure consistency of message • Encourage two-way communication • Provide information to meet specific needs of employees
Involve employees to obtain their ideas and gain their ownership for the transformation	• Use employee teams • Involve employees in planning and sharing performance information • Incorporate employee feedback into new policies and procedures • Delegate authority to appropriate organizational levels
Build a world-class organization	• Adopt leading practices to build a world-class organization

Source: GAO - *Results-Oriented Cultures: Organizational Steps to Assist Mergers and Organizational Transformations*, GAO-03-669, July 2003

United States Department of the Interior
OFFICE OF INSULAR AFFAIRS
1849 C Street, NW
Washington, DC 20240

July 12, 2005

TAKE PRIDE IN AMERICA

Deputy Assistant Secretary

Michael P. Colombo
Regional Audit Manager
Office of Inspector General – Western Region
Federal Building
2800 Cottage Way, Suite E-2712
Sacramento, CA 95825

Subject: Office of Inspector General Draft Report No. P-IN-AMS-0117-2003 "American Samoa: Top Leadership Commitment Needed to Break the Cycle of Fiscal Crisis"

Dear Mr. Colombo:

Thank you for the opportunity to comment on the Office of Inspector General (OIG) Draft Report No. P-IN-AMS-0117-2003, "American Samoa: Top Leadership Commitment Needed to Break the Cycle of Fiscal Crisis" (Report).

We agree with the title's implication that "top leadership commitment" is necessary for the success of the partnership between the Office of Insular Affairs (OIA) and the American Samoa Government (ASG) to achieve fiscal reform in American Samoa. We believe that OIA has demonstrated such commitment, and agree that it is important that we continue to do so. Since I have held this position, it has been one of my top priorities – and hence one of the top priorities of OIA – to work with the ASG to ensure that its fiscal reform efforts are successful. In July 2002, a month after I took office, I traveled to American Samoa and personally negotiated with then Governor Tauese P. Sunia to conclude a fiscal reform agreement, culminating in the signing of the Memorandum of Agreement (MOA) on August 2, 2002.

The MOA attached and incorporated the "Interim Fiscal Reform Plan" (2001 Plan), which had been submitted to OIA by the ASG in 2001 and which the ASG had largely been implementing unilaterally since then. Prior to signing the MOA, I told Governor Tauese that while the 2001 Plan provided a good basis for moving forward with a fiscal reform partnership between the ASG and OIA, it should be updated as soon as possible to reflect any lessons learned from the ASG's efforts to implement the plan since 2001. Furthermore, since certain measures set forth in the 2001 Plan required approval of the Fono (legislature), it would be necessary to update the plan with substitute reform measures in the event that any of the 2001 Plan measures failed to receive the required approval.

In the months following the signing of the MOA, it became clear that certain aspects of the 2001 Plan had been overtaken by events and I pressed the ASG to propose an updated plan. I believed that it was important for the update to be proposed by the ASG, rather than OIA, because the fiscal priorities of the ASG should be determined by the elected representatives of the people of American Samoa. After a number of requests, I came to believe that the ASG was not being sufficiently responsive to my request to update the plan. Also, the ASG had failed to meet the deadline for certain deliverables under the MOA.

