MARSHALL ISLANDS DEVELOPMENT BANK

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

FINANCIAL STATEMENTS, ADDITIONAL INFORMATION AND INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2011 AND 2010

MARSHALL ISLANDS DEVELOPMENT BANK
(A Component Unit of the Republic of the Marshall Islands)

Years Ended September 30, 2011 and 2010
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INDEPENDENT AUDITORS' REPORT

Board of Directors
Marshall Islands Development Bank:

We have audited the accompanying statements of net assets of the Marshall Islands Development Bank (MIDB), a component unit of the Republic of the Marshall Islands, as of September 30, 2011 and 2010, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of MIDB's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of 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 MIDB‟s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Marshall Islands Development Bank as of September 30, 2011 and 2010, and its changes in net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 27 2012, on our consideration of MIDB‟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 purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management‟s Discussion and Analysis on pages 3 through 7 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of MIDB‟s management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements of MIDB taken as a whole. The accompanying Combining Statement of Net Assets and Combining Statement of Revenues, Expenses and Changes in Net Assets as of and for the year ended September 30, 2011 (pages 24 and 25) are presented for purposes of additional analysis and are not a required part of the basic financial statements of MIDB. This additional information is the responsibility of the management of MIDB. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements as of September 30, 2011 and for the year then ended and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Deloitte & Touche LLP

August 27, 2012

Fiscal year October 1, 2010 to September 30, 2011 has been a productive year for the Marshall Islands Development Bank (MIDB). During the fiscal year, the Bank„s resources were utilized to prioritize Consumer Loan Programs with the goal and purpose of improving the living standard and conditions of the people of the Republic of the Marshall Islands.

Management‟s Discussion and Analysis will give you an overview of the Bank‟s financial highlights and activities for the fiscal year ended September 30, 2011.

FINANCIAL HIGHLIGHTS

- MIDB‟s total net assets increased by **$0.84M or 7%** over the course of this year‟s operation. Net assets are funds from the Housing Preservation Grant and the USDA Self-Help Housing Project, which increase collectively by **$0.84M.**

- Revenues virtually remain unchanged while Expenses increased by $0.13M or 6%. MIDB earned $2.71M during the fiscal year, $2.37M of which was generated through Interest on loans. On the other hand, Bank incurred various expenses for banking activities, broken down as $0.17M for Operating Expenses (Interest Expense), and $1.85M for General and Administrative Expenses. Other expenses such as Provision for Loan loss $0.47M was also provided. These expenses were funded by Interest Income on Loans and Other Income of $3.17M and other investment earnings of $0.15M.

ANALYSIS OF MIDB'S FINANCIAL STATUS

This Analysis serves as an overview to MIDB‟s basic financial statements. A Summary of Statements of Net Assets is shown below that will give insight on MIDB‟s resources, liabilities and net assets, priority investments and performance results compared to previous year. At the end of the fiscal year 2011, MIDB‟s assets of $17.92M exceeded liabilities of $4.19M by $13.74M. However, $1.58M or 11% of the net assets are either invested in Capital Assets or Restricted Funds that can only be used for the purpose of which the Fund was created. The Capital Assets are resources used by the Bank during the course of its operation to provide services to the people and are assets that are not easily liquidated. As of September 30, 2011 Unrestricted Net Assets amounted to $12.16M, enough to repay all outstanding debts.

Summary of Statements of Net Assets

	2011	2010	2009
Assets			
Cash and Equivalents	$ 55,361	$ 151,970	$ 17,179
Restricted Cash	500,007	-	-
Restricted TCD	-	576,393	548,492
Loan Receivable, net	15,125,289	15,232,330	15,080,869
Premises and Equipment, net	1,297,801	1,454,291	1,232,384
Other Assets	946,236	813,602	793,741
Total Assets	**$ 17,924,694**	**$ 18,228,586**	**$ 17,672,665**

Summary of Statements of Net Assets, Continued

	2011	2010	2009
Liabilities			
Loan Payable	$ 1,269,120	$ 1,779,767	$ 2,274,976
RepMar Deposit	1,739,989	1,716,236	2,628,328
Other Liabilities	1,179,577	1,835,515	1,064,810
Total Liabilities	**$ 4,188,686**	**$ 5,331,518**	**$ 5,968,114**
Net Assets			
Invested in Capital Assets	$ 1,297,801	$ 1,454,291	$ 1,232,384
Restricted	277,386	275,839	275,839
Unrestricted	12,160,821	11,166,938	10,196,328
Total Net Assets	**$ 13,736,008**	**$ 12,897,068**	**$ 11,704,551**
Total Liabilities and Net Assets	**$ 17,924,694**	**$ 18,228,586**	**$ 17,672,665**

- Restricted TCD decrease tremendously brought by the termination of MIDB"s TCD investment with BOMI, the proceeds of which were used to open a BOG joint escrow account with the USDA Rural Development having an initial deposit of $500K in September 2011.

- Loan approvals for the year were approximately $15.41M, broken down by projects, $15.37M released under various consumer loans and $0.04M granted to housing loans. Loans receivable, net decreased by $0.11M in 2011 compared with $0.15M increase in 2010. Loans released decreased from $17.12M to 15.41M during the fiscal years 2010 and 2011, respectively.

- The Government of the Marshall Islands invested $7M in Time Certificate of Deposit at the rate of 4% in May 9, 2003, maturing May 8, 2018. The money received from such TCD Payable was used to finance the loans granted to RRE and PMI. RMI Government made withdrawals, net of deposits, during fiscal years 2009, 2010 and 2011 to finance some governmental operations and obligations. As of September 30, 2011, Time Certificate Deposit of RMI Government was $1.76M.

