FEDERATED STATES OF MICRONESIA
PETROLEUM CORPORATION

(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED DECEMBER 31, 2017 AND 2016

FEDERATED STATES OF MICRONESIA PETROLEUM CORPORATION
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Years Ended December 31, 2017 and 2016
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INDEPENDENT AUDITORS' REPORT

Board of Directors
Federated States of Micronesia Petroleum Corporation:

Report on the Financial Statements

We have audited the accompanying financial statements of the Federated States of Micronesia (FSM) Petroleum Corporation (the Company) and its discretely presented component unit, collectively a component unit of the FSM National Government, as of and for the years ended December 31, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Company's basic financial statements as set forth in Section III of the foregoing table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. The financial statements of the discretely presented component unit were not audited in accordance with *Government Auditing Standards.* Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Deloitte.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Company and its discretely presented component unit as of December 31, 2017 and 2016, and the respective changes in financial position and, where applicable, cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information:

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 to 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 28, 2018, on our consideration of the Company's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Company's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Company's internal control over financial reporting and compliance.

Deloitte & Touche LLP

June 28, 2018

STRATEGIC OBJECTIVES

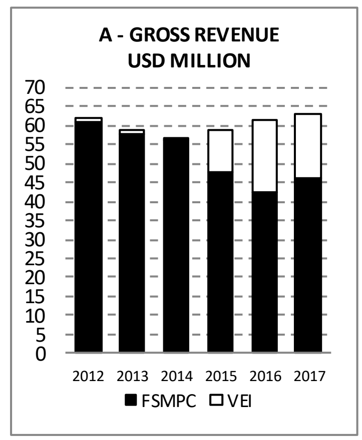
The primary long term role and function of the Federated States of Micronesia Petroleum Corporation (FSMPC or "the Corporation") is to secure a stable supply of petroleum products to meet the nation's core energy needs. In addition, and as a result of Public Law 18-68 entitled "The Coconut Tree Act", the Corporation transitioned the assets, staff and operations of the former FSM Coconut Development Authority (CDA) in September 2014.

The Corporation engages efficiently, responsibly and profitably in the country to ensure that there are sufficient resources to maintain assets, train people, hold strategic oil inventories, and provide petroleum products in full, on-time, and to international specifications, and to provide the necessary resources to develop the coconut industry.

The Corporation is the largest supplier of energy in the FSM and constantly evaluates opportunities to expand vertically into markets which use and supply modern energy services, as well as laterally into alternative energy technologies with an aim of improving the energy security of the nation.

SUMMARY OF OPERATIONS

The Corporation operates a total of eight fuel terminal facilities across the region. It services the international aviation, marine bunkering, and inland market segments. It also owns and operates a copra and coconut processing facility in Pohnpei producing soaps and edible oils.



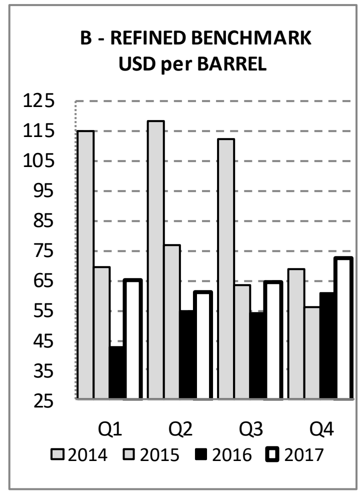
Vital Energy Incorporated (VEI), Guam, is wholly owned by the FSMPC. In 2017, it successfully concluded its five year terminal operations and management contract with the Guam Power Authority (GPA). A supply and terminal operating agreement with the Government of Nauru remains in place. The Corporation stores, handles and delivers over 2.3 million barrels of petroleum products per annum.

An FSM Pricing Policy Framework (PPF) provides a mechanism to stabilize domestic prices, and cushion the effect of international volatility. There are no cross subsidies within the PPF, and the prices reflect the costs of procuring, financing, storing, handling and distribution of fuels in the States that we operate.

A Nauru Pricing Template (NPT) negotiated with the Government of Nauru provides the mechanism to earn a return-on-investment commensurate with the risks of operating in Nauru. The NPT has a similar stabilization mechanism for domestic prices, and cushion the effect of international volatility.

There are no cross subsidies between the PPF or NPT, and the prices in each operating unit reflect the costs of procuring, financing, storing, handling and distribution of fuels in the States that we operate. The Corporation continues to benchmark domestic price competitiveness through comparison of pump prices of island neighbors. Throughout CY17, domestic prices in the FSM remained stable, and by and large remain below benchmark Guam pump prices.

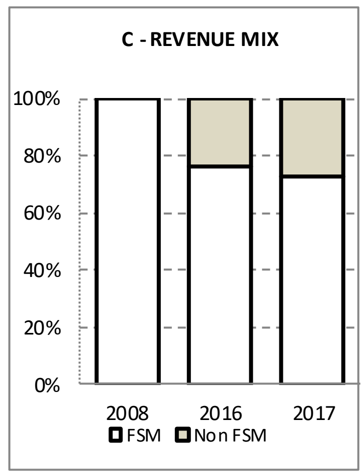
Pricing practices did not change throughout 2017. The PPF and NPT maintained scheduled price adjustments in accordance with various price instruments for contract customers such as utilities, airlines, and a quarterly price change for retail service stations. This strategy continues to provide stable energy prices for homes, businesses, and government however, is expected to undergo a review in 2018.



Revenues

Over 97% of company revenues remain petroleum fuels related. Revenues are directly linked to the international oil markets and the adjustment mechanisms in the PPF and NPT that accommodates international oil price increases or decreases. Therefore, throughout 2017, revenues have increased with rising global oil prices.

2017 started in the mid $US65/bbl. By December 2017, it had reached the mid $70/BBL. The refined product benchmark average for CY2017 was $65/BBL, an increase of approximately 25% over 2016 (graph B).



FSMPC revenues have risen 10% from a low of $43MM in 2016 to $47MM in 2017 (refer Graph A) as higher international prices have been passed on to consumers. In addition, sales volumes continue to be depressed for the second consecutive year. Conversely, VEI has grown to a high of $17MM improving the revenue mix considerably (refer Graph C).

As a result, the Corporation has managed to retain a consolidated gross revenue of the Group at $63.6 million. (refer graph A) with business unit contributions of Kosrae 7%, Yap 11%, Chuuk 21%, Pohnpei 36%, Guam and Nauru 26%. Automotive diesel oil remains the highest revenue component at 48%, followed by unleaded petrol (or gasoline) 33%, and home kerosene and Jet A1 of 14%. Non-fuel related revenues from power plant electricity sales, terminal management fees, as well as coconut related products are approximately 4% of total revenues mix, and lubricants under 1%.

Our petroleum operations throughout the FSM, Guam and Nauru are supported by fuel, lubricant and technical service agreements with Mobil Oil Micronesia Incorporated (MOGI), Total Oil Asia Pacific (TOAP), and ExxonMobil Aviation (EMA). In 2015, we added Winson Oil (HK) Limited and Pacific Bulk Fuels (NZ) Limited as primary product suppliers to the Corporation. There were no changes in primary product suppliers in 2017.

Investment and Business Planning

There has been an update to the Statement of General Business Principles (SGBP) in 2017, to accommodate an additional corporate value, and a new stakeholder group - farmers. Management seeks formal reassurance from each staff member that they operate within these principles annually. The Board confirms their commitment to the SGBP annually. There were no reported breaches of these principles in 2017.

