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, 2012 AND 2011

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

Years Ended September 30, 2012 and 2011
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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, 2012 and 2011, 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 previously present fairly, in all material respects, the financial position of the Marshall Islands Development Bank as of September 30, 2012 and 2011, 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 May 22, 2013, 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.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The 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, 2012 on pages 25 and 26 are presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements as of September 30, 2012 and for the year then ended and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the 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, 2012 are fairly stated in all material respects in relation to the financial statements as a whole.

Deloitte & Touche LLP

May 22, 2013

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

Management's Discussion and Analysis
Years Ended September 30, 2012 and 2011

Fiscal year October 1, 2011 to September 30, 2012 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 and Housing 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, 2012.

FINANCIAL HIGHLIGHTS

- MIDB's total net assets increased by **$1.69M or 12%** over the course of this year's operation. Net assets are funds from local funds, the Housing Preservation Grant and the USDA Self-Help Housing Project, which increased collectively by **$1.69M.**
- Revenues virtually remain unchanged marginally increasing by $0.13M or 4.8% while expenses increased by $0.10M or 5%. MIDB earned $2.83M during the fiscal year, $2.44M of which was generated through Interest on loans. On the other hand, MIDB incurred various expenses for banking activities, broken down as $0.18M for Operating Expenses, and $1.94M for General and Administrative Expenses. Other expenses such as Provision for Loan loss and Bad Debt Expense amounting to $0.21M was also provided. These expenses were funded by Interest Income on Loans and Other Income of $3.04M and by gain on sale of stocks and other investment earnings of $0.98M.

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 incite on MIDB's resources, liabilities and net assets, MIDB's priority investments and performance results compared to previous year. At the end of the fiscal year 2012, MIDB's assets of $22.17M exceeded liabilities of $6.74M by $15.43M. However, $1.73M or 12% 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, 2012, Unrestricted Net Assets amounted to $13.70M, enough to repay all outstanding debts.

Summary of Statements of Net Assets

			2012		2011		2010
Assets	Cash and Equivalents	$	386,349	$	55,361	$	151,970
	Restricted Cash		518,242		500,007		-
	Restricted TCD		128,758		-		576,393
	Loans Receivable, net		18,908,587		15,125,289		15,232,330
	Premises and Equipment, net		1,455,422		1,297,801		1,454,291
	Other Assets		775,684		946,236		813,602
	Total Assets	$	**22,173,042**	$	**17,924,694**	$	**18,228,586**

Summary of Statements of Net Assets, Continued

	2012	2011	2010
Liabilities			
Loans payable	$ 3,690,095	$ 1,269,120	$ 2,543,830
RepMar deposit	1,805,049	1,739,989	1,716,236
Other liabilities	1,248,152	1,179,577	1,071,452
Total liabilities	**$ 6,743,296**	**$ 4,188,686**	**$ 5,331,518**
Net Assets			
Investment in capital assets	$ 1,455,422	$ 1,297,801	$ 1,454,291
Restricted	278,805	277,386	275,839
Unrestricted	13,695,519	12,160,821	11,166,938
Total net assets	**$ 15,429,746**	**$ 13,736,008**	**$ 12,897,068**

- Loan approvals for the year were approximately $23.62M, broken down by projects, $22.95M released under various consumer loans and $0.64M granted to housing loans. Loans receivable, Net increased by $3.78M in 2012 compared with $0.11M decrease in 2011. Loans released increased from $15.41M to $23.62M during the fiscal years 2011 and 2012, 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 two local businesses. RMI Government made withdrawals, net of deposits, during fiscal years 2010, 2011 and 2012 to finance some governmental operations and obligations. As of September 30, 2012, Time Certificate Deposit of RMI Government was $1.81M.

