

June 7, 2010

The Board of Directors
Federated States of Micronesia
Coconut Development Authority

Dear Members of the Board:

In planning and performing our audit of the financial statements of the Federated States of Micronesia (FSM) Coconut Development Authority (the Authority), a component unit of the FSM National Government, as of and for the year ended September 30, 2009 (on which we have issued our report dated June 7, 2010), 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 Authority'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 Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Authority'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. However, in connection with our audit, we identified, and included in the attached Appendix I, deficiencies related to Authority's internal control over financial reporting and other matters as of September 30, 2009 that we wish to bring to your attention.

We have also issued a separate report to the management, also dated June 7, 2010, on our consideration of Authority'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.

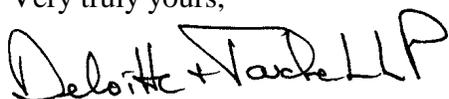
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with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

This report is intended solely for the information and use of the Board of Directors, management and others within the organization, 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 Authority for their cooperation and assistance during the course of this engagement.

Very truly yours,



SECTION I – CONTROL DEFICIENCIES

We identified, and have included below, control deficiencies involving Authority's internal control over financial reporting as of September 30, 2009 that we wish to bring to your attention:

Cash Overage

Comment: The Authority did not deposit cash overages from cash sales until year end.

Recommendation: We recommend that cash overages be deposited on the next business day.

Fixed Asset Register

Comment: A warehouse in the State of Chuuk has not been utilized since FY2008 but this asset was still listed in the fixed asset register and was being depreciated. We further note that the fixed asset register has certain items that may not exist anymore.

Recommendation: We recommend that the Authority update the fixed asset register in a timely manner.

Sales Deposits

Comment: Cash sales were kept in the Authority's safe for a range of 1 to 10 days.

Recommendations: We recommend that cash sales be deposited in a timely manner.

Audit Adjustments

Comment: Numerous audit adjustments were proposed and recorded to the general ledger after year end. This indicates that a more thorough review of the general ledger is required.

Recommendation: We recommend that reviews of the general ledger be timely performed.

Inventory Valuation

Comment: The Authority uses an inventory costing method other than the weighted average, and year-end inventory balances were misstated.

Recommendation: We recommend that the Authority use the weighted average cost method per Authority policy.

SECTION II – DEFINITION

The definition of a control deficiency that is established in AU 325, *Communicating Internal Control Related Matters Identified in an Audit*, is as follows:

A *control deficiency* 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 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 is not always met. A deficiency in *operation* exists when a properly designed control does not operate as designed, or when the person performing the control does not possess the necessary authority or qualifications 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 Authority'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.