

RENEWABLE ENERGY DEVELOPMENT PROJECT

ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM(SF)

FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

FOR THE YEAR ENDED SEPTEMBER 30, 2022

**RENEWABLE ENERGY DEVELOPMENT PROJECT
FOR THE YEAR ENDED SEPTMBER 30, 2022**

TABLE OF CONTENTS

Independent Auditors' Report.....	1 - 2
Financial Statement:	
Statement of Financial Performance.....	3
Statement of Financial Position.....	4
Notes to Financial Statements.....	5 - 12
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.....	13 - 14
Independent Auditors' Report on Compliance with Financial Covenant Requirements of the Grant Agreement	15 - 17
Schedule of Findings and Responses	18 - 20



FEDERATED STATES OF MICRONESIA

Office of The National Public Auditor

P.O. Box PS-05, Palikir, Pohnpei FSM 96941

Tel: (691) 320-2862/2863 Fax: (691) 320-5482

CID Hotline: (691) 320-6768; Website: www.fsmopa.fm

Facebook: FSM Office of the National Public Auditor; E-mail: info@fsmopa.fm

INDEPENDENT AUDITORS' REPORT

Honorable Eugene Amor
Secretary, Department of Finance & Administration
Federated States of Micronesia:

Report on the Financial Statements

We have audited the accompanying financial statements of the Renewable Energy Development Project which comprise the statement of financial position as of and for the year ended September 30, 2022 and 2021, and the related statement of financial performance for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statement

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, and for 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 an opinion 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. 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 judgement, 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 opinion.

Opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Renewable Energy Development Project as of September 30, 2022, and the results of its operations for the year then ended in accordance with accounting principles generally accepted in the United States of America.

We draw attention to Note 2 of the financial statement, which describes the basis of accounting.

Other Matters

In accordance with *Government Auditing Standards*, we have also issued our report dated April 12, 2023 on our consideration of the Project's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and the grant agreement. 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 Project'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 Project's internal control over financial reporting and compliance.



Haser Hainrick
National Public Auditor

Palikir, Pohnpei
April 12, 2023

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM (SF)**

**Statement of Financial Performance
For the Years Ended September 30, 2022 and 2021**

	October 01, 2021 to September 30, 2022 (\$)	December 03, 2019 to September 30, 2021 (\$)
Revenues		
Grant Revenue from ADB	892,583	160,569
Total Revenues	892,583	160,569
Expenditures		
Project Management and Other Expenses		
Output 1: Yap Renewable Energy	331,390	-
Output 2: Kosrae Main Grid Renewable Energy	342,986	-
Output 3: Pohnpei Utilities Corporation SMO	95,107	94,939
Output 4: Efficient Project Management	123,100	65,630
Total Expenditures	892,583	160,569
Excess (deficiency) of revenues over expenditures	-	-

See accompanying notes to the financial statements.

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM (SF)**

**Statement of Financial Position
As of September 30, 2022 and 2021**

	October 01, 2021 to September 30, 2022 (\$)	December 03, 2019 to September 30, 2021 (\$)
Assets		
Current Assets		
Receivables		
Project Coordinator Receivables	12,560	6,075
Finance & Administrative Officer Receivables	6,731	-
Project Assistant Kosrae Receivables	1,300	-
SMO Consultant Receivables	993	10,198
Total Assets	21,584	16,273
Liabilities		
Current Liabilities		
Payables		
Project Coordinator Payables	12,560	6,075
FSM DoFA Payables	6,731	-
Project Assistant Kosrae Payables	1,300	-
SMO Consultant Payables	993	10,198
Total Liabilities	21,584	16,273
Net Position	-	-

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM (SF)**

**Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021**

(1) Organization

On December 03, 2019, the Federated States of Micronesia entered into a grant agreement (Grant Number 0680-FSM(SF)) with the ADB in the amount of \$15 million for the Renewable Energy Development Project (*the Project*), with the grant closing date of August 31, 2023, or such other date as may from time to time be agreed between both parties.

The impact is increased renewable energy generation in the States of Yap and Kosrae in line with the energy targets to achieve 30% renewable energy contribution in Year 1 of operation in each State and increased access to electricity in the State of Kosrae with the electrification of Walung Village.

The outcome is increased generation and utilization of renewable energy in the States of Yap and Kosrae.