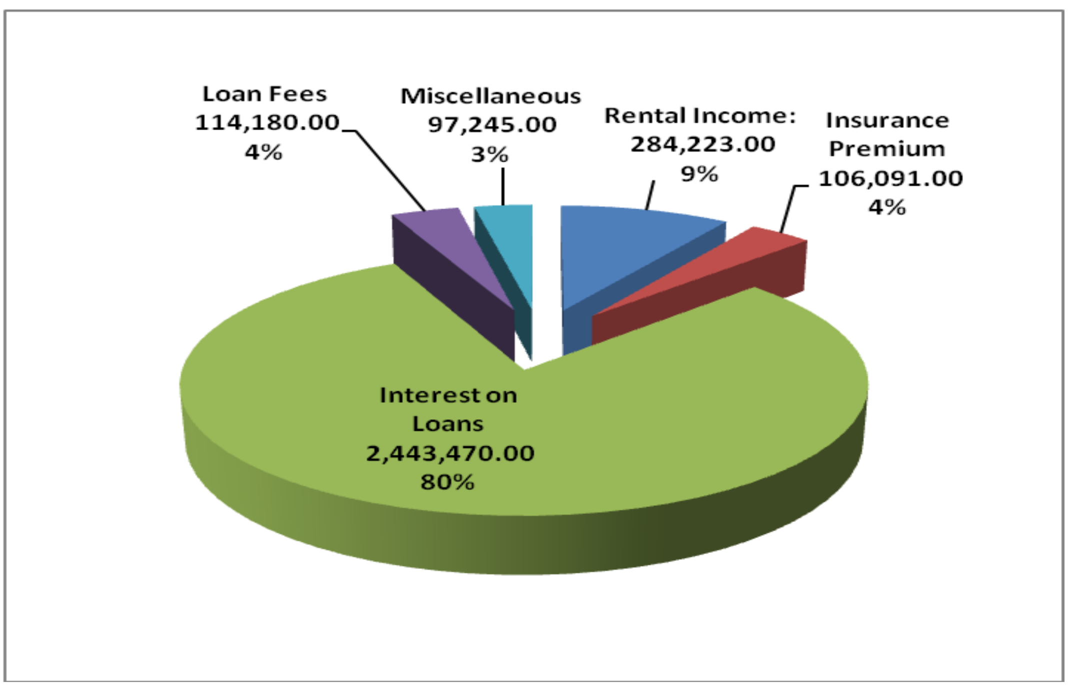
- MIDB continuously liquidates its long-term loan with International Commercial Bank of China (ICBC) by paying approximately $0.40M on principal every year. The loan with ICBC amounting to $5M was granted in August 6, 1999, with an interest rate of 5% per annum, maturing in August 6, 2014, no collateral or security was provided. As of September 30, 2012, outstanding principal balance on ICBC loan was $0.8M.

- MIDB availed of a $2.0M and $1.0M long-term loan with Bank of Marshall Islands on June 14 and August 15, 2012. Interest payment shall be at annual rate of 5% per annum until maturity date in March 14 and October 31, 2017, respectively. As of September 30, 2012, outstanding principal balance on BOMI loan was $1.9M and $0.99M, correspondingly.

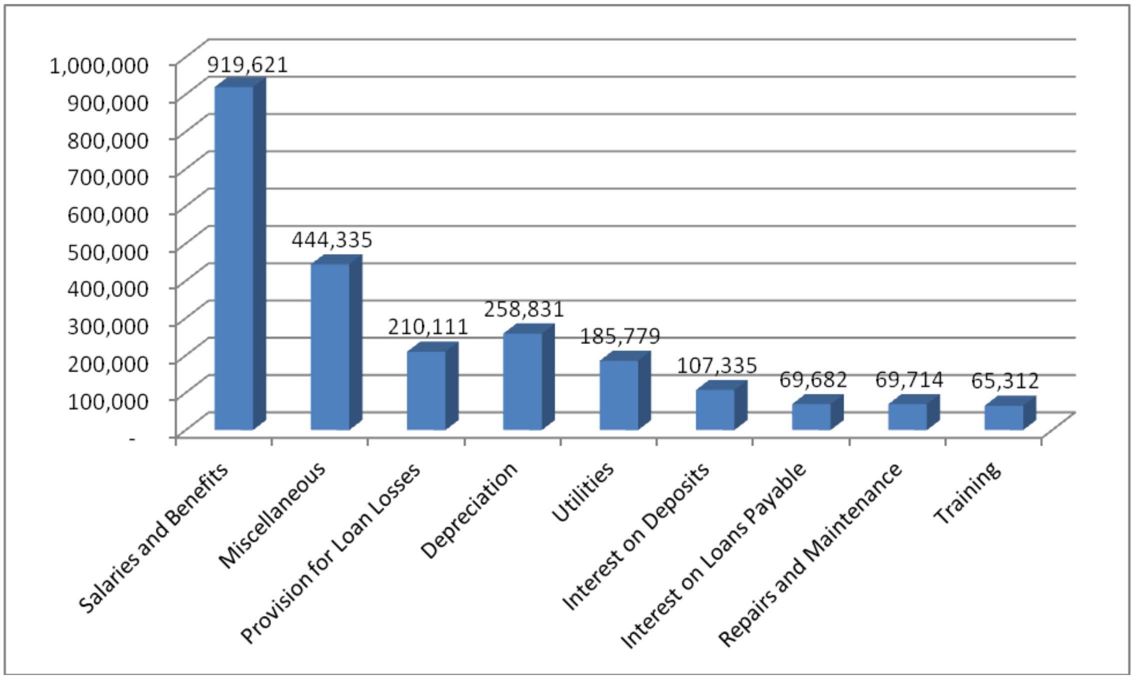
Summary of Statements of Revenues, Expenses and Changes in Net Assets

	2012	2011	2010
Operating revenues	$ 3,045,209	$ 3,174,043	$ 3,246,968
Less: Expenses			
Provision for loan losses	14,987	467,992	307,816
Provision for accounts receivable	195,124	-	-
Operating expenses	177,017	172,835	234,771
General administrative expenses	1,943,592	1,847,618	1,913,706
	2,330,720	2,488,445	2,456,293
Earnings from operations	714,489	685,598	790,675
Non-operating revenues	979,249	153,342	401,842
Increase in net assets	1,693,738	838,940	1,192,517
Net assets at beginning of year	13,736,008	12,897,068	11,704,551
Net assets at end of year	**$ 15,429,746**	**$ 13,736,008**	**$ 12,897,068**

