

**OFFICE OF THE NATIONAL PUBLIC AUDITOR  
FEDERATED STATES OF MICRONESIA**



**IMPROVEMENT NEEDED IN THE OVERSIGHT FUNCTION OF THE  
BOARD OF DIRECTORS FOR THE CAROLINE ISLAND AIR, INC.**

**REPORT NO. 2023-06**





# FEDERATED STATES OF MICRONESIA

## Office of The National Public Auditor

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Friday, July 28, 2023

His Excellency President Wesley W. Simina  
Honorable Members of the 23<sup>rd</sup> Congress  
Members of the Board of Directors, Caroline Islands Air, Inc  
Federated States of Micronesia

### **RE: Performance Audit on the Caroline Islands Air, Inc.**

We have completed the performance audit on the Caroline Islands Air, Inc. (*Corporation*) covering the fiscal years 2020 to June 2023. This report presents the results of our audit, which was conducted in accordance with *Generally Accepted Government Auditing Standards (GAGAS)*.

Our objectives were focused on whether the Corporation is financially viable and able to sustain its operations in the longer run; compliance with the requirements of the Board of Directors By-Laws (dated November 16, 2000), establishing law (Public Law No. 10-072) and amendments thereof regarding the composition and effectiveness of the Board of Directors and the staff adequacy and sufficiency to administer and handle the operations of the Corporation.

We concluded the following:

- a) Lack of indications to support that the Corporation is financially viable to sustain its current and future operations.
- b) Some of the requirements of the Board of Director By-Laws, Establishing Law and its amendments were not complied with.
- c) Due to lack of documentation, we were not able to confirm whether the Corporation has adequate and sufficient staff to administer its operations.

The findings and recommendations were discussed with the Board of Directors and management of the Corporation, and we requested a written management response, which is included in this final report.

We would like to acknowledge the assistance provided by the Board of Directors, management, and staff of the Corporation.

Sincerely,

Haser H. Hainrick  
National Public Auditor

cc: Vice President  
Chief Executive Officer, Caroline Islands Air, Inc.

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**Abbreviations**

<b>Abbreviation</b>	<b>Meaning</b>
aircraft/airplane	In this report, the word 'aircraft' is used interchangeably with 'airplane'
Board	refers to the 'Board of Directors' for the Corporation
CEO	Chief Executive Officer
CIA	Caroline Islands Air, Incorporated
Corporation	refers to the 'Caroline Islands Air' or CIA
FSM	Federated States of Micronesia
FY	Fiscal Years
NG	National Government
PL	Public Law

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**1.0 INTRODUCTION**

1.1 Reason for the Assignment

The Office of the National Public Auditor engaged in a performance audit on the Caroline Islands Air, Incorporated (“CIA or Corporation”). The CIA is a government owned corporation, with its accounts organized as a *proprietary fund*, which means that the Corporation operates in a manner like private business enterprises with the motive of earning profits.

Our review of the Corporation’s financial statements issued for fiscal years (FY) 2018 to 2021, noted that the Corporation generated operating losses as shown in the table below:

*Table 01: Details of Operating Loss*

Fiscal Year	Operating Loss (\$)
2018	420,576.00
2019	256,228.00
2020	676,945.00
2021	280,153.00

*(Source: financial statements for FY 2018 - 2021)*

Included in the financial report for FY2019, the economic outlook for the Corporation which highlighted the challenges faced by the Corporation such as the increase in the costs of insurance, maintenance and operation costs related to fuel, aircraft parts and periodic overhaul of airplane parts. In addition, the continued revenue shortfalls added to the difficulty for the Corporation to adequately cover operating costs, insurance, fuel and parts for airplanes and periodic overhaul of airplane parts.

In FY2020, the Corporation faced a major loss in revenues because of decreased operation from the impacts of COVID-19. The Yap/Palau operation which began operations in January 2018 was discontinued, and the primary aircraft was relocated to Pohnpei to supplement transportation services within the Federated States of Micronesia (FSM).

As reported in the economic outlook for FY2021, the Corporation operated with one plane with continuous mechanical challenges. Due to these revenue shortfalls, the Corporation relied on the subsidies approved and appropriated by Congress since FY2015. Refer to the Table below for details:

*Table 02: Subsidies from the FSM National Government*

Fiscal Year	Operating Loss (\$)	Source
2015	10,000.00	Financial Statement
2016	103,307.00	”
2017	18,571.00	”
2018	187,007.00	”
2019	253,300.00	”
2020	323,429.00	”
2021	93,607.00	”

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Fiscal Year	Operating Loss (\$)	Source
2022	200,000.00	Public Law (PL) No. 22-42
2023	255,000.00	PL No. 22-169

The Corporation’s financial statements are incorporated into the financial statements of the FSM National Government (NG) as a component unit. Under the terms of the amended Compact of Free Association, the FSMNG is required to comply with the Single Audit Act (PL No. 98-502), part of which is to complete and issue its annual financial statements by June 30<sup>th</sup> of the subsequent fiscal year or any dates as approved by the United States of America – Office of Insular Affairs. Considerable delays were noted in the finalization of annual audits for the Corporation as tabulated below.