In February 2003, I sent a letter to the Governor informing him that OIA was preparing to withhold funds from the ASG's operating subsidy because the ASG was not in compliance with the MOA. I also encouraged the Governor to fill a longstanding vacancy in the ASG's public auditor position. Unfortunately, Governor Tauese passed away shortly thereafter. In respect of the tragic event and the resulting reorganization of the ASG, the succeeding Governor Togiola was given additional time to comply with the MOA. In September 2003, Governor Togiola submitted a revised fiscal reform plan. However, this plan did not meet with my satisfaction for a number of reasons. I traveled to American Samoa in December 2003 and met personally with Governor Togiola to discuss my concerns, which I subsequently memorialized in a letter to the Governor. Additional meetings were held with the Governor and his staff, and in May 2004 I hired an Accountability Policy Specialist to work with the ASG to report on the activities completed to date, develop an acceptable revised fiscal reform plan, and continue to monitor the new plan to its full implementation. An updated plan (2004 Plan) was submitted by the Governor in July 2004 and accepted by OIA shortly thereafter. This 2004 Plan includes fiscal reforms measures, both short-term and long-term, for critical areas of the government, and clearly identifies projected completion dates to allow OIA to measure progress. OIA is actively monitoring the ASG's progress. When deemed appropriate, OIA has imposed restrictions and taken corrective actions to promote the continued progress of the ASG, most notably by reductions in the level of OIA funding approved from both the Capital Improvement (Covenant fund) and Technical Assistance programs. In addition, an OIA review completed May 2005 concluded the ASG's progress on implementation of the remaining fiscal reform measures appears to have temporarily stalled, and this conclusion, along with other factors, resulted in OIA declaring the ASG a "high-risk" grantee in June 2005. The development of an action plan is currently underway to identify the process for removing the "high-risk" designation. In addition, OIA is planning to convene a meeting in August 2005 of representatives from all of the major Federal grantors to discuss ways to help improve the administration of Federal programs in American Samoa and the other U.S. territories and freely associated states. OIA will also withhold funds from the annual operational subsidy grant provided to the ASG if such action is deemed necessary to encourage the ASG to be more aggressive in completing the 2004 Plan.

The Report praises a plan that was prepared in 1995, known as the "Immediate Term Financial Recovery Plan for American Samoa" (1995 Recovery Plan). The 1995 Recovery Plan was adopted in 1996 by the then Governor of American Samoa. However, in 1997 the ASG had a change in administration, and the succeeding Governor essentially disavowed the 1995 Recovery Plan. Regardless of whether one believes that the decision to disavow the

1995 Recovery Plan was reasonable, one would have to conclude that this caused a significant delay in American Samoa's fiscal reform process.

The Report includes the following recommendations addressed to the Deputy Assistant Secretary for Insular Affairs, either alone or jointly with the Governor of American Samoa:

Recommendation 1. Actively partner to develop a comprehensive fiscal reform plan using the 1995 Recovery Plan as the framework. The plan should include fiscal reforms for the entire government, with clear benchmarks for measuring performance, to ensure permanent financial stability.

OIA Response:

The Report covers the period prior to time that the 2004 Plan went into effect. We believe that the 2004 Plan is a comprehensive fiscal reform plan that includes both short-term and long-term goals and encompasses the entire government. Therefore, it is not necessary to develop another plan. We agree that the 2001 Plan needed to be updated and, as previously described, insisted on having it updated.

We agree with OIG that the fiscal reform process should be driven by top leadership and, therefore, OIA has been monitoring the ASG's progress on the 2004 Plan very closely. Moreover, OIA believes the responsibility for fiscal reform rests with the ASG. The ASG had been progressing satisfactorily, although the most recently review completed by OIA in May 2005 determined that progress may have temporarily stalled. Due to the results of the review, OIA has requested the ASG to provide implementation steps for each measure that is not yet completed to help verify the progress of the entire process.

Recommendation 2. Apply the best practices in Appendix 3 that have been identified as critical for implementing major change and transforming business cultures and practices.

OIA Response:

The entire process that OIA and the ASG have followed is similar to that identified in Appendix 3. As previously detailed, 1) top leadership from both OIA and the ASG was involved in the preparation and finalization of the current 2004 Plan, 2) OIA is actively monitoring the ASG's progress and 3) there is constant communication between OIA and the ASG through correspondence, emails, telephone calls and on-site reviews which include attendance at meetings amongst ASG agencies. In light of these steps 1 through 3, and as previously discussed in this response, OIA does not agree with the Report's comments on page 8 that indicates there was, and continues to be, little to no active participation amongst agencies of the ASG, top leadership of the ASG and top leadership of OIA.

Recommendation 3 was addressed to ASG.

Recommendation 4. Make greater use of existing authority as a means of ensuring that ASG strengthens management controls and practices and initiate appropriate and timely sanctions *should ASG fail to meet agreed-on fiscal reform goals and milestones. These actions could include withholding grant monies, awarding grants with special protective conditions, and arranging for appropriate technical assistance.*

OIA Response:

OIA has already been making considerable use of the tools available to it in order to keep the fiscal reform process moving forward. OIA is aggressively monitoring the progress of the ASG and communicates on a weekly basis with officials of the ASG Treasury and the Territorial Office of Fiscal Reform. Increased reporting requirements and restricted access to funds are in place. In addition, on-site reviews are conducted to verify progress.