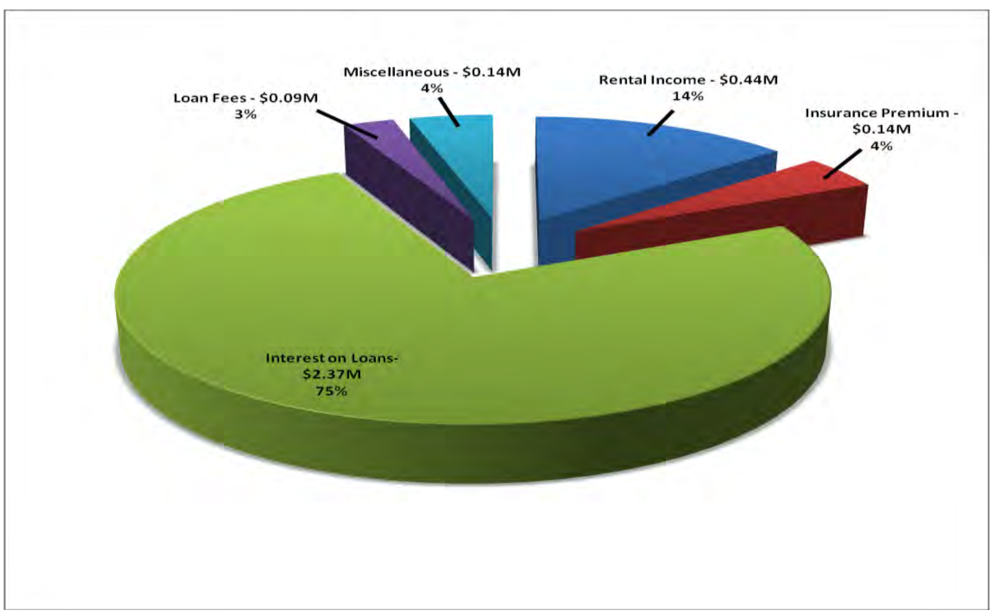
- MIDB continuously liquidates its long-term loan with International Commercial Bank of China (ICBC) by paying approximately $0.40M on principal every year. The loan with ICBC amounting to $5M was granted in August 6, 1999 with an interest rate of 5% per annum, maturing in August 6, 2014 and no collateral or security was provided. As of September 30, 2011, outstanding principal balance on ICBC loan was $1.2M.

- MIDB availed of a $325K long-term loan with Bank of Marshall Islands on behalf of the Government of Marshall Islands on April 15, 2009. Interest payment shall be at annual rate of 7.5% until maturity date in March 28, 2012. All loans proceeds were issued to Air Marshall Islands. As of September 30, 2011, outstanding principal balance on the BOMI loan was $69K.

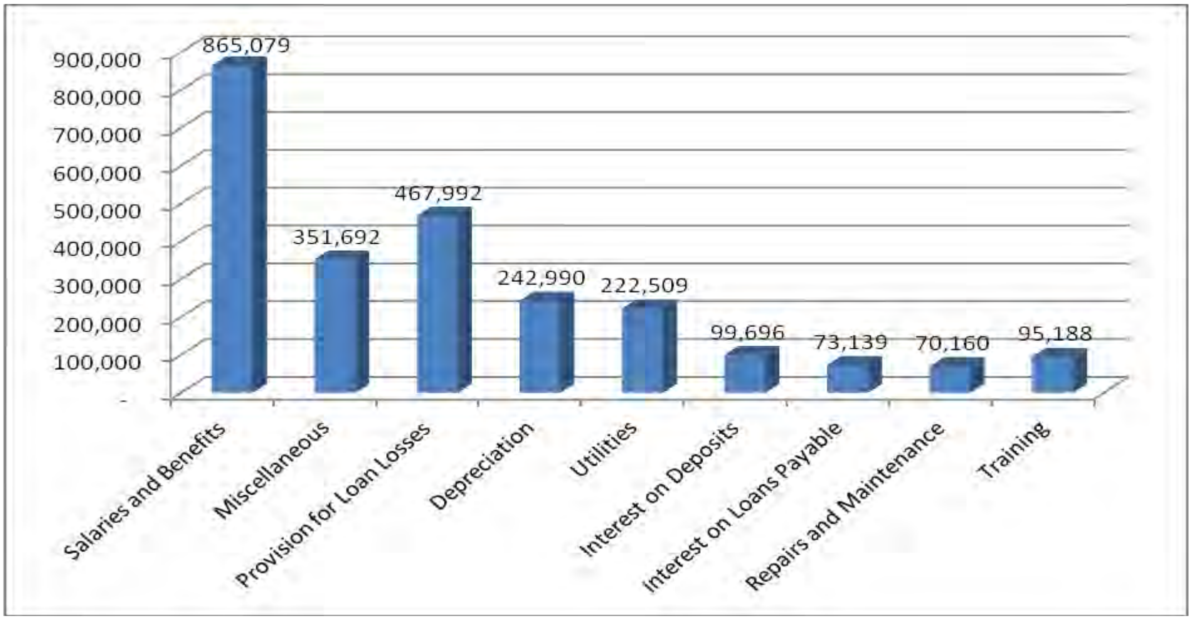
Summary of Statements of Revenues, Expenses and Changes in Net Assets

	2011	2010	2009
Operating Revenues	$ 3,174,043	$ 3,246,968	$ 3,037,056
Less: Expenses			
Provision for loan losses	467,992	307,816	68,882
Operating expenses	172,835	234,771	258,154
General and administrative expenses	1,847,618	1,913,706	1,980,578
	2,488,445	2,456,293	2,307,614
Earnings from Operations	685,598	790,675	729,442
Non-operating Revenues, Net	153,342	401,842	407,542
Increase in Net Assets	838,940	1,192,517	1,136,984
Net Assets at Beginning of Year	12,897,068	11,704,551	10,567,567
Net Assets at End of Year	**$ 13,736,008**	**$ 12,897,068**	**$ 11,704,551**

- MIDB"s total revenues (excluding Non-Operating Revenues of $153K) for current year decreased by $73K compared with fiscal year 2010. About 75% of the Bank"s revenue comes from Interest on Loans, 79% and 15% of which are generated earnings from consumer loans and business loans, respectively. Please see chart below depicting the distribution of the Bank"s revenue.



- The Total cost incurred decreased by $32K compared with last year"s operation. The Bank expenses cover a range of operation, general and administrative expenses. Provision for delinquent loan accounts of $468k or 19% of total expenses was made for this fiscal year. Provision for delinquent loan accounts is provided based on the Bank"s reasonable estimate, wherein the number of days an account is due, the amount of loan outstanding balance, and the borrower"s capability to pay play vital information in the computation of additional allowance to be provided. The graph below will show itemized expenses and will give an overall picture of the Bank"s spending activities.



- Operating Expenses decreased by $62K during fiscal year ended September 30, 2011 compared to fiscal year ended September 30, 2010 due to decrease in interest on loans payable. Interest on loans payable pertains to interest payments and accruals for International Commercial Bank of China (ICBC) loan which decreased by $0.40M.

- General and Administrative Expenses in the aggregate decreased by $66K or 3 % from last year"s operation due to decrease in repairs and maintenance, salaries and employee benefits, and miscellaneous expenses.