*Table 03: Completion Timeline of Annual Audits*

Fiscal Year	Date - Approved Completion Timeline	Date - Auditors Reports Issued	No. of days delayed
2019	December 31, 2020	February 25, 2021	56 days
2020	December 31, 2021	February 11, 2022	42 days
2021	December 15, 2022	April 06, 2023	96 days

Lastly, it has been more than ten (10) years since the last performance audit was conducted on the Corporation.

**1.2 Background**

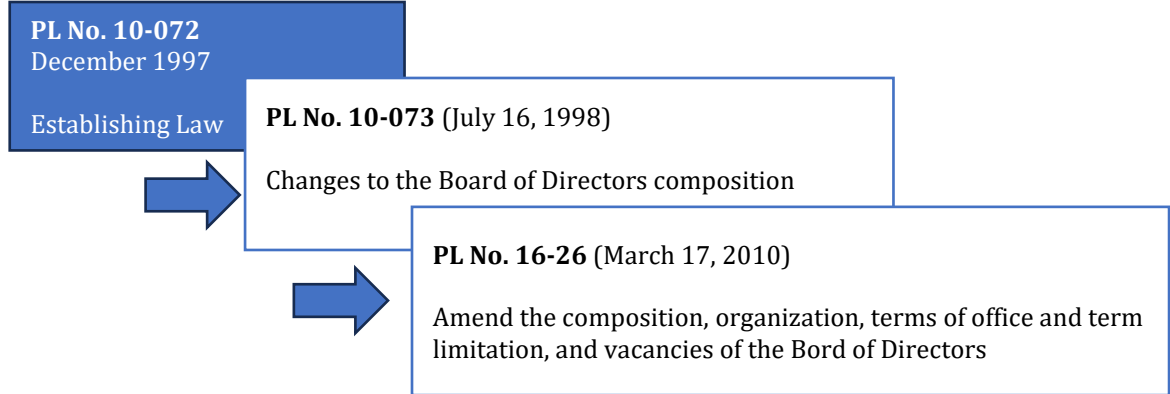
The Corporation was created through PL No. 10-072 for the purpose of providing the following services:

- Provide air transportation services throughout the Nation.
- Contract with domestic and foreign persons and corporations for the provision of aircraft and services.
- Operate domestic air transportation services.
- Train citizens in professions related to aeronautics.
- Act as a “Freely Associated State Air Carrier” within the meaning of the Federal Program and Services Agreement concluded pursuant to the Compact of Free Association.
- Engage in support activities, including, but not limited to, freight terminal and delivery activities and passenger services.
- Enter into joint ventures with other entities to effectuate its operation.

Over the years, the establishing law (PL No. 10-072) was amended to improve the operations and administration of the Corporation as summarized in the diagram below.

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*Diagram 01: Amendments to the Establishing Law*



Section 05 of the establishing law specifies that the affairs of the Corporation are managed and governed by the Board of Directors.

The Corporation is governed by a six-member Board of Directors appointed as follows according to PL No. 16-26:

- One (1) member appointed by the President with the advice and consent of the FSM Congress to represent the FSMNG.
- Four (4) State representatives appointed by the President with the advice and consent of the FSM Congress upon the recommendation to the President by the Governor of the pertinent State.
- The Chief Executive Officer of the Corporation as the ex-officio member but without rights to vote.

## **2.0 OBJECTIVES, SCOPE, METHODOLOGY**

### **2.1 Objectives**

The objectives of the audit were to evaluate whether the Corporation:

- i) Is financially viable and able to sustain its operations in the longer run.
- ii) Complies with the Board of Directors By-Laws (dated November 16, 2000), establishing law (PL No. 10-072) and amendments thereof regarding the composition and effectiveness of the Board of Directors.
- iii) Have adequate and sufficient staff to administer and handle the operations of CIA.

### **2.2 Scope**

The audit focused on the activities of the Corporation relating to the objectives listed under section 2.1 for fiscal years 2020 to 2023.

For FY2023, our focus was from October 01, 2022, to June 30, 2023.

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**2.3 Methodology**

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

In executing the audit, various approaches were exercised which included the review and assessment of the following documents - public laws and related amendments, other laws and regulations relevant to the Corporation, internal policies and procedures, revenues and expenditure reports, personnel files, meeting minutes, subsidy request; and interviewing with the Board of Directors and management in order to evaluate and confirm whether the Corporation is financially viable and able to sustain its operations in the longer run; complied with the Board of Directors By-Laws, establishing law and any amendments regarding the composition and effectiveness of the Board of Directors; and whether there is adequate and sufficient staff to administer and handle the operations of CIA.

