

OFFICE OF THE NATIONAL PUBLIC AUDITOR
FEDERATED STATES OF MICRONESIA



**Performance Audit On Implementation Of Recommendations Of Prior
Audit Report No. 2022-04**

**Improving Enterprise-Wide Risk Management And Procurement For
The FSM Petroleum Corporation**

Report No. 2025-01



FEDERATED STATES OF MICRONESIA

Office of The National Public Auditor

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February 11, 2025

His Excellency President Wesley W. Simina
Honorable Members of the 23rd FSM Congress
Members of the Board of Directors, FSM Petroleum Corporation
Federated States of Micronesia

RE: PERFORMANCE AUDIT ON THE IMPLEMENTATION OF RECOMMENDATIONS OF OUR PRIOR REPORT NO. 2022-04 ON THE FSM PETROLEUM CORPORATION

This report presents the results of our performance audit on the implementation of the audit recommendations from our prior audit on the FSM Petroleum Corporation that was issued as Report No. 2022-04 on July 07, 2022.

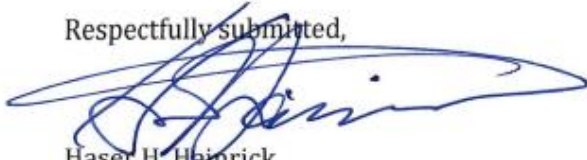
The main objective of this performance audit was to determine whether the management of the FSM Petroleum Corporation have taken actions to address the audit recommendations disclosed in our prior Report No. 2022-04.

Based on our follow-up audit, we found that majority of our prior recommendations have been implemented. The current status of implementation, as indicated in the table below, is as follows: five (5) recommendations were rated “full implementation” (FI), and one (1) was rated partial implementation (PI). The definition of the stages of implementation are provided in [Appendix A](#).

Finding No. & Title	No. of recommendations & stage of Implementation (5)	
	FI	PI
Prior Finding No. 1: Outdated Risk Management Procedure and No Central Monitoring of Enterprise-wide Risks	2	-
Prior Finding No. 2: Procurement Manual Remains in Draft Since 2018 & Does Not Contain Procedures for Procuring Fuel & Lubricants	1	1
Prior Finding No. 3: Inconsistent Documentation of Minutes of Meetings of The Board Committee for Risk and Audit	2	-
Total	5	1
%	83%	17%

Finally, we want to acknowledge the staff, management and the Board of Directors of the FSM Petroleum Corporation for their combined efforts to implement the significant 83% of our prior recommendations and the efforts being taken and planned for the remaining ones.

Respectfully submitted,



Haser H. Heinrick
National Public Auditor

CC: Vice President, FSM National Government
Chief Executive Officer, FSM Petroleum Corporation

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1. INTRODUCTION

1.1 Reason for the Audit

On an annual basis, the Office of National Public Auditor (ONPA) documents the audit or engagements to be conducted during the fiscal year based on risk assessment performance on the ONPA's audit universe.

As per the ONPA Annual Operational Plan for fiscal year 2025, the need to conduct a performance audit on prior audit report no. 2022-04 on FSM Petroleum Corporation (FSMPC) arises to ensure the impact of our audits by verifying that corrective actions are being implemented effectively.

1.2 Background

A performance audit was conducted on the FSMPC, covering fiscal years 2019 to 2021. The audit primarily focused on processes of governance, internal controls, risk management and operations of the Corporation. With this focus, the audit objectives were to assess and determine the:

- a) Extent by which the processes in the Procedure to Manage Enterprise Risk have been implemented to minimize the impact of identified key risks;
- b) Adequacy of the control environment for procuring fuel and lubricants; and,
- c) Extent and effectiveness of implementing section 241 (6) of Chapter 2 of Title 27 of the FSM Code in relation to safety, health, and environment.

On July 7, 2022, the ONPA issued audit report no. 2022-04 titled "*Deficiencies noted reflect the need to improve enterprise-wide risk management*". As a result of the performance audit conducted on the FSMPC, the audit revealed the following issues that management should address:

- I. Outdated risk management procedure and no central monitoring of enterprise-wide risks;
- II. Procurement Manual remains in draft since 2018 & does not contain procedures for procuring fuel & lubricants; and
- III. Inconsistent documentation of minutes of meetings of the Board Committee for Risk and Audit.