In 2017, a Strategy Execution Team (SET) was resourced to implement the initiatives identified within the 2016 Strategic Plan and an enhanced strategy execution framework. The Corporation has maintained its annual business planning process; however it has re-engineered its business processes to incorporate Programs that have a three-year planning and outcomes horizon.

The business anticipates investments in excess of $40M into its FSM operations over the next five years for fuel terminal risk reduction, operational efficiency and coconut industry rehabilitation work. The Board and Management will be looking to outsource activities to enter into equipment leasing arrangements, utilize joint ventures to meet much of this capital requirement as well as to transfer risks as appropriate. The Investment Appraisal Framework adopted by the Board in 2015 remains in place. The appraisal framework provides clear guidelines for Management for all investments made by the Corporation.

Risks & Risk Management

The risk management system is compliant with the ISO31000:2009 international standard for Risk Management. The Corporation has adopted the most recent American Petroleum Institute Standard 653 (API653) for maintenance of petroleum storage tanks, and also seeks to comply with the Joint Implementation Group (JIG) standard for international airports.

Risks are managed proactively. The Board Committee on Risk and Audit (CoRA) has maintained a quarterly meeting schedule, and the CoRA remain accountable for enterprise level risks, remedial action plans, and business internal controls.

Organizational resources continue to be allocated primarily towards risk mitigation. In conjunction with the organizational restructure to implement a Strategy Execution Team (SET), the organization also implemented a clear risk architecture that can demonstrate five (5) levels of assurance across the business to support Board oversight. The three areas that have been and remain a priority, namely i) competent people, ii) asset rehabilitation, and iii) credible scenario planning and preparedness have been elevated into Programs, with resources and dedicated Program Managers.

The largest risks facing the business are:

- *Extreme weather events and natural disasters* are environmental risks that are of a growing risk value in our operations due to both likelihood and consequence. This is consistent with the World Economic Forum (WEF) emerging risks of 2018;

- *Substitute energy products and alternatives*. IRENA has confirmed that after years of steady cost decline for solar and wind technologies, renewable energy for electricity generation is now competitive with fossil fuel generation technology. The global weighted average cost of electricity has reduced to a point that the use of renewable energy for baseload applications in small island states are no longer a political statement towards support for climate change, but are now an economic imperative that threatens the current business models of power utilities and fuel suppliers alike;

- *Cyber security and Cyber Attacks* are increasing in frequency and complexity. The Corporation has been subject to an increased number of attacks in recent years. Technology is a primary enabler of our competitiveness and any threat to our applications or the network will only increase the complexity, and costs of doing business;

- *Aging petroleum distribution infrastructure.* The assets of the Corporation are aging, and while petroleum products remain the primary energy driver of the economy, need to undergo various upgrades to meet the current code requirements for such facilities.

Financial Condition

The Corporation continues to invest all operating surplus into capital improvement projects that are for mandatory compliance, reduction of operating risk, structural cost reduction, improvements in operational efficiency or investment in coconut industry development.

There is a noticeable improvement in the condition and asset value of our oil distribution infrastructure as well as the levels of strategic oil inventory that maintains the current energy security of the nation and the current policies have also positively impacted our debt-to-equity ratio. We are now able to attract competitive long term financing to fund our proposed investments and obligations in the agricultural sector, as well as Phase II of the Asset Rehabilitation Program.

The following table summarizes the Corporation's financial position and results of operations as of and for the years ended December 31, 2017, 2016, and 2015.

Assets:	**2017**	**2016**	**2015**
Capital assets, net	$ 18,938,830	$ 16,350,090	$ 16,888,711
Cash	16,697,519	8,998,024	7,582,852
Inventory, net	6,956,412	6,521,950	5,563,851
Investments	2,300,339	2,007,764	1,871,223
Due from related parties	9,492,876	12,412,524	12,094,999
Receivables and other assets	5,401,352	4,152,451	3,013,444
Total assets	$ 59,787,328	$ 50,442,803	$ 47,015,080
Liabilities and Net Position:			
Current liabilities	$ 8,159,099	$ 5,659,971	$ 8,039,122
Noncurrent liabilities	4,067,394	2,284,049	2,284,049
Net position:			
Net investment in capital assets	16,071,791	16,350,090	16,888,711
Unrestricted	31,489,044	26,148,693	19,803,198
Total net position	47,560,835	42,498,873	36,691,909
Total liabilities and net position	$ 59,787,328	$ 50,442,803	$ 47,015,080
Revenues, Expenses and Changes in Net Position:			
Operating revenues	$ 47,017,995	$ 42,763,730	$ 47,637,303
Cost of goods sold	(30,419,682)	(24,947,476)	(31,190,027)
Gross profit	16,598,313	17,816,254	16,447,276
Operating expenses	(11,828,896)	(12,124,975)	(11,587,295)
Nonoperating revenues (expenses), net	292,635	115,595	(458,401)
Change in net position	$ 5,062,052	$ 5,806,874	$ 4,401,580

Major changes in the profit and loss and statement of net position components for CY17 are a result of:

a) The Corporation increased its one-year term Line of Credit with Bank of Guam (BOG) from US$10M to US$11M. The short term note with banks remained at a zero balance in CY2017 as a result of prudent cash management. The Corporation continues to invest its operating surplus into capital expenditure to reduce operating risks and strengthen oil distribution infrastructure, into strategic oil inventory to increase the energy security of the nation, and to execution of its strategy (VT2025) for the long term sustainability of the Corporation;

b) The lower operating expenses for 2017 are directly attributed to ongoing structured cost reduction initiatives implemented during the year;

c) The total amount received from sales of petroleum products exceeded the amount paid to vendors and employees for goods and services. The net cash provided by operating activities in 2017 was $6,516,303 as compared to $3,569,904 in 2016;

d) A total of $1,651,512 was used for capital and related financing activities mainly for the purchase of capital assets. The Corporation's total investments in capital assets, inclusive of construction in progress as of December 31, 2017 and 2016 were $18,938,830 and $16,350,090, respectively.

CAPITAL ASSETS AND DEBT MANAGEMENT

Capital Assets and Long-Term Debt: At the end of CY2017, the Corporation had $18.9 million net investment in capital assets. This represents an increase in net capital assets (including additions and deletions) of $2.6 million or 16% over the previous year. For additional information about the Corporation's capital assets, refer to Note 3 to the financial statements. The Corporation had a long-term debt of US$2.9 million outstanding at December 31, 2017. For additional information concerning long-term debt, please refer to Note 6 to the financial statements.

ECONOMIC OUTLOOK

Two main forms of energy are supplied in the market economy of FSM: fossil fuels by FSM Petroleum Corporation and electricity by four State owned power utilities, namely: Pohnpei Utilities Corporation (PUC), Kosrae Utilities Authority (KUA), Yap State Public Services Corporation (YSPSC) and Chuuk Public Utility Corporation (CPUC). It was estimated in 2010 that around 55% of households are connected to the electricity network[1].

The Household Income Expenditure Survey (HIES) indicated that with reducing or stressed household budgets and few new economic activities, that there will be a significant challenge in extending electricity access on commercially viable and or affordable arrangements to the remaining 45% of households. It is expected that an increase in the availability of low cost renewable forms of energy, coupled with an increased trade in coconut and coconut related products will ease the pressure on household incomes.

[1] Expression of Interest to Participate in SREP, Micronesia Climate Investment Funds: https://www-cif.climateinvestmentfunds.org/sites/default/files/meeting-documents/federated_states_of_micronesia_eoi_0.pdf

The Corporation is taking aggressive steps to adapt to either counter the hazards or embrace the opportunities that market and industry forces are applying on our business as usual. It has been working with the national government on a "Transformation Bill" that will further support the Strategic Plan for the transformation of the FSMPC business model from a successful fossil fuel importer and distributor to a i) low cost carbon free energy supplier, and ii) a exporter of high value agriculture products.

