

MARSHALLS ENERGY COMPANY, INC.
**(A COMPONENT UNIT OF THE REPUBLIC OF
THE MARSHALL ISLANDS)**

**INDEPENDENT AUDITORS' REPORT ON
COMPLIANCE WITH ASPECTS OF CONTRACTUAL
AGREEMENTS AND REGULATORY REQUIREMENTS**

YEAR ENDED SEPTEMBER 30, 2016

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH ASPECTS OF CONTRACTUAL AGREEMENTS AND REGULATORY REQUIREMENTS

Board of Directors
Marshalls Energy Company, Inc.:

We have audited, 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, the financial statements of the Marshalls Energy Company, Inc. (MEC), which comprise the statement of net position as of September 30, 2016, and the related statements of revenue and expenses, and changes in net position, and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 19, 2017. In accordance with *Government Auditing Standards*, we have also issued our report dated April 19, 2017, on our consideration of MEC'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. No reports other than the reports referred to above and our schedule of findings and response related to our audit have been furnished to management.

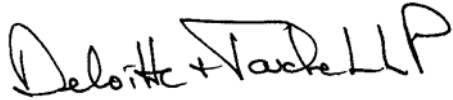
In connection with our audit, nothing came to our attention that caused us to believe that MEC failed to comply with the terms, covenants, provisions, or conditions of their loan, grant, and security instruments as set forth in 7 CFR Part 1773, *Policy on Audits of Rural Utilities Service Borrowers*, §1773.33 and clarified in the Rural Utilities Service (RUS) policy memorandum dated February 7, 2014, insofar as they relate to accounting matters as enumerated below. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding MEC's noncompliance with the above-referenced terms, covenants, provisions, or conditions of the contractual agreements and regulatory requirements, insofar as they relate to accounting matters. In connection with our audit, we noted no matters regarding MEC's accounting and records to indicate that MEC did not:

- Maintain adequate and effective accounting procedures
- Utilize adequate and fair methods for accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expense accounts
- Reconcile continuing property records to the controlling general ledger plant accounts
- Clear construction accounts and accrue depreciation on completed construction
- Record and properly price the retirement of plant
- Seek approval of the sale, lease, or transfer of capital assets and disposition of proceeds for the sale or lease of plant, material, or scrap
- Maintain adequate control over materials and supplies
- Prepare accurate and timely Financial and Operating Reports

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- Obtain written RUS approval to enter into any contract for the management, operation, or maintenance of the borrower's system if the contract covers all or substantially all of the electric system
- Disclose material related party transactions in the financial statements, in accordance with requirements for related parties in generally accepted accounting principles
- Record depreciation in accordance with RUS requirements (See RUS Bulletin 183-1, Depreciation Rates and Procedures)
- Comply with the requirements for the detailed schedule of deferred debits and deferred credits
- Comply with the requirements for the detailed schedule of investments.

The purpose of this report is solely to describe the scope of our testing of compliance, and the result of that testing, and not to provide an opinion on the compliance. Accordingly, this communication is not suitable for any other purpose.

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

April 19, 2017