Capital Assets and Debt

Significant capital asset activity during 2011 includes the completion of MIDB Office located in Wotje amounting to $103K. For additional information concerning capital assets, please refer to Note 7 to the financial statements. The significant debt activity during 2011 is the full payment of $1.0M short term loan from an affiliate bank which is used in funding the withdrawals of RepMar from its certificate of deposit. For additional information concerning debt, please refer to Notes 10 and 11 to the financial statements

Management"s Discussion and Analysis for the year ended September 30, 2010 is set forth in MIDB"s report on the audit of financial statements, which is dated August 12, 2011. That Discussion and Analysis explains the major factors impacting the 2010 financial statements and can be obtained from MIDB"s Managing Director at rmimidb@ntamar.net.

ECONOMIC OUTLOOK

In the next years to come, MIDB is continuing to expect growth in the demand for housing loans and commercial loans, the latter being the major component of MIDB"s loan portfolio. MIDB is involved in improving the living conditions of the RMI people through the housing loan projects under Mutual Self Help Housing Projects and USDA Rural development.

MIDB is currently dependent on investments from RMI Government and its income from new loans. The net assets are just sufficient to pay for MIDB‟s outstanding debts. MIDB may have to look for other sources of funds to maintain the current portfolio and the rising demand for loans.

As more opportunities for work are available outside RMI, cost of living continues to rise and due to the prevalent economic crisis, management is expecting that some borrowers may not be able to comply with their commitments to MIDB, thereby resulting in increased delinquent loans and decreased income.

ADDITIONAL FINANCIAL INFORMATION

This discussion and analysis is designed to provide MIDB‟s customers and other stake holders with an overview of MIDB‟s operations and financial condition as at September 30, 2011. Should the reader have questions regarding the information included in this report, or wish to request additional financial information, please contact the Marshall Islands Development Bank Managing Director at the above email address or at P.O. Box 1048, Majuro, Marshall Islands, MH 96960

MARSHALL ISLANDS DEVELOPMENT BANK
(A Component Unit of the Republic of the Marshall Islands)

Statements of Net Assets
September 30, 2011 and 2010

ASSETS	2011	2010
Cash and cash equivalents	$ 55,361	$ 151,970
Restricted cash	500,007	-
Restricted time certificates of deposit	-	576,393
Investments	423,748	423,748
Receivables:		
Loans, net	15,125,289	15,232,330
Accrued interest, net	75,369	79,972
Other	397,311	214,091
Premises and equipment, net	1,297,801	1,454,291
Foreclosed assets, net	-	32,083
Investment property held for sale, net	49,808	63,708
	$ 17,924,694	$ 18,228,586

LIABILITIES AND NET ASSETS	2011	2010
Liabilities:		
Short-term debt	$ -	$ 764,063
Notes payable	1,269,120	1,779,767
RepMar deposit	1,739,989	1,716,236
Accrued interest payable	33,514	20,159
Accounts payable and accrued expenses	287,424	302,214
Deposits pledged	858,639	749,079
Total liabilities	4,188,686	5,331,518
Commitments and contingency		
Net assets:		
Invested in capital assets	1,297,801	1,454,291
Restricted	277,386	275,839
Unrestricted	12,160,821	11,166,938
Total net assets	13,736,008	12,897,068
	$ 17,924,694	$ 18,228,586

See accompanying notes to financial statements.

MARSHALL ISLANDS DEVELOPMENT BANK
(A Component Unit of the Republic of the Marshall Islands)

Statements of Revenues, Expenses and Changes in Net Assets
September 30, 2011 and 2010

	2011	2010
Operating revenues:		
Interest income on loans	$ 2,371,214	$ 2,378,794
Rental income	440,183	405,625
Insurance premiums	136,283	134,409
Federal grants	91,869	113,816
Loan fees	85,487	100,792
Interest income on time certificates of deposit	9,064	29,016
Miscellaneous	39,943	84,516
Total operating revenues	3,174,043	3,246,968
Provision for loan losses	467,992	307,816
Net operating revenues	2,706,051	2,939,152
Operating expenses:		
Interest expense:		
Interest on deposits	99,696	124,303
Interest on loans payable	73,139	110,468
Total interest expense	172,835	234,771
General and administrative expenses:		
Salaries and employee benefits	865,079	916,883
Depreciation	242,990	222,434
Utilities	222,509	193,903
Travel and training	95,188	68,640
Repairs and maintenance	70,160	77,599
Insurance	51,317	54,704
Printing, stationery and advertising	51,141	70,126
Representation	48,409	45,626
Office and house rental	35,364	28,200
Foreclosed assets, net	32,083	35,000
Promotion and donations	27,203	19,048
Professional fees	24,579	31,825
Land lease	18,639	32,446
Communications	17,726	57,863
Fuel	13,948	15,870
Taxes and licenses	1,950	3,674
Miscellaneous	29,333	39,865
Total general and administrative expenses	1,847,618	1,913,706
Earnings from operations	685,598	790,675
Nonoperating revenues:		
Contributions from RepMar	-	248,500
Investment earnings	153,342	153,342
Total nonoperating revenues	153,342	401,842
Change in net assets	838,940	1,192,517
Net assets at beginning of year	12,897,068	11,704,551
Net assets at end of year	$ 13,736,008	$ 12,897,068

See accompanying notes to financial statements.

MARSHALL ISLANDS DEVELOPMENT BANK
(A Component Unit of the Republic of the Marshall Islands)

Statements of Cash Flows
September 30, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Cash received from customers	$ 2,901,628	$ 3,038,079
Cash payments to suppliers for goods and services	(712,316)	(797,445)
Cash payments to employees for services	(875,021)	(887,164)
Interest received on time certificates of deposit	17,435	28,637
Interest paid	(159,479)	(306,350)
Operating grants received	91,870	113,816
Net cash provided by operating activities	1,264,117	1,189,573
Cash flows from noncapital financing activities:		
(Repayments) borrowings under loan arrangement	(764,063)	764,063
Net change in RepMar deposit	23,753	(912,092)
Net change in pledged deposits	109,560	115,832
Contributions from RepMar	-	248,500
Net cash (used in) provided by noncapital financing activities	(630,750)	216,303
Cash flows from capital and related financing activities:		
Principal repayment of long-term debt	(654,356)	(495,209)
Proceeds from loans	143,709	-
Additions to equipment	(72,600)	(291,948)
Net cash used in capital and related financing activities	(583,247)	(787,157)
Cash flows from investing activities:		
Loan originations and principal collections, net	(376,457)	(609,369)
Net change in restricted cash	(500,007)	-
Net change in restricted time certificates of deposit	576,393	(27,901)
Dividends received	153,342	153,342
Net cash used in investing activities	(146,729)	(483,928)
Net change in cash and cash equivalents	(96,609)	134,791
Cash and cash equivalents at beginning of year	151,970	17,179
Cash and cash equivalents at end of year	$ 55,361	$ 151,970
Cash flows from operating activities:		
Earnings from operations	$ 685,598	$ 790,675
Adjustments to reconcile earnings from operations to net cash provided by operating activities:		
Provision for loan losses	467,992	307,816
Depreciation	242,990	222,434
Provision for losses on foreclosed asset	32,083	35,000
(Increase) decrease in assets:		
Accrued interest receivable	(2,037)	9,566
Other receivables	(183,220)	(79,540)
Increase (decrease) in liabilities:		
Accrued interest payable	13,355	(71,579)
Accrued expenses	(14,790)	(37,611)
Deferred loan fees	6,914	(1,541)
Unearned premiums	15,232	14,353
Net cash provided by operating activities	$ 1,264,117	$ 1,189,573

