

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The Honorable Esmond B. Moses
Speaker, Twenty-Third Congress
Federated States of Micronesia
Second Regular Session, 2023

Dear Mr. Speaker:

Your Committee on Ways and Means, recommends amendments to the Code of the Federated States of Micronesia, to conform the internal fiscal procedures for Compact implementation (chapter 3 of Title 55) with the 2023 Amended Compact. The bill is entitled:

"TO FURTHER AMEND TITLE 55 OF THE CODE OF THE
FEDERATED STATES OF MICRONESIA, AS AMENDED, BY
FURTHER AMENDING CHAPTER 3, AS ENACTED BY
PUBLIC LAW NO. 13-72 AND AMENDED BY PUBLIC LAWS
NOS. 13-85, 13-93, 18-12, 18-25 AND 18-57, TO
BRING THE FSM'S INTERNAL FISCAL PROCEDURES FOR
COMPACT IMPLEMENTATION INTO COMPLIANCE WITH THE
2023 AMENDED COMPACT, AND FOR OTHER PURPOSES.",

begs leave to report as follows:

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

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FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The intent and purpose of this bill are expressed in its title.

Your Committee has conducted a review of C.B. No. 23-36 and the provisions of the 2023 Amended Compact and the 2023 Fiscal Procedures Agreement (2023 FPA). C.B. No. 23-36 proposes amendments to sections in chapter 3 of title 55 of the FSM Code to conform the internal fiscal procedures for Compact implementation with the 2023 Amended Compact and 2023 FPA provisions and requirements.

A summary of the proposed amendments to title 55 found in C.B. No. 23-36 by section follows.

Section 301. Purpose.

The Proposed amendments update the first year of the new Compact period and to update the description of the Compact to the 2023 Amended Compact.

Section 302. Definitions.

The proposed amendments update the definition sections to clarify by year which Compact, Fiscal Procedure Agreement, and Trust Fund Agreement, is referenced. Definitions of the three newly required plans and the two additional financial reports have been added, and the definition of the "Annual Report" modified to conform with the definitions used in the 2023 FPA. A few additional definitions have been added as used in the 2023 FPA.

Section 304. Compact Planning Estimates.

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The proposed amendments clarify the steps the President should take to determine each Government's share of the estimated Compact funds as part of the budgeting process; specifically, that the President should remove from the estimated Compact funds for any year, the funds for the College of Micronesia before applying the distribution formula.

The amendments to this section also clarify that the President should include in each Government's estimated available funds, any unobligated Grant funds that have been allowed to carry-over from prior fiscal years, under the provisions of the new Section 317 of this chapter.

Section 307. Grant Allocations – Approval, Notification, Rejection.

The proposed amendments clarify that it is the 2023 Amended Compact and the 2023 FPA that will apply.

Section 308. Appeal of Special Conditions.

The proposed amendments to this section reflect that there is no longer a process for appeal of the imposition of special conditions on a Sector Grant. However, JEMCO and the Government of the United States are to consult with the Government of the FSM before imposing any restrictions or special conditions. The amendment requires the President to involve in the consultation process any Government that might be impacted by the proposed restrictions.

Section 309. Grant Acceptance.

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The proposed amendments note that under the 2023 FPA, it is no longer necessary for the President to sign and return Grant Awards, acceptance can be by accepting payment. However, to preserve the current process and create a clear record of Grants accepted and rejected, the Committee does not recommend removal of the requirement that the President accept each Grant by signing and returning the Grant Award.

Section 311. Compact Financial Assistance Fund.

The proposed amendments clarify which provision of the 2023 FPA applies and notes that funds for Operational Grants will now be received quarterly (rather than monthly). Funds for Sector Grants for public infrastructure will continue to be provided on the basis of Accrued Expenditure.

Section 312. Operational Reserve Fund.

The proposed amendments clarify the authority for this Fund (the 2004 FPA). It also provides that because the 2023 Amended Compact and the 2023 FPA no longer provide for this fund to exist, any unobligated funds remaining in this Fund at the end of Fiscal Year 2024 will be treated the same as other Compact Funds – per the new Section 317 (that is, unobligated Operational Grants will be transferred to the Trust Fund, unobligated Sector Grants for public infrastructure will remain available for obligation in a subsequent year as described in the terms and conditions of the Sector Grant).

Section 313. Infrastructure Maintenance Fund.

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The proposed amendments remove the requirements of FSM and State Government matching contributions, and reflect that such contributions are now voluntary.

Although not specified in the amendments, under the 2023 FPA Article VII, Section 9 provides that for FY 2024, the U.S. will contribute 7% of the amount made available for Grants to the Infrastructure Maintenance Fund. The table included in the 2023 FPA reflects the 7% of \$140m = \$9.8m for Fiscal Year 2024. The contribution amount will increase each year to a maximum of 10% (\$14M) in FY 2043.

