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July 29, 2013

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, 2012 (on which we have issued our report dated July 29, 2013), 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, 2012 that we wish to bring to your attention.

We have also issued a separate report to the President, His Excellency Christopher J. Loeak, also dated July 29, 2013 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, 2012:

Petty Cash Imprest Accounts

At September 30, 2012, the Ministry of Finance recorded twenty-nine petty cash imprest accounts aggregating $24,745, including two non-existent accounts (G/L A/c # 950000-11044, Ebeye Thyroid, $7,585 and G/L A/c # 950000-12040, Sea Patrol, $4,100) identified in prior audits. As these two accounts total $11,685, which is an amount 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 assess their validity. This matter was discussed in our previous letters to management for the audits of fiscal years 2007 through 2011.

Embassy Imprest Accounts

At September 30, 2012, the Ministry of Finance recorded the following embassy imprest accounts, for which the September 2012 imprest account reconciliations reported unknown shortages.

Embassy	GL A/c #	Imprest Fund	Unknown Shortage
Fiji	950000-12010	$ 19,700	$ 4,291
Japan	950000-12020	$ 100,000	$ 57,712
UN Mission	950000-12030	$ 50,000	$ 17,771
Washington, D.C.	950000-12035	$ 50,000	$ 6,822
Arkansas Consulate	950000-12045	$ 20,000	$ 2,597

Additionally, the following exceptions were noted:

- Accounting Department personnel represented that incomplete bank statements for the months of July and September 2012 were received from the Fiji Embassy.

- No reconciliation for the month of March 2012 was prepared for the Japan Embassy.

- The UN Mission September 2012 reconciliation included two unrecorded deposits of $60,000 and $9,492 representing grant receipts identified in prior years; however, a third unrecorded deposit of $27,846 from an unknown source, also identified in a prior year, was not included as a reconciling item on the reconciliation. No explanation was provided for the omission. Furthermore, the reconciliation included the following reconciling items: (1) two missing checks (#s 10400 and 10432) for $5,525 each and (2) a $26,817 overpayment to the Mission in fiscal year 2011 (the same reimbursement request was paid on 06/30/2011 and again on 07/15/2011), which has not been offset against subsequent reimbursement requests.

- The Washington, DC Embassy September 2012 reconciliation included the following reconciling items: (1) unknown deposits from April, June and August 2012 totaling $2,609, which were not recorded and (2) a $15,191 overpayment to the Embassy in fiscal year 2011 (the same reimbursement request was paid on 09/12/2011 and again on 09/20/2011), which has not been offset against subsequent reimbursement requests.

Embassy Imprest Accounts, Continued

- Certain embassy replenishment requests outstanding at September 30, 2012 were not accrued.

We recommend that the Ministry of Finance require monthly reconciliations of the imprest accounts and documentation and resolution of reconciling items. We further recommend that unknown variances be timely investigated. This matter was discussed in our previous letters to management for the audits of fiscal years 2010 and 2011.

Errors in bank wire transfers and lack of subsequent offset of overpayments to RepMar embassies was reported as a finding in the Single Audits of RepMar for fiscal years 2010 and 2011.

Bank of Marshall Islands (BOMI) Imprest Accounts

At September 30, 2012, the Ministry of Finance recorded cash of $22,268 and $5,042 for the Asian Development Bank Loan # 1791 Imprest Account (GL A/c # 800405-12062) and for the MOE/PEC Imprest Account (GL A/c # 950000-11081), respectively. Bank confirmation responses obtained in prior audits indicated that both accounts had been 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 these account balances and verify whether such were deposited to RepMar's General Fund bank account. This matter was discussed in our previous letters to management for the audits of fiscal years 2008 through 2011.

