

July 3, 2018

Mayor James Matayoshi
Rongelap Atoll Local Government
Republic of the Marshall Islands

Dear Mayor Matayoshi:

In planning and performing our audit of the financial statements of the governmental activities and each major fund of the Rongelap Atoll Local Government (RALGOV) for the year ended September 30, 2013, which collectively comprise RALGOV's basic financial statements and on which we have issued our report dated July 3, 2018, 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 RALGOV'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 RALGOV's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of RALGOV'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 RALGOV's internal control over financial reporting and other matters as of September 30, 2013 that we wish to bring to your attention.

We have also issued a separate report to RALGOV, also dated July 3, 2018 on our consideration of RALGOV'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.

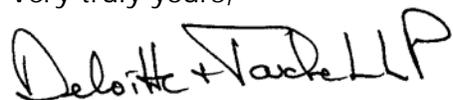
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with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

This report is intended solely for the information and use of management, the Council, others within the organization, and the Office of the Auditor-General 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 RALGOV 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 RALGOV's internal control over financial reporting as of September 30, 2013 that we wish to bring to your attention:

(1) Rongelap Bungalows

Rongelap Bungalow Inc. does not maintain a receivable schedule of store credit sales. Cash collections and deposits are recorded as miscellaneous revenue. Furthermore, inventories are not accounted for at year-end. Thus, no recognition of cost of sales occurs during the year.

We recommend that the US GAAP modified accounting method be adopted.

(2) Capital Asset

Construction in progress was not timely monitored and updated in the accounting records. An adjustment of \$321,298 was recorded through a proposed audit adjustment.

Physical capital asset inventories are not performed. RALGOV-owned vehicles lack city government seals.

We recommend that the construction in progress account be timely monitored and recorded. An inventory of capital assets should be periodically performed. RALGOV may consider attaching city government seals to its vehicles to facilitate monitoring.

(3) Interfund Balances

Interfund balances were not periodically reconciled. The interfund reconciliation for the year ending December 31, 2012 resulted in a net difference of \$52,406. At September 30, 2013, a net difference of \$51,329 was identified and was brought to the attention of the management. A reclassification entry was recorded during the audit process. We recommend that interfund reconciliations be periodically performed.

(4) Bank Reconciliation

Bank reconciliations included outstanding checks of \$140,619, 59% or \$83,357 classified as stale checks.

<u>Fund</u>	<u>Outstanding Checks</u>	<u>Stale Checks</u>
General Fund	\$ 34,388	\$ 18,254
Payroll	14,272	7,449
Resettlement Project	43,479	43,479
Distribution	<u>48,480</u>	<u>45,716</u>
Total	\$ <u>140,169</u>	\$ <u>83,358</u>

General fund bank reconciliation include a long outstanding suspense account of \$2,688. In addition, the outstanding checks of the Distribution bank account resulted in a negative cash balance per the general ledger. A bank account, with an outstanding balance of \$3,788, was not recorded in RALGOV's books.

We recommend that long outstanding checks be revisited and an appropriate course of action be detained. In addition, RALGOV-owned bank accounts should be recorded.

SECTION I – CONTROL DEFICIENCIES, CONTINUED(5) Expenditures

The following instances were noted during tests of expenditures:

- General Fund
 - a. Check numbers 45615 and 45633 in an amount of \$12,330 were paid for international airfare tickets and per diem. Travel forms were processed without adequate description and purpose of travel.
 - b. Check number 45428 amounting to \$456 as payment for car rental of a Councilman for ten days did not evidence approval from an appropriate approver.
 - c. Check numbers 44993 and 44636 in a total amount of \$8,000 paid for death donations lack a death certificate on file.
 - d. Journal entries with document numbers TA598, PR8884 and 7008243 in a total amount of \$7,000 lack supporting invoices and other documentation to validate the transactions.
- Rongelap Bungalows
 - a. Check number 1179 amounting to \$9,999 as payment of store supplies lacks an approved purchase requisition.
- Resettlement Phase One
 - a. Check number 7745 amounting to \$9,451 was paid on behalf of an affiliate company. However, RALGOV failed to recognize a related receivable.
 - b. Check number 7738 amounting to \$34,200 lacks an approved purchase requisition to support independent review of the transaction.
 - c. Check number 7371 and 7651 in a total amount of \$59,150 lacks formal invoices on file.
 - d. Check number 7456 amounting to \$15,000 as payment for a vehicle lacks documentation that competitive procurement occurred.
 - e. Check number 7868 amounting to \$1,500 as payment for consultant's hotel reimbursement lacks a hotel invoice to substantiate the reimbursed amount.
 - f. Of 33 resettlement expenses tested, nine with total amount of \$75,229 relate to consultancy fees and reimbursements. A written consultancy agreement was not on file.
- Distribution Fund
 - a. Check number 96575 amounting to \$75.25 lacks a recipient's signature in the check register to support acknowledgment of actual receipt.