- MIDB's total revenues (excluding Non-Operating Revenues of $979K) for current year decreased by $129K compared with fiscal year 2011. About 81% of the Bank's revenue comes from Interest on Loans, 86% and 10% 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 Expenses incurred decreased by $158K compared from last year's operation. The Bank expenses cover a range of operating, general and administrative expenses. 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 over-all picture of the Bank's spending activities.



- Operating Expenses increased by $4K during fiscal year ended September 30, 2012 compared to fiscal year ended September 30, 2011 due to increase in Interest on Deposits. Interests on Deposits are interest expenses paid and accrued on RepMar TCD and various savings accounts. Savings accounts increased by $141K or 17% from last year's $859K. RepMar TCD, on the other hand, increased by $65K or 4%, from $1.74M to $1.81M, due to interest.

- General and Administrative Expenses on the aggregate increased by $96K or 6 % from last year's operation due to increase in Salaries and Employee Benefits, Depreciation and Miscellaneous Expenses.

Capital Assets and Debt

Significant capital asset activity occurred during 2012 includes the newly installed air condition for MIDB Building amounting to $100K and the fully completed Sample House located in Litakboki compound amounting to $70K . For additional information concerning capital assets, please refer to Note 8 to the financial statements. MIDB obtained two loans from BOMI aggregating $3.0M during 2012. These loans were obtained for the purpose of providing funding for MIDB's loan programs. For additional information concerning debt, please refer to Note 11 to the financial statements.

Management's and Discussion and Analysis for the year ended September 30, 2011 is set forth in MIDB's report on the audit of financial statements, which is dated August 27, 2012. That Discussion and Analysis explains the major factors impacting the 2011 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 consumer 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.

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, 2012. 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, 2012 and 2011

ASSETS	2012	2011
Cash and cash equivalents	$ 386,349	$ 55,361
Restricted cash	518,242	500,007
Restricted time certificate of deposit	128,758	-
Investments	366,748	423,748
Receivables, net:		
Loans	18,908,587	15,125,289
Accrued interest	113,039	75,369
Other	259,989	397,311
Capital assets:		
Non-depreciable capital assets	104,893	45,577
Capital assets, net of accumulated depreciation	1,350,529	1,252,224
Investment property held for sale, net	35,908	49,808
	$ 22,173,042	$ 17,924,694

LIABILITIES AND NET ASSETS	2012	2011
Liabilities:		
Notes payable	$ 3,690,095	$ 1,269,120
RepMar deposit	1,805,049	1,739,989
Accrued interest payable	22,374	33,514
Accounts payable and accrued expenses	225,939	287,424
Deposits pledged	999,839	858,639
Total liabilities	6,743,296	4,188,686
Commitments and contingency		
Net assets:		
Invested in capital assets	1,455,422	1,297,801
Restricted	278,805	277,386
Unrestricted	13,695,519	12,160,821
Total net assets	15,429,746	13,736,008
	$ 22,173,042	$ 17,924,694

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, 2012 and 2011

	2012	2011
Operating revenues:		
Interest income on loans	$ 2,443,470	$ 2,371,214
Rental income	284,223	440,183
Loan fees	114,180	85,487
Insurance premiums	106,091	136,283
Federal grants	55,457	91,869
Interest income on time certificates of deposit	4,995	9,064
Miscellaneous	36,793	39,943
Total operating revenues	3,045,209	3,174,043
Provision for loan losses	14,987	467,992
Bad debts expense	195,124	-
Net operating revenues	2,835,098	2,706,051
Operating expenses:		
Interest expense:		
Interest on deposits	107,335	99,696
Interest on loans payable	69,682	73,139
Total interest expense	177,017	172,835
General and administrative expenses:		
Salaries and employee benefits	919,621	865,079
Depreciation	258,831	242,990
Utilities	185,779	222,509
Insurance	72,004	51,317
Repairs and maintenance	69,417	70,160
Travel and training	65,312	95,188
Printing, stationery and advertising	62,678	51,141
Representation	58,743	48,409
Communications	41,535	17,726
Professional fees	39,279	24,579
Office and house rental	28,967	35,364
Land lease	21,443	18,639
Promotion and Donation	19,830	27,203
Fuel	17,739	13,948
Taxes and licenses	7,553	1,950
Foreclosed assets, net	-	32,083
Miscellaneous	74,861	29,333
Total general and administrative expenses	1,943,592	1,847,618
Earnings from operations	714,489	685,598
Nonoperating revenues:		
Gain from sale of stocks	790,000	-
Investment earnings	187,418	153,342
Other	1,831	-
Total nonoperating revenues	979,249	153,342
Change in net assets	1,693,738	838,940
Net assets at beginning of year	13,736,008	12,897,068
Net assets at end of year	$ 15,429,746	$ 13,736,008

