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June 28, 2011

Mr. Alfred Alfred, Jr.
Secretary of Finance
Republic of the Marshall Islands

Dear Secretary Alfred:

In planning and performing our audit of the financial statements of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Republic of the Marshall Islands (RepMar) as of and for the year ended September 30, 2010 (on which we have issued our report dated June 28, 2011), 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 RepMar'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 RepMar's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of RepMar'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 RepMar's internal control over financial reporting and other matters as of September 30, 2010 that we wish to bring to your attention.

We have also issued a separate report to the President, His Excellency Jurelang Zedkaia, also dated June 28, 2011 on our consideration of RepMar'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 Honorable Members of the Nitijela, 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. However, this report is also a matter of public record.

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 RepMar for their cooperation and assistance during the course of this engagement.

Very truly yours,

Deloitte & Touche LLP

SECTION I – CONTROL DEFICIENCIES

We identified the following control deficiencies involving RepMar's internal control over financial reporting as of September 30, 2010:

Petty Cash Imprest Accounts

At September 30, 2010, the Ministry of Finance recorded twenty-seven (27) petty cash imprest accounts in the aggregate amount of $24,345. We selected one item for testing (G/L Acct # 950000-11044, Ebeye Thyroid Petty Cash) in the amount of $7,585; however, it was determined that this petty cash account no longer existed. As the amount of $7,585 was not considered material to the financial statements, no audit adjustment was proposed. We recommend that the Ministry of Finance examine all recorded petty cash imprest accounts and determine whether such represent valid petty cash accounts.

Fiji Embassy Imprest Account

At September 30, 2010, the Ministry of Finance recorded a $19,700 imprest account for the Fiji Embassy for which the imprest account reconciliation included net unrecorded transactions of $1,914 representing various bank charges and an unreconciled difference between the check register and the bank account. We recommend that the Ministry of Finance ensure that all transactions pertaining to Embassy imprest accounts be recorded.

Japan Embassy Imprest Account

At September 30, 2010, the Ministry of Finance recorded a $100,000 imprest account for the Japan Embassy for which the imprest account reconciliation and bank reconciliation were not available. We recommend that the Ministry of Finance require timely reconciliation pertaining to Embassy imprest accounts.

Washington Embassy Imprest Account

At September 30, 2010, the Ministry of Finance recorded a $50,000 imprest account for the Washington Embassy. The imprest account reconciliation included $19,806 of unrecorded cash receipts; $14,122 of receivables from Embassy staff, the amount which had been outstanding in prior year; and disallowed expenditures for fiscal year 2010 of $8,253. We recommend that the Ministry of Finance ensure that all transactions pertaining to Embassy imprest accounts be recorded. In addition, we recommend that management determine collectability of receivables from staff and resolve long outstanding balances. Furthermore, we recommend management determine the cause of disallowed expenditures and timely resolve any related issues.

Arkansas Consulate Imprest Account

At September 30, 2010, the Ministry of Finance recorded a $20,000 imprest account for the Arkansas Consulate. The imprest account reconciliation included net unrecorded transactions of $3,133 pertaining to unrecorded check payments and various bank charges. We recommend that the Ministry of Finance ensure that all transactions pertaining to the Consulate imprest account be recorded.

United Nation Mission Imprest Account

At September 30, 2010, the Ministry of Finance recorded a $50,000 imprest account for the Mission to the United Nations. The imprest account reconciliation reported a net variance of $30,838. The September 30, 2010 reconciliation indicated a total imprest fund balance of $80,838 while the recorded imprest account is $50,000. The variance of $30,838 was not accounted for.

Additionally, the Ministry of Finance has not recorded $60,000 of grant receipts that the UN Mission received in March 2006. Such funds were deposited into a savings account in the name of the UN Mission separate from the Imprest Account. During fiscal year 2010, the savings account balance decreased by $8,031 from the prior year balance leaving $51,969 in the bank account; however, such withdrawals were not adequately accounted for.

We recommend that the Ministry of Finance require monthly reconciliations of the imprest account and proper documentation of reconciling items.