We recommend that payments be supported by vendor invoices. In addition, we recommend that purchases be supported by documentation that competitive procurement process occurred.

(6) Prepayment

Prepayment of \$24,372 has been long outstanding. We recommend that prepayments be revisited and determine validity of transactions.

SECTION I – CONTROL DEFICIENCIES, CONTINUED

(7) Journal Entries

The test of journal entries noted the following instances:

- a. JV2013-168 lacks a signature of the preparer and the reviewer supporting that an independent review took place.
- b. JV2013-086, JV2013-116, JV2013-133, JV2013-136, JV2013-166, and JV2013-167 lack a reviewer's signature supporting that independent review of the transaction took place.
- c. JV2013-169 documentation supplies expense of \$4,416 lacks invoices to support the liquidation.
- d. Journal entry with document no. PR8234 recognizing per diem, consultancy fees and airline tickets of \$11,000 lacks documentation on file to support reimbursement.

We recommend that independent review of journal entries be performed and be properly documented. Journal entries recorded should be adequately supported by appropriate documentation.

(8) Investment

Monthly investment in savings plan statements were not on file. An insured individual has resigned from his position but no change has been made to the insurance policy.

We recommend RALGOV verify that adequate documentation exists and is properly filed. RALGOV should also determine an appropriate course of action related to its investment in savings plan.

(9) Liabilities

Accounts payable of \$12,059 in the General Fund has been outstanding since 2009. We recommend management review long outstanding liabilities and determine an appropriate course of action.

SECTION II - OTHER MATTERS

Our observations concerning other matters related to operations, compliance with laws and regulations, and best practices involving internal control over financial reporting that we wish to bring to your attention at this time are as follows:

(1) Segregation of Duties

RALGOV's current staffing level limits the number of personnel available for accounting duties. Accordingly, appropriate segregation of duties is not always possible which may result in a weakness in internal control, specifically in the role of the City Manager who has access to assets, has approving authority for disbursements, and also has full access to accounting records. To mitigate this weakness, a critical element in RALGOV's internal control system is the close involvement of management in the day-to-day operations and the review of accounting activities and financial reports.

SECTION II - OTHER MATTERS, CONTINUED

Furthermore, certain duties of the Accounts Payable clerk are incompatible such as processing checks for claims payments and distribution of such to payees. We recommend that management establish controls to require rotation of the check distribution function among RALGOV staff.

We encourage the involvement of management on a continuing basis and thorough review of accounting activities and financial reports as a means to maintain effective internal control until a more structured control environment becomes cost effective.

(2) Sick Leave and Annual Leave Policy

There are currently no policies and procedures governing employee absences including sick leave and vacation leave. Employee paid time off is usually allowed by management. However, no policies are in place that establish limits and authorizations. Furthermore, mandatory vacation policy may be especially beneficial to RALGOV, being a small entity where certain employees may be handling incompatible duties. This would allow management to observe if there is any noticeable change while another person is performing the duties. We recommend that management establish vacation and sick leave policies.

(3) Amendments to Claims Trust Agreement

The original Trust Agreement was approved by the Government of the Marshall Islands (RepMar) through the Ministry of Finance and the Attorney General, as consistent with the Rongelap Agreed Minute, pursuant to Section 8 of the Article II of the Compact Section 177 Agreement. However, it appears that such approval was not obtained for the Amended Claims Trust Agreement. We recommend that management consult with legal counsel as to the need to obtain RepMar approval of the Amended Trust.

(4) Reporting

Management reports were not available. We recommend management consider preparing management reports that assist management and executive officers in monitoring financial transactions and that support a relevant and well-informed decision making process.

(5) Payroll

Timesheets are not kept for employees. However, supervisors are required to submit exception reports for employee absences and other employee matters. Exception reports were not available for examination.

We recommend that management adopt a policy of requiring timesheets to monitor employee attendance.

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

RALGOV'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.