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, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Cash received from customers	$ 2,960,281	$ 2,914,563
Cash payments to suppliers for goods and services	(852,809)	(716,829)
Cash payments to employees for services	(904,399)	(882,493)
Interest received on time certificates of deposit	2,644	17,435
Interest paid	(188,157)	(159,480)
Operating grants received	55,457	91,869
Net cash provided by operating activities	1,073,017	1,265,065
Cash flows from noncapital financing activities:		
Net repayments under loan arrangement	-	(764,063)
Net change in RepMar deposit	65,060	23,753
Net change in pledged deposits	141,200	109,560
Net cash provided by (used in) noncapital financing activities	206,260	(630,750)
Cash flows from capital and related financing activities:		
Principal repayment of long-term debt	(579,025)	(654,356)
Proceeds from long-term debt	3,000,000	143,709
Additions to premises, equipment and foreclosed assets	(404,221)	(72,600)
Proceeds from sale of property and equipment	3,500	-
Net cash provided for (used in) capital and related financing activities	2,020,254	(583,247)
Cash flows from investing activities:		
Loan originations and principal collections, net	(3,855,968)	(377,405)
Net change in restricted assets	(146,993)	76,386
Proceeds from sale of investments	869,000	-
Purchase of investments	(22,000)	-
Dividends received	187,418	153,342
Net cash used in investing activities	(2,968,543)	(147,677)
Net change in cash and cash equivalents	330,988	(96,609)
Cash and cash equivalents at beginning of year	55,361	151,970
Cash and cash equivalents at end of year	$ 386,349	$ 55,361
Cash flows from operating activities:		
Earnings from operations	$ 714,489	$ 685,598
Adjustments to reconcile earnings from operations to net cash provided by operating activities:		
Provision for loan losses	14,987	467,992
Bad debts expense	195,124	-
Depreciation	258,831	242,990
Provision for losses on foreclosed asset	-	32,083
Decrease (increase) in assets:		
Receivables:		
Accrued interest	(52,657)	(1,090)
Other	(57,802)	(183,220)
Increase (decrease) in liabilities:		
Accrued interest payable	(11,140)	13,355
Accrued expenses	(61,485)	(14,790)
Deferred loan fees	21,911	6,914
Unearned premiums	50,759	15,233
Net cash provided by operating activities	$ 1,073,017	$ 1,265,065

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, 2012 and 2011, 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.

(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.

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, 2012 and 2011, the carrying amounts of cash and cash equivalents and time certificates of deposit are $1,033,349 and $555,368 respectively, and the corresponding bank balances are $1,243,460 and $554,868, respectively. Of the bank balances, $643,272 and $505,819, 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 equity method, the investor records, as earnings or loss, its proportionate share 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 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.

(2) Summary of Significant Accounting Policies, Continued

Other Receivables

Other receivables are due from government agencies, businesses and individuals located within the Republic of the Marshall Islands and are interest free and uncollateralized. The allowance for uncollectible accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectibility of these accounts and prior collection experience. Management determines the adequacy of the allowance for uncollectible accounts based upon review of the aged accounts receivable. The allowance is established through a provision for bad debts charged to expense.

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 the year ended September 30, 2012, MIDB implemented the following pronouncements:

- 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 the frequency and timing of measurements for actuarial valuations first used to report funded status information in OPEB plan financial statements. The implementation of this pronouncement did not have a material effect on the accompanying financial statements.

- GASB 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 implementation of this pronouncement 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 that state and local governments are increasingly entering into. 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 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.

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 has not yet determined the effect of implementation of this statement on the financial statements of MIDB.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In April 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of MIDB.

In April 2012, GASB issued Statement No. 66, *Technical Corrections - 2012*, which enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The provisions of this statement are effective for periods beginning after December 15, 2012. Management has not yet determined the effect of implementation of this statement on the financial statements of MIDB.

In June 2012, GASB issued Statement No. 67, *Financial Reporting for Pension Plans*, which revises existing guidance for the financial reports of most pension plans, and Statement No. 68, *Accounting and Financial Reporting for Pensions*, which revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The provisions in Statement 67 are effective for financial statements for periods beginning after June 15, 2013. The provisions in Statement 68 are effective for fiscal years beginning after June 15, 2014. Management has not yet determined the effect of implementation of these statements 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

A summary of MIDB's investments as of September 30, 2012 and 2011 is as follows:

	2012	2011
Bank of Marshall Islands	$ 336,748	$ 393,748
Marshall Islands Service Corporation	30,000	30,000
	$ 366,748	$ 423,748

(3) Investments, Continued

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 14% and 16% of the outstanding shares of BOMI as of September 30, 2012 and 2011, respectively. During the year ended September 30, 2012, MIDB sold 7,900 shares at a price of $110 per share, which resulted in a gain on sale of investments of $790,000. 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, 2012 and 2011, dividend income earned from investees was $187,418 and $153,342, respectively.

