MAJURO RESORT, INC.

(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL AND ON COMPLIANCE

YEAR ENDED SEPTEMBER 30, 2011

Deloitte.

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Directors
Majuro Resort, Inc.:

We have audited the financial statements of Majuro Resort, Inc. (MRI) as of and for the year ended September 30, 2011, and have issued our report thereon dated September 11, 2012. Our report includes an explanatory paragraph regarding the accrual of certain unpaid taxes. We conducted our audit 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.

Internal Control Over Financial Reporting

Management of MRI is responsible for establishing and maintaining effect internal control over financial reporting. In planning and performing our audit, we considered MRI's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of MRI's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of MRI'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, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Responses (pages 3 through 5), we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A *deficiency in internal control* 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 *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Responses as item 2011-1 to be material weaknesses.

A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Responses as item 2011-3 to be significant deficiencies.

<u>Compliance and Other Matters</u>

As part of obtaining reasonable assurance about whether MRI's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as item 2011-2.

We noted certain matters that we reported to management of MRI in a separate letter dated September 11, 2012.

MRI's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. We did not audit MRI's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Board of Directors and management of MRI and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte + Touche LLP

September 11, 2012

MAJURO RESORT, INC.

Schedule of Findings and Responses
Year Ended September 30, 2011

Management Contracts

Finding 2011-1

Criteria: RepMar entered into a Memorandum of Agreement (MOA) with Pacific International, Inc. (PII) effective February 19, 2004 for the purpose of assuming the management and operation of MRI.

Condition: The MOA does not indicate if any management fees will be collected by PII and thus, none has been recorded since February 19, 2004.

Cause: The cause of the above condition is that final discussions between RepMar and PII have yet to be concluded.

Effect: Estimated management fee of $400,613 is uncertain due to the status of the management agreement.

Prior Year Status: Lack of an executed management agreement was reported as a finding in the audits of MRI for fiscal years 2005 through 2010.

Recommendation: We recommend that MRI, in conjunction with RepMar, finalize the terms of the management agreement.

Auditee Response: There have been discussions held for the past years to finalize the agreement between PII and RepMar. Consultations and varying business issues of the Hotel were also presented after the appointment of the new member of the Cabinet, including the proposed management agreement with RepMar.

On August 31, 2009, PII terminated their management and operation of the hotel. MRI has estimated that a total of $400,613 is due to PII for management fees calculated in accordance with previously negotiated management contract between RepMar and the Outrigger Hotel Group. PII assumed the prior management agreement for final negotiation with PII and therefore, MRI has not recorded any accrual for management fees in the financial statements.

According to <C.M. 132 (2011> dated December 30, 2011, RepMar approved to offset PII's tax audit adjustment findings amounting to $239,365.02 against part of its management fee claim $393,441.52.

Sales and Local Government Tax

Finding 2011-2

Criteria: Majuro Atoll Local Government (Malgov) has local ordinances that require the payment of 4% sales tax and three dollar per night room tax by consumers and that these taxes be remitted to Malgov on a monthly basis.

Condition: MRI did not file the sales tax and local government tax returns from 2006 through 2011. The entity had been accruing theses taxes; however, starting May 2009, the entity stopped accruing the sales tax payable.

Cause: MRI did not pay these taxes as management believes that they have already paid for the sales tax when MRI purchased items from the vendors. Paying sales tax would only result in double taxation. Local government hotel room taxes were not paid since by virtue of a signed agreement, MRI is owned by RepMar therefore no tax payment is necessary.

Effect: Non-compliance with local laws and regulations could result from this condition which may result in penalties and interest.

Prior Year Status: Non-filing of sales and local government tax was reported as a finding in the audits of MRI for fiscal years 2006 through 2010.

Recommendation: We recommend that MRI comply with Malgov ordinances.

Auditee Response: MRI neither files tax returns nor pays the sales tax as management believes that food and supplies are subject to tax only on the first sale. Payment of sales tax to Local Government would result in double taxation as taxes have already been paid by MIR upon purchased of the products from the vendors. Further, the hotel is making use of locally produced food items and therefore payment of sales tax is not necessary.

On the other hand, Management has suspended the imposition of local tax on hotel rooms but continue to accrue the $3.00 per night room tax payable as reflected in the financial statements for fiscal year 2011. In addition, the hotel ceased to impose and collect from the customer the 4% local sales tax on its food and beverage sales and as a result, sales tax payable has not been accrued since May 2009.

Reconciliation of Sub-ledger and General Journal

Finding 2011-3

Criteria: Reconciliation of subsidiary ledger and general ledger should occur.

Condition: A difference of $6,300 was noted between the Direct Bill accounts receivable subsidiary and General ledger accounts; while a difference of $6,336 was noted between the trade accounts payable subsidiary ledger and General ledger. The difference was discussed with the Financial Controller, who indicated that the difference may be due to timing differences. Our verification also showed that the difference is due to posting some transactions directly to the General ledger and the subsidiary ledger was not updated.

Cause: Subsidiary ledger was not timely reconciled to general ledger.

Effect: The variance between AR subledger and General ledger is subjected to client requested adjustment, and the variance between AP subledger and General ledger is subjected to passed adjustment.

Recommendation: We recommend that reconciliations between the general ledger and subsidiary ledger be performed every month-end.

Auditee Response: Based on our review of the variances, the differences between the Subsidiary Ledger and the General Ledger is due to timing differences in posting collections or payments and adjustments in the Accounts Receivable and Accounts Payable modules of the systems. In addition, certain entries affecting the Accounts Receivable and the Accounts Payable modules were made through the General Ledger module.

Ideally, all entries for Accounts Receivable and Accounts Payable should be made in the appropriate modules so that the balances between the General Ledger and the Subsidiary Ledgers are in agreement. An adjusting entry is made in order to bring the AR Direct Bill Subsidiary Ledger and General Ledger into agreement at the end of FY2011. To date, timely review and reconciliations are performed to ensure that entries are properly posted in the appropriate modules, differences are resolved in an orderly manner and adjustments, if any, are reflected in the proper period.

MAJURO RESORT, INC.

Unresolved Prior Year Findings
Year Ended September 30, 2011

The status of unresolved prior year findings is discussed within the Schedule of Findings section (pages 3 through 5) of this report.