

May 7, 2007

To the Board of Directors of
Kosrae Utilities Authority:

In planning and performing our audit of the financial statements of Kosrae Utilities Authority (the Company), as of and for the year ended September 30, 2006, on which we have issued our report dated May 7, 2007, we developed the following recommendations concerning matters related to the Company's internal control and certain observations and recommendations on other accounting and administrative matters. Our observations and recommendations are summarized below.

Inventory

Comment:

- Inventory balances are only adjusted at year-end based on physical counts, which contributes to the possibility of returned items not being recorded.
- There were no procedures present to prevent double-counting or omitting counts of inventory. In some stockrooms, index cards were utilized. However, no signatures were present indicating when the count was taken.
- Inventories in the Pole Hardening Stockroom were not safeguarded and were easily accessible. Subsequent to the fiscal year end, KUA installed physical barriers to assist in ensuring materials are only accessible by authorized persons.
- Although a system is in place to ensure inventory usage is supported by material issuance slips, this was not consistently followed. Consequently, during the physical inventory count, certain discrepancies were encountered.

Recommendation:

KUA should implement a perpetual inventory system.

* * * * *

This report is intended solely for the information and use of Board of Directors and management of the Company, and is not intended to be and should not be used by anyone other than these specified parties.

We would like to thank the accounting staff and management for their assistance during the course of our audit. Should you have any questions regarding the matters discussed herein, please contact our office at your convenience.

Very truly yours,