(4) Loans Receivable

Loans receivable as of September 30, 2012 and 2011 are summarized as follows:

	2012	2011
Investment Development Fund	$ 1,294,319	$ 4,330,669
Compact Section 211	316,054	942,716
Republic of the Marshall Islands	29,315,810	25,888,673
Housing Preservation Grant	10,683	12,011
Gross loans	30,936,866	31,174,069
Less: net deferred loan fees	(106,335)	(84,424)
Less: unearned premiums	(273,827)	(223,068)
Less: allowance for loan losses	(11,648,117)	(15,741,288)
	$ 18,908,587	$ 15,125,289

An analysis of the change in the allowance for loan losses during the years ended September 30, 2012 and 2011 is as follows:

	2012	2011
Beginning balance	$ 15,741,288	$ 15,296,590
Provision (Recoveries) for loan losses	-	461,352
Charge-offs	(4,093,171)	(16,654)
Ending balance	$ 11,648,117	$ 15,741,288

The loan portfolio is comprised of consumer, housing and business loans. The majority of the 2012 and 2011 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 5.5% - 6.5% 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, 2012 and 2011 is summarized as follows:

	2012	2011
Republic of the Marshall Islands	$ 130,716	$ 94,433
Investment Development Fund	14,987	389
Gross accrued interest receivable	145,703	94,822
Less: allowance for doubtful interest	(32,664)	(19,453)
	$ 113,039	$ 75,369

An analysis of the change in the allowance for interest receivable losses during the years ended September 30, 2012 and 2011 is as follows:

	2012	2011
Beginning balance	$ 19,453	$ 13,760
Provision for loan losses	14,987	6,640
Charge-offs	(1,776)	(947)
Ending balance	$ 32,664	$ 19,453

(6) Other Receivables

Other receivables as of September 30, 2012 and 2011, are as follows:

	2012	2011
Rental	$ 306,368	$ 264,453
Other	148,745	122,858
	455,113	397,311
Allowance for uncollectible accounts	(195,124)	-
	$ 259,989	$ 397,311

(7) Restricted Deposits

MIDB maintains a savings deposit as of September 30, 2012 and 2011 in the amount of $518,242 and $500,007, respectively, that is 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.

MIDB also maintains a time certificate of deposit as of September 30, 2012 with an affiliated bank in the amount of $128,758 that is restricted to collateralize a loan payable.

(8) Premises and Equipment

Capital asset activity during the years ended September 30, 2012 and 2011 is as follows:

	2012			
	October 1, 2011	Additions	Deletions/ Transfers	September 30, 2012
Building and houses	$ 2,281,046	$ 260,854	$ -	$ 2,541,900
Computer systems	247,093	890	(3,036)	244,947
Motor vehicles	165,961	72,695	(27,000)	211,656
Office furniture	54,841	3,183	-	58,024
Office equipment	381,900	7,283	-	389,183
	3,130,841	344,905	(30,036)	3,445,710
Less accumulated depreciation	(1,878,617)	(244,931)	28,367	(2,095,181)
	1,252,224	99,974	(1,669)	1,350,529
Construction in progress	45,577	156,934	(97,618)	104,893
	$ 1,297,801	$ 256,908	$ (99,287)	$ 1,455,422

	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

(9) Foreclosed Assets

Foreclosed assets are presented net of an allowance for losses. Foreclosed assets as of September 30, 2012 and 2011 are summarized as follows:

	2012	2011
Foreclosed assets	$ 350,000	$ 350,000
Allowance for losses	(350,000)	(350,000)
	$ -	$ -

An analysis of the allowance for losses on foreclosed assets for the years ended September 30, 2012 and 2011 is as follows:

	2012	2011
Balance at beginning of year	$ 350,000	$ 317,917
Provision for losses	-	32,083
Balance at end of year	$ 350,000	$ 350,000

(10) 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, 2012 and 2011, the property is presented net of accumulated depreciation of $103,092 and $89,192, respectively. Depreciation expense of $13,900 was recognized during each of the years ended September 30, 2012 and 2011.

(11) Long-term Debt

Long-term debt at September 30, 2012 and 2011 is as follows:

	2012	2011
Loan payable to the Mega International Commercial Bank (formerly the International Commercial Bank of China) in the amount of $5,000,000, dated August 6, 1999, interest at 5% per annum, due in semi-annual installments of $200,000 plus interest through August 6, 2014, uncollateralized.	$ 800,000	$ 1,200,000
Note payable to an affiliate bank in the amount of $143,709, dated January 11, 2011, interest at 7.5% per annum, due in monthly installments of principal and interest of $10,085 through May 28, 2012, uncollateralized. This loan was repaid in full during 2012.	-	69,120
Note payable to an affiliate bank in the amount of $2,000,000, dated June 14, 2012, interest at 5% per annum, due in monthly installments of principal and interest of $40,000 through March 14, 2017, collateralized by loans receivable in the amount of $15,232,330. Loan proceeds were used to fund housing loans.	1,903,004	-
Note payable to an affiliate bank in the amount of $1,000,000, dated August 15, 2012, interest at 5% per annum, due in monthly installments of principal and interest of $18,920 through August 31, 2017, collateralized by the MAKO building and a time certificate of deposit. Loan proceeds were used to fund housing loans.	987,091	-
	$ 3,690,095	$ 1,269,120