The audit was performed at the Corporation's Office in Dekehtik, Pohnpei.

**3.0 LEGAL MANDATES/STANDARDS**

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

*"The Public Auditor shall inspect and audit transactions, accounts, books and other financial records of every branch, department, office agency, board, commission, bureau, and statutory authority of the National Government and of other public legal entities, including, but not limited to, States, subdivisions thereof, and nonprofit organizations receiving public funds from the National Government".*

**4.0 PRIOR AUDIT COVERAGE**

The previous performance audit was conducted in 2010 covering the period October 2008 to June 2010.

However, annually, financial statement audit (single audit engagement) is conducted on the Corporation as a component unit of the FSM National Government. The issues identified from the single audit engagement for fiscal year 2021 were:

- A Disclaimer of Opinion was issued due to the inadequacies in the books of original entry, the general and subsidiary ledgers and substantially all corroborating evidence in support of the financial statements.
- Lack of periodic reconciliation of the general ledger which resulted in the un-timely record keeping and preparation of financial statement.

The audit team reviewed the adequacy and sufficiency of the staff in the Finance Department, as part of the procedures under Objective 3.



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**5.0 COMMENDATION**

Our sincere appreciation is extended to the management and staff of the Corporation for the assistance and cooperation rendered during the audit. The ONPA looks forward to the continuation of such fruitful relationship.

**6.0 CONCLUSION**

Based on the results of our audit, we concluded the following:

- d) Lack of indications to support that the Corporation is financially viable to sustain its current and future operations.
- e) Some of the requirements of the Board of Director By-Laws, Establishing Law and its amendments were not complied with.
- f) Due to lack of documentation, we were not able to confirm whether the Corporation has adequate and sufficient staff to administer its operations.

The results of this audit are discussed in detail in the following pages.

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**7.0 FINDINGS AND RECOMMENDATIONS**

**7.1 Lack of indicators to support that the Corporation is financially viable to sustain its operations in the longer run.**

Financial viability refers to an organization's ability to generate the required cash flow to fulfill ongoing operational costs and debt repayments. It also refers to the organization's ability to continue growing at the desired rate while still meeting customer expectations through high performance.<sup>1</sup>

As specified under the *Background Section (No. 1.2)* of this report, amongst other services, the Corporation was established through PL No. 10-072 to provide air transportation services throughout the FSM and to operate a domestic air transportation service.

Article 1, Section 1 of the Board of Directors By-Laws specifies that *"all corporate powers and the business and affairs of Caroline Islands Air, Inc. shall be controlled by the Board of Directors. Such powers shall be exercised by the Board consistent with Public Law No. 10-72, as amended, and these By-Laws."*

The following findings supported our conclusion of the lack of indicators to support that the Corporation is financially viable to sustain its current and future operations.

**7.1.1 Insufficient Funding to Invest in Quality Aircrafts**

We were provided with manifest documents for January 2021 to December 2022.

Our review and inquiry of the manifest documents confirms that only one aircraft, registration no. V6-04FM was operating until February 2022. Effective from March 2022 to June 2023, a period of more than one (1) year, the V6-04FM aircraft was grounded, awaiting aircraft parts to arrive from Australia. We were informed that the delay in obtaining aircraft parts was due to the lack of funding to purchase the parts.

On September 16, 2022, a 'pre-owned' aircraft was purchased for \$350,000 from a private vendor in the Philippines. The aircraft, registration V6-05FM landed in Pohnpei on March 24, 2023, and commenced operations from April 05 – 15, 2023, before it started having mechanical problems.

There were no air services provided by the Corporation from March 2022 - April 2023, and from April 15 - June 26, 2023, a period of more than one (1) year as the aircraft was grounded for repair work.

Even though we were provided with documentations to support that the Board of Directors had requested for funding to invest in quality aircrafts, these documents were draft copies. Therefore, we cannot confirm whether the request was submitted to Congress.

Cause:

Insufficient funding provided to the Corporation is limited to the ranges offered for 'pre-owned' aircrafts and not sufficient to acquire quality aircrafts.

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<sup>1</sup> <https://www.oneadvanced.com/news-and-opinion/the-importance-of-fiancial-viability-for-businesses/>

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Effects:

As a result, the:

- required service to be provided to the FSM as per the establishing law is disrupted.
- The Corporation is not meeting its mandate when services are not provided.
- Potential revenue that could be earned from the period in which the service was disrupted is lost.
- Additional or unnecessary costs incurred by the Corporation because of the continued mechanical problems.

Recommendation:

We recommend that the Board of Directors and management of the Corporation to continue their initiative to request and obtain support from the Congress to invest and fund quality aircrafts.

**7.1.2 Absence of an approved and documented procedures regarding the involvement of the Corporation in the acquisition of aircrafts**

We were informed that all the aircraft with the Corporation are the property of the FSM National Government.