The Secretary of Finance and Administration of the Federated States of Micronesia (FSM) National Government is designated as the representative of the FSM. The Department of Finance & Administration (DoFA) is the executing agency (EA) for the Project and is responsible for the majority of all disbursement approvals, accounting and fiscal oversight. The Department of Resources & Development (DoRD) is the implementing agency (IA) for the Project, and is responsible for the day-to-day implementation of the Project, manages the Project Management Unit (PMU) and maintains all documentation.

The Project is governed by a Project Steering Committee (PSC) who should meet at least twice per year, and quarterly (if possible) to receive project updates, make key decisions and provide overall guidance to the PMU. The membership of the PSC includes: Kosrae Utilities Authority (KUA), Yap State Public Service Corporation (YSPSC), Pohnpei Utilities Corporation (PUC), DoRD, DoFA, and PMU.

(2) Summary of Significant Accounting Policies

The accompanying financial statements of the Project have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the Project's accounting policies are described below.

Basis of Accounting

The Project's financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM (SF)**

**Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021**

Receivables

The Project's receivable is recognized when the Project has received invoices from the consultants (external party) in accordance with agreed conditions/requirements, and is entitled to receive the agreed funding. Where uncertainty exists in relation to the receipt of grant funding, a receivable (and associated revenue) would not be recognized unless it was more probable than not that payment would be made hence allowances for uncollectible amounts is not necessary.

Payables

Payables refers to consultants (external party) invoices received as of September 30, 2022 and yet to be paid.

Reporting Period

The accompanying financial statements cover the fiscal year from October 01, 2021 to September 30, 2022. The period for the comparative balances covers the period December 03, 2019 to September 30, 2021. An extended fiscal year was utilized because no withdrawal applications were requested or recorded during the period December 03, 2019 to September 30, 2020.

For financial reporting purposes, the Project was administered and executed by the Department of Finance and Administration and implemented by the Department of Resources and Development of the FSM National Government, and it is a standalone and a separate donor-funded project from the FSM National Government funds and activities. The FSM National Government funds are separately audited and issue their own financial statements. These statements may be obtained by directly contacting the FSM National Government or obtaining them directly from the Office of the National Public Auditor:

P.O. Box PS05
Palikir, Pohnpei State, FM 96941

Presentation of currency

The FSM currency is the US Dollar. In the presentation of the financial statements, cost estimates and financing plan, the Project uses the US Dollar.

(3) Direct Payments made by ADB

Direct payment procedures are used for civil works, consulting services, and equipment. Project management unit (PMU) support such as the project coordinator, consultant and project steering committee meeting costs are reimbursed.

The executing agency and/or implementing agency covered the PMU support costs directly, and submitted withdrawal applications to ADB for reimbursement.

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM (SF)**

**Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021**

(3) Direct Payments made by ADB (cont'd)

From September 30, 2021 to September 30, 2022 direct payments and obligations by ADB to the consultant amounted to \$911,912.

(4) Procurement of Goods and Consulting Services

The procurement of goods, works and consulting services were based on an ADB-approved Procurement Plan (version 2 dated September 14, 2021 with a duration of 18 months). The Plan requires International Competitive Bidding.

(5) Withdrawals from Grant Account

The proceeds of the grant were allocated to items of expenditure, and disbursement on the basis of withdrawal percentage for each item of expenditure.

For fiscal year 2022, the Project has taken on three additional contracts for Outputs 1, 2 and 4. No taxes and duties were imposed on goods or works acquired during the period.

Description (Invoice no)	Withdrawal Application No.	Date	Amount (\$)	Payee
2021-10	WA007	12/01/21	7,554.99	PCS
7	WA008	12/09/21	7,797.45	Tetra Tech, Inc
2021-11	WA009	01/24/22	6,000.00	PCS
2021-12	WA009	01/24/22	6,000.00	PCS
8	WA010	01/28/22	13,138.95	Tetra Tech, Inc
2021-13	WA011	02/01/22	17,000.00	PCS
2022-01	WA012	03/10/22	10,144.98	PCS
9	WA013	03/15/22	35,135.79	Tetra Tech, Inc
10	WA014	03/15/22	8,219.80	Tetra Tech, Inc
2022-02	WA015	05/23/22	5,100.00	PCS
2022-03	WA017	05/23/22	7,950.00	PCS
11	WA018	05/16/22	7,839.02	Tetra Tech, Inc
2022-04	WA019	05/26/22	8,545.54	PCS
F22060097	WA020	07/12/22	135,117.60	Vergnet SA
F22060099	WA020	07/12/22	103,144.70	Vergnet SA
F22060096	WA021	06/30/22	196,272.66	Vergnet SA
F22060098	WA021	06/30/22	239,840.90	Vergnet SA
12	WA022	07/20/22	2,494.46	Tetra Tech, Inc
2022-05	WA023	08/18/22	8,800.00	PCS
2022-06	WA023	08/18/22	8,800.00	PCS
2022-07	WA024	08/18/22	8,800.00	PCS
72022	WA025	09/29/22	1,200.00	Andy George