(11) Long-term Debt, Continued

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

Year ending September 30,	Principal	Interest	Total
2013	$ 963,700	$ 178,381	$ 1,142,081
2014	995,232	127,058	1,122,290
2015	628,533	78,507	707,040
2016	663,568	43,472	707,040
2017	439,062	8,584	447,646
	$ 3,690,095	$ 436,002	$ 4,126,097

Long-term debt changes during the years ended September 30, 2012 and 2011 are as follows:

	Balance October 1,	Additions	Reductions	Balance September 30,	Due Within One Year
2012:					
Notes payable	$ 1,269,120	$ 3,000,000	$ (579,025)	$ 3,690,095	$ 963,700
2011:					
Notes payable	$ 1,779,767	$ 143,709	$ (654,356)	$ 1,269,120	$ 469,120

(12) Related Party Transactions

As of September 30, 2012 and 2011, MIDB has deposits with a bank of $389,577 and $49,050, respectively, in which MIDB has an equity investment. The deposits accrue interest at rates of 0.25% to 2.5% per annum. Interest earned for the years ended September 30, 2012 and 2011 was $4,995 and $9,064, respectively.

As of September 30, 2012 and 2011, MIDB employees have loans outstanding of $764,670 and $734,202, respectively. In addition, the directors of MIDB have loans outstanding as of September 30, 2012 and 2011, of $89,010 and $72,496, respectively. All loans were made at normal commercial terms and conditions.

As of September 30, 2012 and 2011, MIDB has an outstanding certificate of deposit, totaling $1,805,049 and $1,739,989, 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, 2012 and 2011, interest payable relating to this deposit amounted to $28,485 and $24,681, 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, 2012 and 2011 are as follows:

	Balance October 1,	Additions	Reductions	Balance September 30,
2012:				
RepMar deposit	$ 1,739,989	$ 69,600	$ (4,540)	$ 1,805,049
2011:				
RepMar deposit	$ 1,716,236	$ 47,784	$ (24,031)	$ 1,739,989

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, 2012 and 2011 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 March 31, 2012, MIDB entered into an agreement to manage the hotel 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. The term of the agreement is for as long as is required to bring the loan current. Loan balances as of September 30, 2012 and 2011 of $1,064,224 and $1,049,458, 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 $63,407 and $3,259 as of September 30, 2012 and 2011, respectively.

Further, certain loans recorded in the books of USDA are subject to MIDB guarantee, the balance of which amounted to $10,638,147 and $10,304,811 as of September 30, 2012 and 2011, 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.

On January 15, 2010, MIDB entered into a fifty-year ground lease agreement for a portion of Awao Weto property expiring on January 14, 2060.

Future minimum lease payments under these leases are as follows:

Year ending September 30,	
2013	$ 10,164
2014	10,457
2015	10,554
2016	10,554
2017	10,554
2018-2022	54,234
2023-2027	37,184
2028-2032	14,733
2033-2037	7,421
2038-2042	7,421
2043-2047	7,421
2048-2052	7,421
2053-2057	7,421
2058-2061	3,249
	$ 198,788

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,	
2013	$ 221,973
2014	168,280
2015	124,110
2016	34,360
2017	30,360
2018-2022	151,800
2023-2027	151,800
2028-2030	68,310
	$ 950,993

(14) Commitments and Contingency, Continued

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, 2012

ASSETS	Marshall Islands Development Bank	Housing Preservation Grant	USDA Self-Help Housing Project	Total
Cash and cash equivalents	$ 107,932	$ 278,805	$ (388)	$ 386,349
Restricted cash	518,242	-	-	518,242
Restricted time certificates of deposit	128,758	-	-	128,758
Investments	366,748	-	-	366,748
Receivables, net:				
Loans	18,908,587	-	-	18,908,587
Accrued interest	113,039	-	-	113,039
Other	257,834	-	2,155	259,989
Premises and equipment, net	1,433,246	-	22,176	1,455,422
Investment property held for sale, net	35,908	-	-	35,908
	$ 21,870,294	$ 278,805	$ 23,943	$ 22,173,042
LIABILITIES AND NET ASSETS				
Liabilities:				
Notes payable	$ 3,690,095	$ -	$ -	$ 3,690,095
RepMar deposit	1,805,049	-	-	1,805,049
Accrued interest payable	22,374	-	-	22,374
Accrued expenses	210,477	-	15,462	225,939
Deposits pledged	999,839	-	-	999,839
Total liabilities	6,727,834	-	15,462	6,743,296
Net assets:				
Invested in capital assets	1,433,246	-	22,176	1,455,422
Restricted	-	278,805	-	278,805
Unrestricted	13,709,214	-	(13,695)	13,695,519
Total net assets	15,142,460	278,805	8,481	15,429,746
	$ 21,870,294	$ 278,805	$ 23,943	$ 22,173,042