Bank of Marshall Islands (BOMI) Imprest Accounts

At September 30, 2010, the Ministry of Finance recorded cash of $22,268 for the Asian Development Bank Loan # 1791 Imprest Account and cash of $5,042 for the MOE/PEC Imprest Account. We obtained bank confirmations from BOMI and were informed that both accounts were closed; however, we were unable to ascertain the final disposition of the remaining account balances. We recommend that the Ministry of Finance determine the final disposition of the remaining account balances and ensure that such was deposited to RepMar's General Fund bank account.

General Fund Bank Account

At September 30, 2010, the bank reconciliation for the Ebeye General Fund account (G/L Acct # 950000-13010) included $526,177 of unrecorded cash receipts and $355,965 of unrecorded disbursements of which a total of $24,554 represents unrecorded returned customer checks. Through the performance of audit procedures, which resulted in proposed audit adjustments, total unrecorded cash receipts was reduced to $220,107, while unrecorded disbursements were reduced to $8,841.

Of the remaining unrecorded cash receipts, a total of $132,736 appears to pertain to taxes deposited directly to RepMar's bank account for withholding income taxes, import taxes and other taxes. However, since relevant documents such as tax returns or deposit advices were not available, the Ministry of Finance accounting office could not record such to specific revenue accounts. The remaining $87,371 appeared to represent unrecorded cash receipts from various customers and/or grantors.

We recommend that the Ministry of Finance determine the disposition of these unrecorded transactions in a timely manner.

Ebeye General Fund Account

At September 30, 2010, the bank reconciliation for the Ebeye General Fund account (G/L Acct # 950000-13015) included $421,763 of unrecorded cash receipts and unrecorded disbursements of $658,449. Through the performance of audit procedures, which resulted in proposed audit adjustments, the total unrecorded cash receipts was reduced to $35,943, while unrecorded disbursements were reduced to $14,513. We recommend that the Ministry of Finance determine the disposition of these unrecorded transactions in a timely manner.

Bank Errors

At September 30, 2010, the bank reconciliation for the General Account (G/L Acct # 950000-13010) and the Payroll Account (G/L Acct # 950000-13020) included bank errors in the amounts of $42,524 and $13,126, respectively, which date back as far as fiscal year 2003 without apparent follow-up with the financial institution. Given the aging of these balances, collectability from the financial institution may be doubtful. We recommend that the Ministry of Finance follow-up on all bank errors with the financial institution in a more timely manner.

Ministry of Education Maintenance Account

During fiscal year 2010, we noted the use of a checking account by the Ministry of Education that was not recorded by RepMar. Bank statements and account reconciliations for such were not available for examination. We recommend that the Ministry of Finance require recording and reconciliation of all bank accounts of RepMar's ministries and agencies that are not authorized by enabling legislation to have separate financial reporting.

Miscellaneous Receivables

At September 30, 2010, the Ministry of Finance recorded the following receivable balances that were not supported by underlying subledgers:

G/L Acct #	G/L Balance	G/L Acct #	G/L Balance	G/L Acct #	G/L Balance
100100-20200	$ 71,473	100100-24012	$ 2,367	100100-24060	$ 13,875
100100-22005	$ 33,419	100100-24020	$ 12,053	100100-24090	$ 15,467
100100-22020	$ 18,956	100100-24027	$ 1,298	100100-24100	$ 248,876
				950000-24100	$ (1,566)

No audit adjustments were proposed for the above items as these receivable balances were offset by a $461,423 allowance for uncollectible accounts. We recommend that the Ministry of Finance reconcile these receivables and determine their ultimate collectability.

Travel Advances

At September 30, 2010, the Ministry of Finance recorded travel advances within the general ledger that were not reconciled to the supporting DILOG subledger. Details are as follows:

G/L Acct #	G/L Balance	Subledger Balance	G/L Acct #	G/L Balance	Subledger Balance
100100-28010	$ 24,361	$ 40,703	$ (710)	200515-28010	$ -
200090-28010	2,734	2,186			
200330-28010	(302)	-	(13,521)	410150-28010	12,079
200332-28010	2,659	3,273	25,447	600350-28010	(15,216)
200340-28010	(320)	(920)	(2,422)	700360-28010	(2,210)

Total general ledger balances for travel advances did not agree to the supporting DILOG subledger, resulting in a net unreconciled variance of $1,969. No audit adjustment was proposed as this amount was not considered material to the financial statements. In addition, $121,817 of credit balances were included in the above net variance, which appears to relate to erroneous recordings of travel advance liquidations.

