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June 22, 2021

Mr. Faustino Yangmog
General Manager

P.O. Box 667
Colonia, Yap 96943

Dear Mr. Yangmog:

In planning and performing our audit of the financial statements of the Yap State Public Service Corporation (the Corporation), a component unit of the State of Yap, as of and for the year ended September 30, 2020, (on which we have issued our report dated June 22, 2021), 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, we considered the Corporation's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Corporation's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, in connection with our audit, we identified, and included in the attached Appendix I, deficiencies related to the Corporation's internal control over financial reporting as of September 30, 2020 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated June 22, 2021, on our consideration of the Corporation'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 definition of a deficiency is also set forth in the attached Appendix I.

A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with this report.

This report is intended solely for the information and use of the Board of Directors, management, others within the organization, and the Office of the FSM National Public Auditor and is not intended to be and should not be used by anyone other than these specified parties.

We will be pleased to discuss the attached comments with you and, if desired, to assist you in implementing any of the suggestions.

We wish to thank the staff and management of the Corporation for their cooperation and assistance during the course of this engagement.

Very truly yours,

Deloitte & Touche LLP

SECTION I - DEFICIENCIES

We identified the following deficiencies involving the Company's internal control over financial reporting as of September 30, 2020 that we wish to bring to your attention:

<u>Bank Reconciliation</u>

Stale dated payroll checks of $3,130 were noted as of September 30, 2020.

<u>Recommendation:</u> We recommend YSPSC determine appropriate action to resolve outstanding stale checks. This matter was reported in the prior year letter to management.

<u>Inventories</u>

Of 22 inventory items counted on 06/07/21, the Company was unable to rollback 6 counts to the 09/30/20 inventory listing due to unreported stock returns, issuance slips and receipts.

Further, the following were noted during our physical count:

- Inventories returned from customers (conventional meters) were counted during the physical count and added back to inventory. However, no receipts were prepared for the returned items.
- Obsolete, used, old or non-inventory items stored in the warehouse are not properly segregated and marked as non-inventory items.
- Second counts were not performed by a different count team.
- Work orders and stock issuance reports were not consistently provided to the supply office.

Also, documentation of the FY20 inventory obsolescence assessment was not provided.

<u>Recommendation</u>: We recommend YSPSC adopt and implement appropriate internal control policies over counting, recording, monitoring, and valuation of inventories. Further, we recommend YSPSC assess and document the adequacy of the allowance for inventory obsolescence. This matter was reported in the prior year letter to management.

<u>Investments</u>

We noted a difference between investments per the general ledger and investments per confirmation of $11,010 which was corrected with an audit adjustment.

<u>Recommendation:</u> We recommend YSPSC obtain investment statements and timely record adjustments, if necessary.

<u>Utility Plant</u>

A physical verification of fixed assets was not performed during the year. Also, the source of funding was not indicated in the fixed asset register. Also, a year-end $43,576 adjustment was capitalized which resulted from a reconciliation of major repairs with actual inventory on hand. Materials issuances to the project supported by signed issuance slips were not timely recorded, reviewed and monitored.

<u>Recommendation</u>: We recommend YSPSC perform periodic physical counts and update the fixed asset register to reflect the source of funding. Also, YSPSC should perform periodic reconciliation of fixed assets and all issuances to projects should be supported by signed issuance slips.

SECTION I –DEFICIENCIES, CONTINUED

Capital Assets Capitalization Policy

YSPC has not formalized a capital asset capitalization policy.

Recommendation: We recommend that YSPSC formalize a capital asset capitalization policy. This matter was reported in the prior year letter to management.

Allowance for Doubtful Accounts

Documentation of the allowance assessment for FY20 was not provided. We further noted that YSPSC did not regularly review cash power accounts to identify nonmovements.

Recommendation: We recommend that YSPSC maintain and document the allowance rationale and continue to assess its adequacy. We further recommend that YSPSC perform at least a quarterly review of cash power accounts for nonmovement. This matter was reported in the prior year letter to management.

Line and Water losses

Power and water generation and internal consumption from outer island power and water plants do not appear to be adequately monitored.

Recommendation: We recommend that YSPSC adopt appropriate measures to monitor and analyze line and water losses. This matter was reported in the prior year letter to management.

Inventory Issuances

A year-end $49,967 adjustment was recorded to materials and supplies inventory which resulted from a reconciliation with actual inventory on hand. Inventory issuances supported by signed issuance slips were not timely recorded, reviewed and monitored.

Recommendation: We recommend YSPC perform periodic reconciliation of inventories and that all inventory issuances be supported by signed issuance slips. This matter was reported in the prior year letter to management.

Beginning Net Position

Beginning net position did not agree with prior year audited net position. This was corrected during the audit process.

Recommendation: We recommend YSPSC review beginning net position and verify that such agrees with the prior audited balance.

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SECTION II – DEFINITION

The definition of a deficiency is as follows:

A *deficiency* in internal control over financial reporting 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 deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when (a) a properly designed control does not operate as designed, or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.

MANAGEMENT'S RESPONSIBILITY FOR, AND THE OBJECTIVES AND LIMITATIONS OF, INTERNAL CONTROL OVER FINANCIAL REPORTING

The following comments concerning management's responsibility for internal control over financial reporting and the objectives and inherent limitations of internal control over financial reporting are adapted from auditing standards generally accepted in the United States of America.

Management's Responsibility

The Corporation's management is responsible for the overall accuracy of the financial statements and their conformity with generally accepted accounting principles. In this regard, management is also responsible for establishing and maintaining effective internal control over financial reporting.

Objectives of Internal Control over Financial Reporting

Internal control over financial reporting is a process affected by those charged with governance, management, and other personnel and designed to provide reasonable assurance about the achievement of the entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. Internal control over the safeguarding of assets against unauthorized acquisition, use, or disposition may include controls related to financial reporting and operations objectives. Generally, controls that are relevant to an audit of financial statements are those that pertain to the entity's objective of reliable financial reporting (i.e., the preparation of reliable financial statements that are fairly presented in conformity with generally accepted accounting principles).

Inherent Limitations of Internal Control over Financial Reporting

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.