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK - GRANT NUMBER 0680-FSM (SF)**

**Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021**

(5) Withdrawals from Grant Account (cont'd)

Description (Invoice no)	Withdrawal Application No.	Date	Amount (\$)	Payee
82022	WA025	09/29/22	1,250.00	Andy George
13	WA026	08/17/22	13,100.44	Tetra Tech, Inc
2022-08	WA027	10/06/22	8,800.00	PCS
14	WA028	09/08/22	4,063.13	Tetra Tech, Inc
15	WA028	09/08/22	2,324.87	Tetra Tech, Inc
2022-09	WA030	11/16/22	8,000.00	PCS
090322	WA031	11/16/22	1,300.00	Andy George
16	WA032	11/16/22	993.29	Tetra Tech, Inc
01	MS222995	07/06/22	961.54	Nicole Solomon
02	MS222808	07/15/22	961.54	Nicole Solomon.
03	MS223091	08/01/22	961.54	Nicole Solomon
04	MS223314	08/17/22	961.54	Nicole Solomon
05	MS223516	08/26/22	961.54	Nicole Solomon
06	MS223630	09/13/22	961.54	Nicole Solomon
07	Not Specified	09/13/22	961.54	Nicole Solomon
08	MS230102	10/11/22	823.30	Nicole Solomon
Total withdrawals from grant account			892,582.62	

(6) Contract and Disbursement S-Curve

The graph below shows the quarterly contract awards and disbursements for FY 2022. The S-Curve is only for ADB financing and it does not include in-kind contributions as there were no taxes or duties imposed on the goods or works acquired during the period.

Category Code	Contract Awards and Disbursements Allocation	Contracts Awarded
3201	US \$15,000,000	US \$9,193,067
<u>Breakdown:</u>		
Palikir Consulting Services, Project Coordinator		US \$289,520
Tetra Tech, ES Inc: SMO		US \$730,000
Hydro Electric Corporation trading as Entura		US \$870,000
Vergnet SA (EPC)		US \$7,257,747
Andy George, Project Assistant (PMU)		US \$20,800
Nicole Solomon, Finance & Administrative Officer (PMU)		US \$25,000

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK - GRANT NUMBER 0680-FSM (SF)**

**Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021**

(6) Contract and Disbursement S-Curve (cont'd)

Description: Disbursements in FY2022

Quarter End	Cumulative Awards (\$)	Disbursements (\$)	Cumulative Disbursements (\$)
31/12/21	1,730,240.00	15,352.44	160,569.00
31/03/22	1,730,240.00	95,939.52	175,921.44
30/06/22	9,461,786.51	465,548.12	271,860.96
30/09/22	9,482,586.51	315,742.54	737,409.08
		892,582.62	1,345,760.48

Contract Award and Disbursement S-Curve



The contract award to Vergent SA, the selected contractor for major EPC works for Kosrae and Yap, was completed in Q2, highlighted by the blue S-Curve.

(7) Procurement

All procurement of project goods and works were undertaken in accordance with ADB's Procurement guidelines (2015, as amended from time to time). An 18-month procurement plan indicating threshold and review procedures, goods, works, and consulting service contract packages and national competitive bidding guidelines includes the following:

Method	Threshold
International Competitive Bidding for Works	Above \$3,000,000
International Competitive Bidding for Goods	Above \$1,000,000
National Competitive Bidding for Works	Below or Equal to \$3,000,000
National Competitive Bidding for Goods	Below or Equal to \$1,000,000
Shopping for Works/Goods	Below or Equal to \$300,000

RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM (SF)

Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021

(8) Statement of Budgeted versus Actual Expenditures

The schedule below shows the estimated project cost and actual expenditures incurred in FY 2022.