Supplemental disclosure of non-cash financing activity:

On June 25, 2010, MIDB entered into a purchase agreement for a certain property for which the total purchase price was adjusted for the seller's outstanding loan balance of $138,493.

See accompanying notes to financial statements.

(1) Organization

The Marshall Islands Development Bank (MIDB), a component unit of the Republic of the Marshall Islands (RepMar), was incorporated under the laws of RepMar as a non-stock corporation pursuant to the Marshall Islands Development Bank Act of 1988 (Public Law 1988-1). MIDB was established to promote the development and expansion of the economy of the Marshall Islands in order to improve the standard of living of the people and is governed by a seven-member Board of Directors appointed by the Cabinet of RepMar. The primary activities of MIDB have been designed to strengthen the nation's economic base, increase employment and production, improve the standards of housing, promote exports, and reduce the country's dependence on imports and foreign aid through the approval of viable development loans. MIDB has received funds under Section 211 of the Compact of Free Association (the Compact), direct contributions from RepMar and funds from the U.S. Department of Agriculture (USDA) under the Rural Housing and Community Development Service Housing Preservation and Self-Help Housing Program Grants. MIDB also assumed the assets and liabilities of the former Marshall Islands Economic Development Loan Office, Inc.

MIDB‟s financial statements are incorporated into the financial statements of RepMar as a component unit.

(2) Summary of Significant Accounting Policies

The accounting policies of MIDB conform to accounting principles generally accepted in the United States of America (GAAP), as applicable to governmental entities, specifically proprietary funds. Governmental Accounting Standards Board (GASB) Statements No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. MIDB has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989. The preparation of MIDB‟s financial statements conforms to general practices within the banking industry, which includes the presentation of an unclassified statement of net assets.

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and modified by Statement No. 38, *Certain Financial Statement Note Disclosures,* establish financial reporting standards for governmental entities, which require that management‟s discussion and analysis of the financial activities be included with the basic financial statements and notes and modifies certain other financial statement disclosure requirements.

(2) Summary of Significant Accounting Policies, Continued

To conform to the requirements of GASB 34, equity is presented in the following net assets categories:

- Invested in capital assets; capital assets, net of accumulated depreciation, plus construction or improvement of those assets.

- Restricted: Nonexpendable - Net assets subject to externally imposed stipulations that require MIDB to maintain them permanently. At September 30, 2011 and 2010, MIDB does not have nonexpendable net assets. Expendable - Net assets whose use by MIDB is subject to externally imposed stipulations that can be fulfilled by actions of MIDB pursuant to those stipulations or that expire by the passage of time.

- Unrestricted; net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of the fund are included in the statements of net assets. Proprietary fund operating statements present increases and decreases in net total assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Classification of Revenues

MIDB has classified its revenues as either operating or nonoperating according to the following criteria:

- *Operating Revenues* - Operating revenues include activities that have the characteristics of exchange transactions, such as (1) insurance premiums, loan fees and interest income on loans and Certificates of Deposit, (2) rental occupancy income associated with MIDB assets, and (3) USDA federal grant revenues.

- *Nonoperating Revenues* - Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement No. 34, such as RepMar appropriations and investment income.

Reclassifications

Certain reclassifications have been made to the 2010 financial statements to conform with the 2011 presentation.

(2) Summary of Significant Accounting Policies, Continued

Cash and Cash Equivalents and Time Certificates of Deposit

For purposes of the statements of net assets and cash flows, cash and cash equivalents is defined as amounts in demand deposits as well as short-term investments maturing within three months of the date acquired. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified.

GASB Statement No. 3 previously required government entities to present deposit risks in terms of whether the deposits fell into the following categories:

Category 1 Deposits that are federally insured or collateralized with securities held by MIDB or its agent in MIDB"s name;

Category 2 Deposits that are uninsured but fully collateralized with securities held by the pledging financial institution"s trust department or agent in MIDB's name; or

Category 3 Deposits that are collateralized with securities held by the pledging financial institution"s trust department or agent but not in MIDB's name and non-collateralized deposits.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, MIDB"s deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government"s name. MIDB does not have a deposit policy for custodial credit risk.

As of September 30, 2011 and 2010, the carrying amounts of cash and cash equivalents and time certificates of deposit are $555,368 and $728,363 respectively, and the corresponding bank balances are $554,868 and $780,085, respectively. Of the bank balances, $505,819 and $12,144, respectively, are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. MIDB does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

Investments

Investments of 20% or more of the voting stock of an investee are presumed to give the investor significant influence and are carried using the equity method. Under the eqiuty method, the investor records, as earnings or loss, its propotionate shate of the investee"s earnings or loss.

Loans Receivable, Interest Receivable and Allowances for Losses

Loans and interest receivables are due from customers, both individuals and businesses, located within the Republic of the Marshall Islands and are stated at the unpaid balances less the allowances for losses, any deferred fees or cost on originated loans, and unearned insurance premiums. Interest on loans is calculated using the simple interest method on daily balances of the principal amount outstanding. Loan origination fees are deferred and recognized as an adjustment

(2) Summary of Significant Accounting Policies, Continued

Loans Receivable, Interest Receivable and Allowances for Losses, Continued

of the related loan yield using the straight-line method over the contractual life of the loans. Direct loan origination costs are expensed as incurred. Differences between this method and the method prescribed by current accounting guidance are not significant and do not otherwise materially affect the accompanying financial statements.

The allowances for loan losses and interest receivable losses are established through a provision for losses charged to expense. Loans and interest receivables are charged against the allowance for losses when management believes that collection is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans and interest receivables that may be uncollectible, based on evaluations of the collectibility and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans and current economic conditions that may affect the borrowers" ability to pay.