The team followed up on the recommendations for the three (3) findings listed above.

2. AUDIT MANDATE

We conducted this performance audit pursuant to the authority vested in the National Public Auditor as codified under Chapter 5, Title 55 of the FSM Code which states in part the following:

"The Public Auditor shall inspect and audit transactions, accounts, books and other financial records of every branch, department, office, agency, board, commission, bureau,

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and statutory authority of the National Government and of other public legal entities, including, but not limited to, States, subdivisions thereof, and nonprofit organizations receiving public funds from the National Government.”

3. OBJECTIVE, SCOPE, AND METHODOLOGY

3.1 Objective

The objective of this audit was to determine whether the FSMPC has taken appropriate corrective actions to address our audit findings and recommendations outlined in the prior audit report no. 2022-04.

3.2 Scope

The scope of this audit was focused on the responses and documents received from the FSMPC on the extent of the implementation of the recommendations highlighted in the prior audit report no. 2022-04.

The team performed this performance audit at FSMPC Headquarter in Kolonia, Pohnpei.

3.3 Methodology

We conducted this audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

The audit fieldwork was conducted at the Headquarter office in Kolonia, Pohnpei. To achieve the objective, the team reviewed and assessed the matrix and all supporting documents.

4. PRIOR AUDIT COVERAGE

The first audit report is the one that we performed this performance audit on, that is, report no. 2022-04 entitled *“Deficiencies Noted Reflect The Need To Improve Enterprise-Wide Risk Management.”* It was the result of implementing our Medium-Term Risk Based Audit Plan for fiscal years 2019 to 2021, and as part of our duties and responsibilities set forth under the Public Auditor’s Act, Chapter 5 of Title 55 of the FSM Code.

5. COMMENDATION

We commend the FSMPC for the progress made in implementing 83% of our prior recommendations. Specifically, out of the six recommendations from audit report no. 2022-

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04, five have been fully implemented, and one have been partially implemented. This achievement is commendable and demonstrates a strong commitment to improvement.

6. CONCLUSION

Based on the results of this performance audit, we concluded with reasonable assurance that the FSMPC has made substantial progress in implementing the recommendations outlined in audit report no. 2022-04. Specifically, of the six (6) recommendations, five (5) have been fully implemented, demonstrating complete adherence to our suggestions, while one (1) has been partially implemented, indicating ongoing efforts to address the remaining areas. This progress is a commendable achievement for the FSMPC.

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7. IMPLEMENTATION STATUS OF OUR RECOMMENDATIONS IN THE PRIOR AUDIT REPORT NO. 2022-04.

7.1. Implementation of Recommendations on prior Finding 1: Outdated risk management procedure and no central monitoring of enterprise-wide risks

We had issued two recommendations under prior Finding 1

7.1.1 Prior Finding 1: Recommendation 1 of 2

We recommended that: The Chief Executive Officer should ensure the effectiveness of the new Chief Risk and Compliance Officer (CRCO) position to carry out enterprise-wide communication, monitoring and reporting of risks and include in his job description the duty of reviewing and improving the procedure to manage risks to include:

- a. periodic review of the procedure and frequency of review;
- b. the necessary amendments to ensure that the procedure is complete, relevant and aligned to ISO 31000 (with standard templates for identifying, analyzing, evaluating and treating risks); and
- c. a procedure for (Committee on Risk and Audit) CoRA to require all functions and business units of the Corporation to report on their key risks so it provides them a holistic view of the organization's risks.

Management Response to the prior audit was: They concurred with the audit findings and recommendation. Management acknowledged the identified anomalies and acknowledged gaps, and they expressed a commitment to enhancing risk management processes.

Current Implementation Status: Full Implementation

The role/job description (JD) for the CRCO has been finalized and approved. The CRCO is responsible for implementing and periodically reviewing the compliance framework, regularly assessing risk action plans for effective management, and continuously developing training programs to promote a strong risk culture within the organization. Below is the breakdown of our assessment of the first prior recommendation:

1. Oversight of Risks:
 - The JD specifies that the CRCO is responsible for overseeing risks across Vital Energy and its subsidiaries, ensuring that risks align with the Board's Risk Appetite Statement. This aligns well with the recommendation for effective oversight.
2. Periodic Review of Risk Procedures:
 - The JD mentions the development and review of the Risk Management Framework, which includes the consistent review and assessment of risk identification, assessment, and mitigation. This suggests that there is an

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intention for periodic reviews, though specific frequencies are not mentioned.