Management's Discussion and Analysis for the year ended December 31, 2016 is set forth in the report on the audit of FSMPC's financial statements, which is dated April 28, 2017. That Discussion and Analysis explains the major factors impacting the 2016 financial statements and may be obtained from the contact show below.

CONTACT

Questions associated with the above Management's Discussion and Analysis may be sent by post, addressed to Mr. Johnny Adolph, Chief Financial Officer, P.O. Box 1762, Kolonia, Pohnpei, FSM 96941 or via email to petrocorp@fsmpc.com.

FEDERATED STATES OF MICRONESIA PETROLEUM CORPORATION
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Net Position
December 31, 2017 and 2016

ASSETS	2017	2016
Current assets:		
Cash and cash equivalents	$ 16,697,519	$ 8,998,024
Trade receivables	1,545,563	2,239,873
Due from component unit	1,504,747	12,327,520
Other receivables	92,560	85,004
Inventory, net	6,956,412	6,521,950
Prepaid expenses	2,275,885	1,412,578
Total current assets	29,072,686	31,584,949
Investments	2,300,339	2,007,764
Prepaid expenses, net of current portion	892,584	-
Due from component unit, net of current portion	7,988,129	-
Other noncurrent asset	594,760	500,000
Capital assets:		
Nondepreciable capital assets	7,087,413	3,174,562
Other capital assets, net of accumulated depreciation	11,851,417	13,175,528
	$ 59,787,328	$ 50,442,803
LIABILITIES AND NET POSITION		
Current liabilities:		
Current portion of long-term debt	$ 547,028	$ -
Accounts payable - fuel	3,597,309	2,241,889
Accounts payable - other	1,065,112	622,922
Accrued liabilities and others	2,949,650	2,795,160
Total current liabilities	8,159,099	5,659,971
Long-term debt, net of current portion	2,320,011	-
Due to States and the FSM National Government	1,747,383	2,284,049
Total liabilities	12,226,493	7,944,020
Commitments and contingencies		
Net position:		
Net investment in capital assets	16,071,791	16,350,090
Unrestricted	31,489,044	26,148,693
Total net position	47,560,835	42,498,783
	$ 59,787,328	$ 50,442,803

See accompanying notes to financial statements.

VITAL ENERGY, INC.

Statements of Net Position
December 31, 2017 and 2016
Discretely Presented Component Unit

ASSETS		2017		2016
Current assets:				
Cash	$	8,896,598	$	12,529,991
Time certficates of deposit		400,000		400,000
Trade receivables		276,060		498,783
Inventory		5,616,378		5,489,067
Prepaid expenses		318,508		60,587
Total current assets		15,507,544		18,978,428
Property and equipment, net		139,045		223,277
	$	15,646,589	$	19,201,705
LIABILITIES AND NET POSITION				
Current liabilities:				
Accounts payable	$	79,542	$	2,078,382
Accrued liabilities and others		1,072,434		871,198
Current portion of long-term debt		480,000		-
Income tax payable		46,000		119,589
Due to primary government		1,504,747		12,327,520
Other current liabilities		53,333		467,730
Total current liabilities		3,236,056		15,864,419
Deferred tax liability		8,000		30,000
Long-term debt, net of current portion		1,680,000		-
Due to primary government, net of current portion		7,988,129		-
Other noncurrent liability		463,844		2,080,388
Total liabilities		13,376,029		17,974,807
Commitments and contingencies				
Net position:				
Net investment in capital assets		139,045		223,277
Unrestricted		2,131,515		1,003,621
Total net position		2,270,560		1,226,898
	$	15,646,589	$	19,201,705

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA PETROLEUM CORPORATION
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Revenue, Expenses, and Changes in Net Position
Years Ended December 31, 2017 and 2016

	2017	2016
Operating revenue:		
Sales and service income	$ 46,738,447	$ 42,630,453
Other	279,548	133,277
	47,017,995	42,763,730
Cost of goods sold	30,419,682	24,947,476
Gross profit	16,598,313	17,816,254
Operating expenses:		
Salaries and benefits	2,793,617	2,373,429
Depreciation and amortization	1,929,811	1,854,881
Professional fees	1,240,935	1,845,194
Taxes	1,212,082	1,237,844
Rent	1,022,226	865,489
Staff travel, training and development	802,972	981,324
Repairs and maintenance	674,019	762,729
Communications	321,841	215,428
Insurance	310,789	337,039
Contracted services	301,407	332,473
Corporate governance	272,142	440,591
Office supplies	176,303	247,021
Utilities	169,692	149,716
Fuel	65,569	60,260
Miscellaneous	535,491	421,557
Total operating expenses	11,828,896	12,124,975
Operating income	4,769,417	5,691,279
Nonoperating revenues (expenses):		
Investment income	292,575	136,541
Interest income (expense), net	60	(20,946)
Total nonoperating revenues (expenses), net	292,635	115,595
Change in net position	5,062,052	5,806,874
Net position at beginning of year	42,498,783	36,691,909
Net position at end of year	$ 47,560,835	$ 42,498,783

See accompanying notes to financial statements.

VITAL ENERGY, INC.

Statements of Revenue, Expenses, and Changes in Net Position
Years Ended December 31, 2017 and 2016
Discretely Presented Component Unit

	2017	2016
Operating revenue:		
Sales and service income	$ 16,567,138	$ 17,296,781
Cost of sales and services	(13,184,689)	(13,726,840)
Gross profit	3,382,449	3,569,941
Operating expenses:		
Rent	576,304	499,152
Insurance	474,485	349,423
Salaries and benefits	444,519	435,613
Professional fees	383,331	148,817
Corporate office shared services	224,280	107,682
Gross revenue/receipt tax	178,017	76,197
Travel and entertainment	167,471	91,438
Contracted services	147,841	185,884
Repairs and maintenance	129,808	178,902
Utilities	107,554	106,545
Communications	85,280	78,003
Depreciation	73,430	60,692
Bank charges	57,013	35,185
Income taxes	40,446	114,589
Office supplies	34,392	51,631
Fuel	34,256	26,730
Staff training and development	23,838	134,826
Miscellaneous	90,575	67,691
Total operating expenses	3,272,840	2,749,000
Operating income	109,609	820,941
Nonoperating revenues (expenses), net:		
Foreign exchange	733,765	(336,270)
Interest income	200,288	30,397
Total nonoperating revenues (expenses), net	934,053	(305,873)
Change in net position	1,043,662	515,068
Net position at beginning of year	1,226,898	711,830
Net position at end of year	$ 2,270,560	$ 1,226,898

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA PETROLEUM CORPORATION
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Cash Flows
Years Ended December 31, 2017 and 2016

	2017	2016
Cash flows from operating activities:		
Cash received from customers	$ 47,712,305	$ 42,441,341
Cash paid to suppliers for goods and services	(38,402,385)	(36,498,008)
Cash paid to employees for services	(2,793,617)	(2,373,429)
Net cash provided by operating activities	6,516,303	3,569,904
Cash flows from capital and related financing activities:		
Proceeds from long-term debt	3,000,000	-
Repayment of long-term debt	(132,961)	-
Acquisition of capital assets	(4,518,551)	(1,316,261)
Net cash used for investing activities	(1,651,512)	(1,316,261)
Cash flows from investing activities:		
Collections from (advances) to related parties	2,834,644	(317,525)
Investment income (loss)	60	(20,946)
Increase in other non-current asset	-	(500,000)
Net cash provided by (used for) investing activities	2,834,704	(838,471)
Net change in cash	7,699,495	1,415,172
Cash and cash equivalents at beginning of year	8,998,024	7,582,852
Cash and cash equivalents at end of year	$ 16,697,519	$ 8,998,024
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$ 4,769,417	$ 5,691,279
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	1,929,811	1,854,881
(Increase) decrease in assets:		
Trade receivables	694,310	(322,388)
Other receivables	(7,556)	-
Inventory and related deposit with supplier	(434,462)	(958,099)
Prepaid expenses	(1,755,891)	(316,619)
Other assets	(94,760)	-
Increase (decrease) in liabilities:		
Accounts payable	1,797,610	(5,883)
Accrued liabilities and others	154,490	(2,373,267)
Due to States and primary government	(536,666)	-
Net cash provided by operating activities	$ 6,516,303	$ 3,569,904

See accompanying notes to financial statements.