Foreclosed Assets

Assets acquired through, or in lien of, loan foreclosures are held for sale and are initially recorded at the lower of loan carrying amount or fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of the carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

Premises and Equipment

Premises and equipment with a cost that equals or exceeds $500 are capitalized. Such assets are carried at cost less accumulated depreciation. Depreciation is calculated using the straight-line method based on the estimated useful lives of the respective assets. The estimated useful lives of these assets are as follows:

Building and houses	10 - 15 years
Trailers and mobile houses	5 years
Computer systems	5 years
Motor vehicles	3 years
Office furniture	5 years
Office equipment	5 years

Taxes

Corporate profits are not subject to income tax in the Republic of the Marshall Islands. The Government of the Republic of the Marshall Islands imposes a gross revenue tax of 3% on revenues. MIDB is specifically exempt from gross revenue tax pursuant to Section 817 of Public Law 1988-1.

Recognition of Premium Revenues

Loan insurance premiums are generally recognized as revenue on a pro rata basis up to a three year term. The portion of premiums that will be earned in the future is deferred and reported as unearned premiums.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During fiscal year 2011, MIDB implemented the following pronouncements:

- GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions.

- GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which amends Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and addresses issues related to measurement of OPEB obligations by certain employers participating in agent multiple-employer OPEB plans.

- GASB Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting of certain financial instruments and external investment pools.

The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements,* which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MIDB.

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus,* which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity,* and No. 34*, Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MIDB.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MIDB.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MIDB.

In July 2011, GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions* (*an amendment of GASB Statement No. 53*), which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty‟s credit support provider, is replaced. The provisions of this statement are effective for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MIDB.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and valuation of foreclosed assets.

(3) Investments

GASB Statement No. 3 previously required government entities to present investment risks in terms of whether the investments fell into the following categories:

Category 1 Investments that are insured or registered, or securities held by MIDB or its agent in MIDB‟s name;

Category 2 Investments that are uninsured and unregistered for which the securities are held by the counterparty‟s trust department or agent in MIDB‟s name; or

Category 3 Investments that are uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in MIDB‟s name.

GASB Statement No. 40 amended GASB Statement No. 3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No. 3.

(3) Investments, Continued

A summary of MIDB's investments as of September 30, 2011 and 2010 is as follows:

	2011	2010
Bank of Marshall Islands	$ 393,748	$ 393,748
Marshall Islands Service Corporation	30,000	30,000
	$ 423,748	$ 423,748

The investment in Bank of Marshall Islands (BOMI) is recorded at cost as MIDB does not exercise significant influence over the operating and financial policies of the investee. The investment comprises approximately 16% of the outstanding shares of BOMI as of September 30, 2011 and 2010. In addition, MIDB has an equity interest in Marshall Islands Service Corporation, an affiliate of BOMI. This investment is recorded at cost as MIDB does not exercise significant influence over the operating and financial policies of the investee. During each of the years ended September 30, 2011 and 2010, dividend income earned from investees was $153,342.

(4) Loans Receivable

Loans receivable as of September 30, 2011 and 2010 are summarized as follows:

	2011	2010
Investment Development Fund	$ 4,330,669	$ 4,094,747
Compact Section 211	942,716	981,762
Republic of the Marshall Islands	25,888,673	25,724,688
Housing Preservation Grant	12,011	13,068
Gross loans	31,174,069	30,814,265
Less: net deferred loan fees	(84,424)	(77,510)
Less: unearned premiums	(223,068)	(207,835)
Less: allowance for loan losses	(15,741,288)	(15,296,590)
	$ 15,125,289	$ 15,232,330

An analysis of the change in the allowance for loan losses during the years ended September 30, 2011 and 2010 is as follows:

	2011	2010
Beginning balance	$ 15,296,590	$ 15,017,769
Provision for loan losses	461,352	306,603
Charge-offs	(16,654)	(27,782)
Ending balance	$ 15,741,288	$ 15,296,590

(4) Loans Receivable, Continued

The loan portfolio is comprised of consumer, housing and business loans. The majority of the 2011 and 2010 loan portfolio is unsecured, while the remaining portion is secured by various forms of collateral. Additionally, these loans are normally cosigned by third parties. The basis for expected repayment of a majority of the consumer loans and housing loans is the continued employment of the borrower and allotment agreements between MIDB and the borrower‟s employer. All loans are at fixed rates ranging from 4.0% - 8.5% for Investment Development Fund loans, 4.0% - 6.5% for Compact Section 211 loans, 1.0% -14.0% for Republic of Marshall Islands loans, and 2.0%-6.0% for Housing Preservation Grant loans.

(5) Accrued Interest Receivable

Accrued interest receivable as of September 30, 2011 and 2010 is summarized as follows:

	2011	2010
Republic of the Marshall Islands	$ 94,433	$ 93,732
Investment Development Fund	389	-
Gross accrued interest receivable	94,822	93,732
Less: allowance for doubtful interest	(19,453)	(13,760)
	$ 75,369	$ 79,972

An analysis of the change in the allowance for interest receivable losses during the years ended September 30, 2011 and 2010 is as follows:

	2011	2010
Beginning balance	$ 13,760	$ 12,547
Provision for loan losses	6,640	1,213
Charge-offs	(947)	-
Ending balance	$ 19,453	$ 13,760

(6) Restricted Deposits

MIDB has outstanding savings deposit and time certificates of deposit as of September 30, 2011 and 2010 in the amount of $500,007 and $576,393, respectively, that are restricted to collateralize loans funded by Rural Housing Service (RHS). The Memorandum of Understanding signed with the RHS requires MIDB to create and maintain an escrow account with an initial deposit of $500,000. If the account falls below $500,000, MIDB shall deposit in the escrow account 5% of all RHS loans issued until such time that the account has reached $500,000.

