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June 28, 2016

Mr. Jared C. Morris  
Chief Executive Officer  
Federated States of Micronesia Petroleum Corporation  
P.O. Box 1762  
Kolonias, Pohnpei FM 96941

Dear Mr. Morris:

In planning and performing our audit of the financial statements of the Federated States of Micronesia Petroleum Corporation (the Company), a component unit of the FSM National Government, as of December 31, 2015, (on which we have issued our report dated June 28, 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 Company'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 Company's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Company'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 Attachment I, deficiencies related to the Company's internal control over financial reporting and other matters as of December 31, 2015 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated June 28, 2016, on our consideration of the Company'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 Attachment I.

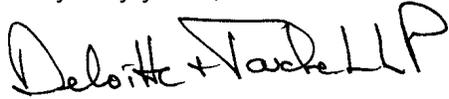
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Attachment II and should be read in conjunction with 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 Company for their cooperation and assistance during the course of this engagement.

Very truly yours,

A handwritten signature in black ink that reads "Deloitte + Tatchell LLP". The signature is written in a cursive, slightly stylized font. The word "Deloitte" is on the left, followed by a plus sign, and "Tatchell LLP" is on the right. The letters are connected and fluid.

## SECTION I –DEFICIENCIES

We identified the following deficiencies involving the Company's internal control over financial reporting as of December 31, 2015 that we wish to bring to your attention.

### (1) Unrecorded Liability

#### Comment:

Unpaid invoice (#INT2015-09) dated November 25, 2015 for items shipped and in transit in December 2015 was not recorded as a liability as of December 31, 2015. This was corrected through an adjusting entry when brought to management's attention.

#### Recommendation:

The Company should strengthen control procedures to verify the completeness of liabilities at each reporting date.

### (2) Letter of Credit (LOC)

#### Comment:

A written agreement or equivalent documentation to establish the terms of letters of credit (LOC) and basis of LOC rates between FSMPC and two utilities companies were not available.

#### Recommendation:

The Company should establish written agreements with the utility companies.

## SECTION II –OTHER MATTERS

We noted below other matters related to our observations concerning operations, compliance with laws and regulations, and best practices involving internal control over financial reporting that we wish to bring to your attention.

### (1) Accounts Receivable (A/R)

#### Comment:

As of December 31, 2015, AR subsidiary ledger (SL) included receivable of \$27,413 that was paid by customer before year-end. The payment was posted in the general ledger (GL) but the SL was not updated.

#### Recommendation:

Timely reconciliation of AR SL and AR GL should be performed, and differences should be timely investigated.

**SECTION II –OTHER MATTERS, CONTINUED**

(2) Inventory

Comment:

For all locations other than Chuuk, the Company did not add back inventory quantities sold after December 31, 2015 but prior to closing date on January 1-4, 2016. This was corrected through a proposed audit adjustment.

Recommendation:

The Company should improve its control procedures over yearend inventory closing.

(3) Accounts Payable (A/P)

Comment:

As of December 31, 2015, we noted an unidentified difference of \$23,342 between AP SL and GL.

Recommendation:

AP SL and AP GL should be timely reconciled, and differences should be timely investigated.

(4) Customer Credits

Comment:

As of December 31, 2015, an unapplied customer credit of \$36,761 dated back to 2010 was noted. The latest sales transaction with the customer was in December 2015 but the customer credit was not applied to the customer's purchases.

Recommendation:

Regular monitoring of customer credits should be performed and applied to customer purchases.

(5) Lease Agreements

Comment:

For one of sixteen lease transactions tested, an updated signed lease agreement after expiration of February 2014 was not made available.

Recommendation:

Regular monitoring of lease agreements should be performed.

(6) Contract Copy

Comment:

A contract or equivalent obligating document was not provided for \$247,426 of advisory services.

Recommendation:

The Company should improve its filing system and maintain contracts and other pertinent documents in file.

**SECTION III – 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 Company'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.