

May 2, 2019

Mr. Jemi Nashion  
General Manager  
Tobolar Copra Processing Authority:

Dear Mr. Nashion:

In planning and performing our audit of the financial statements of Tobolar Copra Processing Authority (the Authority) as of and for the year ended September 30, 2018 (on which we have issued our report dated May 2, 2019 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 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, 2018 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated May 2, 2019, 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.

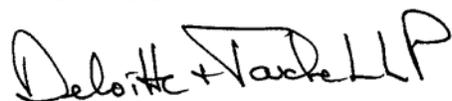
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with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

This report is intended solely for the information and use of the 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 the Authority for their cooperation and assistance during the course of this engagement.

Very truly yours,

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is written in a cursive, stylized font.

**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, 2018 that we wish to bring to your attention:

(1) Accounts Receivable

Analyses of the allowance for doubtful accounts are not performed. The Authority did not implement a review process over receivables and the related allowance for doubtful accounts. We recommend that management perform counterparty reconciliation, review and evaluation of balances that will facilitate invalid receivables being written-off and doubtful accounts being adequately provided for. The Authority should determine and document the methodology and assumptions to be used as the basis for its bad debt provision. 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 aging analysis. This matter was reported as a finding in the audits of the Authority for fiscal years 2009 through 2017.

(2) Employee Receivables

At September 30, 2018, employee receivables pertaining to cash shortages from copra purchases and advances for merchandise ordered and collected through salary deductions amounted to \$14,922 and \$23,715, respectively. However, monitoring of these receivable accounts did not appear to be performed. These amounts have been fully provided for within the allowance for doubtful accounts. We recommend that management establish policies and procedures to govern monitoring and review of employee receivables. This matter was reported as a finding in the audits of the Authority for fiscal years 2005 through 2017.

(3) Inventory

It has been the Authority's practice to record inventories as an expense upon purchase and then to record an inventory adjustment at year end based on the annual physical count. Although certain control procedures are maintained, deficiencies are present in the actions implemented. We recommend that adequate recordkeeping of inventory purchases occur, periodic cyclical counts be performed, and complete and timely reconciliations be performed to properly account for available inventories. The Authority should establish adequate internal controls over inventories. This matter was reported as a finding in the audits of the Authority for fiscal years 2005 through 2017.

(4) Cost of Goods Sold – Copra Purchases

We were unable to verify the completeness of copra purchase tickets due to missing tickets that were not properly filed. We recommend management establish internal control over copra purchases and require monitoring and sequential filing of copra purchase tickets. This matter was reported as a finding in the audits of the Authority for fiscal year 2014 and 2017.

(5) Fixed assets physical count and tagging

A physical count of fixed assets was not performed during fiscal year 2018. Upon further verification, there were fixed assets that have no tags and cannot be identified. We recommend management to perform periodic physical counts and tag all fixed assets.

(6) Advances to a supplier

Of the total \$181,403 advances to a supplier, \$66,419 has been outstanding for more than 9 months as of September 30, 2018. We recommend that management continuously follow up on the delivery of these capital assets.

**SECTION I - CONTROL DEFICIENCIES, CONTINUED**

(7) MISSA and RMI withholding taxes

Examination of SS tax payments revealed late filing of SS tax returns for the quarter ended 09/30/18, which was filed and paid on 11/14/18.

SS tax returns are due on the 10th day of the month following the quarter-end. The Authority was non-compliant with this requirement.

Examination of withholding tax payments (Form 1178) revealed late filing of tax returns for the payroll period ending 09/03/18 to 09/30/18, which was filed and paid on 10/25/18.

Form 1178 is due within two weeks following the preceding four week payperiod. Tobolar was noncompliant with this requirement.

We recommend management timely file and remit SS tax and withholding tax payments in accordance with established requirements.

**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) Inventory

Copra oil, copra cake and soap and materials are valued at the lower of production cost, which includes raw copra, direct labor and factory overhead, or market (net realizable value or NRV). The Authority adopted a new methodology to determine the value of inventory at cost wherein the basis of unit cost for copra meal is estimated at 20% of the unit cost of crude oil. Year-end valuation is based on computed production unit costs without comparison to NRV. We recommend that management adopt the valuation of inventory at the lower of production cost or NRV.

(2) Product Costing

The Authority established control procedures over the calculation of unit inventory cost per product which is used to value ending inventory. However, the unit cost used to value ending inventory was not updated for the current cost of materials, labor and overhead. We recommend management apply consistency in calculated unit costs to value ending inventories and cost of sales.

(3) Journal Vouchers

Some journal vouchers are not prepared and therefore, such are not reviewed by supervisory personnel independent of the preparation process.

We recommend management establish policies and procedures in place requiring the preparation, review and approval of journal vouchers.

**SECTION III - DEFINITIONS**

The definition of a deficiency 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**

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.