(7) Premises and Equipment

Capital asset activity during the years ended September 30, 2011 and 2010 is as follows:

	2011			
	October 1, 2010	Additions	Deletions/ Transfers	September 30, 2011
Building and houses	$ 2,178,480	$ 102,566	$ -	$ 2,281,046
Computer systems	245,392	1,701	-	247,093
Motor vehicles	162,461	3,500	-	165,961
Office furniture	53,538	1,303	-	54,841
Office equipment	374,626	7,274	-	381,900
	3,014,497	116,344	-	3,130,841
Less accumulated depreciation	(1,649,527)	(229,090)	-	(1,878,617)
	1,364,970	(112,746)	-	1,252,224
Construction in progress	89,321	45,577	(89,321)	45,577
	$ 1,454,291	$ (67,169)	$ (89,321)	$ 1,297,801

	2010			
	October 1, 2009	Additions	Deletions/ Transfers	September 30, 2010
Building and houses	$ 1,928,480	$ 250,000	$ -	$ 2,178,480
Computer systems	214,295	31,097	-	245,392
Motor vehicles	122,516	39,945	-	162,461
Office furniture	46,970	6,568	-	53,538
Office equipment	361,116	13,510	-	374,626
	2,673,377	341,120	-	3,014,497
Less accumulated depreciation	(1,440,993)	(208,534)	-	(1,649,527)
	1,232,384	132,586	-	1,364,970
Construction in progress	-	89,321	-	89,321
	$ 1,232,384	$ 221,907	$ -	$ 1,454,291

(8) Foreclosed Assets

Foreclosed assets are presented net of an allowance for losses. Foreclosed assets as of September 30, 2011 and 2010 are summarized as follows:

	2011	2010
Foreclosed assets	$ 350,000	$ 350,000
Allowance for losses	(350,000)	(317,917)
	$ -	$ 32,083

(8) Foreclosed Assets, Continued

An analysis of the allowance for losses on foreclosed assets for the years ended September 30, 2011 and 2010 is as follows:

	2011	2010
Balance at beginning of year	$ 317,917	$ 282,917
Provision for losses	32,083	35,000
Balance at end of year	$ 350,000	$ 317,917

(9) Investment in Property

In April 2005, MIDB purchased property for $139,000, with the intention of selling the property in the near future. Currently, the property is being leased to tenants. Depreciation is recognized by use of an estimated 10-year life and the straight line method. As of September 30, 2011 and 2010, the property is presented net of accumulated depreciation of $89,192 and $75,292, respectively. Depreciation expense of $13,900 was recognized during each of the years ended September 30, 2011 and 2010.

(10) Short-Term Debt

In July 2010, MIDB obtained a $1,000,000 loan from an affiliate bank with interest at 7.5% per annum and payable on May 6, 2011. The proceeds were used to fund partial withdrawals by RepMar from its certificate of deposit with MIDB. As of September 30, 2010, the amount outstanding and payable on this loan facility was $764,063. This loan was settled in full in May 2011.

Short-term debt changes during the years ended September 30, 2011 and 2010 are as follows:

	Balance October 1,	Drawdowns	Repayment	Balance September 30,
2011:				
Loan payable	$ 764,063	$ -	$ (764,063)	$ -
2010:				
Loan payable	$ -	$1,000,000	$ (235,937)	$ 764,063

(11) Notes Payable

On August 6, 1999, MIDB entered into a loan agreement with the Mega International Commercial Bank (formerly the International Commercial Bank of China) in the amount of $5,000,000, due August 6, 2014, for the purpose of funding private enterprise purchase of transportation ships. The loan is uncollateralized, bears interest at 5% per annum, with interest due semi-annually commencing March 6, 2000. Repayment of principal commenced August 6, 2002 in semi-annual installments of $200,000. As of September 30, 2011 and 2010, the amount outstanding and payable was $1,200,000 and $1,600,000, respectively.

(11) Notes Payable, Continued

On April 15, 2009, MIDB obtained a loan from an affiliate bank in the amount of $325,000, interest at 7.5% per annum, payable in monthly installments of $10,000 inclusive of interest, and due on March 28, 2012. The proceeds were used to fund partial withdrawals by RepMar from its certificate of deposit with MIDB. As of September 30, 2010, the amount outstanding and payable was $179,767. On January 11, 2011, the loan was refinanced, with a new principal amount of $143,709, interest at 7.5% per annum, payable in monthly installments of $10,085 inclusive of interest, and due on May 28, 2012. As of September 30, 2011, the amount outstanding and payable was $69,120.

Annual debt service requirements to maturity for principal and interest are as follows:

Year ending September 30,	Principal	Interest	Total
2012	$ 469,120	$ 57,692	$ 526,812
2013	400,000	35,041	435,041
2014	400,000	15,250	415,250
	$ 1,269,120	$ 107,983	$ 1,377,103

Long-term debt changes during the years ended September 30, 2011 and 2010 are as follows:

	Balance October 1,	Additions	Reductions	Balance September 30,	Due Within One Year
2011:					
Notes payable	$ 1,779,767	$ 143,709	$ (654,356)	$ 1,269,120	$ 469,120
2010:					
Notes payable	$ 2,274,976	$ -	$ (495,209)	$ 1,779,767	$ 511,325

(12) Related Party Transactions

As of September 30, 2011 and 2010, MIDB has deposits with a bank of $49,050 and $767,941, respectively, in which MIDB has an equity investment. The deposits accrue interest at rates of 0.25% to 5.0% per annum. Interest earned for the years ended September 30, 2011 and 2010 was $9,064 and $29,016, respectively.

MIDB is a component unit of RepMar and is therefore affiliated with all RepMar-owned and affiliated entities, including the Marshall Islands Development Authority. As of September 30, 2011 and 2010, MIDB has loans outstanding with affiliated entities of $185,000. These loans are fully provided for in the allowance for loan losses. All loans were made at normal commercial terms and conditions.

As of September 30, 2011 and 2010, MIDB employees have loans outstanding of $734,202 and $767,569, respectively. In addition, the directors of MIDB have loans outstanding as of September 30, 2011 and 2010, of $72,496 and $78,262, respectively. All loans were made at normal commercial terms and conditions.

As of September 30, 2011 and 2010, MIDB has an outstanding certificate of deposit, totaling $1,739,989 and $1,716,236, respectively, payable to RepMar. The deposit is for a fifteen-year term and accrues interest at 4% per annum. This deposit is withdrawable in full or in part before maturity date with the consent of MIDB. As of September 30, 2011 and 2010, interest payable relating to this deposit amounted to $24,681 and $6,681, respectively, and is included within the statements of net assets as accrued interest payable.

(12) Related Party Transactions, Continued

Movements in long-term liabilities during the years ended September 30, 2011 and 2010 are as follows:

	Balance October 1,	Additions	Reductions	Balance September 30,
2011:				
RepMar deposit	$ 1,716,236	$ 47,784	$ (24,031)	$ 1,739,989
2010:				
RepMar deposit	$ 2,628,328	$ 102,972	$ (1,015,064)	$ 1,716,236

On August 7, 2000, MIDB entered into an agreement with RepMar whereby MIDB loaned RepMar $1,800,000 for the purpose of paying off debts owed by the Marshall Islands Social Security Administration. The amount outstanding as of September 30, 2011 and 2010 is $24,973.