General Fund Bank Account

The September 2012 bank reconciliation for the General Fund account (G/L Acct # 950000-13010) included three wire transfer payments dated 10/01/2011, 02/17/2012 and 06/11/2012, totaling $112,986 which remained unprocessed as of September 30, 2012. Since timely bank reconciliations did not occur during the year, the aforementioned payments were not timely identified and resolved. We recommend that the Ministry of Finance require periodic and timely bank account reconciliations and resolution of reconciling items.

Bank Accounts

At September 30, 2012, the Ministry of Finance did not record a new $12,000 time certificate of deposit (TCD) account opened during the year with First Hawaiian Bank. Audit procedures performed identified the new TCD account, which was subsequently recorded by management. Furthermore, the Ministry of Finance recorded cash of $14,999 and $218 (GL A/c #s 950000-15086 and 950000-15087, respectively) for which the associated bank accounts were confirmed by the bank to be either closed or nonexistent. We recommend that the Ministry of Finance establish policies and procedures to facilitate recording of new and closed bank accounts.

Bank Errors

The September 2012 bank reconciliation for the Payroll Account (G/L Acct # 950000-13020) included $16,622 in net bank errors, including some dating back to October 2011. We recommend that the Ministry of Finance require periodic and timely bank account reconciliations and that bank errors are investigated and resolved with financial institutions in a timely manner. This matter was discussed in our previous letters to management for the audits of fiscal years 2007 through 2011.

Ministry of Education Maintenance Account

The Ministry of Education continues to maintain and use a checking account that is not recorded by RepMar. Fiscal year 2012 bank statements and account reconciliations for such were not available for examination. We recommend that the Ministry of Finance record and require reconciliation of all bank accounts of RepMar's ministries and agencies that are not authorized by enabling legislation to have separate financial reporting. This matter was discussed in our previous letters to management for the audits of fiscal years 2010 and 2011.

Miscellaneous Receivables

At September 30, 2012, the Ministry of Finance recorded the following receivable balances that were not supported by underlying subsidiary ledgers:

G/L A/c #	G/L Balance
100100-24100	$ 234,780
950000-24100	$ (1,566)

No audit adjustments were proposed for the above accounts as these receivable balances were offset by a corresponding allowance for uncollectible accounts. We recommend that the Ministry of Finance reconcile these receivables and determine their ultimate collectability. This matter was discussed in our previous letters to management for the audits of fiscal years 2007 through 2011.

Fixed Assets Register

The fixed assets register (FAR) as of September 30, 2012 included the following exceptions:

- A prior year addition (central aircon unit for Ebeye hospital) costing $136,584 was not recorded in the FAR.

- One item (dry dock) which had been disposed of during the year was not removed from the FAR.

- One item (oxygen generating equipment) representing a fiscal year 2013 acquisition, which acquisition cost was overstated by $5,258.

Adjustments to the FAR were proposed for the above exceptions. However, we recommend that management establish policies and procedures pertaining to timely and accurate update of the fixed assets register for additions and disposals. This matter was discussed in our previous letter to management for the audit of fiscal year 2011.

Accounts Payable - Other

At September 30, 2012, the Ministry of Finance recorded $6,037 of accounts payable in GL A/c # 700370-50020 that were not supported by an underlying subsidiary ledger. No audit adjustment was proposed as this amount was not considered material to the financial statements. We recommend that the Ministry of Finance reconcile accounts payable to the supporting subsidiary ledgers on a monthly basis. This matter was discussed in our previous letter to management for the audit of fiscal year 2011.

Labor Bonds Payable

At September 30, 2012, the following labor bonds payable accounts had debit balances:

GL A/c #	Debit Balance
100100-50030	$ 3,645
200319-50030	$ 1,500

It appears that the debit balances resulted from the issuance of labor bond refunds for which a corresponding payable could not be identified. No audit adjustment was proposed as the above amounts were not considered material to the financial statements. We recommend that the Ministry of Finance perform regular reconciliations of the labor bonds payable accounts and ensure that refunds are issued based on valid labor bonds recorded. This matter was discussed in our previous letters to management for the audits of fiscal years 2010 and 2011.