We recommend that the Ministry of Finance reconcile travel advances to the supporting DILOG subledger on a monthly basis.

Accounts Payable

At September 30, 2010, the Ministry of Finance recorded accounts payable within the general ledger that was not reconciled to the supporting DILOG subledger. Details of these are as follows:

G/L Acct #	Unadjusted G/L Balance	Subledger Balance	Variance
100100-50010	$ 14,629	$ 78,692	$ (64,063)
410100-50010	204,235	95,090	109,145
410102-50010	194,140	302,486	(108,346)
410110-50010	30,906	60,133	(29,227)
410150-50010	120,161	138,387	(18,226)
600350-50010	394,363	415,583	(21,220)
700100-50010	304	276	28
700370-50010	80,108	79,912	196
200090-50010	2,977	3,055	(78)
200330-50010	(145)	-	(145)
200332-50010	6,492	6,747	(255)
200515-50010	43	-	43
	$ 1,048,213	$ 1,180,361	$ (132,148)

The unreconciled variance of $132,148 was not considered material to the financial statements, thus no audit adjustment was proposed. In addition, a total of $137,831 in debit balances was included in the above net variance, which appears to relate to erroneous recordings of vendor payments. Furthermore, the Ministry of Finance was not able to generate the DILOG A/P by Fund or Subledger reports as of September 30, 2010; however, we performed alternative audit procedures to verify and support year-end accounts payable balances.

We recommend that the Ministry of Finance reconcile accounts payable to the supporting DILOG subledger on a monthly basis.

Accounts Payable – Other

As of September 30, 2010, RepMar recorded $641,681 of other accounts payable. Such balance included vendor accounts with debit balances totaling $29,267. The validity of these debit balances was unknown. We recommend that management execute monthly reconciliation of accounts payable balances.

Accounts Payable – Landowners

At September 30, 2010, the Ministry of Finance recorded a $27,013 payable to landowners (G/L Acct # 100100-55040), which represented amounts received from Mobil Oil Micronesia, Inc. (MOMI) for a land lease at the airport not yet paid to the landowners. Of this amount, $16,499 represented an amount carried over from fiscal year 2007. As the amount of $16,499 was not considered material to the financial statements, no audit adjustment was proposed. We recommend that the Ministry of Finance determine the validity of amounts payable to landowners for the MOMI land lease at the airport.

Accounts Payable – Labor Bonds

At September 30, 2010, the Ministry of Finance recorded $83,760 of accounts payable for labor bonds (G/L Acct#200319-50035), which included debit balances totaling $8,500. It appears that the debit balances resulted from the issuance of labor bond refunds for which a corresponding payable could not be identified. We recommend that the Ministry of Finance perform reconciliations of the accounts payable labor bonds account and ensure that refunds are issued based on valid labor bond payable balances.

Payroll Allotment Liabilities

At September 30, 2010, the Ministry of Finance recorded various payroll allotment liability accounts, totaling $1,004,710 pertaining to the last payroll period of the fiscal year whereas the actual amount withheld and payable amounted to $997,394, resulting in a variance of $7,316. As this amount was not considered material to the financial statements, no audit adjustment was proposed; however, we recommend that the Ministry of Finance reconcile payroll allotment liability accounts on a bi-weekly basis.