(13) Risk Management

MIDB is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. MIDB has elected to purchase commercial automobile insurance and fire, lightning and typhoon insurance covering office contents from independent third parties for the risks of losses to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. MIDB does not maintain general liability insurance and fire, lightning and typhoon insurance for its office building and properties. In the event of an insurable loss, MIDB may be self-insured to a material extent.

(14) Commitments and Contingency

Commitments

On April 12, 1999, MIDB entered into an agreement to manage the entertainment complex of a delinquent loan customer. Under the terms of the agreement, MIDB is required to manage the operations and to apply the proceeds less operating expenses to the customer‟s outstanding balance. In return, MIDB receives a management fee of $12,000 per year. The term of the agreement is for as long as is required to bring the loan current. Loan balances as of September 30, 2011 and 2010 of $1,600,792 and $1,599,745, respectively, were fully provided with an allowance for loan losses.

MIDB committed to guarantee certain loans recorded in the books of an affiliate bank, with principal balances totaling $3,259 and $24,043 as of September 30, 2011 and 2010, respectively.

Further, certain loans recorded in the books of USDA are subject to MIDB guarantee, the balance of which amounted to $10,304,811 and $10,526,402 as of September 30, 2011 and 2010, respectively.

During the year ended December 31, 2001, MIDB assumed the payment obligations under a fifteen-year ground lease, expiring on January 14, 2003, with an option to renew for an additional five years. On January 17, 2005, MIDB entered into an amended lease agreement with the landowners for the property. The term of the amended lease is twenty years, expiring on January 13, 2023. On May 14, 2003, MIDB assumed the payment obligations under a thirty-year ground lease, expiring on December 31, 2028, with an option to renew for two additional terms of thirty years each.

(14) Commitments and Contingency, Continued

On June14, 2010, MIDB entered into a fifty-year ground lease agreement for a portion of Kabilwe Weto property expiring on May 31, 2060.

Future minimum lease payments under these leases are as follows:

Year ending September 30,	
2012	$ 9,144
2013	9,144
2014	9,437
2015	9,534
2016	9,534
2017-2021	48,744
2022-2026	35,694
2027-2031	15,483
2032-2060	13,304
	$ 160,018

MIDB has entered into several lease agreements expiring over various years through December 31, 2029. Total future minimum lease income for subsequent years ending September 30 are as follows:

Years ending September 30,	
2012	$ 256,036
2013	205,773
2014	152,080
2015	113,310
2016	34,360
2017-2021	151,800
2022-2026	151,800
2027-2030	98,670
	$ 1,163,829

Contingency

MIDB participates in a number of federally assisted programs from the U.S. Department of the Interior and the U.S. Department of Agriculture. These programs are subject to financial and compliance audits to ascertain if federal laws and guidelines have been followed. The United States Department of the Interior, Office of the Inspector General, in their audit report "Marshall Islands Development Bank, Republic of the Marshall Islands", dated August 1999, have identified loans funded under Sections 111 and 211 of the Compact (CFDA # 15.875) totaling $12,410,148, and loans converted to an equity interest in Air Marshall Islands, Inc. totaling $2,933,321, as questionable. The ultimate disposition of these questionable loans can be determined only by final action of the grantor agency. Therefore, no provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements. If these loans are ultimately denied, MIDB could be charged for the necessary reimbursement to the grantor agency.

MARSHALL ISLANDS DEVELOPMENT BANK
(A Component Unit of the Republic of the Marshall Islands)

Combining Statement of Net Assets
September 30, 2011

ASSETS	Marshall Islands Development Bank	Housing Preservation Grant	USDA Self-Help Housing Project	Total
Cash and cash equivalents	$ (211,368)	$ 277,386	$ (10,657)	$ 55,361
Restricted cash	500,007			500,007
Investments	423,748	-	-	423,748
Receivables:				
Loans, net	15,125,289	-	-	15,125,289
Accrued interest, net	75,369	-	-	75,369
Other	387,449	-	9,862	397,311
Premises and equipment, net	1,297,801	-	-	1,297,801
Investment property held for sale, net	49,808	-	-	49,808
	$ 17,648,103	$ 277,386	$ (795)	$ 17,924,694
LIABILITIES AND NET ASSETS				
Liabilities:				
Notes payable	$ 1,269,120	$ -	$ -	$ 1,269,120
RepMar deposit	1,739,989	-	-	1,739,989
Accrued interest payable	33,514	-	-	33,514
Accounts payable and accrued expenses	284,550	-	2,874	287,424
Deposits pledged	858,639	-	-	858,639
Total liabilities	4,185,812	-	2,874	4,188,686
Net assets:				
Invested in capital assets	1,297,801	-	-	1,297,801
Restricted	-	277,386	-	277,386
Unrestricted	12,164,490	-	(3,669)	12,160,821
Total net assets	13,462,291	277,386	(3,669)	13,736,008
	$ 17,648,103	$ 277,386	$ (795)	$ 17,924,694

See accompanying independent auditors' report.

MARSHALL ISLANDS DEVELOPMENT BANK
(A Component Unit of the Republic of the Marshall Islands)

Combining Statement of Revenues, Expenses and Changes in Net Assets
September 30, 2011

	Marshall Islands Development Bank	Housing Preservation Grant	USDA Self-Help Housing Project	Total
Operating revenues:				
Interest income on loans	$ 2,370,769	$ 445	$ -	$ 2,371,214
Rental income	440,183	-	-	440,183
Insurance premiums	136,283	-	-	136,283
Federal grants	-	-	91,869	91,869
Loan fees	85,487	-	-	85,487
Interest income on time certificates of deposit	9,064	-	-	9,064
Miscellaneous	38,829	1,102	12	39,943
Total operating revenues	3,080,615	1,547	91,881	3,174,043
Provision for loan losses	467,992	-	-	467,992
Net operating revenues	2,612,623	1,547	91,881	2,706,051
Operating expenses:				
Interest expense:				
Interest on deposits	99,696	-	-	99,696
Interest on loans payable	73,139	-	-	73,139
Total interest expense	172,835	-	-	172,835
General and administrative expenses:				
Salaries and employee benefits	788,456	-	76,623	865,079
Depreciation	240,190	-	2,800	242,990
Utilities	222,509	-	-	222,509
Travel and training	93,698	-	1,490	95,188
Repairs and maintenance	70,160	-	-	70,160
Insurance	49,131	-	2,186	51,317
Printing, stationery and advertising	51,141	-	-	51,141
Representation	48,409	-	-	48,409
Office and house rental	28,200	-	7,164	35,364
Foreclosed assets, net	32,083	-	-	32,083
Promotion and donations	27,203	-	-	27,203
Professional fees	24,579	-	-	24,579
Land lease	18,639	-	-	18,639
Communications	17,486	-	240	17,726
Fuel	12,937	-	1,011	13,948
Taxes and licenses	1,950	-	-	1,950
Miscellaneous	28,977	-	356	29,333
Total general and administrative expenses	1,755,748	-	91,870	1,847,618
Earnings from operations	684,040	1,547	11	685,598
Nonoperating revenues:				
Investment earnings	153,342	-	-	153,342
Total nonoperating revenues	153,342	-	-	153,342
Change in net assets	837,382	1,547	11	838,940
Net assets at beginning of year	12,624,909	275,839	(3,680)	12,897,068
Net assets at end of year	$ 13,462,291	$ 277,386	$ (3,669)	$ 13,736,008

See accompanying independent auditors' report.