We noted from our review of the Board of Directors meeting minutes that the Corporation is involved to some extent in the acquisition of aircraft. The research and selection of suitable and preferred aircraft is done by the Corporation; inspection of aircrafts is jointly performed by the Corporation and the FSMNG (represented by the Department of Transportation, Communication & Infrastructure and Attorney General's Office); and the payment process is facilitated by the FSMNG Department of Finance & Administration.

We noted that there were no approved procedures to guide the Corporation in their involvement in the acquisition of aircraft.

Cause:

Lack of oversight by the Board of Directors to safeguard and protect the Corporation from risks and liability by ensuring that standard operating procedures are in place relating to the Corporation's involvement in the acquisition of aircraft.

Effects:

- Inconsistent approaches taken in the acquisition of aircraft by those involved in the process.
- Lack of proper guidance provided to those involved in the acquisition process that all required and mandatory processes are complied with.

Recommendation:

The Board of Directors should strengthen their oversight function by ensuring that standard operating procedures on the Corporation's involvement in the acquisition of aircraft is in place, and to also consider having the appropriate resources to draft the procedures.

**7.1.3 Lack of Strategic Planning**

Strategic planning is the process of defining and aligning an organization's vision, goals, and actions to achieve its desired outcomes in a changing environment. It is not a one-time event, but a continuous

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cycle in considering the effect of changing business, industry, legal and regulatory conditions.<sup>2</sup> The product of strategic planning is a strategic plan which documents the mid-to-long-term goals of the organization for a certain period. It establishes a sequence in which those goals should be realized so that the organization achieves its stated vision(s).

For FY2020 to FY2023, there was no approved strategic plan. The Chief Executive Officer (CEO) is currently drafting the strategic plan for submission to the Board of Directors for approval.

Causes:

- Lack of oversight from the Board of Directors to ensure that a documented plan is in place which should define the purpose and direction of the Corporation, goals and the steps and milestones to achieve these goals.
- It is not a documented requirement that a strategic plan should be in place for the Corporation, and who will be responsible for developing and updating the Plan and its submission to the Board of Directors for approval.

Effect:

Without an approved strategic plan, it can be implied that the Corporation will not be able to measure success and demonstrate results, value, and performance.

Recommendations:

We recommend that the Board of Director's strengthen its oversight function by ensuring that:

- A strategic plan is in place for the Corporation; and
- It is clearly documented who will be responsible for developing and updating the Plan, and its submission to the Board of Directors for approval.

#### **7.1.4 Absence of an approved Business Continuity Plan (BCP)**

The operations of the Corporation were halted for more than a year, when the only aircraft providing air service was grounded due to mechanical problems. Other disruptions that have also impacted the Corporation are pandemics and natural disasters.

To mitigate these risks, it is imperative that the Corporation develops a BCP. The main objective of having a business continuity plan is to support the key activities of the organization during a crisis, ensuring that the organization can restart operations swiftly following disruptions, shortens the period of disruptions, reduces the risks and effects of risks on the organizations.

For FY2020 to FY2023, there was no approved business continuity plan. We were provided with a draft business continuity plan and there is no evidence that it has been submitted to the Board of Directors for review and approval.

Causes:

- Lack of oversight from the Board of Directors to ensure that an approved BCP is in place; and

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<sup>2</sup> [Linkedin.com/advice/1/what-best-tools-methods-strategic-planning-dynamic](https://www.linkedin.com/advice/1/what-best-tools-methods-strategic-planning-dynamic)

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- It is not a documented requirement that a BCP should be in place for the Corporation, and who will be responsible to develop the BCP, submit for Board approval and the continuous update so that the BCP remains relevant and effective.

Effects:

As a result of not having an approved BCP, the Corporation will not be able to:

- Navigate through potential disruptions and maintain its operations;
- Enhance the Corporations resilience and minimize the impact of disruptions; and
- Adapt swiftly to changing business environment, safeguarding the Corporation’s reputation, and secure long-term success benefitting the people of the FSM.

Recommendations:

We recommend that the Board of Director’s strengthen its oversight function by ensuring that:

- A BCP is in place for the Corporation; and
- It is clearly documented who will be responsible for developing and submitting the BCP to the Board of Directors for approval and updating it so that the BCP remains effective and relevant.

**7.1.5 Operating at a Loss**

Our review of the Corporation’s audited financial records for FY2020 and FY2021 confirms that the Corporation generated operating losses as shown in Table 01.

As the accounts of the Corporation is currently being audited for FY2022, we reviewed the Profit & Loss statements for FY2022 and part of FY2023 (covering the period from October 01, 2022, to May 2023), and noted that the Corporation operated at a net loss as shown in the Table 4.0 below.

