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June 7, 2016

Mr. Faustino Yangmog
General Manager
Yap State Public Service Corporation
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, 2015, (on which we have issued our report dated June 7, 2016), 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 and other matters as of September 30, 2015 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated June 7, 2016, 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, 2015 that we wish to bring to your attention:

Fuel Meters

The Corporation relies on FSMPC's meter readings and the loading manifest to measure the quantity of fuel delivered and invoiced. YSPSC has no control procedure in place to independently verify actual gallons of fuel delivered as tank meters are not fully functional.

Recommendation: We recommend YSPSC maintain functional meters to verify actual gallons of fuel received. This matter was reported in the prior year letter to management.

Other Income

The Corporation recognized $6,000 of income from selling two containers acquired from a former vendor that were used to transport solar power systems. The containers were subsequently sold and resulted in the offset of an outstanding liability. Adequate documentation was not available on file to support the transaction and the valuation of the sold containers.

Recommendation: We recommend the Corporation improve internal control policies and procedures by documenting recorded transactions with invoices and relevant documents to support valuations.

Line Losses

For the year ended September 30, 2015, the Company generated 12,200,148 kwh while it billed (including internal use) 10,017,365 kwh. The calculated line loss appears to be 2,182,783 kwh or 18%. Power generation and internal consumption from outer island power plants do not appear to be adequately monitored.

Recommendation: We recommend that the Company adopt appropriate measures to monitor line losses and facilitate line loss reduction.

Procurement

Of eighteen for operating expenses tested, we noted the following:

1. PO 8777 dated July 9, 2014 and paid on December 18, 2014 amounting to $12,413 did not evidence adequate documentation of the vendor selection process. The selected vendor was not the lowest bidder.

2. The following POs did not evidence a competitive procurement process. Supporting vendor quotations were not on file.

PO Number	PO Date	Amount
20142	April 15, 2015	$37,250
20247	July 6, 2015	$15,314

3. A purchase of $1,213 of office supplies via credit card on March 16, 2015 did not evidence competitive procurement processes. No quotations from qualified vendors and no formal invoice was on file.

4. Check no. 37278 dated May 1, 2015 for $6,000 was issued to a consultant as payment for services rendered. Adequate documentation was not provided to evidence the request and the necessity of acquiring the consultant's services, including related qualifications.

SECTION I –DEFICIENCIES, CONTINUED

Procurement, Continued

Recommendation: We recommend the Company adhere to compliance with its procurement policy and improve documentation of the competitive procurement process.

Grant Expenses

Expenses of $19,615 were recorded to a grant (GL 58008) after it ended in February 2015. The amount should have been reclassed as an operating expense due to term restrictions, while awaiting grant extension approval. The grantor requires a narrative report prior to grant extension which the Corporation has yet to submit.

Recommendation: We recommend expenses be properly classified. We further recommend YSPSC revisit its long outstanding WIP and timely comply with grant requirements.

Payroll and Employee Advances

Advance paid time off (PTO) of $13,926 was incorrectly recorded as salaries expense instead of as employee advances. The advanced PTOs cover 2 to 3 employment contract years that had yet to be earned. An additional $5,554 of employee advances were incorrectly reversed on September 30, 2015.

Employee receivables included in GL account 11057 of $11,297 as of September 30, 2015 did not indicate significant collection in comparison with the prior year outstanding balance.

Overtime charges of $14,708 were not adequately supported by detailed calculations.

Recommendation: We recommend YSPSC monitor PTO advances and review journal entries and supporting documentation. Overtime charges should be adequately supported and reviewed. Collection of employee receivables should be enforced. The Corporation may wish to consider limiting employee advances.

Inventories

Cost testing of 20 inventory items, yielded 11 with a net understatement of $22,515. The total extrapolated difference per the test was $44,022. Tests also noted that inventory issuance forms are not properly utilized as a basis for recording materials and supplies expense.

Recommendation: We recommend management perform adequate review of inventory valuation. YSPSC should also perform regular assessments of inventory obsolescence for non-moving items.

Revenues and Billing

Two of seventy-five revenue items tested noted zero consumption for three billed months without corresponding collection. Adequate documentation was not on file to indicate that consideration of possible disconnection occurred.

Tests of 25 new meter installations resulted in the following:

1. One was not supported by documentation of the collection of the $45 installation fee.
2. Two were billed late. A one month delay occurred in billing the installed meters.
3. One outer island installation was not supported by an application and a meter installation report.

SECTION I –DEFICIENCIES, CONTINUED

Revenues and Billing, Continued

Of 23 accounts receivable tested, one indicated no collection for seven billing periods as of September 30, 2015. The customer was disconnected nine months after nonpayment. YSPSC policy provides for disconnection after three months' missed payments.

Recommendation: We recommend YSPSC perform timely meter readings and billings of installed meters. Furthermore, we recommend adequate review and reconciliation of daily collections. We also recommend the Corporation review nonpaying customers and determine timely appropriate action.

Journal Entries

Journal entries lack a preparer and a reviewer signature that evidences independent review prior to posting.

Recommendation: We recommend that adequate review and approval of journal entries occur.

Allowance for Doubtful Accounts

A $30,763 understatement of the allowance for doubtful accounts occurred as of September 30, 2015. As the amount was not considered material to the financial statements, an audit adjustment was not recorded. Adequate documentation was not available to indicate that the Corporation performed an assessment of the adequacy of the allowance for doubtful accounts.

Recommendation: We recommend YSPSC perform periodic assessments of the adequacy of the allowance for doubtful accounts.

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.