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, 2012

	Marshall Islands Development Bank	Housing Preservation Grant	USDA Self-Help Housing Project	Total
Operating revenues:				
Interest income on loans	$ 2,443,378	$ 92	$ -	$ 2,443,470
Rental income	284,223	-	-	284,223
Insurance premiums	106,091	-	-	106,091
Federal grants	-	-	55,457	55,457
Loan fees	114,180	-	-	114,180
Interest income on time certificates of deposit	4,995	-	-	4,995
Miscellaneous	35,466	1,327	-	36,793
Total operating revenues	2,988,333	1,419	55,457	3,045,209
Provision for loan losses	14,987	-	-	14,987
Bad debts expense	195,124	-	-	195,124
Net operating revenues	2,778,222	1,419	55,457	2,835,098
Operating expenses:				
Interest expense:				
Interest on deposits	107,335	-	-	107,335
Interest on loans payable	69,682	-	-	69,682
Total interest expense	177,017	-	-	177,017
General and administrative expenses:				
Salaries and employee benefits	883,885	-	35,736	919,621
Depreciation	256,007	-	2,824	258,831
Utilities	185,779	-	-	185,779
Insurance	71,464	-	540	72,004
Repairs and maintenance	68,400	-	1,017	69,417
Travel and training	65,312	-	-	65,312
Printing, stationery and advertising	62,678	-	-	62,678
Representation	58,743	-	-	58,743
Communications	41,465	-	70	41,535
Professional fees	39,279	-	-	39,279
Office and house rental	28,967	-	-	28,967
Land lease	21,443	-	-	21,443
Promotion and Donation	19,830	-	-	19,830
Fuel	15,304	-	2,435	17,739
Taxes and licenses	7,508	-	45	7,553
Miscellaneous	74,221	-	640	74,861
Total general and administrative expenses	1,900,285	-	43,307	1,943,592
Earnings from operations	700,920	1,419	12,150	714,489
Nonoperating revenues:				
Gain from sale of stocks	790,000	-	-	790,000
Investment earnings	187,418	-	-	187,418
Other	1,831	-	-	1,831
Total nonoperating revenues	979,249	-	-	979,249
Change in net assets	1,680,169	1,419	12,150	1,693,738
Net assets at beginning of year	13,462,291	277,386	(3,669)	13,736,008
Net assets at end of year	$ 15,142,460	$ 278,805	$ 8,481	$ 15,429,746

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 the Marshall Islands Development Bank (MIDB) as of and for the year ended September 30, 2012, and have issued our report thereon dated May 22, 2013. 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 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, 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 2012-1 and 2012-2 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 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 items 2012-03 and 2012-04.

We noted certain matters that we reported to management of MIDB in a separate letter dated May 22, 2013.

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 Auditor-General, 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

May 22, 2013

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

Schedule of Findings and Responses
Year Ended September 30, 2012

Finding No. 2012-1 – 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:

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 an independent person not responsible for loan data and processing verifies document completeness per policy before loans are approved.

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

c. Promissory notes and loan agreements, should contain sufficient detail. The Bank does not include information such as loan number and maturity date on these documents. Additionally, safeguarding documents should be strengthened. For ten loans, credit folders containing the promissory note, loan agreement, collateral documents and other loan-related information could not be located.

d. For three loans, promissory note terms differed from that indicated in the loan system.

e. The Bank's policy requires that loans of deceased borrowers be immediately charged off. Two such loans should have been charged off as of September 30, 2012.

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

g. For eight commercial loans, casualty insurance policies were not obtained.

h. The Bank's policy requires that approved salary allotment forms be executed for consumer loans secured through allotments. For four consumer loans, no allotments were obtained.

i. For one loan, the agreement was not signed by the Managing Director.

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.

Finding No. 2012-1 – 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 over lending and credit administration.

Prior Year Status: Similar issues on loan documentation have been reported as a finding in the audits of MIDB for fiscal years 2007 through 2011.

Auditee Response and Corrective Action Plan:

A, B, C - Management has already been using a document checklist form to verify the completeness of the documents from the start of application before forwarding it to the loan officer for interview and for approval by the Managing Director. For the some of the loans, the management will try it best to locate the loan folders. Currently, the bank's operation requires scanning of the loan documents for better safeguarding of files.

D- The error for the above loans has already been corrected.

E- Charging off loans of deceased borrowers is only upon the receipt of the death certificate and after the managing director reviewed and approves it for write-off. Management will pursue securing the death certificate to facilitate the write-off of this loan account.

