

August 31, 2007

CONFIDENTIAL

Mr. Amon Tibon
Managing Director
Marshall Islands Development Bank

Dear Mr. Tibon:

In planning and performing our audit of the financial statements of the Marshall Islands Development Bank (MIDB) for the year ended September 30, 2006, on which we have issued our report dated August 31, 2007, we developed the following recommendations concerning certain matters related to MIDB's internal control and certain observations and recommendations on other accounting, administrative and operating matters. Our principal recommendations are summarized below:

(1) Enhancement of IT Department

The Bank has an IT department staffed by two employees who also perform other functions in the accounting and loan departments. As the Bank does not have its own set of technically - equipped IT staff, the overall management of IT is highly dependent on assistance provided by an affiliate.

Per observation, certain reports may not be prepared timely due to the Bank's dependency on the availability of affiliate staff. Also, immediate corrective action may not be possible due to limited knowledge of MIDB IT staff.

The IT environment is a key area that the Bank should consider investing in but it appears that due to limited human technical resources, the Bank is maximizing the use of its employees in such a way that IT is not a full-time task. We recommend that the Bank assess the need to strengthen the IT department by either hiring additional staff or investing in education programs for existing staff.

(2) Review of Bank Reconciliation Reports

Bank reconciliations and float item reconciliations appear to have been regularly prepared during the year. This is in line with the Bank's extensive efforts to bring all accounting records current. However, based on sampled reports, signatures of the preparer and the reviewer were not always affixed on the reports. We recommend that to ensure adequate segregation over the preparation and review function, such reports be signed by preparers and reviewers/approvers.

(3) Negative Balances in Savings Deposits Pledged

The Bank, as of September 30, 2006, initially recorded \$467,416 of negative balances in "savings deposits pledged" and as "Other receivables". Prior to updating the Bank's records, checks appear to have been refunded to borrowers as it was thought that these customers had paid in excess of required loan payments. When records were updated, it was determined that these balances were actually collections that were not applied to corresponding loans.

Additionally, expenses advanced by the Bank on the management of certain properties remained in this account and were not transferred to corresponding loan accounts. Currently, the Bank charges customers 4% for these overdraft accounts, which is less than what should have been charged had these been transferred to loans. Subsequently, 57.9% (\$270,821) of the total amount has been identified by the Bank as accounts with outstanding loans, which was therefore reclassified. The Bank should ensure that a thorough investigation be conducted prior to allowing a customer to withdraw from the savings account to prevent overdrafts and financial losses. Moreover, management should request Board approval of the 4% interest rate applied to overdraft accounts.

(4) Debit Balances in Payable Account

Accrued expenses primarily consist of allotments payable, but \$2,667 as of September 30, 2006 comprises debit balances. This same finding was cited in our prior year letter dated August 28, 2007.

The Bank should ensure that accounts with abnormal balances are identified and are timely adjusted.

(5) Insurance Premium Liability

The Bank, as of September 30, 2006, has an outstanding liability to the Individual Assurance Company (IAC). Historically, the Bank contracted IAC to provide credit life insurance. In 2003, the Bank's self-insurance policy was approved and became effective in fiscal year 2004. It appears that the Bank may not have had formal communication with IAC as to the termination of the insurance contract. Consequently, the Bank has received billings from IAC for a \$35,141 liability outstanding for several years.

This same finding was also mentioned in our prior year letter dated August 28, 2007.

(6) Depreciation of Fixed Assets

The Bank's depreciation basis for motor vehicles is 3 years, regardless of whether the vehicle was purchased brand new or used. Motor vehicles are normally depreciated over 5 years but in certain cases, 3 years may be appropriate if it is actively used in field assignments. We recommend that management consider whether this policy should be amended. This same finding was also mentioned in our prior year letter dated August 28, 2007.

(7) Written Agreement on Sample Houses

Written agreements between the Bank and landowners were not executed to evidence the arrangement on the ownership of the sample houses. This same finding was also mentioned in our prior year letter dated August 28, 2007.

(8) Disposition on Long Outstanding Advances

Unliquidated travel advances totaling \$22,273 as of September 30, 2006, have been long outstanding. This finding was cited in our prior year letter dated August 28, 2007. We recommend that management ensure disposition of these items.

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(9) Lease Agreements

The Bank recognized 2006 rent income of \$247,113 from leased office space and apartment units. No lease agreement was presented supporting the rental income for the first quarter of fiscal year 2006, amounting to \$15,278.

This matter was mentioned in our prior year letter dated August 28, 2007.

(10) Discrepancy in Savings Account

We noted a savings account discrepancy as follows:

Account no.: BOM03

Balance per general ledger	\$ 5,012
Balance per subsidiary ledger	<u>5,727</u>
Difference	\$ <u>715</u>

(11) Policy on Capitalization of Major Repairs

The Bank does not have a formal policy on capitalization of major repairs of fixed assets. Therefore, all repairs and maintenance items have been expensed outright, regardless of amount and nature.

We recommend that the Bank consider formulating a policy relative to the capitalization of the cost of major repairs.

(12) Supporting Documents for Expense Items

Copies of cancelled checks for the following expense accounts were not located:

<u>Expense Account</u>	<u>Check No.</u>	<u>Check Amount</u>
Utilities	19606	\$ 17,937
Utilities	19606	11,632
Utilities	1865	9,734
Utilities	22763	10,261
Travel	21097	10,015

Cancelled checks should be available on file.

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(13) Payroll Documents

Payroll documents for the following were not located:

<u>PPE</u>	<u>Check Number</u>	<u>Gross Salary</u>	<u>Net Pay</u>	<u>Missing Document</u>
11/25/2005	19125	\$ 864.8	\$ 107.26	Time cards and time sheets "
12/9/2005	19465	572.4	4.33	"
12/23/2005	19886	655.74	22.33	"
2/3/2006	20395	759.32	96.47	"
3/3/2006	20845	1,135.39	459.38	"
8/18/2006	22476	864.77	0	"
9/1/2006	22825	968.37	787.41	Cancelled check
9/26/2006	22797	1,076.92	882.93	"

We recommend that management ensure safekeeping of payroll documents such as timesheets and cancelled checks. This finding was also mentioned in our prior year letter dated August 28, 2007

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We have also communicated matters noted during our audit of the financial statements of MIDB for the year ended September 30, 2006, which we considered to be reportable conditions in our report dated August 31, 2007.

This report is intended solely for the information and use of management, and others within the organization and is not intended to be used and should not be used by anyone other than these specified parties.

We would like to thank the accounting staff and management for their assistance during the course of our audit. Should you have any questions regarding the matters discussed herein, please contact our office at your convenience.

Very truly yours,