Particulars	Budgeted	Actual Expenditures (millions - USD)		Variance
		FY 2021	FY 2022	
Yap				
1 BESS at power station	1.31	-	0.33	0.98
2 Ground mount solar photovoltaic array near power station	4.47	-	-	4.47
3 Rooftop solar photovoltaic extension at sports center	0.49	-	-	0.49
4 Upgrade to power station SCADA and controls	0.31	-	-	0.31
Total Capital Expenditure (CAPEX)	6.58	-	0.33	6.25
Total Import Taxes and Duties	0.26	-	-	0.26
Total for the Yap Project	6.84	-	0.33	6.51
Kosrae				
1 KUA Main Grid	3.69	-	0.34	3.35
2 Walung mini-grid and solar home system	1.16	-	-	1.16
Total Capital Expenditure (CAPEX)	4.85	-	0.34	4.51
Total Import Taxes and Duties	0.20	-	-	0.20
Total for the Kosrae Project	5.05	-	0.34	4.71
Pohnpei				
1 SMO Consultant	0.74	0.09	0.10	0.64
Total for the Pohnpei Project	0.74	0.09	0.10	0.64
FSM				
1 Project Implementation Consultants (PIC)	0.87	0.07	-	0.80
2 Project Management Unit (PMU) Support	0.23	-	0.12	0.11
Total Project Management Support	1.10	0.07	0.12	0.98
Contingency	1.78	-	-	1.78
Total Project Costs	15.51	0.16	0.89	14.62

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680-FSM (SF)**

**Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021**

(9) Cost and Financing

The Project is financed as follows: Equipment, Works, Project Implementation Consultants, and Supplemental Management Operations from ADB Supplemental Fund in the amount of \$15 million and FSM Government in-kind counterpart financing consisting of exemptions from import taxes and duties estimates of \$0.51 million. No in-kind disbursement from the FSM Government was paid during the period and no import duties were recorded in FY 2022.

Detailed Estimates Financier	Cost by	ADB		Government		Total Costs	
		Amount	% of cost category	Amount	% of cost category	Amount	Taxes and Duties
Output 1: Yap Main Grid Renewable Energy							
1	BESS	1.31	96%	0.05	4%	1.36	0.05
2	Ground PV	4.47	96%	0.18	4%	4.65	0.18
3	Roof PV	0.49	96%	0.02	4%	0.51	0.02
4	Upgrade control system	0.31	96%	0.01	4%	0.32	0.01
	Total	6.58	96%	0.26	4%	6.84	0.26
Output 2: Kosrae Main Grid Renewable Energy							
1	Main Grid PV and BESS	3.69	96%	0.15	4%	3.84	0.15
2	Walung Mini-grid and solar home system	1.16	96%	0.05	4%	1.21	0.05
	Total	4.85	96%	0.19	4%	5.05	0.19
Output 3: Pohnpei Utilities Corporation SMO							
1	SMO Consultant	0.74	100%	-	-	0.74	-
	Total	0.74	100%	-	-	0.74	-
Output 4: Efficient Project Management							
1	PIC	0.87	100%	-	-	0.87	-
2	PMU Support	0.23	100%	-	-	0.23	-
	Total Support	1.10	100%	-	-	1.10	-
	Subtotal (A)	13.27	97%	0.45	3%	13.73	0.45
Contingency							
1	Physical	1.33	97%	0.05	3%	1.37	0.05
2	Price	0.40	97%	0.01	3%	0.41	0.01
	Subtotal (B)	1.73	97%	0.06	3%	1.78	0.06
	Total (A + B)	15.00	97%	0.51	3%	15.51	0.51

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK - GRANT NUMBER 0680-FSM (SF)**

**Notes to Financial Statements
For the Years Ended September 30, 2022 and 2021**

(10) Subsequent Events

On December 17, 2021, an additional financing grant agreement was executed by ADB and the FSM of \$4 million. This additional financing – referred to as the Disaster Risk Reduction (DRR) component of the Project (a new component 5) – was endorsed and approved on December 02, 2022 by the 22nd FSM Congress. The additional financing was made effective by the FSM Department of Justice on February 27, 2023, and confirmed by the ADB on March 02, 2023.



FEDERATED STATES OF MICRONESIA

Office of The National Public Auditor

P.O. Box PS-05, Palikir, Pohnpei FSM 96941

Tel: (691) 320-2862/2863 Fax: (691) 320-5482

CID Hotline: (691) 320-6768; Website: www.fsmopa.fm

Facebook: FSM Office of the National Public Auditor; E-mail: info@fsmopa.fm

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

Honorable Eugene Amor
Secretary of Finance & Administration
FSM Department of Finance & Administration:

Report on the Financial Statements

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 the *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Renewable Energy Development Project (the Project), which comprise the statement of financial position as of September 30, 2022, and the related statement of financial performance for year then ended and the related notes to the financial statements, and have issued our report thereon dated April 12, 2023.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Project's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Project's internal control. Accordingly, we do not express an opinion on the effectiveness of the Project'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 statement 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 preceding paragraph 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 have not been identified. We consider the deficiency in the accompanying Schedule of Findings and Responses as item 2022/01 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Project's 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 financial statements. 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 an instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings and Responses as item 2022/02.