*Table 4.0: Details of Net Losses for FY2022 to May 2023*

<b>Fiscal Years</b>	<b>Net Loss (\$)</b>
2022	154,811.47
2023 (until May)	96,390.41
<b>Total</b>	<b>251,201.88</b>

We also reviewed the Corporation’s budget for FY2023 and noted that even though it includes estimated revenues that will be earned from two (2) aircrafts, it was not sufficient to cover the estimated expenses by \$834,753.98. The Corporation budgeted for a loss in their FY2023 budget.

Cause:

Lack of funding to invest in quality aircraft which limited the Corporation’s selection within the ‘pre-owned’ aircraft ranges.

Effects:

As a result of continuously operating at a loss, the Corporation:

- will not be financially viable to support its current and future operations.
- continued to receive subsidies from the FSM Congress to cover and pay for fuel, insurance and some operation costs as indicated under Table 02.

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Recommendation:

We recommend that the Board of Directors and management of the Corporation to continue their initiative to request and obtain support from the Congress to invest and fund quality aircrafts.

**7.2 Non-compliance with the requirements of the Board of Directors By-Laws, Establishing Law and amendments to the composition and effectiveness of the Board of Directors were noted.**

The Board of Directors By-Laws was adopted by the then Board of Directors on November 16, 2020, which has the following articles: Article I - Board of Directors; Article II – Officers; Article III – Indemnification of Directors and Employees; and Article IV – Amendment of By-Laws.

PL No. 10-072 is the establishing law that created the Corporation to operate, maintain and administer an inter-island air service within the nation, and for other purposes.

The establishing law was amended through PL No. 16-26 to improve the administration of the Corporation which included the amendments to the composition, organization, terms of office and term limitation, and vacancies for the Board of Directors.

**7.2.1 Lack of documentations on the Board of Directors meeting minutes**

Article I Section 12 (b) allows the Board members to be paid meeting allowance for attending regular or special meetings, hence a report was extracted from QuickBooks on all meeting allowances paid to the Board members for FY2020 to FY2023.

The payment date as per the QuickBooks report was verified against the meeting minutes provided to reconcile and confirm whether all meeting minutes were provided for our verification.

We noted that not all meeting minutes for the Board of Directors were provided for verification. Refer to the Table below for the details of the dates the meeting allowances were paid however there were no minutes.

*Table 05: Date Meeting Allowances were paid and minutes not provided*

No. of meetings	Fiscal Year	Payment date of meeting allowance
8	2020	<ul style="list-style-type: none"> <li>• May 07 &amp; 12, 2020</li> <li>• June 17 &amp; 22, 2020</li> <li>• July 27 &amp; 31, 2020</li> <li>• August 14, 2020</li> <li>• September 01 &amp; 28</li> </ul>
10	2021	<ul style="list-style-type: none"> <li>• November 10 &amp; 25, 2020</li> <li>• December 18, 2020</li> <li>• January 14, 2021</li> <li>• February 02, 2021</li> <li>• March 23, 2021</li> <li>• June 25, 2021</li> <li>• August 13, 2021</li> <li>• September 01 &amp; 17, 2021</li> </ul>

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No. of meetings	Fiscal Year	Payment date of meeting allowance
3	2022	<ul style="list-style-type: none"> <li>• December 10, 2021</li> <li>• May 10, 2022</li> <li>• August 01, 2022</li> </ul>
3	2023	<ul style="list-style-type: none"> <li>• October 07, 2022</li> <li>• January 13, 2023</li> <li>• March 31, 2023</li> </ul>

Contrary to the requirements of Article 1 Section 5 (b) and Article II Section 3(c) the meeting minutes were prepared by the staff of the Corporation.

In addition, we were not provided with all the notice of meetings or documentations to support that notice of meetings for all Board meetings was issued by the Chairman of the Board or the Chief Executive Officer.

Cause:

Lack of oversight by the Board of Directors Secretary to ensure that all meeting minutes are properly documented, endorsed, and maintained for future references.

Effects:

- In the absence of the Board of Directors meeting minutes:
  - appropriate audit procedures cannot be confirmed such as establishing compliance with the following requirements on Article I: Section 2 – regular meetings, Section 4 – notice of meetings, Section 5 – procedures for the conduct of business, and Section 11 – Executive Committee meeting.
  - Important decisions made by the Board of Directors cannot be verified.
- Non-compliance with the requirements of Article I Section 5 (b) and Article II Section 3 (c) on the preparation of Board meeting minutes.

Recommendation:

We recommend that the oversight function performed by the Board of Directors Secretary to be strengthened to ensure that all meeting minutes are properly documented, endorsed, and maintained for future references.

**7.2.2 Absence of adequate documentation for the increase in meeting allowance**

Article I Section 12 specifies that the Board members are entitled to meeting allowances not exceeding \$75 for attending regular or special meetings. Contrary to this requirement, the Board members were paid \$100 per meeting for FY2020 to FY2023 which amounted to \$22,300.

During the entry meeting on May 30, 2023, we were informed that the increase in the meeting allowance to \$100 was approved by the Board of Directors and the By-Laws were also amended to reflect the increase in the allowance. However, we were not provided with any documentation to support these statements.