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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*

The Board of Directors
Marshall Islands Development Bank:

We have audited the financial statements of Marshall Islands Development Bank (MIDB) as of and for the year ended September 30, 2011, and have issued our report thereon dated August 27, 2012. 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 MIDB is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered MIDB"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 MIDB"s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of MIDB"s intemal 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, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

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 items 2011-1 and 2011-2 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether MIDB‟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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of MIDB in a separate letter dated August 27, 2012.

MIDB‟s response to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. We did not audit MIDB‟s response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Board of Directors and management of MIDB, others within the entity, the Office of the Public Auditor, federal awarding agencies, pass-through entities, the cognizant audit and other federal agencies and is not intended to be and should not be used by anyone other than these specified parties. However, this report is also a matter of public record.

Deloitte & Touche LLP

August 27, 2012

Finding No. 2011-1 – Loans Receivable

Criteria: A comprehensive set of policies and procedures should be in place to govern the lending and credit administration processes, which should include, at a minimum, internal control procedures over processing loan approvals, loan boarding, completeness of loan documentation, safeguarding of pertinent loan documents and monitoring of loan covenant requirements.

Conditions:

Our tests of a representative sample of 75 loans revealed several weaknesses in the design, implementation and adherence to internal controls in the lending and credit administration areas.

a. Current operating procedures do not provide for a system wherein a person who is not responsible for loan data input independently verifies pertinent information (e.g. borrower name, addresses, loan amount, interest rate, loan date, maturity date), so that erroneous inputs may be timely identified and corrected.

b. The Bank‟s lending policy does not provide for a waiver of credit background checks; however, no checks were performed for five loans granted to Bank employees.

c. Promissory notes and loan agreements, which are the pertinent legal documents, should contain sufficient detail. Currently, the Bank does not include information such as loan number and maturity date on these documents. Additionally, safeguarding of pertinent documents should be strengthened. For ten loans, the credit folders containing the promissory note, loan agreement, collateral document and other loan-related information cannot be located. Additionally, for one loan, the origination date is not indicated on the promissory note.

d. For two loans, the loan term on the promissory notes differ from that indicated in the loan system.

e. The Bank‟s policy requires that loans of deceased borrowers be immediately charged off. One such loan should have been charged off as of September 30, 2011.

f. For eight commercial loans, financial statements were not obtained.

g. For seven commercial loans, no casualty insurance policies protecting collateral have been obtained.

h. For seven loans, the monthly payment information was not indicated in the promissory notes or in the loan system:

Cause: The cause of the above condition appears to be noncompliance with the criteria.

Effect: The effect of the above is the potential occurrence of errors in the loan portfolio balances. This condition also gives rise to potential losses due to insufficient safeguarding of legal and collateral documents which support the Bank‟s legal claims.

Finding No. 2011-1 – Loans Receivable, Continued

Recommendation: The Bank should perform a comprehensive review of its current policies and procedures and strengthen internal controls and the monitoring of such controls in the lending and credit administration areas.

Prior Year Status: Similar issues on loan documentation have been reported as a finding in the audit of MIDB for fiscal years 2007 through 2010.

Auditee Response and Corrective Action Plan:

Item a and b - Management has already designated an employee who shall be responsible in checking and reviewing that proper loan documents are executed and at the same to validate the information encoded in the loan system.

Item c – Management was eventually able to locate the credit folders for three loans and for the rest, management will try to look for those. Management has already implemented that all loan documents of approved loans shall be scanned to assure better safekeeping.

Item d - Management will establish a separate monitoring for all loans with open date of 1999 in the loan system.

Item e - Loan of deceased borrowers are only charged off upon the receipt of death certificate and approval of the managing director for write-off. Management will pursue securing the death certificate to facilitate the write-off of this loan account.

Items f to h - These loans are already under the review of the managing director and that management is working on ensuring that policies and procedures on proper loan documentation shall be complied with.

Finding No. 2011-2 Significant Delay in the Accounting Records

Criteria: Day-to-day transactions should be posted timely to keep up-to-date and completed accounting records. Reconciliation of key accounts, including bank reconciliations and review of such reconciliations, should be performed monthly.

Condition: The Bank does not have an established set of policies, procedures and controls in place to ensure the timely processing and posting of transactions, and timely preparation and review of reconciliations and reports. During the year ended September 30, 2011, various accounting records do not appear to have been processed and timely updated as evidenced by the following:

- Posting of payment transactions to the loan system and the general ledger were not up to date. Collections during 2011 were only posted in February 2012. As of April 12, 2012, payment recording and posting was completed for December 31, 2011 transactions. Consequently, reconciliation of outstanding balances in the loan system with the general ledger was not performed regularly (i.e., monthly basis)

- Bank reconciliations were prepared and were independently reviewed but this review did not occur promptly. The September 30, 2011 reconciliations were completed in March 2012.

- Interest income posted in the general ledger is based on cash collections. The Bank adjusts accrued interest at the end of the year, and as such, accrued interest receivable and interest income in the monthly financial statements was not properly presented based on the accrual method of accounting.

Cause: The cause of the above condition appears to be noncompliance with the criteria.

Effect: The effect of the above is the delayed identification and correction of errors and misstatements in the financial statements.

Recommendation: Management should implement procedures that require the timely posting of daily transactions and a checklist of accounts that should be reconciled and reviewed on a monthly basis. Prudence would indicate that posting of daily transactions be performed within a week, and the reconciliation of key balance sheet accounts be performed within a month.

Auditee Response and Corrective Action Plan: The managing director has already met with the accounting officers to resolve and correct this matter.

Schedule of Prior Year Findings
Year Ended September 30, 2011

Unresolved Prior Audit Findings and Responses

The status of unresolved prior year finding is stated on page 29.

There are no unresolved prior year questioned costs.