OIA is working to help strengthen the management controls and practices of the ASG. Under the OIA Technical Assistance Program, the ASG, along with the other territories and freely associated states, developed a "Financial Management Improvement Plan" to enhance internal controls and procedures of the general accounting offices. OIA funds training and workshops necessary to implement the plan and build capacity. In addition, OIA provides funding directly to the ASG to improve its financial management. In the past three years, this assistance has included:

- Experts to assist in the development of procedures, accounting data, financial statements and Single Audits ($408,000).
- Upgrades to the automated financial management system ($951,350).
- Training to build capacity ($319,000)
- Assistance to the Territorial Auditor's Office ($55,050)
- General workshops and conferences that benefit all of the territories and freely associated states ($1.6 million).

While OIA regularly provides positive support for capacity-building efforts that are necessary for fiscal reform, OIA will not hesitate to use other means available to it as appropriate. OIA has on a number of occasions informed the ASG that sanctions would be imposed if specific actions were not completed, and these matters are typically resolved in a satisfactory manner. OIA withheld $2 million of capital improvement funds from fiscal year 1997 until September 2004, when it determined that the ASG was in substantial compliance with the MOA and the 2004 Plan. Also, OIA has instituted a competitive procedure for awarding capital improvement funds according to a formula that rewards good fiscal management, among other things. In the two years that this new allocation system has been in effect, American Samoa has received less than its baseline allocation because of fiscal management issues.

OIA will continue to monitor the ASG's progress and, as necessary, impose authorized sanctions.

While we recognize that much remains to be accomplished in the ASG's fiscal reform process, and are deeply troubled by several recent reports that public funds have been misused, we believe that the ASG should be given credit for making progress.

The ASG successfully ended fiscal year 2002 with a surplus (audited), one year ahead of the required MOA deadline, and the ASG is reporting surpluses for both fiscal years ended 2003 and 2004. In addition, the ASG is in compliance with the agreed upon schedule for completion of delinquent single audits and expects to be in compliance with the Single Audit Act for fiscal year 2005.

The Report asserts that "ASG met revenue targets but did not control expenditures, which in fiscal year 2003 were $5.7 million more than in fiscal year 2001." We, too, would like to see greater progress in expenditure control. We would point out, however, that the ASG is reporting a General Fund operating surplus for fiscal year 2003, irrespective of any insurance proceeds. We would also point out that some of the increased expenditures were anticipated and have been used to bolster the fiscal reform effort. Examples include hiring contract accountants, an attorney and a systems analyst, and a government reorganization to create a Revenue Bureau to include the Tax Office, the Customs Office and the Credit and Collections Office.

Although the ASG has shown considerable progress in improving its financial management systems and procedures, OIA, for several reasons, recently declared the ASG to be a "high-risk" grantee. An action plan to identify the actions the ASG must complete to be removed from the "high-risk" designation is being developed. In addition, as previously discussed, OIA is determining if additional sanctions against the ASG will help encourage completion of the actions necessary to remove the "high-risk" designation and bring the ASG back into compliance with the MOA of 2002 and the 2004 Fiscal Reform Plan.

Recommendation 5. Take the lead in coordinating efforts with other federal agencies that provide financial assistance to ASG to ensure accountability and resolve cross-cutting issues related to management controls.

OIA Response:

OIA is already coordinating closely with other Federal agencies on a number of relevant issues, including the resolution of issues raised in ASG audits. I am planning to expand this coordination by convening a meeting of major Federal grantors to discuss the administration of Federal programs in American Samoa, and expand the agenda to include issues pertaining to each of the U.S. territories and freely associated states. During a recent conference of the Island Government Financial Officers Association (IGFOA), the members requested OIA's assistance to schedule a meeting with grant recipients and their Federal program coordinators to discuss outstanding issues. I am looking into coordinating such events as part of the Inter-governmental Group on Insular Areas (IGIA) and through conferences and training contracts funded by OIA.

Thank you for the opportunity to respond to this draft report. Please do not hesitate to contact me or Nikolao Pula, OIA Director, at (202)-208-4736 if you have any questions or need additional information.