Unclaimed Property

On November 28, 2002, the Secretary of Finance received $93,737 from the Bank of Hawaii representing unclaimed customer accounts when the bank closed its branch, and recorded such as a liability within G/L Acct # 300430-50080. In accordance with Public Law No. 1999-89, any unclaimed property, which escheats to RepMar under the provisions of the law, shall be deposited into an Abandoned Business Interests account within the Unclaimed Business Property Fund. The Secretary of Finance is required to publish the existence of such property within one year after receipt. As of September 30, 2010, the Secretary of Finance has not published the existence of such property in the local newspaper. We recommend that the Ministry of Finance publish the existence of escheated property in accordance with the enabling legislation.

Tax Revenues

Of seventy-five (75) General Fund tax revenue receipts tested, we noted the following exceptions:

- Ebeye cash receipt # 09017940 in the amount of $57,971 recorded as expatriate income tax revenue was not supported by Form 1178a attachment.

- Majuro cash receipt# 0364171 in the amount of $2,607 pertaining to business gross revenue tax was inadvertently miscalculated and reflected an error amounting to $220.

- Majuro cash receipt# 0377102 in the amount of $6,771 for withholding income tax and related penalty and interest indicated incorrect calculation of penalties and interest. Calculated error amounted to $192.

- Majuro cash receipt# 0382659 in the amount of $2,988 for business gross revenue tax and related penalty and interest indicated incorrect calculation of penalties and interest. Calculation error amounted to $4.

- Supporting tax forms/ calculations for the following tax payments were not been provided:
  Import tax - $123,797 (Ref # G11-127G)
  Fuel Import Tax - $46,990 (Ref # G10-021B)

Tax Revenues, Continued

We recommend that the Ministry of Finance require that tax revenue receipts are supported by underlying documentation such as Form 725, Withholding Tax returns and Gross Receipts Tax returns. In addition, we recommend that management adopts policies and procedures for review of tax and penalties and interest calculations.

Grants Drawdown

During fiscal year 2010, the following cash receipts recorded by the Ministry of Finance were not supported by a copy of the draw down request verifying recorded grants revenue:

Fund	Date	Amount
410102	May 3, 2010	$ 91,544
510100	Jun 1, 2010	$ 7,721
600350	Dec 30, 2009	$ 213,192

We recommend that management implement policies and procedures so that all recorded grants revenues are adequately supported by draw down requests and other documents or reports as may be required by grant agreements.

Fees and Other Revenues

Of four (4) Other Governmental Fund revenue receipts tested, we noted a Majuro cash receipt #00362686 in the amount of $11,500 was not supported by underlying fees calculation. We recommend that the Ministry of Finance ensure that revenue receipts are supported by underlying documentation and that calculations be reviewed for accuracy.

General Fund Payroll Expenditures

Of forty-seven (47) General Fund payroll expenditures tested, we noted that pay rates for the following employees were not adequately supported by a personnel action form or contract:

Employee #	PPE	Gross Pay
37548	12/05/09	$ 395
42003	09/24/10	$ 395
6747	09/24/10	$ 395

General Fund Non-payroll Expenditures

Of eighty (80) General Fund non-payroll expenditures tested, the following exceptions were noted:

- Fuel expenditures of $20,000 paid through check# 69780 pertains to a vendor prepayment. However, invoices for re-fueling were not available.
- Per diem allowance for an employee travel paid through check# 77308 in the amount of $2,568 was overpaid by $375 representing per diem for 3 days in excess of the actual trip’s length.
- Purchase of supplies and materials paid through check# 77855 in the amount of $1,095 was not supported by original copies of vendor price quotations.

General Fund Non-payroll Expenditures, Continued

- International subsidies and fees of $44,404 paid through wire transfer #428 were not supported by an invoice from the vendor.

- Purchase of a $28,000 vehicle paid through check# 70942 was not supported by vendor selection and other documents evidencing compliance with the provisions of RepMar's Procurement Code for purchases over $25,000.

In addition, examination of General Fund account bank reconciliation indicated an expenditure pertaining to purchase of a vehicle for the Ministry of Finance paid through an electronic fund transfer of $25,328. We noted that the purchase was authorized through C.M. 013 (2010). However, the procurement process was not documented for this purchase.

We recommend that the Ministry of Finance establish policies and procedures so that payments to vendors are adequately supported by vendor invoices, contract and other. In addition, we recommend that policies and procedures be established to govern procurement of goods and services to comply with RepMar's Procurement Code.