(1) Organization and Basis of Presentation

Federated States of Micronesia Petroleum Corporation (FSMPC or the Company) is a component unit of the Federated States of Micronesia (FSM) National Government (FSMNG). FSMPC was created under Public Law 15-08, as passed by the FSM Congress and which was signed into law on September 11, 2007, for the purpose of providing oil and gas distribution for the entire FSM.

FSMPC is governed by a seven-member Board of Directors appointed as follows:

- 1 member appointed by the President with the advice and consent of the FSM Congress to represent the FSMNG.
- 4 members appointed by each State governor to represent each of the States.
- 2 members from the private sector, appointed by the President with the advice and consent of the FSM Congress.

Coconut Development Unit (CDU) was established through Public Law No. 18-68 enacted on June 16, 2014, which dissolved the FSM Coconut Development Authority (CDA) and transferred the responsibility of coconut development to FSMPC. Effective January 1, 2015, CDU started operations and was created as a division of FSMPC; therefore, its financial position and activities are included in FSMPC's financial statements.

FSMPC's financial statements are incorporated into the financial statements of the FSM National Government as a component unit.

Basis of Accounting

The accounts of FSMPC are organized as a discretely presented component unit - proprietary fund of the FSM National Government. Proprietary funds are used by governmental units to account for operations that are financed and operated in a manner similar to a private business. This accounting is appropriate when costs of providing goods or services to the general public are to be financed primarily through user charges or where the periodic determination of net income is appropriate for accountability purposes. The accrual basis of accounting is utilized by proprietary funds. Under the accrual basis, revenues are recorded when earned, and expenses are recorded at the time the liabilities are incurred.

FSMPC utilizes the flow of economic resources measurement focus. Its financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units using the accrual basis of accounting. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The Statement of Net Position presents all of the FSMPC's assets and deferred outflows of resources, and liabilities and deferred inflows of resources, with the difference reported as net position. Net position is classified for accounting and reporting purposes into the following three net position categories:

- Net investment in capital assets - capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets as well as deferred outflows of resources and deferred inflows of resources that are attributable to those assets or related debt.

(1) Organization and Basis of Presentation, Continued

Basis of Accounting, Continued

- Restricted - restricted assets reduced by liabilities and deferred inflows of resources related to those assets that are subject to externally imposed stipulations.

- Unrestricted - the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All other revenues are reported as nonoperating. Operating expenses includes the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Operating revenues and expenses generally result directly from the operation and maintenance of the Company. Non-operating revenues and expenses result from capital and related financing activities as well as certain other non-recurring income and expense items.

Reporting Entity

Vital Energy, Inc. (Vital)

Vital Energy, Inc. is a legally separate entity which meets the criteria set forth for component units. Vital was incorporated on February 10, 2012 in Guam for the purpose of carrying on the operation of importation and sale of petroleum products, and operation, management and maintenance of petroleum storage terminals, international marine bunkering services, operation of road and aviation bridging tankers, and aviation refueling operations. On May 22, 2015, Vital established Vital Energy, Inc. (Nauru) (the "Nauru Branch"), a foreign branch operation in the Republic of Nauru for the purpose of providing fuel supply and distribution in Nauru under an agreement with the Government of Nauru (GON). Vital's main operations are in Guam and Nauru effective June 2015. Copies of Vital's report can be obtained by contacting Vital management. Vital's significant notes are summarized in Note 2J.

(2) Summary of Significant Accounting Policies

A. Cash and Cash Equivalents

Custodial credit risk is the risk that in the event of a bank failure, the Company's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. FSMPC does not have a deposit policy for custodial credit risk.

(2) Summary of Significant Accounting Policies, Continued

A. Cash and Cash Equivalents, Continued

For purposes of the statements of net position and of cash flows, cash and cash equivalents represent cash on hand, cash in bank accounts and time certificates of deposits with maturity of up to ninety days. As of December 31, 2017 and 2016, total carrying amounts of cash and cash equivalents were $16,697,519 and $8,998,024, respectively, and the corresponding bank balances were $17,223,075 and $9,151,765, respectively, which were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2017 and 2016, bank deposits in the amount of $250,000 were subject to FDIC insurance. Bank balances in excess of FDIC insurance are not collateralized.

B. Investments

Investments held by the Company consist of money market funds, fixed income securities, exchange-traded funds, and common stock. Investments and related investment earnings or loss are recorded at fair value using quoted market prices. Fair value is the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the date of which the fair value of an asset or liability is determined.

As of December 31, 2017 and 2016, investments at fair value are as follows:

	2017	2016
Fixed income securities:		
Domestic fixed income	$ 495,666	$ 476,703
International fixed income	205,829	200,567
	701,495	677,270
Other investments:		
Common equities	1,020,710	828,406
Exchange traded funds	539,007	443,864
Money market funds	39,127	58,224
	1,598,844	1,330,494
	$ 2,300,339	$ 2,007,764

As of December 31, 2017, the Company's fixed income securities had the following maturities:

Investment Type	Fair value	Less than 1 year	1 to 5 years	5 to 10 years	More than 10 years
International bonds	$ 205,829	$ 205,829	$ -	$ -	$ -
Corporate bonds	213,784	-	14,456	168,731	30,597
U.S. Government Agency Bonds	281,882	-	159,280	80,578	42,024
	$ 701,495	$ 205,829	$ 173,736	$ 249,309	$ 72,621

(2) Summary of Significant Accounting Policies, Continued

B. Investments, Continued

As of December 31, 2016, the Company's fixed income securities had the following maturities:

Investment Type	Fair value	Less than 1 year	1 to 5 years	5 to 10 years	More than 10 years
Mortgage and asset-backed securities	$ 81,868	$ -	$ 81,868	$ -	$ -
International bonds	200,567	200,567	-	-	-
Corporate bonds	208,238	-	14,248	164,819	29,171
U.S. Government Agency Bonds	186,597	-	92,863	48,936	44,798
	$ 677,270	$ 200,567	$ 188,979	$ 213,755	$ 73,969

The Company's exposure to credit risk at December 31, 2017 and 2016, was as follows:

Moody's Rating	2017	2016
AAA	$ 281,882	$ 268,464
A1	-	13,844
A2	43,943	29,518
A3	108,407	90,642
BAA1	30,740	28,956
BAA2	15,291	30,088
BAA3	15,403	15,191
Not rated	205,829	200,567
	$ 701,495	$ 677,270

The Company categorizes its fair value measurements within the fair value hierarchy established by GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The Company has the following recurring fair value measurements as of December 31, 2017 and 2016:

		Fair Value Measurements Using		
	December 31, 2017	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level:				
Fixed income securities	$ 701,495	$ -	$ 701,495	$ -
Equity securities	1,020,710	1,020,710	-	-
Exchange-traded funds	539,007	539,007	-	-
Total investments by fair value level	2,261,212	$ 1,559,717	$ 701,495	$ -
Investments measured at amortized cost:				
Money market funds	39,127			
	$ 2,300,339			

(2) Summary of Significant Accounting Policies, Continued

B. Investments, Continued

		Fair Value Measurements Using		
	December 31, 2016	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level:				
Fixed income securities	$ 677,270	$ -	$ 677,270	$ -
Equity securities	828,406	828,406	-	-
Exchange-traded funds	443,864	443,864	-	-
Total investments by fair value level	1,949,540	$ 1,272,270	$ 677,270	$ -
Investments measured at amortized cost:				
Money market funds	58,224			
	$ 2,007,764			

C. Accounts Receivable

Accounts receivable are due from businesses and individuals located in the FSM and are interest free and uncollateralized, except those from utility companies. The allowance for doubtful accounts is stated at an amount which management believes will be adequate to absorb potential losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. Bad debts are written-off against the allowance based on the specific identification method. At December 31, 2017 and 2016, the Company is of the opinion that an allowance for doubtful accounts is not necessary.

D. Inventory

Inventory is substantially carried at the lower of cost (moving average cost) or market value. At December 31, 2017 and 2016, inventory consists of the following:

	2017	2016
Inventory on hand:		
Fuel	$ 5,971,356	$ 5,400,487
Lubricants	398,375	485,355
Chemicals	86,226	89,627
Others	457,054	407,326
	6,913,011	6,382,795
Inventory in transit:		
Fuel	93,988	189,742
	7,006,999	6,572,537
Less allowance for obsolescence	(50,587)	(50,587)
	$ 6,956,412	$ 6,521,950

(2) Summary of Significant Accounting Policies, Continued

E. Prepaid Expenses

Advance payments relating to goods and services not yet received are recorded as prepaid expenses. Prepayments that are expected to be utilized beyond one year, mainnly relating to prepaid land leases (see Note 10), are presented as noncurrent assets.

F. Property, Plant and Equipment

The Company capitalizes individual items with estimated useful lives of more than one year without regard to a capitalization threshold. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the assets. Estimated useful lives of property and equipment are as follows:

Buildings	15 years
Motor vehicles	5 years
Plant and equipment	3 to 15 years
Furniture and fixtures	4 years
Office equipment	4 to 8 years
Machinery and equipment	4 years

G. Capitalized Interest

Interest cost for assets that require time to bring them to the condition and location necessary for their intended use is capitalized as part of the asset cost until such time as the assets are placed in service. The Company did not have capitalized interest for the years ended December 31, 2017 and 2016.

H. Taxes

The Company is responsible for gross receipt taxes, sales taxes and import taxes on its operations in the FSM.

I. New Accounting Standards

During the year ended December 31, 2017, the Company implemented the following pronouncements:

- GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements 67 and 68 with the reporting requirements in Statement 68.

- GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, as amended*, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and addresses financial reporting requirements for governments whose employees are provided with postemployment benefits other than pensions (other postemployment benefits or OPEB).

- GASB Statement No. 80, *Blending Requirements for Certain Component Units - an amendment of GASB Statement No. 14*, which improves financial reporting by clarifying the financial statement presentation requirements for certain component units.

(2) Summary of Significant Accounting Policies, Continued

I. New Accounting Standards, Continued

- GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements,* which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement.
- GASB Statement No. 82, *Pension Issues - an amendment of GASB Statements No. 67, No. 68, and No. 73*, which addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

The implementation of these statements did not have a material effect on the accompanying financial statements.

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which addresses accounting and financial reporting for certain asset retirement obligations (AROs) associated with the retirement of a tangible capital asset. The provisions in Statement No. 83 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*, which establishes criteria for identifying fiduciary activities of all state and local governments. The provisions in Statement No. 84 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In March 2017, GASB issued Statement No. 85, *Omnibus 2017*, which address practice issues that have been identified during implementation and application of certain GASB Statements including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits). The provisions in Statement No. 85 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In May 2017, GASB issued Statement No. 86, *Certain Debt Extinguishment Issues*, which improves consistency in accounting and financial reporting for in-substance defeasance of debt. The provisions in Statement No. 86 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

(2) Summary of Significant Accounting Policies, Continued

I. New Accounting Standards, Continued

In June 2017, GASB issued Statement No. 87, *Leases*, which establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. The provisions in Statement No. 87 are effective for fiscal years beginning after December 15, 2019. Management has yet to determine whether the implementation of this statement will have a material effect on the financial statements.

J. Management Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

K. Vital's Accounting Policies

Cash and Cash Equivalents and Time Certificates of Deposit. Custodial credit risk is the risk that in the event of a bank failure, Vital's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. Vital does not have a deposit policy for custodial credit risk.

For purposes of the statements of net position, cash and cash equivalents represent cash on hand, cash in bank accounts and time certificates of deposits with maturity of up to ninety days. Time certificates of deposit with original maturities greater than ninety days are separately classified. As of December 31, 2017 and 2016, total carrying amounts of cash and cash equivalents and time certificates of deposits were $2,652,154 and $3,802,564, respectively, and the corresponding bank balances were $2,370,875 and $3,813,739, respectively, which were maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2017 and 2016, bank deposits in the amount of $250,000 were subject to FDIC insurance. Bank balances in excess of FDIC insurance are not collateralized.

Cash with Bendigo Adelaide Bank Limited

As of December 31, 2017 and 2016, Vital maintains bank balance of $6,644,444 and $9,127,427, respectively, with Bendigo Adelaide Bank Limited (Bendigo), an authorized deposit-taking institution (ADI) subject to the Australian Government Financial Claims Scheme (FCS). FCS provides guarantee on deposits up to a limit of AUD$250,000 for each account holder, which was extended to branches of Bendigo in Nauru. As of December 31, 2017 and 2016, bank deposits of approximately $192,000 and $180,000, respectively, were subject to FCS guarantee. Balances in excess of FCS guarantee are not collateralized.

(2) Summary of Significant Accounting Policies, Continued

K. Vital's Accounting Policies, Continued

Trade Receivables. Vital grants credit to customers, the majority of whom are located in Nauru. Accounts receivable are recorded at the invoiced amount, net of an allowance for doubtful accounts, and do not bear interest. The allowance for doubtful accounts is stated at an amount which management believes will be adequate to absorb potential losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. Bad debts are written-off against the allowance based on the specific identification method. At December 31, 2017 and 2016, Vital deems it not necessary to establish an allowance for doubtful accounts.

Due to Primary Government. Due to Primary Government are amounts due to FSM Petroleum Corporation for fuel purchases and advances. Balances with FSMPC are non-interest bearing. As of December 31, 2017, the parties agreed that the balance is to repaid over the remainining term of Vital's Petroleum Supply and Facility Management Agreement with GON through 2025, and as such $7,988,129 is presented as noncurrent.

Inventory. Inventory mainly represents fuel and is substantially carried at the lower of cost (moving average cost) or market value.

Revenue Recognition. Vital's revenues are derived mainly from sale of fuel. Fuel sales are recognized when charged to customers' charge accounts, when merchandise is delivered to customers, and when title is passed and collectability is reasonably assured. Service income is recognized based on GPA contract through September 30, 2017 (see note 9), typically earned monthly. Other income, mainly representing cost reimbursements for major operation and maintenance project activities, is billed and accrued upon completion of the project.