We also noted that a former staff of the Corporation who attended the Board meetings was also receiving meeting allowance during the FY2020 & FY2021 of \$1,100.

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In addition, Article IV Section 2 states that *“the CEO shall keep or cause to be kept a book of By-Laws. The book of By-Laws shall contain the original By-Laws and any amendments made thereto.”* From our enquiry, there were no books of By-Laws maintained.

Causes:

Ineffective oversight function by the Board of Directors to ensure that:

- decisions made that will necessitate the amendments to the By-Laws are properly documented and maintained;
- the By-Laws are updated to reflect the changes;
- the updated By-Laws are properly maintained for future references; and
- requirements of the By-Laws on those eligible to receive meeting allowance are adhered to.

Effect:

Due to lack of supporting documentations, we cannot confirm whether approval was granted by the Board of Directors to increase the meeting allowance and whether the By-Laws were updated to reflect the changes.

Recommendations:

Oversight function by the Board of Directors to be strengthened to ensure that:

- important decisions that will necessitate the amendments to the By-Laws are properly documented and maintained;
- the By-Laws are updated to reflect the changes and maintained for future references; and
- the requirements of the By-Laws are adhered to.

### **7.2.3 Inconsistency in the documentation of the Terms of Office for the Board of Directors**

PL No. 16-26 Section 8 specifies the following requirements for the terms of office for the Board members:

*“Terms of office shall be for a period of **three years** and shall be staggered such that not more than two of the five terms expire in one year, except that the initial terms of office and the filling of vacancies shall be as provided by this act. The terms of office shall commence on the date of the organizational meeting of the board. However, the rights and powers of a member whose terms has expired shall remain in effect until the first meeting of the Board following the appointment of that member’s successor; except that no member shall remain in office in this manner for longer than one year after the end of his or her term.”*

We noted the inconsistent approaches followed in the appointment of its Board of Directors.

- There were no documentations to support the appointments of the representatives from the States of Yap and Kosrae.
- Congressional resolutions were provided on the appointment of the Board members representing the States of Pohnpei and Chuuk.
- The terms of office were not specified in the resolution for the Board member representing the State of Pohnpei.
- The terms of office as per the congressional resolution for the Board member representing the State of Chuuk had expired, the term was from November 01, 2017, to November 01, 2020.



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Cause:

Ineffective oversight by the Board of Directors to ensure that requirements of the public law are adhered to on the appointment of the Board members.

Effect:

We cannot determine if the current Board were appointed as per the requirements of PL No. 16-26 and establishing law.

Recommendation:

The oversight function of the Board of Directors to be improved to ensure that the requirements of the public law are adhered to on the appointment of the Board members.

**7.3 Lack of documentation, hence we could not confirm whether the Corporation has adequate and sufficient staff to administer its operations.**

Section 19 of PL No. 10-072 states that *“there shall be a chief executive officer of the Corporation, whose compensation, title, and term of office shall be determined by the Board. The chief executive officer shall be responsible for the management of the operations of the Corporation, and shall, in accordance with the policies established by the Board, retain, direct, and terminate the services of employees.”*

Therefore, it is the Board of Directors that establishes the policies.

According to the CIA Exposition, Part II, 2.13, Procedure 1, *“the Management Review team will periodically review resources to ascertain whether they are sufficient to ensure that air operations can be conducted with safety and in compliance with the exposition.”*

Article 1, Section 1 of the Board of Directors By-Laws specifies that *“all corporate powers and the business and affairs of Caroline Islands Air, Inc. shall be controlled by the Board of Directors. Such powers shall be exercised by the Board consistent with Public Law No. 10-72, as amended, and these By-Laws.”*

Included in the Operations Manual dated February 12, 2023, is a section on personnel files which states that *“Personnel files will be maintained by Caroline Islands Air on all employee and management personnel. They will contain the following information: physical description, date of hire, duties of employee, place of birth, medical certificate for pilots, all license or certificate pertinent to job, and resume.”*

To determine whether the Corporation have adequate and sufficient staff to handle its operations, we requested for the policy on employee selection & recruitment, an approved organization structure and chart, job announcements, job descriptions and the employment contracts for all the staff. There are thirteen (13) staff employed by the Corporation; eleven (11) are in Pohnpei and two (2) staff in Chuuk.

The following findings supported our conclusion that we were not able to confirm whether the Corporation has adequate and sufficient staff to handle its operations.

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**7.3.1 Absence of an approved organization structure**

We requested an approved organization structure and chart as it will show a graphic representation of the Corporation, the relationships of the positions and the jobs within it such as who reports to whom, and who makes decisions about what.