Other Governmental Fund Non-payroll Expenditures

Of four (4) Governmental Fund expenditures tested, we noted one item paid through check# 72173 for $53,555 that was not supported by competitive bids or other relevant documents evidencing compliance with RepMar's Procurement Code. We recommend that policies and procedures be established to govern procurement of goods and services to comply with RepMar's Procurement Code.

Subsidies and Contributions

The check file, including payment requests, could not be located for subsidies and contributions to component units paid through check# 13172 and 73523, in the amount of $150,000 and $156,547, respectively. Alternative audit procedures were performed on these aforementioned payments. We recommend that the Ministry of Finance establish internal control policies and procedures to maintain check files and underlying invoices or payment requests to support expenditures.

Payroll Leave Accrual

RepMar's policy for annual leave in excess of the limit of 208 hours at the end of the calendar year is that it will be forfeited. We tested payroll leave accruals, and noted that the leave balances exceeding 208 hours carried forward from December 2009 to January 2010 were not reduced to 208 hours. This resulted in an extrapolated overstatement of $463,362 of the detailed payroll leave accrual sub ledger. The general ledger balance, however, did not reflect the error as it was not adjusted to agree with the sub ledger.

Payroll Leave Accrual, Continued

We recommend that the Ministry of Finance require adjustment of leave hour balance at the end of the calendar year to comply with the Annual Leave Policies of the Public Service Commission.

In the annual pay rate for employee #55558 per the personnel action form was $31,160 while the payroll system indicated $31,075. The error may be due to input or an undocumented adjustment. We recommend that the Ministry of Finance establish control and procedures that require review and approval of changes to the payroll master file prior to its effectivity.

Encumbrances

Of fifteen encumbrances tested for the Grants Assistance Fund, underlying purchase orders or contracts verifying the recorded encumbrance for the following were not provided:

PO#/ Contract#	Outstanding Encumbrance
C0310201	$ 109,183
C0315201	10,500
P1711701	42,234
P3716001	2,637
Q1158401	6,300
Total	$ 170,854

In addition, we tested two (2) outstanding encumbrances for the Other Governmental Funds (PO#3546701 and P3546001) in the amount of $20,995 and $6,894, respectively. Both encumbrances were no longer considered valid as of September 30, 2010.

We recommend that the Ministry of Finance periodically examine the encumbrance sub ledger and de-obligate items no longer considered valid. Furthermore, we recommend that the Ministry of Finance ensure all recorded encumbrances are evidenced by underlying supporting documentation.

Net Assets

At September 30, 2010, opening fund balances of the following accounts did not agree with the audited closing balances at September 30, 2009:

Fund Code	GL account #	Opening Balance per GL	Closing Balance per 2009 Audited F/S	Variance
100100	92040	$ (2,403,195)	$ (2,403,466)	$ 271
510130	92040	(252,805)	-	(252,805)
600350	92040	(2,273)	31,721	(33,994)
		$ (2,658,273)	$ (2,371,745)	$ (286,528)

We recommend that appropriate financial closing and reconciliation procedures, including related reversal of closing balances in the subsequent period, be implemented. Management recorded proposed audit adjustments to correct the opening net asset balances above.

SECTION II – OTHER MATTERS

We also identified, and have included below, other matters involving RepMar's internal control over financial reporting as of September 30, 2010 that we wish to bring to your attention:

Access Control of End-User

The Payroll Director is configured to be a super user in the Unix environment because he is also a backup staff of the IT department. The user is able to make unauthorized modifications to the data and system configurations, which will affect the consistency and integrity of the information system operation. We recommend a review of the activities logs of super users, including the Payroll Director, to monitor their activities in the EDP environment.

Enhancement of Network Security

There is a lack of control on network activities resulting in a higher chance of data integrity and confidentiality issues. For example, hackers may be able to access to the network and modify/view sensitive information. Therefore, network vulnerability testing and/or network penetration testing should be performed at least annually to identify control weaknesses.

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

RepMar'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.