

MARSHALL ISLANDS SHIPPING CORPORATION

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

**INDEPENDENT AUDITORS' REPORT ON
INTERNAL CONTROL AND ON COMPLIANCE**

YEAR ENDED SEPTEMBER 30, 2010

**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**

Chairman
Board of Directors
Marshall Islands Shipping Corporation:

We have audited the financial statements of the Marshall Islands Shipping Corporation (MISC) as of and for the year ended September 30, 2010, and have issued our report thereon dated July 27, 2011. 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

In planning and performing our audit, we considered MISC'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 MISC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of MISC'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 (pages 3 through 9), 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 2010-1 through 2010-5 to be material weaknesses.

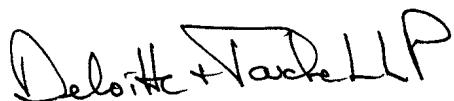
Compliance and Other Matters

As part of obtaining reasonable assurance about whether MISC's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 2010-6 and 2010-7.

We noted certain matters that we reported to management of MISC in a separate letter dated July 27, 2011.

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

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

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

July 27, 2011

MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses Year Ended September 30, 2010

Finding No. 2010-1

Inventory

Criteria: Inventory should be monitored and reconciled on a periodic basis and in a timely manner.

Condition: An audit adjustment was proposed in the amount of \$12,350 to correct year end inventory balances. MISC performs periodic inventory counts when vessels return from their field trips; however, such inventory balances are not timely reconciled to the general ledger.

Cause: The cause of the above condition is the lack of established policies and procedures pertaining to inventory.

Effect: The effect of the above condition is a possible misstatement of inventory balances and invalid cost of goods sales.

Recommendation: We recommend that management establish policies and procedures pertaining to reconciliation of inventory assets.

Prior Year Status: Lack of policies and procedures over the reconciliation of inventory balances was reported as a finding in the audit of MISC for fiscal year 2009.

Auditee Response and Corrective Action Plan:

Who: Head Accounting Officer

What: MISC will utilize the Quickbooks Inventory Module to record inventory activity for recording and posting to the General Ledger. Once this exercise has been completed, the Head Accounting Officer will reconcile the inventory assets accounts to the general ledger to date for FY 2011. Currently, a physical count of the inventory assets is performed upon the return of the shipping vessels from their field trips. After the physical count of the inventory assets is performed by a separate staff member from the Accounting Department, the Head Accounting Officer will reconcile the inventory balances to the general ledger. Once reconciliation has been completed to date for FY 2011, the inventory assets reconciliation policy as it pertains to the frequency will be completed upon the return of the shipping vessels from their field trips.

For FY 2011, a reconciliation policy to include the inventory assets reconciliation will be developed to document the General Ledger accounts to be reconciled, the reconciliation processing steps (to include review and approval), and frequency of reconciliations.

When: Next Fiscal Year 2011

MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses, Continued Year Ended September 30, 2010

Finding No. 2010-2

Fixed Assets

Criteria: Adequate internal control policies and procedures should be established to require that the subsidiary fixed asset register includes appropriate detail, a physical inventory of fixed assets is taken and the results reconciled with the fixed asset register, and fixed assets are adequately safeguarded. Furthermore, policies over actual estimated useful lives and capitalization thresholds should be adopted.

Condition: MISC has not established policies and procedures pertaining to fixed assets, specifically asset lives and capitalization thresholds. Furthermore, fixed assets are not tagged.

Further, fixed assets should be included in the subsidiary register with accurate descriptions and acquisition dates. We noted two line items with the same descriptions, but different acquisition dates, under motor vehicles in the fixed assets register that pertain to one vehicle.

Cause: The cause of the above condition is the lack of established policies and procedures pertaining to fixed assets.

Effect: The effect of the above condition is a possible misstatement of fixed assets.

Recommendation: We recommend that MISC adopt policies and procedures pertaining to fixed assets.

Prior Year Status: Lack of policies and procedures pertaining to fixed assets was reported as a finding in the audits of MISC for fiscal years 2007 through 2009.

Auditee Response and Corrective Action Plan:

Who: Head Accounting Officer

What: A fixed asset policy had been developed in prior fiscal years but has yet to be approved by the Board. For FY 2011, management will review the current draft policy to ensure it remains in line with the accounting needs of MISC and it addresses any possible internal control gaps. Until then, the Accounting Department will utilize the draft policy as a guideline for FY 2011. It is the goal of the Accounting Department to review the fixed assets subsidiary ledger and address the issues of accurate descriptions and acquisition dates, to include the possible duplicated data as noted above for one vehicle.