3. Alignment with ISO 31000 (Risk Management standards) that the Corporation had adopted in the past :
 - While the JD does not clearly state that procedures will be aligned with ISO 31000, it does emphasize the importance of compliance and risk management frameworks. It would be helpful to include a specific commitment to ISO 31000 alignment or any other applicable risk standard that the Corporation will adopt.
4. Holistic Reporting of Key Risks:
 - The JD outlines responsibilities for maintaining a company-wide Risk Register and ensuring that major risks are identified and reported. This supports the recommendation for a holistic view of organizational risks.

7.1.2 Prior Finding 1: Recommendation 2 of 2

We recommended that: The Chief Executive Officer should ensure the success of the new project on the centralized system for recording, monitoring and reporting key enterprise-wide risks and ensuring that the function managers are periodically updating their relevant risk registers for monitoring by the CRCO and his team.

Management Response to the prior audit was: They concurred with the audit finding and recommendation. Management acknowledged the identified anomalies and acknowledged gaps, and they expressed a commitment to enhancing risk management processes.

Current Implementation Status: Full Implementation

The team reviewed the comments by management on our follow-up implementation matrix and found that the new Vintra Risk Assessment Tool is up and running, with over twenty risks successfully moved into it. The company is still adding more risks. Automated reports will be generated for everyone from the Board of Directors to staff. In our assessment, the function of the system meets our prior audit recommendation of having a single system for reporting risks.

The Risk Register module in Vintra has been finished and launched in the second quarter with the Production and Quality team.

Based on the Operational Risk Compliance and Assurance (ORCA) report, the team noticed that risk assessment workshops take a lot of time, especially with the new Vintra Risk Assessment Tool, which has its own challenges. However, we share the understanding with management that like any other new system, the process will become easier and faster over time as they continue to streamline the risk management process.

7.2. Implementation of Recommendations on prior Finding 2: Procurement Manual remains in draft since 2018 & does not contain procedures for procuring fuel & lubricants

We issued two recommendations under prior Finding 2

7.2.1. Prior Finding 2: Recommendation 1 of 2:

We recommended that: For increased accountability and monitoring, the Chief Executive Officer should consider:

- a) assigning the responsibility of ensuring that the Procurement Manual is finalized and approved to a personnel/Unit that has the capabilities to complete this task;
- b) having this responsibility and the assignment thereof documented; and
- c) the responsible personnel/Unit made aware of the responsibility and its expectations.

The Management Response to the prior audit was: They generally agreed with some findings, clarified some information and provided some new information. (Note: the prior final audit report contained minor changes that were made after new information were received through the management response)

Current Implementation Status: Full Implementation

The recommendation for increased accountability and monitoring has been implemented as the Business Plan for 2024 shows that the Chief Finance Officer (CFO) was assigned the responsibility of ensuring that the Procurement Manual is finalized and approved. From interviews, the CFO confirmed she was assigned this responsibility in October 2022.

7.2.2. Prior Finding 2: Recommendation 2 of 2:

We recommended that: The oversight function by the Board and Management needs to improve with regards to:

- a) Expediting the approval of the draft Procurement Manual
- b) Reviewing and making amendments to the draft Procurement Manual to also include the entire procurement processes for fuel and lubricants.

The Management Response to the prior audit was: They generally agreed with some findings, clarified some information and provided new information. (Note: the final audit report contained minor changes that were made after new information were received through the management response)

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Current Implementation Status: Partial Implementation (In Progress)

From our assessment, the Board and Management still need to strengthen their oversight function and provide timely support to ensure the completion of the Procurement Manual. The project to implement this has been assigned to the CFO since October 2022. It has been a rolled over project over the past 2 years and remains pending in 2024.

Based on the quarterly Finance Accounting Performance Reports to the Board for the 3rd Quarter of 2024, the project for completing the draft Procurement Manual is under topic 5 on “Strengthening Business Process”. This project was targeted for completion in November 2024; however, due to slow progress it has been registered as a company project and managed through project management to expedite the process under the supervision of Project Management Office. This is commendable indicating the executive management’s commitment to completing the project.