Property and Equipment. Vital capitalizes individual items with estimated useful lives of more than one year without regard to a capitalization threshold. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the assets. Estimated useful lives of property and equipment are as follows:

Motor vehicles	5 years
Computer equipment	5 years
Furniture and fixtures	7 years
Machinery and equipment	7 years

Taxes. Vital is taxed and files its income tax return in Guam. The Guam income tax code is similar to that of the United States of America. Vital also pays a Business Profits Tax (BPT) in Nauru under the Republic of Nauru Business Tax Act (the "Act"), which was enacted and became effective in July 2016. BPT is generally 10% of taxable income, as defined in the Act, for tax payers with annual taxable income under $15 million. BPT is taken as a foreign tax credit (FTC) on the Guam income tax return, with certain limitations. Disallowed FTC in a given tax year, due to difference in statutory tax rates between the jurisdictions, may be carried over up to 10 years. Total BPT approximated $156,210 and $39,305, respectively, for the years ended December 31, 2017 and 2016 and are included as a component of taxes in Vital's statements of revenues, expenses and changes in net position.

(2) Summary of Significant Accounting Policies, Continued

K. Vital's Accounting Policies, Continued

Taxes, Continued., Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and net operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income or expense in the period that includes the enactment date.

For Guam income tax purposes, a tax year generally remains open to assessment and collection for three years after the later of the due date for filing a tax return or the date on which the tax payer files its return.

Income tax expense for the years ended December 31, 2017 and 2016 consisted of the following:

	2017	2016
Current	$ 62,446	$ 95,589
Deferred	(22,000)	19,000
Total	$ 40,446	$ 114,589

The differences between the effective income tax rate and the statutory rate of 34% in 2017 are principally due to correction of prior year accrual, recognition of foreign tax credits for Nauru operations and recognition of net operating losses carryovers that were previously fully allowed in 2016.

At December 31, 2017 and 2016, deferred tax liability of $8,000 and $30,000, respectively, relates mainly to difference in fixed assets depreciation.

In December 2017, the "U.S. Tax Cut and Jobs Act" was signed into law, which includes a change in corporate income tax rate. The change resulted in approximately $5,000 income tax benefit adjustment to recorded deferred taxes based on the new tax rate of 21% in the period of tax enactment.

L. Reclassifications

Certain balances in the 2016 financial statements have been reclassified to conform with the 2017 financial statement presentation.

(3) Capital Assets

FSM Petroleum Corporation

Capital asset activities for the years ended December 31, 2017 and 2016 are as follows:

(3) Capital Assets, Continued

FSM Petroleum Corporation, Continued

	Balance at January 1, 2017	Transfers and Additions	Transfers and Deletions	Balance at December 31, 2017
Buildings	$ 999,086	$ 53,317	$ -	$ 1,052,403
Motor vehicles	1,483,084	28,166	-	1,511,250
Plant and equipment	13,056,862	260,634	-	13,317,496
Furniture and fixtures	292,824	4,957	-	297,781
Office equipment	5,064,815	154,284	-	5,219,099
Machinery and equipment	916,231	104,342	-	1,020,573
	21,812,902	605,700	-	22,418,602
Less accumulated depreciation	(8,637,374)	(1,929,811)	-	(10,567,185)
	13,175,528	(1,324,111)	-	11,851,417
Construction in progress	3,174,562	4,504,918	(592,067)	7,087,413
	$ 16,350,090	$ 3,180,807	$ (592,067)	$ 18,938,830

	Balance at January 1, 2016	Transfers and Additions	Transfers and Deletions	Balance at December 31, 2016
Buildings	$ 990,486	$ 8,600	$ -	$ 999,086
Motor vehicles	1,173,216	471,617	(161,749)	1,483,084
Plant and equipment	11,787,068	1,269,794	-	13,056,862
Furniture and fixtures	217,973	74,851	-	292,824
Office equipment	4,904,549	160,266	-	5,064,815
Machinery and equipment	742,781	173,450	-	916,231
	19,816,073	2,158,578	(161,749)	21,812,902
Less accumulated depreciation	(6,865,675)	(1,854,881)	83,182	(8,637,374)
	12,950,398	303,697	(78,567)	13,175,528
Construction in progress	3,938,313	1,135,313	(1,899,064)	3,174,562
	$ 16,888,711	$ 1,439,010	$ (1,977,631)	$ 16,350,090

Vital Energy, Inc.

Capital asset activities for the years ended December 31, 2017 and 2016 are as follows:

	Balance at January 1, 2017	Transfers and Additions	Transfers and Deletions	Balance at December 31, 2017
Motor vehicles	$ 64,309	$ -	$ -	$ 64,309
Plant and equipment	1,207	78	-	1,285
Computer equipment	204,129	2,451	-	206,580
Furniture and fixtures	27,619	6,888	-	34,507
Machinery and equipment	37,866	810	(5,400)	33,276
	335,130	10,227	(5,400)	339,957
Less accumulated depreciation	(131,253)	(73,430)	3,771	(200,912)
	203,877	(63,203)	(1,629)	139,045
Construction in progress	19,400	-	(19,400)	-
	$ 223,277	$ (63,203)	$ (21,029)	$ 139,045

(3) Capital Assets, Continued

Vital Energy, Inc., Continued

	Balance at January 1, 2016	Transfers and Additions	Transfers and Deletions	Balance at December 31, 2016
Motor vehicles	$ 33,158	$ 31,151	$ -	$ 64,309
Plant and equipment	1,224	-	(17)	1,207
Computer equipment	165,635	38,494	-	204,129
Furniture and fixtures	9,741	17,878	-	27,619
Machinery and equipment	20,943	16,923	-	37,866
	230,701	104,446	(17)	335,130
Less accumulated depreciation	(70,561)	(60,692)	-	(131,253)
	160,140	43,754	(17)	203,877
Construction in progress	-	19,400	-	19,400
	$ 160,140	$ 63,154	$ (17)	$ 223,277

(4) Due to States and the FSM National Government

In 2008, the FSMNG was extended a ¥200,000,000 grant by the Government of Japan ("the Grant"). The Grant and accrued interest shall be used by the FSMNG properly and exclusively for the purchase of products enumerated in a list to be mutually agreed upon between the two governments. The Grant shall be received by the FSMNG in Yen currency, shall be used as described above within a period of twelve months and any excess amounts shall be refunded to the Government of Japan thereafter. The FSMNG is required to deposit in Micronesian currency (US dollars) all the proceeds from the sale and lease of the products purchased referred to above. The amount of the proceeds to be deposited shall not be less than half of the total yen disbursement paid with respect to the purchase of the products. The deposit shall be made within the period of three years from the date of entry into force of the understanding between the two governments. The deposited fund shall be utilized for economic and social development purposes in the FSM.

In 2009, FSMPC signed a memorandum of agreement with the FSMNG that the Grant be utilized for the supply of petroleum fuels to FSMPC to assist in the implementation of a number of initiatives aimed at mitigating the social and economic difficulties caused by volatile and sustained high oil prices. The Grant was paid directly by the Government of Japan through an independent procurement agent, Crown Agents, to FSMPC's supplier of fuel instead of to the FSMNG. FSMPC received the equivalent gallons of fuel from the supplier and this is now maintained as strategic inventory in each State. As of December 31, 2017 and 2016, FSMPC recognized a liability to the States and the FSMNG of $1,247,383 and $1,784,049, respectively.

At December 31, 2017 and 2016, the remaining $500,000 represents a non-interest bearing advance payable to the FSMNG. There is no specific repayment terms and management has classified the advance as long-term since it has no expectation that such will have to be repaid before December 31, 2018.