Sincerely,

Nikolao Pula for

David B. Cohen

cc: Roy Kime, Audit Liaison Officer, OIG
Marina Tinitali, Audit Liaison Officer, OIA

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OFFICE OF THE GOVERNOR

PAGO PAGO, AMERICAN SAMOA 96799

TOGIOLA T.A. TULAFONO
GOVERNOR

AITOFELE T.F. SUNIA
LIEUTENANT GOVERNOR

TELEPHONE: (684) 633-4116
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April 22, 2005

Serial: 658

Mr. Michael P. Colombo, Regional Audit Manager
Office of Inspector General, Western Region
United States Department of the Interior
Federal Building
2800 Collage Way, Suite E-2712
Sacramento, CA 95825

Re: Draft OIG Audit Report No. P-IN-AMS-0117-2003, March 2005
"American Samoa: Top Leadership Commitment Needed to Break the Cycle of Fiscal Crisis"

Dear Mr. Colombo:

Thank you for the opportunity to respond to the captioned draft audit report. We disagree strongly with information provided in the report and the resultant conclusions.

The major conclusion of the report as stated in the Executive Summary, page ii, is that "We believe that without an immediate course correction that embodies these key practices, the 2001 Reform Plan will fail to break ASG's cycle of fiscal crisis."

Well, the results are in, and the cycle of fiscal crisis has been broken. In the baseline year of 2001, before Fiscal Reform, the ASG General Fund had an operating loss of ($9,340,161). In the year in which the Fiscal Reform Plan was implemented, FY 2002, the General Fund showed an operating surplus of $5,170,037. In FY 2003, there was an operating surplus estimated at $695,540. In FY 2004 there was an operating surplus estimated at $4,232,223.

These figures are all net of the property insurance settlements and the Tobacco Loan. The report makes erroneous and misleading statements at the bottom of page 2, that "it is important to note that the surpluses (in 2002 and 2003) were due to $38 million in long awaited insurance settlement proceeds for hurricane damage...". In fact, the operating surpluses were net of the insurance settlement and Tobacco Loan.

If we factor in these payments, the surpluses become quite large. However, these payments were used in 2001 and 2002 to reduce the accumulated deficits from prior years. The deficit General Fund fund balance in FY 1997 was ($44,321,880). At the end of 2001, the deficit had been reduced to ($24,158,374), thanks to the tobacco loan, the insurance settlement and other one-time adjustments (and in spite of continued operating deficits). The report seems to find the use of these payments to reduce the prior accumulated deficit to be somehow wrong (chart on page 2). In fact, this shows ASG's commitment to good financial management. The insurance settlements were first used to retire the old debts, rather than to spend the monies on new items and to ignore the old debts.

At the end of FY 2002, the General Fund fund balance was a positive $4,158,910.

The ASG has shown a balanced budget, as required by the Tobacco Loan covenants, in each of the last three years. The ASG eliminated the deficit fund balance in the General Fund in FY 2002. Our conclusion is that the ASG has achieved Fiscal Reform and has broken the cycle of fiscal crisis.

It is odd that the OIG audit report would recommend returning to the 1995 Immediate Term Financial Recovery Plan, which was in place for the years 1996 through 2001, without any noticeable impact. During these years, the ASG experienced continued operating loses in the General Fund.

The July 30, 2001 Interim Fiscal Reform Plan adopted some of the recommendations from the 1995 Plan, but included many more specific revenue enhancements, cost cutting measures and collection improvements. These were successfully achieved in 2002 and 2003. The Plan was then updated again in FY 2004.

Contrary to statements implied in the report, the 2001 Plan was based on a balanced budget and timely financial reporting as the two critical essentials for financial solvency in the long run. This is exactly what the OIG audit report recommends at the top of page 2. However, the report implies that the ASG Plan did not adopt these goals.

The report also implies a lack of commitment from the top leadership at DOI and ASG. Nothing could be further from the truth. The ASG created the Territorial Office of Fiscal Reform ("TOFR") to report directly to the Governor to manage the Fiscal Reform process. This office was given wide powers, and the TOFR manager even served one year as manager of the Revenue Branch of Treasury, including the Tax Office, the Customs Office and the Office of Credit and Collection. During this one year, FY 2002, revenues increased by over $18 million (net of insurance settlements, tax accruals and the tobacco loan).