Capitalization thresholds have been established per the draft policy and will be utilized accordingly for FY 2011. Management will take every step to engage the MISC Board to review and approve the fixed policy prior to the end of FY 2011. Regarding fixed assets tags, initial efforts will be made in FY 2011 to address this issue. However, it is more likely that the fixed asset tags issue will be in addressed during the FY 2012 period.

When: Next Fiscal Year 2011 – FY 2012

MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses, Continued Year Ended September 30, 2010

Finding No. 2010-3

Copra Purchases

Criteria: Payment of copra purchases should be made directly to the individual grower or to authorized representatives of the grower.

Condition: Payments for copra purchases from growers are made based on check payments that are initially made out to a MISC employee who cashes the check and then distributes the cash to the respective growers.

Cause: The cause of the above condition is the lack of established policies and procedures over payments to growers for copra purchases.

Effect: The effect of the above condition is possible misappropriation of funds designated for copra purchases.

Recommendation: We recommended that management establish policies and procedures requiring payments be made directly to individual growers or to authorized representatives.

Prior Year Status: Lack of policies and procedures pertaining to payments of copra purchases was reported as a finding in the audit of MISC for fiscal year 2009.

Auditee Response and Corrective Action Plan:

Who: Head Accounting Officer

What: It is the expectation of management that this issue will continue to be an audit finding due to the fact that most growers do not have a bank account to cash their checks. In some cases, growers (especially from the lesser developed outer islands) do not have the appropriate identification required by the banking institution. Although not the most ideal of a process, MISC copra purchase process will ensure that adequate controls are in place to safeguard the funds designated for copra purchases.

The Accounting Department will ensure that all supporting documentation is clearly marked with appropriate signatures and copra purchase reports to identify the check written to an MISC employee (typically an Accounting Staff and separate from the vessel staff) and then the cash is transferred to the custody of the captain of the departing vessel. Upon return of the vessel, the copra purchase is reconciled and validated by the Accounting Department.

When: Next Fiscal Year 2011

MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses, Continued Year Ended September 30, 2010

Finding No. 2010-4

Revenues

Criteria: Adequate internal control policies and procedures should be established requiring that revenues be accurately supported, identified, recorded, and collected. Furthermore, pre-numbered forms should be utilized to facilitate the completeness of recording revenue. In addition, proper sales cut-off should be monitored for year-end sales.

Condition: The following exceptions concerning revenue tests were noted:

1. Pre-numbered charter request forms are not utilized. Charters are invoiced based on the information provided by management. In addition, freight is invoiced based on oral declarations from customers without further verification due to lack of adequate space and equipment.
2. Sales invoices, payment receipts, and validated deposit receipts for various other miscellaneous revenue items were not provided during the audit.
3. A cut-off error for September 2010 sales that were recorded in October 2010 was noted, which resulted in a proposed audit adjustment in the amount of \$155,272.

Cause: The cause of the above condition is the lack of established policies and procedures that require that revenues be accurately supported, identified, recorded, and collected.

Effect: The effect of the above condition is a possible misstatement of revenues.

Recommendation: We recommended that management establish policies and procedures requiring that all supporting documentation (e.g. invoices, receipts, set sales price, etc.) be arranged and kept in file for future reference. Furthermore, we recommend that MISC require that proper cut-off and recording of revenues be established.

Prior Year Status: Lack of established policies and procedures pertaining to revenues was reported as a finding in the audits of MISC for fiscal years 2007 through 2009.

Auditee Response and Corrective Action Plan:

Who: Head Accounting Officer

What: Management will establish MISC revenue policies and procedures to be in effect for FY 2012. Given the timing that FY 2011 is coming to end, there may not be sufficient time to develop and implement the policy process. However, at a minimum, the Accounting Department do the following prior to the end of FY 2011.

- Pre-number charter invoices
- Review all revenues collected during the FY 2011 is adequately supported as much as possible. Any insufficient documented revenues will be noted accordingly.
- To be effective October 1, 2011, MISC will develop revenue policies and procedures for proper and accurate recording and documentation for the posting to the General Ledger.
- Procedures will include the process steps for each revenue source (i.e. Charter Sales), what constitutes as adequate supporting documentation and the proper filing process upon completion of the sales activity.

When: Next Fiscal Year 2011 – FY 2012

MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Finding No. 2010-5

Purchases/Disbursements

Criteria: Expenses should be supported by adequate documentation such as authorizing purchase orders.