From our review, we acknowledge that the Corporation has an organization chart, however we noted the following:

- There was no evidence that it is the approved structure.
- It is outdated as it includes staff who have left the Corporation. Discussion with the management team noted that there are only thirteen staff (13) currently employed by the Corporation however the organization structure had twenty-three (23) staff including the staff for the stations at the States of Yap and Kosrae. We were informed that the two stations were closed during the COVID-19 period.

Causes:

- Lack of proper oversight function by the management team as they were not aware that it is imperative to have an approved organization structure.
- There is no mechanism in place to prompt the revision of the organization structure.

Effect:

The above can result in miscommunication as there are no approved lines of reporting and communication.

Recommendations:

We recommend strengthening the oversight function by the management team to:

- have an updated and approved Organization Structure; and
- implement a mechanism to prompt the revision and update of the organization structure.

**7.3.2 Absence of an approved employee selection & recruitment policy**

The Corporation does not have an approved policy/procedure on employee selection & recruitment.

We were provided with an Operation Manual dated February 12, 2023. However, we cannot establish whether the Manual has been reviewed and approved by the Board of Directors and if approved, awareness made to all staff. The Manual has a section on the personnel files and does not include any other procedures on human resource matters such as employee selection & recruitment.

The current practice explained by the management team is that potential candidates are 'headhunted', and after agreeing to the salary and conditions of the job, are offered the positions.

Causes:

Ineffective oversight by the Board of Directors to ensure that:

- there are approved policies on human resource matters, especially on employee selection & recruitment.
- Resources are identified to develop the policy.
- Timelines are outlined for when the policy should be approved.

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- Adequate documentation is maintained on the approval of the Operation Manual and awareness made to all staff.

Effects:

- There is no clear guidance for the management team to deliver a fair and consistent recruitment and selection process.
- It will be difficult to confirm whether the right candidate is placed in the right role, without discrimination.

Recommendations:

We recommend that the Board of Directors strengthen their oversight function by ensuring that:

- there are approved policies on human resource matters, especially on employee selection & recruitment.
- appropriate resources are identified to develop the policy and timelines outlined when the policy should be approved.
- documentations on the approval of the Operation Manual and awareness made are properly maintained.

### **7.3.3 Absence of a Proper Filing Records Management System**

The following were noted from our review of the personnel files:

- We were not provided with the job announcements for all the positions except for the CEO and the Chief Financial Officer (CFO).
- The job announcement for the CFO did not include the job description or the minimum requirement to be met by the applicant and the job announcement for the CEO was in a word format and not dated. Hence it was difficult to confirm and ascertain whether the same job announcement was used for the advertisement of the CEO position.
- Seven (7) out of the twenty-three (23) staff did not have valid employment contracts. The employment contracts were either not dated, not endorsed by both parties, or the term of the contract has expired.
- Eight (8) employment contracts were not provided for verification. Two (2) employment contracts are for current employees while six (6) employment contracts are for staff who are no longer employed by the Corporation as of May 30, 2023.
- Personnel files were not updated with the staff qualifications and certificates.

We further noted that the Corporation has an Operation Manual which was dated February 12, 2023. Due to lack of adequate documentations, we cannot confirm whether the Manual has been reviewed and approved by the Board of Directors and if approved, awareness made to all staff.

Causes:

- The Operations Manual does not include the requirements for filing of job announcements and valid contract agreements.
- Lack of proper oversight from the management team to ensure that valid employment contracts are available and maintained for all staff.

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- Absence of a mechanism/system to prompt the staff responsible for human resource matters on the renewal of contracts.
- Absence of a proper records management system to enable records and information pertaining to human resource matters are properly captured to ensure that human resource decisions are based on complete and reliable information.

Effects:

As a result:

- Appropriate audit procedures could not be performed due to limitation of scope.
- Information maintained about the Corporation staff is incomplete.
- Files and records not properly maintained and updated.
- We were not able to confirm whether the Corporation has adequate and sufficient staff to handle its operations.
- We could not confirm whether the staff at the Finance Department have the necessary qualifications and experience to perform its function which includes the timely completion of the single audit requirements.