As Governor, I receive monthly reports from the Treasury on the status of revenue collections. I meet with my top financial team of the Treasurer, Budget Director, TOFR Manager and Chief Counsel on at least a monthly basis to review the status of the budget as compared to actual expenditures and revenues. ASG submits quarterly reports to DOI OIA showing the status of the current year's financial condition.

OIA has appointed a new position in their office whose chief duties are to monitor the ASG Fiscal Reform program. If we do not meet our goals and maintain a balanced budget, OIA is authorized to withhold our operations grant.

Each year, our top financial managers meet with OIA officials in Washington D.C. to discuss fiscal reform and other financial issues.

In short, there is an ongoing commitment from ASG and OIA to maintain the success we have already achieved. We can not understand the draft report's findings that this commitment does not exist.

Recommendations:

1. "Actively partner to develop a comprehensive fiscal reform plan using the 1995 Recovery Plan as the framework. The plan should include fiscal reforms for the entire government, with clear benchmarks for measuring performance, to ensure permanent financial stability."

ASG Response: Why should we adopt an outdated and failed plan to replace the current plan that has had so much success? The 2001 Plan was updated in 2004. The current Plan has clear benchmarks for performance and is being monitored by the OIA.

2. "Apply the best practices in Appendix 3 that have been identified as critical for implementing major changes and transforming business cultures and practices."

ASG Response: We have already adopted and have used these practices as part of the successful Fiscal Reform Plan now in place.

3. "Ensure that the underlying financial system problems are corrected, including:

a. Implementing procedural changes necessary to enable the Treasurer's office to produce timely CAFR's and single audits,
b. Enforcing the existing prohibition against making or authorizing expenditures in excess of appropriations, and
c. Establishing a comprehensive audit follow-up system and implementing agreed-upon recommendations.

ASG Response: ASG has already taken the above steps as part of its Fiscal Reform Plan.

a. The ASG has completed the FY 1998, 1999, 2000, 2001, and 2002 CAFR's and Single Audits within the past year. The FY 2003 CAFR and Single Audit are scheduled for completion in June 2005, followed by the 2004 audits in December 2005. The ASG will then be up to date on all audit requirements.

b. The Budget Office is committed to enforcing the prohibition against budget overruns. Part of this problem is being solved with more reasonable budgets based on ASG's enhanced revenues and collections. Our overriding goal is to have a balanced budget, not necessarily a low budget. Controlling expenditures is important, but delivering reasonable service levels to the community in health, education and welfare is also very important. The audit seems to imply that because ASG has increased its expenditure base, there is something wrong. In fact, expenditures have increased as ASG has hired more teachers, accountants and computer programmers. ASG has given salary increases, especially to teachers. These are essential improvements to our services to the citizens of American Samoa made possible by Fiscal Reform and improved revenues and collections. The bottom line is that ASG has generated sufficient revenues to cover these increased expenses. We have shown surpluses each of the last three years.

c. We have established a comprehensive audit follow-up system and we are implementing agreed-upon recommendations coming out of our audits. The number of findings in the Single Audit is being reduced dramatically every year. The OIA is following up on all findings in the audits.

Summary:

Thus ASG has already accomplished Fiscal Reform, and has taken the steps recommended in this audit. Of course, fiscal reform is a never-ending process. We continue to work to improve our services to the public and to improve our financial management. I, along with my entire administration, are committed to this goal.

Sincerely,

TOGIOLA T.A. TULAFONO
Governor of American Samoa

cc: Mr. David B. Cohen, Office of Insular Affairs
Nikolao Pula, Office of Insular Affairs
Marina Tinitali, Office of Insular Affairs
Francis Leasiolagi, Deputy Treasurer
Magalie Logovi'i, Budget Director
Jack Kachmarik, TOFR Manager

United States Department of the Interior

OFFICE OF INSULAR AFFAIRS
1849 C Street, NW
Washington, DC 20240
June 9, 2005

Deputy Assistant Secretary

Honorable Togiola T.A. Tulafono
Governor of American Samoa
Office of the Governor
Executive Office Building
Pago Pago, American Samoa 96799

Dear Governor Togiola:

The purpose of this letter is to inform you that the U.S. Department of the Interior's Office of Insular Affairs (OIA) is designating the American Samoa Government (ASG) a "high-risk" grantee as provided for in 43 CFR 12.52, and as recommended by the General Accounting Office (GAO) and the Office of Inspector General (OIG). This designation allows OIA to require American Samoa grantees to comply with special conditions for future or existing grants.