The Infrastructure Maintenance Fund can be used only for the purpose of the repair and maintenance of United States funded infrastructure within the Federated States of Micronesia. It may not be used to fund extensions, expansions or for repurposing of previous infrastructure projects, these requirements are found in the 2023 FPA at Article VII, Section 9(f).

The proposed amendments also specify that the Infrastructure Maintenance contribution is to be distributed among the five Governments using the distribution formula that applies to Compact funds generally (contained in section 303).

The Infrastructure Maintenance Fund will be available for use after the President transmits a consolidated infrastructure maintenance plan each year (this requirement is included in the amendments to Section 320 on external reporting below).

In addition to using the U.S. contribution to the Infrastructure Maintenance Fund to maintain infrastructure, the FSM may make voluntary contributions to the Fund. Also, the 2023 FPA Article

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

VII, Section 9(g) specifies that portions of the Health and Education Sector Grants may also be allocated to infrastructure maintenance.

Section 314. Drawdown Procedures – Cash Disbursement to National and State Treasuries.

The proposed amendments to this section update reference to the FPA to the 2023 version.

The proposed amendments also record the change to the frequency of advance payment for Compact Sector Operational Grants, from monthly (under the Amended Compact) to quarterly (under the 2023 Amended Compact).

If the FSM wants a distribution of more than one-quarter of the year's Compact funds, it will need to prepare an outlay analysis and seek concurrence of the Government of the U.S. to receive payment on that basis.

Section 315. Reprogramming/Re-Allocation of Compact Funds.

The proposed amendments to this section record the change in the 2023 FPA Article VI(1)(d) that allows reprogramming of funds by a Government only between October 1 and June 30 each year, unless the reprogramming is necessary in an emergency to protect public health and safety.

The proposed amendments also record that as part of the Annual Financial Report, the Governments are required to provide a summary document of all reprogramming, by sector.

Section 316. Internal Reporting Requirements.

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The proposed amendments revise the internal reporting forms that the five Governments must provide to the President quarterly for all Sector Grants.

The President must compile this information and provide it to JEMCO and the Government of the United States only annually under the 2023 Amended Compact (compared to quarterly under Compact 2), however, the Committee believes it is advisable to continue with the quarterly reporting requirement internally, as it will allow easier compliance with the annual external reporting requirement (which is detailed in Section 320).

Section 317. Availability of Grant Funds.

The proposed amendments remove the section heading of "Compact Quarterly Financial Report Requirements" and move the contents that remain relevant to the new Section 320 on external reporting.

The proposed new heading for this section is "Availability of Grant Funds."

The new section sets out, for Fiscal Year 2025 and thereafter, the treatment of unobligated Sector Grant funds will be governed by Article XI, Section 4 of the 2023 FPA – that is, for Operational Grants made under Section 261(a)(1)-(5) and (7) of the 2023 Amended Compact, the unobligated portion shall be deposited into the Trust Fund, as required by Article IX, Section 4(a) of the 2023 FPA.

The unobligated portion of Sector Grants that is required to be deposited into the Trust Fund at year end, will be held in

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

Account 3 of the Trust Fund. These amounts can be requested as "Unspent Economic Assistance Distributions" under the conditions specified in Article 20 of the *Agreement Between the Government of the Federated States of Micronesia and the Government of the United States of America Regarding the Compact Trust Fund*. Requests for such distributions are to be submitted to the Joint Trust Fund Committee. If such a distribution is requested and approved, then there is an obligation for the FSM Government to submit an Annual Financial Report and an Annual Performance Report in relation to those funds to the Joint Trust Fund Committee.

For Sector Grants for public infrastructure under Section 261(a)(6) of the 2023 Amended Compact, the funds shall remain available for obligation in subsequent Fiscal Years, as described in the terms and conditions of the Sector Grant (this is pursuant to Article IX, Section 4(b) of the 2023 FPA).

The new section also specifies how carry-over fund will be treated in the 2024 Fiscal Year. This is detailed in Article IX, Section 3(a)&(b) – that is, the unobligated Sector funds granted under Section 211 of the Amended Compact (Compact 2) shall remain available for use in the same sector during Fiscal Year 2024. These funds will continue to be governed by the 2004 FPA.

Section 318. Internal Annual Final Cash Transactions Report.

The proposed amendments clarify that reporting by the five Governments to the President on unobligated Operational Grants that carry-over is only through Fiscal Year 2023.

Section 319. Compact Annual Final Cash Transactions Report.

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The proposed amendments clarify that the President's report to the Government of the United States includes unobligated Operation Grants that carry-over, only through Fiscal Year 2023.

Section 320. Plans and Reports of the President to the Government of the United States.

The proposed amendments change the title of the section from "Annual Report" to "Plans and Reports". This section pulls together in one place all external reporting requirements in relation to Sector Grants under the 2023 Amended Compact

The proposed amendments set out the 3 plans that are pre-award requirements (they must be accepted before Grants will be released):

- (1) The Strategic Development Plan;
- (2) The Infrastructure Development Plan; and
- (3) The Annual Implementation Plan.

