

June 15, 2009

Mr. Amon Tibon  
Executive 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) as of and for the year ended September 30, 2008 (on which we have issued our report dated June 15, 2009), 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, we considered MIDB's 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 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. However, in connection with our audit, we identified, and included in the attached Appendix I, deficiencies related to MIDB's internal control over financial reporting and other matters as of September 30, 2008 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated June 15, 2009, 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 definition of a deficiency is also set forth in the attached Appendix I.

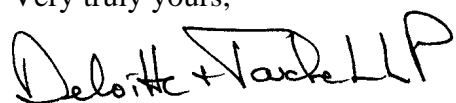
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with this report.

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

We will be pleased to discuss the attached comments with you and, if desired, to assist you in implementing any of the suggestions.

We wish to thank the staff and management of MIDB for their cooperation and assistance during the course of this engagement.

Very truly yours,



## SECTION I – CONTROL DEFICIENCIES

We identified, and have included below, control deficiencies involving MIDB's internal control over financial reporting as of September 30, 2008 that we wish to bring to your attention:

### 1. Overdraft

Comment: As of September 30, 2008, a checking account had a \$36,068 negative balance. This was caused by checks drawn against an account with insufficient funds. Per inquiry, bank practice has allowed an overdraft. However, no written agreement was provided to support this practice.

Recommendation: Management should ensure that checks are drawn against sufficient funds and if an overdraft is allowed, the agreement should be documented.

### 2. Long Outstanding Travel Advances

Comment: As of September 30, 2008, MIDB recorded travel advances of \$16,448 that include balances that have been outstanding for a number of years. This same finding was contained in the prior year letter dated June 30, 2008.

Recommendation: Management should ensure timely disposition of these items.

### 3. Useful Life

Comment: MIDB depreciation basis for motor vehicles is 3 years, regardless of whether the vehicle was purchased new or used. Motor vehicles are normally depreciated over 5 years but in certain cases, 3 years may be appropriate if such are actively being used in field assignments. This same finding was contained in the prior year letter dated June 30, 2008.

Recommendation: Management should consider whether this policy should be amended.

### 4. Capitalization Threshold

Comment: MIDB fixed asset policy requires that assets with acquisition costs of \$500 and above are capitalized and depreciated based on estimated useful lives. Examination of the fixed asset register indicated ninety-four items that did not meet the capitalization threshold.

Further, MIDB does not have a formal policy on capitalization of major repairs of fixed assets. Therefore, all repairs and maintenance items have been expensed. This matter was included in the prior year letter dated June 30, 2008.

Recommendation: Management should ensure compliance with its capitalization policy and consider formulating a policy relative to the capitalization of the cost of major repairs.

**5. Missing Rental Agreement**

Comment: The underlying rental agreement was not provided for the following.

<u>Acct. #</u>	<u>Account name</u>	<u>Doc #</u>	<u>Transaction Date</u>	<u>Amount</u>
5055	Housing rental	36771	11/30/07	\$4,000

Recommendation: Management should ensure all related documentation is on file.

**6. Accounting Period**

Comment: For one item tested, it appears that a portion of insurance expense relates to the subsequent year but was recorded in fiscal year 2008.

<u>Acct. #</u>	<u>Account name</u>	<u>Doc #</u>	<u>Transaction Date</u>	<u>Fiscal Year related to</u>	<u>Amount relating to FY 2009</u>
6080	Insurance	31031	03/28/08	2009	\$ 5,245

Recommendation: Management should ensure that expenses are recorded in the correct accounting period.

**7. Written Agreement on Sample House**

Comment: MIDB was able to provide a copy of the agreement relating to the sample house. However, we noted insufficient information on the agreement, i.e. agreed interest rate, amount of total receivable, etc. This finding was also mentioned in the prior year letter dated June 30, 2008.

Recommendation: Management should ensure that agreements are properly documented.

**8. Enhancement of IT Department**

Comment: MIDB has an IT department staffed by two employees who also perform other functions in the accounting and loan departments. As MIDB 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.

Certain reports may not be prepared timely due to MIDB'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 MIDB should consider investing in but it appears that due to limited human technical resources, MIDB is maximizing the use of its employees in such a way that IT is not a full-time task. This finding was also in the prior year letter dated June 30, 2008.

Recommendation: Management should assess the need to strengthen the IT department by either hiring additional staff or investing in education programs for existing staff.

**SECTION III – DEFINITIONS**

The definition of a deficiency that is established in AU 325, *Communicating Internal Control Related Matters Identified in an Audit*, is as follows:

A *deficiency* 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 deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when (a) a properly designed control does not operate as designed, or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.

## **MANAGEMENT'S RESPONSIBILITY FOR, AND THE OBJECTIVES AND LIMITATIONS OF, INTERNAL CONTROL OVER FINANCIAL REPORTING**

The following comments concerning management's responsibility for internal control over financial reporting and the objectives and inherent limitations of internal control over financial reporting are adapted from auditing standards generally accepted in the United States of America.

### **Management's Responsibility**

MIDB's management is responsible for the overall accuracy of the financial statements and their conformity with generally accepted accounting principles. In this regard, management is also responsible for establishing and maintaining effective internal control over financial reporting.

### **Objectives of Internal Control over Financial Reporting**

Internal control over financial reporting is a process affected by those charged with governance, management, and other personnel and designed to provide reasonable assurance about the achievement of the entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. Internal control over the safeguarding of assets against unauthorized acquisition, use, or disposition may include controls related to financial reporting and operations objectives. Generally, controls that are relevant to an audit of financial statements are those that pertain to the entity's objective of reliable financial reporting (i.e., the preparation of reliable financial statements that are fairly presented in conformity with generally accepted accounting principles).

### **Inherent Limitations of Internal Control over Financial Reporting**

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.