

ANNUAL FINANCIAL AUDIT MANAGEMENT LETTER

For the Fiscal Year Ended December 31, 2023

PRIVATE & CONFIDENTIAL

February 15, 2024

Board of Directors

DeepShield Systems, Inc.

1750 Innovation Drive, Suite 400

Wilmington, DE 19801

I. INTRODUCTION

We have completed our annual financial audit of DeepShield Systems, Inc. (the "Company") for the fiscal year ended December 31, 2023. This management letter accompanies our formal audit report and highlights key observations, control recommendations, and business considerations identified during our examination.

II. EXECUTIVE SUMMARY

The audit was conducted in accordance with Generally Accepted Auditing Standards (GAAS) and examined the Company's financial statements, internal controls, and operational procedures. While our overall assessment indicates sound financial management, we identified several areas warranting management attention and process enhancement.

III. KEY FINDINGS AND RECOMMENDATIONS

A. Revenue Recognition Practices

****Observation**:** The Company's revenue recognition for multi-year contracts with tiered pricing structures requires enhanced documentation and standardization.

****Risk Level**:** Moderate

****Recommendation**:** Implement standardized revenue recognition templates for complex contracts, particularly those involving the Maritime Security Module and Subsea Infrastructure Protection solutions.

B. Internal Controls

****Observation**:** While core financial controls are robust, subsidiary controls for international operations require strengthening.

****Risk Level**:** Low to Moderate

****Recommendations**:**

- Establish additional oversight mechanisms for European operations
- Implement enhanced documentation requirements for inter-company transactions
- Standardize approval workflows for contracts exceeding \$500,000

C. Research & Development Cost Allocation

****Observation**:** Current R&D cost allocation methodologies between product lines could be more granular.

****Risk Level**:** Low

****Recommendation**:** Develop more detailed cost allocation frameworks for the AI-driven threat detection systems development.

IV. FINANCIAL REPORTING MATTERS

A. Balance Sheet Items

****Accounts Receivable**:**

- Current aging profile is appropriate
- Recommend enhanced monitoring of receivables exceeding 60 days
- Collection procedures are adequate but could be more proactive

****Fixed Assets**:**

- Capital expenditure controls are effective
- Depreciation policies align with industry standards
- Asset tracking systems require minor updates

B. Income Statement Items

****Revenue Recognition**:**

- Current practices comply with ASC 606
- Multi-year contract revenue allocation requires additional documentation
- Channel partner revenue sharing agreements need standardization

****Operating Expenses**:**

- Cost allocation methodologies are appropriate
- Travel and entertainment policies are well-documented
- Vendor management controls are adequate

V. OPERATIONAL CONSIDERATIONS

A. Information Technology Systems

****Current Status**:**

- Financial systems integration is effective
- Backup procedures meet industry standards
- Disaster recovery protocols are well-documented

****Recommendations**:**

- Enhance system access controls for remote workers
- Implement additional automated reconciliation tools
- Update user access review procedures

B. Process Improvements

****Contract Management**:**

- Standardize terms for enterprise agreements
- Implement automated contract tracking system
- Enhance approval workflow documentation

****Procurement Procedures**:**

- Current procedures are adequate
- Recommend additional controls for international vendors
- Consider implementing automated purchase order system

VI. COMPLIANCE AND REGULATORY MATTERS

A. Corporate Governance

****Board Oversight**:**

- Committee structure is appropriate
- Meeting documentation is comprehensive
- Recommend quarterly compliance reviews

****Policies and Procedures**:**

- Employee handbook is current
- Ethics policies are well-documented
- Whistleblower procedures are adequate

B. Regulatory Compliance

****Industry Regulations**:**

- Cybersecurity compliance is strong
- Export control procedures are adequate
- GDPR compliance requires minor updates

VII. FUTURE CONSIDERATIONS

A. Growth Management

****Scalability**:**

- Current systems can support projected growth
- Additional controls needed for international expansion
- Consider ERP system upgrade in next 18-24 months

****Resource Planning**:**

- Staff augmentation may be needed in finance department
- Consider additional technical accounting expertise
- Evaluate shared service center options

VIII. CONCLUSION

While our audit revealed no material weaknesses in internal controls or financial reporting, we

recommend management attention to the items noted above. The Company's overall financial health and control environment remain strong, with opportunities for enhancement in specific areas.

IX. ACKNOWLEDGMENT

This management letter is provided solely for the use of the Board of Directors and management of DeepShield Systems, Inc. and should not be used for any other purpose.

Respectfully submitted,

[Signature]

Sarah Thompson, CPA

Lead Engagement Partner

Global Audit Associates, LLP

[Signature]

Michael Rodriguez, CPA

Senior Audit Manager

Global Audit Associates, LLP

Date: February 15, 2024

cc:

Dr. Marcus Chen, Chief Executive Officer

Robert Kessler, Chief Financial Officer

Audit Committee Members