Effect(s) of Partial Implementation: The risk of knowledge gaps in which an undue burden is placed on an employee who is well-versed with the process of procurement. This can also result in disruption to relevant operations when that employee leaves or is no longer working for the Corporation.

Additionally, not having a Procurement Manual (especially one for fuel and lubricants; being the main products of FSMPC) will create inconsistencies in practice due to absence of guidance on important information such as step by step tasks (system and manual processes), identification of responsible employees and timelines. There is possibility that procurement actions may appear to be arbitrary and unfair in the absence of documented procedures that should ideally be known and practiced by all relevant employees including those being groomed to take up management roles (within the procurement process) in the future.

As a result, we are not able to provide assurance on the adequacy of the control environment for the procurement of fuel and lubricants.

Cause(s) of Partial Implementation: According to the Finance Accounting Performance reports for the 1st, 2nd and 3rd Quarter of 2024, Item 5.1 (Launch Procurement Manual & alignment to all purchasing activities) under the Topic 5 “Strengthen Business Process” has been delayed due to the following reasons:

- Other tasks were prioritized for Q1, however, to ensure that this initiative moves along this year, Procurement Team & CFO have set a weekly recurring session to ensure that time is set aside every week to complete this initiative.

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- The Procurement team experienced several shifts due to shortage of staff due to leave and resignation. Therefore, operational duties had to be redistributed amongst the team and prioritized.
- While there was some progress in the year in terms of documenting processes & procedures in CPP format, sessions to complete this were infrequent and inconsistent because there was no proper direction & focus.

7.3. Implementation of Recommendation on prior Finding 3: Inconsistent documentation of minutes of meetings of the Board Committee on Risk and Audit (CoRA)

We issued two recommendations under prior Finding 3

7.3.1. Prior Finding 3: Recommendation 1 of 2

We recommended that: Governance to be strengthened by the Board of Directors on the issue of or amendments of existing policies to include the documentation and maintenance of minutes of meetings for all Board committees established within the Corporation;

The Management Response to the prior audit was: They acknowledged the gaps in documentation during these activities and appreciated the audit team's findings. Management plans to collaborate with the Board to improve documentation practices while ensuring accurate outputs reflect their decisions and judgments.

Current Implementation Status: Full Implementation

The FSMPC mandates the documentation and maintenance of meeting minutes. The Bylaw was approved on November 25, 2022, which specifically mentioned the requirements for meeting minutes from Board meetings. According to Section 3.6, all minutes must be available to the public in compliance with Public Law No. 15-08, and the Secretary is responsible for keeping meeting minutes. FSMPC Bylaw section 5.1 emphasizes that special committees must also maintain regular minutes of their meetings.

7.3.2. Prior Finding 3: Recommendation 2 of 2

We recommended that: The Chief Executive Officer should assign suitable personnel(s) the role of documenting the minutes of meetings of CoRA and other committees of the Board.

The Management Response to the prior audit was: They acknowledged the gaps in documentation during these activities and appreciated the audit team's findings.

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Management plans to collaborate with the Board to improve documentation practices while ensuring accurate outputs reflect their decisions and judgments.

Current Implementation Status: Full Implementation

Based on the minutes of the last two CoRA meetings (held in June and August 2022 respectively), it was noted that the Executive Assistant (EA) was designated to document the minutes. Additionally, the questionnaire completed by the EA as well as the Job Description confirmed that he is the designated individual responsible for documenting the meeting minutes of the Board and its committees. He prepares the CoRA minutes that the CoRA Chairperson reports to the Board meeting where they are included as part of the minutes of meetings of the Board.

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8. APPENDIX A: STAGES OF IMPLEMENTATION OF AUDIT RECOMMENDATIONS

Summary

There are four stages used to assess the status of implementation of the recommendations which are listed below:

1. Not Implemented (NI)

No progress or insignificant progress

Actions such as having meetings and generating informal plans.

2. Partial Implementation (PI)

When formal plans for organizational changes have been created and approved by the appropriate level of management with appropriate resources and a reasonable timeframe.

If the entity took action to implement a recommendation by hiring or training staff or developing or acquiring the necessary resources to implement the recommendation.

