

March 13, 2012

Mr. Jemi Nashion  
General Manager  
Tobolar Copra Processing Plant, Inc.:

Dear Mr. Nashion:

In planning and performing our audit of the financial statements of the Tobolar Copra Processing Plant, Inc. (TCPPI) as of and for the year ended September 30, 2011 (on which we have issued our report dated March 13, 2012 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 TCPPI'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 TCPPI's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of TCPPI'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 TCPPI's internal control over financial reporting and other matters as of September 30, 2011 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated March 13, 2012, on our consideration of TCPPI'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.

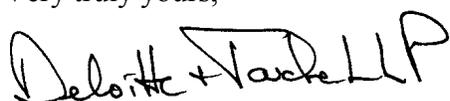
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with 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 Auditor-General 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 TCPPI 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 TCPPI's internal control over financial reporting as of September 30, 2011 that we wish to bring to your attention:

### (1) QuickBooks Accounting System Set-up

The customer sub ledger accounts were not properly set-up in the QuickBooks accounting system when balances were migrated from the previous accounting system. We recommend appropriate set-up of customer accounts in QuickBooks to facilitate generation of reliable reports. This matter was reported as a finding in the audit of TCPPI for fiscal year 2010.

### (2) Accounts Receivable

No allowance for doubtful accounts analysis is performed. TCPPI does not implement a review process of receivables and related allowance for doubtful accounts. We recommend that management perform counterparty reconciliation, review and evaluate balances to ensure that invalid receivables are written off and that doubtful accounts are adequately provided for. TCPPI should determine and document the methodology and assumptions to be used as the basis for provisioning. Balances should be evaluated, collective efforts be implemented, and provisions be provided as appropriate. Historical loss experience and publicly observable data on loss experience by the industry or the risk profile of the counterparty should be considered rather than provisioning based solely on an ageing analysis. This matter was reported as a finding in the audits of TCPPI for fiscal years 2009 and 2010.

### (3) Employee Receivables

At September 30, 2011 and 2010, receivables from employees included credits of \$6,603 resulting from the lack of proper monitoring of employee accounts. Additionally, suspense accounts maintained for temporary postings of employee charges and deductions had a credit balance of \$11,603 at year-end. We recommend that management establish policies and procedures to govern monitoring and review of receivables from employees. This matter was reported as a finding in the audits of TCPPI for fiscal years 2005 through 2010.

### (4) Inventory

It has been TCPPI's practice to record inventories as an expense upon purchase and then record an inventory adjustment at year end based on annual physical count. We noted that although the following control procedures are maintained, deficiencies are present in the actions implemented.

The production department performs daily counts of copra raw materials and copra oil. However, no independent checks and verification of inventory on hand is performed and periodic reconciliations of book to actual inventory on hand are not carried out.

Previously, monthly inventory reports were prepared to assist production analysis. This practice assisted TCPPI's production efficiency; however, since the assigned employee resigned, these reports were not prepared during the year.

We recommend that adequate recordkeeping of inventory purchases be made, periodic cyclical counts be performed during the year, and complete and timely reconciliations be performed to properly account for available inventories. TCPPI should ensure that adequate internal controls over inventories are established to properly safeguard inventories against susceptibility of pilferage and misappropriation. This matter was reported as a finding in the audits of TCPPI for fiscal years 2005 through 2010.

(5) Advances to Suppliers and Prepayments

We noted a delay of four months or more in the receipt of goods/supplies ordered. Considering the significant dollar amount of advance payments, we recommend that management consider the inclusion of clauses providing for adjustment in prices, time of performance or other appropriate contract provisions covering delays in delivery or performance by the supplier.

(6) Cash

The financial officer handles the following incompatible duties: (a) authorized check signatory, (b) safekeeping of cash, and (c) bank reconciliation preparation. Segregation of duties should exist such that (1) approval, (2) asset custody, and (3) accounting/reconciling functions are not handled by only one person. Lack of segregation of duties may allow irregularities to go undetected. We recommend that management revisit the authorized check signatories and require that access to cash and responsibility for maintaining the accountability for such asset is assigned to personnel not responsible for other cash functions.

**SECTION II - OTHER MATTERS**

Our observations concerning other 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 at this time are as follows:

(1) Journal Entries and Bank Reconciliation

Based on our review of manual journal entry files and bank reconciliation, we noted that sign-offs by the preparer and reviewer are not dated. We recommend that the date be specified to determine timeliness of control procedures performed.

(2) Inventory

Copra oil, copra cake and soap and materials are valued at lower of production cost, which includes raw copra, direct labor and factory overhead, or market (net realizable value). However, TCPPI has not established a methodology to determine the production cost of such inventories. Valuation done at year-end is based on net realizable value without comparison of such to cost. In addition, basis of cost to sell for copra meal cannot be provided. We recommend that management adopt a methodology to determine the value of inventory at cost. This matter was reported as a finding in the audits of TCPPI for fiscal years 2008 through 2010.

(3) Accrued Expenses

A net debit balance amounting to \$3,457 is included in liabilities relating to payable to Treasurers or purchasers of copra. These remain in TCPPI's books despite inactivity for several years. We recommend that management verify the balances to determine if such should be removed from the books. This matter was reported as a finding in the audits of TCPPI for fiscal years 2008 through 2010.

**SECTION III - DEFINITIONS**

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 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**

TCPPI'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.