The Project's Response to Findings

The Project's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Responses. The Project's response was not subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on it.

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 Project'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 Project's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.



Haser Hainrick
National Public Auditor

Palikir, Pohnpei
April 12, 2023



FEDERATED STATES OF MICRONESIA

Office of The National Public Auditor

P.O. Box PS-05, Palikir, Pohnpei FSM 96941

Tel: (691) 320-2862/2863 Fax: (691) 320-5482

CID Hotline: (691) 320-6768; Website: www.fsmopa.fm

Facebook: FSM Office of the National Public Auditor; E-mail: info@fsmopa.fm

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH THE FINANCIAL COVENANTS AND OTHER REQUIREMENTS OF THE GRANT AGREEMENT

Honorable Eugene Amor
Secretary of Finance & Administration
FSM Department of Finance & Administration:

Report on Compliance with the Financial Covenants and Other Requirements of the Grant Agreement

We have audited the Renewable Energy Development Project (*the Project's*) compliance with the types of compliance requirements described in the Grant Agreement dated December 03, 2021, with the Asian Development Bank, that could have a direct and material effect on the Project for the year ended September 30, 2022.

Management's Responsibility

Management is responsible for compliance with the financial covenants and other requirements of the grant agreement.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance with the financial covenants and other requirements of the grant agreement referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of the Grant Agreement. Those standards and the Grant Agreement require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on the Project occurred. An audit includes examining, on a test basis, evidence about the Project's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our qualified opinion on compliance with the financial covenants and other requirements of the grant agreement. However, our audit does not provide a legal determination of the Project's compliance.

Basis for Qualified Opinion

As described in Finding 2022/02 in the accompanying Schedule of Findings and Responses, the Project did not comply with the requirements of Section 15 of the Grant Agreement dated December 03, 2019, with the Asian Development Bank, regarding the financial covenants. Compliance with such requirements is necessary, in our opinion, for the Project to comply with the requirements applicable to the financial covenants of the grant agreement.

Qualified Opinion

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the Project complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the Project for the year ended September 30, 2022.

Other Matters

The results of our auditing procedures disclosed one other instance of noncompliance which is required to be reported in accordance with the Grant Agreement and which is described in the accompanying Schedule of Findings and Responses as item 2022/01. Our opinion on the Project is not modified with respect to this matter.

The Project's response to the noncompliance findings identified in our audit is described in the accompanying Schedule of Findings and Responses. The Project's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control over Compliance

Management of the Project is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Project's internal control over compliance with the types of requirements that could have a direct and material effect on the Project to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance and to test and report on internal control over compliance in accordance with the grant agreement, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Project's internal control over compliance.

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, we identified a deficiency in internal control over compliance that we consider to be significant deficiency described in the accompanying Schedule of Findings and Responses as item 2022/01.

The Project's response to the internal control over compliance findings identified in our audit is described in the accompanying Schedule of Findings and Responses. The Project's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The Project is responsible for preparing a corrective action plan to address each audit finding included in our auditors' report. The Project's corrective action plan was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on it.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the grant agreement. Accordingly, this report is not suitable for any other purpose.



Haser Hainrick
National Public Auditor

Palikir, Pohnpei
April 12, 2023

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680 (SF)**

**Schedule of Findings and Responses
September 30, 2022**

2022/01: Non-Maintenance of separate accounts and records for the Project

Criteria: Section 4.02 of Article IV of the grant agreement dated 12/03/19 states that the recipient shall maintain separate accounts and records for the project.

Condition: Despite the efforts by DoRD and DoFA in recruiting a Project Finance and Administration Officer who is responsible for maintaining the project accounts, the following anomalies were noted:

- Separate accounts and records specifically for the project were not maintained such as reconciliations, trial balances, subsidiary ledgers and approved journal adjustments;
- Reliance on the Asian Development Bank Client Portal for Disbursements to prepare the financial statements for REDP.
- Fundware was not updated to reflect the transactions that have been processed and paid for the Project. As of 03/14/23, transactions posted in the Fundware amounted to \$16,610.67.