If the structure or processes are in place and integrated within at least some parts of the organization, and some achieved results have been identified.

3. Full Implementation (FI)

If the structure or processes are operating as intended and are fully implemented.

4. No Longer Applicable (NLA)

If the recommendation that was issued no longer applies to the current processes or systems.

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9. MANAGEMENT RESPONSE



File Ref. PC/J/8

January 29, 2025

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

Transmitted via e-mail: Haser Hainrick hhainrick@fsmopa.fm;

SUBJECT: Management's Response
Performance Audit on Implementation of Recommendations of Audit No. 2022-04

Dear Mr. Hainrick:

Greetings to you and the FSMOPA team.

Please find enclosed Management's Response to the 2024 Follow-up Performance Audit, and specifically the 6 assessments on three findings from the prior report:

- i) 7.1 Finding 1 Recommendation 1 of 2: Full Implementation
- ii) 7.1 Finding 1 Recommendation 2 of 2: Full Implementation
- iii) 7.2 Finding 2 Recommendation 1 of 2: Full Implementation
- iv) 7.2 Finding 2 Recommendation 2 of 2: Partial Implementation
- v) 7.3 Finding 3 Recommendation 1 of 2: Full Implementation
- vi) 7.3 Finding 3 Recommendation 2 of 2: Full Implementation

Should there be any further questions or comments, feel free to contact me via e-mail at cmendiola@fsmc.com

Regards,

A handwritten signature in black ink, appearing to read 'Cherish A. Mendiola'.

Cherish A. Mendiola
Chief Finance Officer

Cc:
Miriam Naivalu mnaivalu@fsmopa.fm;
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January 29, 2025

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

No. 2022-04 Finding 7.1

Management Response:

- We thank you for the full implementation assessment on Recommendation 1.
- We thank you for the full implementation assessment on Recommendation 2.

No. 2022-04 Finding 7.2

Management Response:

- We thank you for the full implementation assessment on Recommendation 1.
- We agree with Partial Implementation (In Progress) for Recommendation 2 – Procurement manual completion and adoption, and the reports notes.
 - We have updated our strategy and plan to move this forward. This shall be rolled out as a project that is compliant with our project management processes. This will see specific activities, milestones, and deliverables being scheduled and then be reported on, monitored and corrective actions taken when needed.
 - Initial project documents – charter, scope, work breakdown structure and schedule - have been developed and submitted to the executive team at their first meeting of 2025. Final drafts are expected to be approved in February, with us moving into the execution phase immediately after.

No. 2022-04 Finding 7.3

Management Response:

- We thank you for the full implementation assessment on Recommendation 1.
 - We thank you for the full implementation assessment on Recommendation 2.
-

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10. ONPA EVALUATION OF MANAGEMENT RESPONSE

We requested an official Management Response from the FSM Petroleum Corporation. A written response (provided on the above [Section 9](#) of this report) was received where the entity generally agreed with our findings and shared the new strategy that has been taken to progress implementation for the remaining prior recommendation. This indicates management's strong commitment to complete and finalize the Procurement Manual as a guiding document for the procurement process especially considering our initial emphasis to include in the manual the procedures for procuring fuel and lubricants.

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11. NATIONAL PUBLIC AUDITOR'S COMMENTS

We would like to thank the staff and management of the FSM Petroleum Corporation (FSMPC) for their assistance and cooperation during the performance audit on prior audit report 2022-04.

We have provided copies of the final audit report to the President and Members of the 23rd FSM Congress as well as the Board of Directors for the FSMPC. Furthermore, we will make copies available to other interested parties upon request.

If there are any questions or concerns regarding this report, please do not hesitate to contact our office. Contact information for the office can be found on the last page of this report along with the National Public Auditor and staff that conducted the performance audit and prepared this report.



Haser H. Hainrick
National Public Auditor

Date: February 11, 2025

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12. ONPA CONTACTS AND STAFF ACKNOWLEDGEMENT

ONPA CONTACT: Haser H. Hainrick, National Public Auditor
 Email: hhainrick@fsmopa.fm

ACKNOWLEDGEMENTS In addition to the contact named above, the following staff made key contributions to this report:

Miriam Naivalu, Audit Manager
Brenda Carl, Auditor-In-Charge
Shelolyn Neth, Staff Auditor

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