(5) Short-Term Borrowings

As of December 31, 2017 and 2016, the Company has a bank line of credit facility (LOC) to facilitate fuel inventory purchases of $7,000,000 and $10,000,000, respectively, expiring on September 13, 2018 and July 30, 2017, respectively.

Additionally, on September 15, 2017, the Company obtained an LOC of $11,000,000 for working capital requirements for 12 months and $6,034,500 for the coconut production facility contractor for 12 months.

The LOCs and the related long-term obligations are secured and collateralized by an executed Pledge and Security Agreement for the assignment of the Reserve Bank Account and Revenue, an executed Notice of Security Interest and Chattel Mortgage and are guaranteed by the FSM National Government.

Borrowings against the LOCs bear interest at the bank's effective reference rate plus 0.75%, with minimum rate of 5.75% per annum, with interest payable monthly and principal due within 180 days. No drawdowns were made against the LOCs during the years ended December 31, 2017 and 2016. Furthermore, no borrowings are outstanding against the LOCs at December 31, 2017 and 2016.

(6) Long-term Debt

FSM Petroleum Corporation

In 2017, the Company obtained a $3,000,000 bank note from the FSM Development Bank (FSMDB), a component unit of the FSM National Government, for capital assets acquisition. Long-term debt is due in quarterly installments of $170,461 beginning August 31, 2017 to September 25, 2022, with interest fixed at 5% per annum. The loan is collateralized by the Company's inventories and related petroleum products. Future minimum loan repayments are as follows:

Year Ending December 31,	Principal	Interest	Total
2018	$ 547,028	$ 134,817	$ 681,845
2019	576,123	105,722	681,845
2020	605,225	76,620	681,845
2021	636,307	45,538	681,845
2022	502,356	12,960	515,316
	$ 2,867,039	$ 375,657	$ 3,242,696

Vital Energy, Inc.

In 2017, Vital obtained a $2,400,000 non-interest bearing, uncollateralized advance from its fuel vendor to fund capital project expenditures incurred on behalf of the GON under the Agreement (see note 9). The advance is payable in equal quarterly installments of $120,000, beginning on September 5, 2017. Future repayments are $480,000 for each of the years ending December 30, 2018 through 2021 and $240,000 in the year ending December 31, 2022.

(7) Changes in Long-Term Liabilities

Changes in long-term liabilities for the years ended December 31, 2017 and 2016 are as follows:

FSM Petroleum Corporation

	Balance at January 1, 2017	Additions	Repayments	Balance at December 31, 2017	Due Within One Year
Due to States and the FSM National Government	$ 2,284,049	$ -	$ (536,666)	$ 1,747,383	$ -
Long-term debt	-	3,000,000	(132,961)	2,867,039	547,028
	$ 2,284,049	$ 3,000,000	$ (669,627)	$ 4,614,422	$ 547,028

	Balance at January 1, 2016	Additions	Repayments	Balance at December 31, 2016	Due Within One Year
Due to States and the FSM National Government	$ 2,284,049	$ -	$ -	$ 2,284,049	$ -

Vital Energy, Inc.

	Balance at January 1, 2017	Additions	Reductions	Balance at December 31, 2017	Due Within One Year
Deferred tax liability	$ 30,000	$ -	$ (22,000)	$ 8,000	$ -
Long-term note payable	-	2,400,000	(240,000)	2,160,000	480,000
Due to primary government	12,327,520	-	(2,834,644)	9,492,876	1,504,747
Other noncurrent liability	2,080,388	3,291,223	(4,907,767)	463,844	-
	$ 14,437,908	$ 5,691,223	$ (8,004,411)	$ 12,124,720	$ 1,984,747

	Balance at January 1, 2016	Additions	Reductions	Balance at December 31, 2016	Due Within One Year
Deferred tax liability	$ 11,000	$ 19,000	$ -	$ 30,000	$ -
Due to primary government	12,001,569	325,951	-	12,327,520	12,327,520
Other noncurrent liability	653,858	1,658,452	(231,922)	2,080,388	-
	$ 12,666,427	$ 2,003,403	$ (231,922)	$ 14,437,908	$ 12,327,520

(8) Risk Management

Insurance Risk

FSM Petroleum Corporation

The Company purchases commercial insurance to cover its potential risks from refueling operations, inventory and facilities. It also maintains workmen's compensation coverage. It is substantially self-insured for all other risks. Management is of the opinion that no material losses have been sustained as a result of this practice during the past three years.

(8) Risk Management, Continued

Vital Energy, Inc.

Vital purchases commercial insurance to cover potential risks from managing, operating and maintaining GPA's fuel bulk storage facility and Government of Nauru bulk fuel facilities. Vital is substantially sell-insured for all other risks. Management is of the opinion that no material losses have been sustained as a result of this practice.

Foreign Currency Risk

Vital's transactions in its Nauru branch are settled in a foreign currency. Vital is exposed to the risk of unfavorable changes in the exchange rate that may occur.

(9) Concentration Risk and Significant Customers

FSM Petroleum Corporation

Revenue from one major customer, Pohnpei Utilities Corporation, for the years ended December 31, 2017 and 2016 approximated 16% and 15%, respectively, of the Company's total revenue, and receivable of $619,212 and $1,017,391 as of December 31, 2017 and 2016, respectively.

The Company purchased substantially all fuel from one supplier in 2017 and 2016.

Vital Energy, Inc.

Guam Power Authority (GPA)

Vital had a contract with GPA to manage, operate and maintain GPA's fuel bulk storage facility which was terminated effective September 30, 2017. The contract was for an annual fixed fee of $675,273 payable monthly by GPA. Vital was required to seek approval from GPA for all major operation and maintenance activities exceeding $5,000 which are to be billed separately from monthly payments. Service fee revenues of $511,692 and $679,773 were earned from the GPA contract for the years ended December 31, 2017 and 2016, respectively. As of December 31, 2017 and 2016, Vital has $0 and $114,010, respectively, receivable from GPA. In connection with the agreement, Vital is exposed to certain compliance requirements by the U.S. Environmental Protection Agency (USPA) that may result in penalties and fines. At December 31, 2017, Vital has accrued for a potential liability of $190,000.

Government of Nauru (GON)

Effective June 1, 2015, Vital entered into a Petroleum Supply and Facility Management Agreement (the Agreement) with the GON for a period of five years, with an option to extend for another five years. Vital was appointed to perform: (a) procure the supply of fuel and delivery to the facilities, (b) operate and maintain the facilities for the receipt, storage and distribution of products, (c) sell and distribute products to meet all inland demand, and (d) provide expert advice, technical assistance and other services as GON may reasonably require in related to the matters of the agreement. Vital uses nine tankers in GON's facilities at the storage terminal located in Aiwo District, Republic of Nauru.

(9) Concentration Risk and Significant Customers, Continued

Government of Nauru (GON), Continued

The Agreement allows Vital to charge prices based on Nauru Price Template (NPT). For the years ended December 31, 2017 and 2016, Vital recorded fuel sales of $16.0 million and $16.6 million, respectively. As of December 31, 2017 and 2016, Vital recorded mooring fees liability of $452,199 and $533,170, respectively, and throughput fee liability of $11,645 and $1,547,217, respectively, for the purpose of funding the facilities' mooring system repairs and improvements and Compliance and Integrity Projects, which are included in the other noncurrent liability account in the statements of net position.

Vital's revenue from three major customers for the years ended December 31, 2017 and 2016 approximated 71% and 67%, respectively, of Vital's total revenue, and total receivable of $227,662 and $402,663 at December 31, 2017 and 2016, respectively.