Condition: An authorizing purchase order (PO) was not provided for examination for the following expenses:

<u>Check#</u>	<u>Amount</u>
16238	\$15,073
16341	\$13,550
16455	\$21,680
16482	\$11,595
16870	\$19,416
17089	\$18,926
17090	\$ 1,772
17471	\$ 4,826
18362	\$ 2,784

Cause: The cause of the above condition is the lack of established policies and procedures requiring that non-payroll expenses be supported by authorizing purchase orders.

Effect: The effect of the above condition is the possibility of unauthorized and invalid expenses.

Recommendation: We recommended that management establish policies and procedures to require that expenses are supported by authorizing purchase orders.

Prior Year Status: Lack of established policies and procedures over non-payroll expenses was reported as a finding in the audits of MISC for fiscal years 2007 through 2009.

Auditee Response and Corrective Action Plan:

Who: Head Accounting Officer

What: Effective FY 2011, the Head Accounting Officer will ensure that all non-payroll disbursements are supported by adequate documentation and compliance is adhered to in accordance to the accounts payable policy established during FY 2010. As needed, the disbursement policy may be updated to define what constitutes as the minimum requirements for adequate documentation.

When: Next Fiscal Year 2011

MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses, Continued
Year Ended September 30, 2010

Finding No. 2010-6

Local Noncompliance

Criteria: Public Law 2005-41 established MISC and authorized all movable and immovable property of shipping services under the Ministry of Transportation and Communication be vested absolutely in MISC. Furthermore, all assets, liabilities, rights, duties and obligations, and all contracts and agreements relating to shipping services existing on the date of MISC's establishment shall stand transferred and be vested in MISC.

Condition: No documentation was provided to indicate that all assets, liabilities, rights, duties and obligations, and all contracts and agreements relating to shipping services existing on the date of MISC's establishment have been transferred to MISC. Specifically, four vessels (Aemman, Jelet Ae, Langdrik, and Ribuuk Ae) operated by MISC and vehicles previously with the Ministry of Transportation and Communications are not recorded by MISC.

Cause: The cause of the above condition is the lack of official documentation transferring all assets and liabilities, rights, duties and obligations, and all contracts and agreements relating to shipping services existing on the date of MISC's establishment.

Effect: The effect of the above condition is noncompliance with requirements of Public Law 2005-41.

Recommendation: We recommend that management comply with the requirements of Public Law 2005-41.

Prior Year Status: Noncompliance with Public Law 2005-41 was reported as a finding in the audits of MISC for fiscal years 2007 through 2009.

Auditee Response and Corrective Action Plan:

Who: Head Accounting Officer

What: The noncompliance issue with the Public law 2005-41 has been escalated to the MISC Board. Management's understanding of the progress to have the assets transferred to MISC, as appropriate is slow and at a standstill. Management will revitalize the issue with the MISC Board and document the steps taken to address the issue, the RMI contact points, and most importantly the RMI contact point response to noncompliance issue. If all else fails, MISC Board may engage the services of the Auditor General to push the issue and require that both RMI T&C and MISC comply with the requirements of the Public Law 2005-41.

When: Next Fiscal Year 2011

MARSHALL ISLANDS SHIPPING CORPORATION

Schedule of Findings and Responses, Continued Year Ended September 30, 2010

Finding No. 2010-7

Local 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 supply, service, or construction item without completion when it is determined in writing that there is only one source for the required supply, service, or construction item.

Condition: MISC does not have a formal procurement policy requiring documentation indicating the history of procurement to be maintained on file.

Cause: The cause of the above condition is the lack of established policies and procedures requiring documentation of procurement procedures to ensure compliance with RepMar's Procurement Code.

Effect: The effect of the above condition is the lack of established policies and procedures requiring documentation of procurement procedures to ensure compliance with RepMar's Procurement Code.

Recommendation: We recommend that management establish policies and procedures requiring compliance with RepMar's Procurement Code.

Prior Year Status: Noncompliance with RepMar's Procurement Code was reported as a finding in the audits of MISC for fiscal years 2007 through 2009.

Auditee Response and Corrective Action Plan:

Who: Head Accounting Officer

What: Prior to the end of FY 2011, MISC will adopt the RepMar Procurement policy requiring a minimum of three quotes. In addition, MISC will tailor its Procurement policy to meet the specialized needs of MISC. In some cases, MISC access to vendors in the shipping industry is limited for ordering shipping vessel parts. In the case where a minimum of three quotes cannot be met, the Accounting Department will ensure to clearly document the deviation.

When: Next Fiscal Year 2011

MARSHALL ISLANDS SHIPPING CORPORATION

Unresolved Prior Year Findings
Year Ended September 30, 2010

The status of unresolved prior year findings is disclosed within the schedule of Findings and Responses sections (pages 3 through 9) of this report.