We acknowledge that the postings to Fundware is not performed by the Project, however the overall responsibility to ensure that Fundware is updated rests with the Project.

Effects: As a result of not maintaining separate accounts and records for the Projects:

- There were delays in the preparation and submission of draft financial statements for audit. The draft financial statements was submitted to ONPA on February 06, 2023 with an expected audit completion timeline of March 31, 2023.
- The draft financial statements were resubmitted on March 09, 2023, March 17, 2023 and March 27, 2023 to correct the errors and misstatements.
- Non-compliance to the requirements of the Project Administration Manual.

Root-Causes: Oversight function is not effective to ensure that:

- records are maintained and updated for the Project.
- adequate guidance (capacity building, awareness, procedural guidance drafted & approved) is provided to the Project Finance & Administration Officer.
- financial statements are thoroughly reviewed prior to submission for audit verification.

Recommendations: Oversight function to be strengthened by:

- Increased monitoring by the National Project Coordinator to ensure that records are maintained and updated for the Project.
- Adequate guidance such as capacity building, and/or approved procedural guidance provided to the Project Finance & Administration Officer on the day-to-day activities to be completed for the Project.
- Ensuring that financial statements are thoroughly reviewed, checking that all balances are properly supported and free from errors and misstatements, prior to submission for audit verification.

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK - GRANT NUMBER 0680 (SF)**

**Schedule of Findings and Responses
September 30, 2022**

Management Responses: Unfortunately, the FY22 AT finding in this regard has shown that a number of key weaknesses continue to be present, despite the hiring of a full-time FAO, including a lack of effective oversight on FAO activities by the NC, to ensure that reconciliations, trial balances, subsidiary ledgers and approved journal adjustments were being maintained, and to thoroughly review and submit the annual FS in an efficient manner. We agree with your recommendations and expect to address this finding immediately through implementation of appropriate actions in order to effectively improve the PMU staffing and management practices. These shall include:

- Emphasis on improving and maintaining separate accounts on the REDP financials at DoRD, working with DoFA. In addition, we will also develop a monthly internal financial reporting mechanism to be monitored by the NC and the Assistant Secretary for Energy to ensure that separate records are maintained and updated, including adhering to a process for quarterly and annual review.
- Recruitment and hiring of one or more additional, qualified Finance and Accounting staff into the PMU that will be primarily responsible for maintaining a separate project ledger and to collaborate with DOFA to ensure that Fundware and fixed asset registry is updated for REDP.
- Pursue capacity building opportunities with ADB and relevant partners to support and improved financial reporting.

2022/02: Non-Compliance with Financial Covenants

Criteria: Section 9 of Schedule 4 of the grant agreement for Additional Financing Grant Agreement dated December 17, 2021 states that “*the recipient shall ensure that, for the purposes of the Initial Project and this Project, each Project Beneficiary achieves and maintains, from December 2021 and annually thereafter, an operating ratio not exceeding 1.0.*”

Condition: From our review of the operating ratio of the project beneficiaries for the year ended 31 December 2021, we noted that none of the project beneficiaries achieved the required ratio. Refer to the table below for details:

Project Beneficiaries	Operating Ratio Achieved
Pohnpei Utilities Corporation	1.053
Kosrae Utilities Corporation	1.029
Yap State Public Service Corporation	1.007

Effects: The above resulted in non-compliance to the financial covenants of the grant agreements.

**RENEWABLE ENERGY DEVELOPMENT PROJECT
ASIAN DEVELOPMENT BANK – GRANT NUMBER 0680 (SF)**

**Schedule of Findings and Responses
September 30, 2022**

Root-Cause: The grant agreement does not specify how the Department of Finance & Administration and Department of Resources and Development of the FSM National Government can assist the project beneficiaries in complying with the financial covenants as both Departments do not have any controls on the operations of the project beneficiaries.

Recommendations: We recommend that the financial covenant requirements of the grant agreement be reviewed to specify how the Departments (DOFA and DORD) of the FSM National Government can assist the project beneficiaries comply with the financial covenant requirements.

Management Responses: To address the identified root cause of this finding, as well as to follow the ONPA recommendations, we shall undertake the following actions to support the project beneficiaries to comply with this financial covenant:

- Revisit with ADB and the Project Steering Committee (PSC) the financial covenant requirements.
- Other actions as needed, including effective implementation of the REDP so that it delivers the intended outcomes, including a substantial reduction of fossil fuel use for both KUA and YSPSC, and a subsequent reduction in expenditures for fuel, currently the largest expense.