

June 4, 2010

The Board of Directors
Chuuk Public Utility Corporation:

In planning and performing our audit of the financial statements of the Chuuk Public Utility Corporation (CPUC), as of and for the year ended September 30, 2009 (on which we have issued our report dated June 4, 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 CPUC'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 CPUC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of CPUC'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 CPUC'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 4, 2010, on our consideration of CPUC'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.

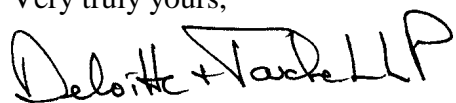
The definition of a deficiency is also set forth in the attached Appendix I.

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.

Very truly yours,



SECTION I – CONTROL DEFICIENCIES

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

Bank Reconciliation

Comment: CPUC should perform monthly reconciliations of its bank accounts. Management could not explain the unlocated amount of \$44,069 in the September 30, 2009 bank reconciliation.

Recommendation: We recommend that reconciliations be performed on a monthly basis and differences be investigated and resolved.

Fixed Assets

Comment: The fixed asset register should detail assets owned. CPUC has not performed a physical count of its fixed assets during the past several years.

Recommendation: We recommend that management verify its assets and reconcile such against the fixed asset register.

Construction in Progress

Comment: Project completion dates should be followed. The Pole Hardening Project is still in progress and has passed its extended completion deadline of October 11, 2006. No additional extension was obtained.

Recommendation: Management should submit and obtain a project extension.

Construction in Progress

Comment: Construction in progress (CIP) during the year should be capitalized upon completion. Certain projects have been recorded as CIP for a long period of time and management could not advise whether the project was ever completed.

Recommendation: We recommend that management closely monitor construction projects to ensure that completed projects are properly capitalized and related depreciation expense is recorded.

Other Accounts Payable

Comment: A detail schedule is maintained to support the other accounts payable account. No documents, such as vendor invoices, could be provided to support \$135,248 of recorded payables. Management subsequently provided documentation to allow for the write-off this account in May 2010.

Recommendation: We recommend that details of accounts payable be maintained and be reconciled to ensure proper recording of liabilities.

Long Overdue Account

Comment: CPUC should review the account receivable subsidiary ledger and follow up on accounts that are over ninety days past due. Numerous receivable balances are over ninety days past due, including several more than one year old. In addition, delinquent accounts over ninety days are not subject to timely follow up.

Recommendation: We recommend the following:

- To avoid future collectibility problems, management should emphasize the importance of timely follow-up on outstanding invoices by implementing a system of customer contact when receivable balances become greater than thirty days old.
- A policy be established whereby a listing of all accounts with balances ninety days and older is submitted to management to review for collectibility, to increase collection efforts wherever possible and to write off all uncollectible receivable balances.

Inventory Physical Count

Comment: For 2 (or 16%) of 13 items counted, we noted the following discrepancies.

<u>Item</u>	<u>Part Number</u>	<u>Per Entity</u>	<u>Per D&T</u>	<u>Difference</u>
O' Ring	6V-7681	2	1	1
O' Ring	1H-8278	1	3	(2)

Recommendation: We recommend that second counts be performed and inventory count procedures be followed.

Cash Receipts and Collection Report

Comment: Per examination of cash receipts and related cash collection reports, we noted the following:

1. For three of fifty accounts receivable accounts tested, the cash collection report balance did not agree with the validated deposit slip.
2. For seventeen of fifty-two cash power revenues tested, the cash collection report balance did not agree with the validated deposit slip.
3. For eight of fifty-two cash power revenues tested, cash receipts were not available for examination.

Recommendation: We recommend that differences be investigated and be resolved in a timely manner. Also, cash receipts should be maintained and be properly stored.

Written off Accounts

Comment: Customer accounts written off in previous years continue to be included in the account receivable subledger.

Recommendation: We recommend that customer accounts previously written off be deleted from the accounts receivable subledger.

Cash Collected Used for Operation

Comment: Cash collected for the day was frequently used for small purchases for operating purposes. This increases the risk of misappropriation of cash and makes errors difficult to trace.

Recommendation: We recommend that daily cash collections be deposited intact. In addition, the petty cash fund may be considered for small purchases.

Erroneous in Recording of Power Usage

Comment: For two of forty four revenue transactions tested, actual power usage and revenue were not properly recorded.

Recommendation: We recommend that management ensure that actual power usage and revenue is properly recorded and captured.

Production Fuel Transactions

Comment: Production fuel transactions should be supported by invoices and a cashier's check, check, or payment slip. These documents should be maintained on file and be available for examination. We noted the following conditions:

1. For eleven of seventy-six samples tested, no invoices could be provided.
2. For nine of seventy-six samples tested, no invoice and cashier check, check, or payment slip could be provided.

Recommendation: CPUC should strengthen its controls to ensure invoices and cashier checks, checks, or payment slips are maintained on file.

Payroll Transactions

Comment: Payroll transactions should be supported by employee personnel action forms, timesheets, and other underlying documentation to validate calculations and recording.

1. For one of seventeen samples tested, a personnel action form could not be provided
2. For one of seventeen samples tested, the timesheet could not be provided.

Recommendation: CPUC should require payroll documents to be maintained on file and be available for examination.

Proper Recordkeeping of Documents

Comment: No invoice and cancelled check could be provided to substantiate the recorded amount of \$1,982 per JE-J0360.

Recommendation: CPUC should strengthen its controls to ensure the proper safekeeping of its documents.

Recording of Transactions in Proper Period

Comment: Payroll of \$17,382 for the pay period ending August 30, 2008 was not recorded in the correct accounting period. Rather, it was recorded during the year ended September 30, 2009.

Recommendation: We recommend that payroll transactions be recorded in the proper period.

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

CPUC'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.