For these reports, it is a requirement that JEMCO concur with (or reject portions of the plan that relate to the use of Sector Grants). The details of these Plans are in Article V of the 2023 FPA.

The proposed amendments then set out the requirement that an Infrastructure Maintenance Plan be provided by the President to the Government of the U.S. before the funds contributed by the U.S. to the Infrastructure Maintenance Fund can be used.

The proposed amendments also provide the requirements for the biennial Section 264 Report.

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The proposed amendments set out the two post-award reports that are required:

- (1) The Annual Financial Report; and
- (2) The Annual Performance Report.

The FSM is required to retain a qualified third-party (agreed to by the U.S.) to assist in the preparation of these reports. The FSM will need to pay this costs itself, but Sector Grant funds under the new, seventh category of Sector Grants for "Enhanced Reporting and Accountability" can be used.

This seventh Sector or category of Grant is contained in Section 261(7) of the 2023 Amended Compact. Your Committee re-iterates a point raised in Standing Committee Report 23-04 of the Committee on External Affairs – the U.S. is no longer providing half of the reasonable cost, or \$500,000 (whichever is less) for the required annual audit. This was provided under Section 212(b) of the Amended Compact and was in addition to all other Sector Grants.

However, it is not included in the 2023 Amended Compact. In fact Section 262(b) of the 2023 Amended Compact explicitly states that the FSM is to bear the cost of the annual audit required under Article VIII, Section 2 of the 2023 Amended Compact, although this payment may be made from Sector Grant funds.

These two items of expert fees (for reporting and auditing) will be a significant budgetary item the National Government will need to plan for each year starting in Fiscal Year 2024.

For Fiscal Year 2023, the Annual Financial Report is to be provided to the President of the U.S. and to JEMCO. For Fiscal

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

Year 2024 and thereafter, the Annual Financial Report is to be provided to the Government of the U.S. and JEMCO.

The Annual Performance Report must be provided to the Government of the U.S. and to JEMCO each year.

The details of the requirements of the Annual Financial Report are in Article VI, Section 1(b) of the 2023 FPA. The details of the requirements of the Annual Performance Report are in Article VI, Section 2(a)(ii) of the 2023 FPA.

The amendments also set out the requirements that the President provide a Federal Form SF-425 annually to the Government of the U.S., with regards to the Infrastructure Maintenance Fund. This report must include accounting information and the status of progress for each project funded by the U.S. contribution to the Infrastructure Maintenance Fund. This is a requirement of Article VII, Section 10 of the 2023 FPA.

Section 321. Accounting and Record Keeping.

The proposed amendments to this section specify that the financial information generated from the Government's reporting systems shall include not just the information required for the Annual Financial Report (as required by Compact 2), but also information required for the Annual Performance Report, the Strategic Development Plan, the Infrastructure Development Plan, the Infrastructure Maintenance Plan, the Form SF-425 Report (on uses of the U.S. contribution to the Infrastructure Maintenance Fund), the Annual Implementation Plan and the biennial Section 264 Report.

Section 323. Enforcement.

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

The proposed amendments to this section update the Compact and FPA references to the 2023 versions.

C.B. No. 23-36, C.D.1

Your Committee recommends the following changes to C.B. No. 23-36:

- (1) Re-insert the definition for "original compact" for ease of historical reference and the term is used elsewhere in title 55 of the Code of the FSM
- (2) Remove proposed amendments to section 303 and 306 of title 55, as those sections are amended in C.B. No. 23-33
- (3) Miscellaneous clarifying language and technical corrections

Conclusion

Your Committee has carefully reviewed C.B. No. 23-36. Your Committee on Ways and Means is in accord with the intent and purpose of C.B. No. 23-36, and recommends its passage on First Reading and that it be placed on the Calendar for Second and Final Reading in the form attached hereto as C.B. NO. 23-36, C.D.1.

Respectfully submitted,

/s/ Isaac V. Figir
Isaac V. Figir, chairman

/s/ Perpetua S. Konman
Perpetua S. Konman, vice chairwoman

STANDING COMMITTEE REPORT NO. 23-31

RE: C.B. NO. 23-36/W&M

SUBJECT: TO CONFORM THE FSM'S INTERNAL FISCAL PROCEDURES
FOR COMPACT IMPLEMENTATION WITH THE PROVISIONS
OF THE 2023 AMENDED COMPACT.

SEPTEMBER 21, 2023

/s/ Peter M. Christian
Peter M. Christian, member

/s/ Tiwiter Aritos
Tiwiter Aritos, member

Joseph J. Urusemal, member

/s/ Paliknoa K. Welly
Paliknoa K. Welly, member

/s/ Victor V. Gouland
Victor V. Gouland, member