F, G, H, I - Management has already met with the Loan Officers to correct and resolve these findings relating to the above loans. Findings related to salary allotments, as per stated in the bank's consumer loan policy one of the criteria and guidelines in approving a consumer loans are follows (a) the applicant's financial ability to repay loan; the consumer loan will be made and sealed through salary allotments only, except otherwise approved by the Managing Director. The above loans have been duly approved by the Managing Director.

Finding No. 2012-2 Significant Delay in the Accounting Records

Criteria: Duly transactions should be timely posted. Reconciliations of key accounts, including bank reconciliations, and review of such reconciliations, should be performed monthly.

Condition: The Bank does not have established policies, procedures and controls in place to ensure the timely processing and posting of transactions, and the timely preparation and review of reconciliations. During the year ended September 30, 2012, various accounting records do not appear to have been timely processed as evidenced by the following:

- Payment transaction postings to the loan system and the general ledger were not current. Collections during 2012 were only posted in November 28, 2012. As of March 25, 2013, payment recording and posting was completed for November 30, 2012 transactions. Consequently, reconciliation of outstanding loan system balances with the general ledger was not regularly performed (i.e., monthly).

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

- Interest income postings to the general ledger are based on cash collections. The Bank adjusts accrued interest at the end of the year. Accrued interest receivable and interest income in the monthly financial statements is therefore 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 timely posting of daily transactions and a checklist of accounts that should be reconciled and reviewed on a monthly basis. Prudence indicates that posting of daily transactions be performed within a week, and the reconciliation of key balance sheet accounts should be performed within a month.

Auditee Response and Corrective Action Plan: The board members together with the managing director met the staff and address this issue to resolve and correct as to timeliness. Staffs have been required to update the books in the soonest period of time.

Finding No. 2012-3 Local Non-Noncompliance

Criteria: RepMar's Procurement Code states the following:

(a) Section 124 - unless otherwise authorized by law, all Government contracts shall be awarded by competitive sealed bidding.

(b) Section 127 - procurement of goods and services not exceeding $25,000 may be made in accordance with small purchase procedures promulgated by RepMar's Policy Office. Small purchase procedures are those relatively simple and informal methods for securing services, supplies, or other property that do not cost more than $25,000. RepMar's Ministry of Finance has previously declared that if small purchase procedures are used, price or rate quotations shall be obtained from an adequate number of qualified sources.

(c) Section 128 - a contract may be awarded for a supply, service, or construction item without competition when it is determined in writing that there is only one source for the required supply, service, or construction item.

Condition: RepMar requires that procurement actions for goods and services provide full and open competition and compliance with this provision should be appropriately documented in procurement files. We noted the following items where documentation in file was inadequate to evidence the procurement process:

Item Description	Amount	Comment
New Air conditioner unit	$100,719	Written award notice to supplier was not complete.
Lexgen SUV	$29,995	Procurement procedures do not appear to have been followed.
Sangyong Kyron Pick-up 2012 model	$25,000	Price quotations from vendors were not available
Mazda Pick-up Truck	$17,700	Price quotations from vendors were not available

Cause: The cause of the above condition is the lack of adequate internal control policies and procedures requiring documentation of procurement procedures to comply with RepMar's Procurement Requirements.

Effect: The effect of the above condition is potential noncompliance with RepMar's Procurement Code.

Recommendation: We recommend that management establish adequate internal control policies and procedures to conform to RepMar's Procurement Code.

Auditee Response and Corrective Action Plan: Before the bank purchase certain materials we always try to seek quotations from local suppliers and due to the small number of local supplier we are already aware of the existing prices and the bank always go to the best deals because sometimes choosing the cheapest turns out to be not the best idea. Same is true with the purchase of vehicles.

Finding No. 2012-4 Loan agreement with International Commercial Bank of China

Criteria: In accordance with International Commercial Bank of China (ICBC) loan covenants, MIDB will not, without the prior written consent of ICBC, permit any obligation of, or loan, financing and credit available to MIDB to have any priority or to be entitled to any preferential arrangement, whether or not constituting a security agreement, in favor of any creditor or class of creditors, as to security, the payment of interest or repayment of principal or the right to receive income or revenue.

Conditions: MIDB obtained a bank loan and pledged collateral without prior ICBC written consent.

Cause: The cause of the above condition is the lack of adequate control policies and procedures requiring compliance with existing agreements.

Effect: The effect of the above condition is potential noncompliance with the criteria.

Recommendation: We recommend that management establish adequate internal control policies and procedures requiring compliance with contractual provisions.

Auditee Response and Corrective Action Plan: The bank is aware of its obligation towards International Commercial Bank of China and hasn't missed even one single payment from the beginning of the loan until it will mature and will be fully paid by 2014. The bank is religiously complying its responsibility towards its debt in terms of payment it maybe in local or international banks.

Unresolved Prior Year Findings
Year Ended September 30, 2012

The status of unresolved prior year findings is disclosed within the Schedule of Findings and Responses section (pages 29 through 33) of this report.