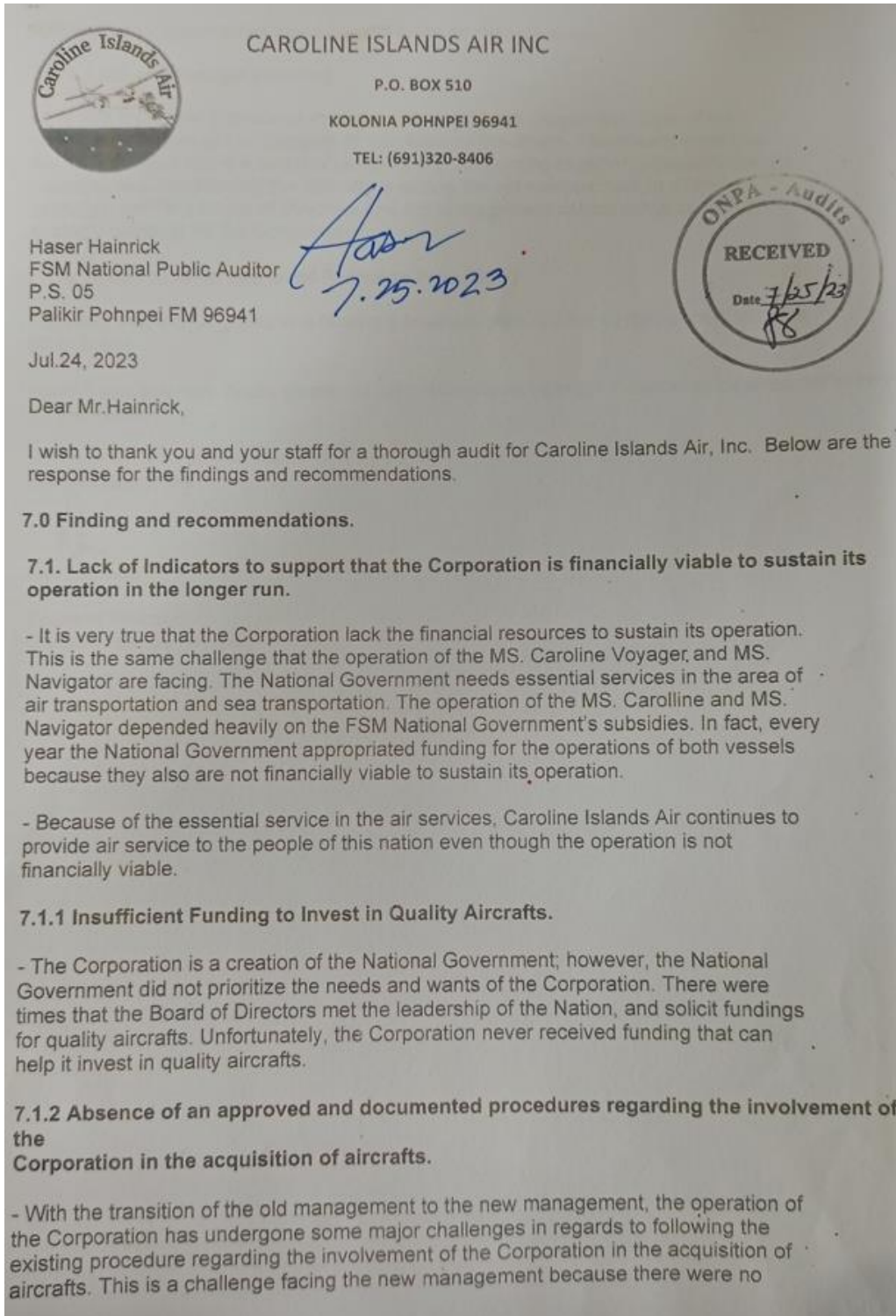
Recommendations:

We recommend that the oversight function by the management team to be strengthened to ensure that:

- The Operations Manual is amended to include the requirements on the filing of job announcements and valid contract agreements in all personnel files.
- A mechanism or system is established that will prompt the persons responsible for human resource matters on the renewal of employment contracts.
- a proper records management system is established to allow for the records and information of staff to be properly captured, resulting in employment decisions made based on complete and reliable information.

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**8.0 MANAGEMENT RESPONSE**



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**8.0 MANAGEMENT RESPONSE (cont'd)**

approved and documented procedures in place for them to follow.

**7.1.3. Lack of Strategic Planning**

- It is true that there is a lack of strategic planning for the Corporation. One of the contributing factors is the changing of members on the Board. There were times that the management and the board of directors are not working together, especially the old management. Considering the difficulty in calling the old management to sit on meetings, both the Board of Directors and the Management cannot come up with good strategic planning for the Corporation.

**7.1.4. Absence of an approved Business Plan (BCP)**

- It is true that the Corporation is lacking a business plan, we are trying our best to come up with one.

Again thank you very much, please do not hesitate to let us know if additional inquiries necessary for the audits.

Respectfully yours



Alik Jackson  
Chairman  
Board of Directors  
Caroline Islands Air, Inc.

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**9.0 ONPA EVALUATION OF MANAGEMENT RESPONSE**

The audit team requested written management responses from the management of the Corporation on Monday, July 17, 2023. Overall, the Board of Directors and management agreed with the findings and recommendations in the report. However, the management did not submit a plan of action on how the recommendations will be implemented.

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**10.0 NATIONAL PUBLIC AUDITOR COMMENTS**

We would like to thank the Board of Directors, management, and staff of the Corporation for their assistance and cooperation during the audit. We anticipate positive implementation results when we carry out a follow-up of this audit.

We have provided copies of the final report to the President and members of the 23<sup>rd</sup> FSM Congress. Furthermore, the report is made available to the public through our official website and upon request.

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



Haser H. Hainrick  
National Public Auditor  
Friday, July 28, 2023