Vital purchased substantially all fuel from one supplier in 2017 and 2016.

(10) Commitments and Contingencies

Leases

FSM Petroleum Corporation

The Company leases land, warehouse, airport facilities and other such space through various leases expiring through 2035. Certain lease agreements contain options to renew with rent escalations. Three lease agreements require additional lease payments contingent on the level of gallons sold by the Company from that leased facility. In 2017, the Company entered into sixteen lease agreements for land situated on Tonoas Island, Chuuk State, for the new CDU project site. The agreements have an initial term of twenty-years, with certain options to renew, and require an initial seven-year prepayment. At December 31, 2017, unamortized balance of prepayments totaling $1,086,610, of which $194,026 is presented as current in the accompanying statement of net position.

Future minimum lease payments are as follows:

Year Ending December 31,	
2018	$ 578,000
2019	347,000
2020	317,000
2021	320,000
2022	306,000
2023-2027	1,247,000
2028-2032	1,070,000
2033-2037	909,000
	$ 5,094,000

(10) Commitments and Contingencies, Continued

Leases

Vital Energy, Inc.

In connection with Vital's exclusive right to access, use and occupy the GON bulk fuel facilities, Vital is required to pay annual rent fee of $529,168 over the 5-year term of the agreement from June 1, 2015 to May 31, 2020. Future minimum lease payments are as follows:

Year Ending December 31,	
2018	$ 529,168
2019	529,168
2020	220,487
	$ 1,278,823

Sales

The Company has entered into agreements to sell fuel at an agreed pricing method. The agreements are for one year and automatically renew at the end of their respective terms every 30 days unless terminated by either party.

Bank Loan

In September 2017, the Company entered into a $5 million commitment letter with a bank. No loan disbursement was received as of December 31, 2017.

Litigation

The Company is a defendant in several legal actions. The ultimate outcome is presently undeterminable; however, Company management is of the opinion that resolution of these matters will not have a material effect on the accompanying financial statements.

(11) Related Parties

FSMPC sells fuel to the four utility companies in the FSM namely: Pohnpei Utilities Corporation, Chuuk Public Utility Corporation, Kosrae Utility Authority, and Yap State Public Corporation. Total fuel sales of $15.2 million and $13.0 million was earned from the four utility companies for the years ended December 31, 2017 and 2016, respectively. As of December 31, 2017 and 2016, FSMPC has total receivables of $1.1 million and $1.8 million, respectively, from the four utility companies. In addition, as of December 31, 2017 and 2016, FSMPC has accrued liabilities in the form of letters of credit to the Pohnpei Utilities Corporation and Chuuk Public Utility Corporation totaling $1,206,606 and $1,006,036, respectively, in connection with fuel purchases price variances, which are included as a component of accrued liabilities and others in the statements of net position.

(11) Related Parties, Continued

FSMPC purchased fuel on behalf of Vital in 2015. As of December 31, 2017 and 2016, FSMPC recorded $9,129,289 and $11,803,666, respectively, as a receivable from Vital for fuel purchases which is included as a component of Due from related parties account in the statements of net position, of which $1,504,748 is presented as current portion as of December 31, 2017. The remaining receivable of $363,587 and $523,854 as of December 31, 2017 and 2016, respectively, included advances and non-fuel disbursements made on behalf of Vital and other related parties.

Additionally, effective June 1, 2016, the Company entered into a Shared Services Agreement (the Agreement) with Vital. Under the agreement, which expires May 31, 2025, the Company charges Vital for certain administrative and support costs. Total costs charged by the Company approximated $224,280 and $107,682 for the years ended December 31, 2017 and 2016, respectively, and are included as a component of other income in the accompanying statement of revenues, expenses, and changes in net position.

(12) Subsequent Events

On April 24, 2018, the Company entered into a joint venture (JV) agreement with SB Energy Corporation for a project to contruct and operate a solar facility and energy storage system in state of Chuuk in the FSM.

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

The Board of Directors
Federated States of Micronesia Petroleum Corporation:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Federated States of Micronesia Petroleum Corporation (the Company), which comprise the statement of net position as of December 31, 2017, and the related statements of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated June 28, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Company's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we do not express an opinion on the effectiveness of the Company's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as item 2017-002 that we consider to be significant deficiencies.

Deloitte.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as item 2017-001.

The Company's Response to Findings

The Company's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Responses. The Company's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Company's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Deloitte & Touche LLP

June 28, 2018

Finding No.: 2017-001

Procurement Documents

Criteria: Procurement transactions shall provide for full and open competition that is best suited to the circumstances.

Condition: Procurement documents evidencing full and open competition or vendor selection were either not provided or partially provided for all expenditures tested aggregating $2,159,000. For procurement documents partially provided amounting to $1,812,000, we are unable to determine whether proper procurement procedures were followed as the entity does not have completed or finalized procurement policy procedures in place.

Cause: The cause of the above condition is lack of established procurement policies and regulations.

Effect: The effect of the above condition is potential noncompliance with competitive procurement.

Recommendation: We recommend that the Company complete a procurement manual entailing standard procedures to maximize full and open competition.

Identification as a Repeat Finding: Finding 2016-001

Auditee Response and Corrective Action Plan: Management concurs with the finding. To complement and strengthen what was rolled out last year by Ultima Training & Consulting Services last year, the Company has engaged with Procurement and Supply Institute of Asia (PASIA) to produce a procurement policy and provide training for the staff. It is expected to drive Value-for-Money (VFM) and to be compliant with the most recent Multilateral Development Banks harmonized procurement guidelines.

Finding No.: 2017-002

Construction-in-Progress (CIP) Project Monitoring

Criteria: An effective system of internal control includes policies and procedures related to periodic monitoring of capital project status that includes coordination between project management and the finance and accounting personnel.

Condition: The following construction in progress matters were noted:

1. Project status reports or equivalent documentation could not be provided timely, which resulted in various adjusting entries during the course of audit in March 2018.

2. Seven (7) open projects approximating $860,000 with no recent costs incurred was noted as of December 31, 2017, Specifically, two projects with cost of $358,000 is on hold as such ultimate realization is uncertain. Moreover, no invoices provided for one project amounting to $156,000.

3. Expense items (e.g., food allowance, travel, hotel expenses and professional fees not directlt attributable in bring the asset on its working condition) approximately amounting to $195,000 was capitalized as CIP. Approximately $19,000 was corrected through adjusting journal entries while the remaining balance is still under review.

Cause: The cause of the above condition is lack of periodic monitoring of capital projects status between project management and accounting personnel.

Effect: The effect of the above condition is a potential misstatement of capitalized assets and related expenses.

Recommendation: We recommend that management conduct a comprehensive and periodic review of CIP projects. Quarterly reports as to percentage of completion should be obtained from the project managers. FSMPC should also review all project codes to determine those that are no longer relevant and valid. Further, FSMPC should strengthen control procedures over determining and identifying costs that are allowed to be capitalized in accordance with applicable accounting standards.

Identification as a Repeat Finding: Finding 2016-002

Auditee Response and Corrective Action Plan: Management concurs with the finding. A project management unit called Strategy Execution Team has been established. It is staffed with full time personnel comprising process guidance officers, project managers, project engineers, economists and accountants. The Team primary goal is aimed at improving the effectiveness of results delivery in the Company, improve Client engagement, and deliver projects on time, on scope, and within budget. The Team is now in its second year and while the progress is slow in the early stages, the Company expects to see results after year 2 or 3 after everything from policies, procedures, and systems are completely embedded in its day to day activities.