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May 9, 2011

Mr. Welson Panuel
Executive Director
Pohnpei State Housing Authority
P.O. Box 1109
Kolonia, Pohnpei 96941

Dear Mr. Panuel:

In planning and performing our audit of the financial statements of the Pohnpei State Housing Authority (the Authority), a component unit of the Pohnpei State Government, as of and for the year ended September 30, 2010 (on which we have issued our report dated May 9, 2011), 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 the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the 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 the Authority's internal control over financial reporting and other matters as of September 30, 2010 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated May 9, 2011, on our consideration of the 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 management, others within the organization, and the Office of the National Public Auditors 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,

Deloitte & Touche LLP

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SECTION I – CONTROL DEFICIENCIES

We identified, and have included below, control deficiencies involving the Authority's internal control over financial reporting as of September 30, 2010 that we wish to bring to your attention:

Fixed Assets

Comment: Controls do not appear to be in place to require periodic physical verification of fixed assets.

Recommendation: We recommend that the Authority perform periodic verifications of fixed assets.

Employee Advances

Comment: Employee advances are not repaid per documented payment schedules and $149,300 remains uncollected at year end. As the entire amount has been previously included in the allowance for uncollectable accounts, no impact on the financial statements is anticipated.

Recommendation: We recommend that the Authority prepare and send billings to these formerly employees. We also recommend that the Authority review its credit policy.

Loan Receivable Balance

Comment: We noted one instance where the restructured balance of an outstanding loan did not agree with the subsidiary ledger balance by $1,583. Furthermore, we noted that one employee loan balance transferred to the loan database was incorrect by $388.

Recommendation: While the difference was immaterial and did not require adjustment, we recommend that management review amounts entered into the loan database to ensure that the subsidiary ledger balance reflects actual outstanding loans.

Assigned Loan Receivable Balance

Comment: Per the Memorandum of Understanding (MOU) with the U.S. Department of Agriculture (USDA), the Authority is to work closely with USDA to collect payments or to foreclose on loans. Section 6.1 states that after an account has been accelerated and all appeals have been exhausted, within 30 days of receipt of a letter from USDA stating that the loan has been accelerated, the promissory note(s) will be assigned to the Authority and the debt will be paid in full by the Authority . It appears that the Authority was notified over ten years after the loans appeared to be deemed delinquent by USDA.

Recommendation: We recommend examination of the MOU to determine whether all parties complied with the promises and obligations, and whether these loans were valid receivables per local statutes, since they had been outstanding for what appears to be over a decade since being deemed delinquent by USDA.

SECTION II – OTHER MATTERS

We noted no matters related to operations, compliance with laws and regulations, and best practices involving internal control over financial reporting that we wish to bring to your attention.

SECTION III – DEFINITION

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

A *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 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 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.