The special conditions may include: payment of grant funds on a reimbursable basis, withholding of approval to proceed from one project phase to another until receipt of acceptable evidence of current performance, additional project monitoring, and requiring the grantee to obtain technical or management assistance.

OIA is designating the ASG as a "high-risk" grantee due to the fact that the audits of the ASG completed for each of the fiscal years from 1998 through 2002, inclusive, resulted in disclaimed and qualified opinions from the independent auditors. The reportable conditions were of such severity that the auditors determined that "[t]here were significant failures in the operation of the internal control structure related to general accounting and grants administration," and further that there was "evidence of a failure of these identified controls in preventing or detecting misstatements of accounting information." All of the reportable conditions identified by the independent auditors were determined to be material weaknesses. The independent auditors also stated they could not express any assurances that the ASG was in compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the years ended September 30, 2002 (the most recent completed audit).

In addition, as a result of an OIA compliance review completed in May 2004, we have concluded that the ASG has missed deadlines to complete certain reform actions as required under the Memorandum of Agreement executed by the ASG and the Department of the Interior on August 2, 2002 (MOA) and the fiscal reform plan attached thereto, as updated in 2004 (FRP). Since we have not received sufficient justification for the ASG's request to extend such deadlines, we consider the ASG currently to be out of compliance with the MOA and the FRP.

The "high-risk" designation will be removed once the ASG shall be in compliance with each of the following conditions: (a) the government shall have completed Single Audits by the statutory deadline for the two most recent consecutive years, resulting in opinions that are not disclaimed and do not contain qualifications that OIA determines in its reasonable discretion to be material; (b) the ASG shall have a balanced budget, as confirmed by independent auditors, for the two most recent consecutive years, without regard for nonrecurring windfalls such as insurance settlements; and (c) the ASG shall be in substantial compliance with the MOA and FRP. The ASG's high-risk status shall not affect any rights or remedies that OIA may have under applicable law, the MOA or otherwise, all of which shall continue to apply.

Notwithstanding the foregoing, OIA recognizes that American Samoa has made significant and commendable progress in achieving the objectives outlined in the MOA. OIA looks forward to working with American Samoa to implement improvements in the areas detailed above which will allow OIA to remove the "high-risk" designation.

Sincerely,

David B. Cohen

cc: P. Lynn Scarlett, Assistant Secretary
Earl E. Devaney, Inspector General
Anne Richards, Deputy Inspector General for Audits
Carol Sampson, PFM

Appendix 7

Status of Audit Recommendations

Recommendations	Status	Action Required
With Respect to OIA		
1, 2, 4, and 5	Resolved and Implemented	No further response to the Office of Inspector General is required.
With Respect to the Governor of American Samoa		
1, 2, and 3	Unresolved	In light of ASG being designated a "high-risk" grantee, provide a response that expresses concurrence or nonconcurrence with each recommendation. If concurrence is indicated, provide a plan of action that includes target dates and the titles of the officials responsible for implementing corrective action. If nonconcurrence is indicated, provide the reason for nonconcurrence and a plan of action that includes alternative corrective action and target dates for addressing the underlying deficiencies.

Report Fraud, Waste, Abuse, and Mismanagement

Fraud, waste, and abuse in government concerns everyone: Office of Inspector General staff, Departmental employees, and the general public. We actively solicit allegations of any inefficient and wasteful practices, fraud, and abuse related to Departmental or Insular Area programs and operations. You can report allegations to us in several ways.

By Mail:

U.S. Department of the Interior
Office of Inspector General
Mail Stop 5341 MIB
1849 C Street, NW
Washington, D.C. 20240

By Phone:

24-Hour Toll Free	800-424-5081
Washington Metro Area	202-208-5300

By Fax:

202-208-6081

By Internet:

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