Cancelled Checks

At September 30, 2012, the Ministry of Finance recorded general and payroll fund cancelled check liabilities (G/L A/c #s 100100-50060 and 100100-55020, respectively) of $473,153 and $57,422, respectively, which were not supported by reconciled subsidiary ledgers. Alternative audit procedures were performed to verify and support the account balances. We recommend that the Ministry of Finance monitor and reconcile stale checks in accordance with the Financial Management Act 1990, Section 150. This matter was discussed in our previous letter to management for the audit of fiscal year 2011.

Additionally, at September 30, 2012, unclaimed checks held at the Treasury Department included certain which had been cancelled and adjusted to general fund revenue in prior years. We recommend that the Accounting Department recall cancelled checks from the Treasury Department for review and proper disposition.

Tax Revenues

Of $25,229,449 General Fund tax revenue receipts, seventy-nine (79) items totaling $4,245,308 were tested and we noted the following exceptions:

- Ebeye cash receipt #s 09021195 and 09023218 were not supported by import tax forms and associated cash receipts and deposit tickets.

- Majuro cash receipt #s 00411265 and 00412163 did not include related penalties of $911 and $486, respectively.

We recommend that the Ministry of Finance require that tax revenue receipts are supported by underlying tax returns. In addition, we recommend that management adopt policies and procedures for following up on unpaid penalties and interest. Requirement for tax revenue receipts to be supported by underlying tax returns was reported in our previous letters to management for the audits of fiscal years 2007 through 2011. Following up on unpaid penalties and interest was reported in our previous letter to management for the audit of fiscal year 2011.

Other Governmental Funds Revenues

Of $1,050,775 other governmental funds revenues, four (4) items totaling $7,985 were tested, and we noted one cash receipt (# 09021641) for which the underlying cash receipt and deposit ticket were not provided. We recommend that the Ministry of Finance require that revenues are supported by underlying documentation.

General Fund Payroll Expenditures

Of $14,903,523 in payroll expenditures, seventy-five (75) items totaling $56,971were tested and we noted the following exceptions:

- Personnel action forms (PAF) provided for the following employees indicated their status as probationary despite having been employed for over a year as of the pay period tested.

Employee #	Pay Period Ended
050099	02/11/2012
207209	03/10/2012
207308	07/28/2012
209229	08/11/2012
213170	09/22/2012
214200	11/05/2011
224750	06/16/2012

- Employee # 205040 was underpaid by 16 hours or $60 for pay period ended 11/19/2011.
- For employee # 19497, the employment contract provided to support the employee’s gross wages for pay period ended 11/19/2011 had expired on 10/19/2011; consequently, employee was overpaid a total of $2,307 representing two pay periods.
- For employee # 213890, supervisory approval of timesheet hours for pay period ended 12/03/2011 was not documented.

We recommend that management establish policies and procedures to ensure that current PAFs are maintained on file and to facilitate accurate payroll processing.

Grants Fund Payroll Expenditures

Personnel action forms (PAF) provided for the following employees indicated their status as probationary despite having been employed for over a year as of the pay period tested:

Employee #	Pay Period Ended
040228	08/11/2012
061306	10/22/2011
074138	04/07/2012
208779	02/11/2012
211552	09/22/2012
211813	09/22/2012
213481	12/03/2011
216347	05/05/2012
216635	10/22/2011
219587	01/28/2012
230210	05/19/2012

Additionally, for one employee (# 069229), there was no current personal action form on file. Alternative audit procedures were performed to confirm the employee’s continued and authorized employment.

We recommend that management establish policies and procedures to ensure that current PAFs are maintained on file.

General Fund Non-payroll Expenditures

Of $14,245,088 General Fund non-payroll expenditures, seventy-two (72) items totaling $4,034,283 were tested and the following exceptions were noted:

- Supporting documentation was not available for the following checks:

Check #	APV #	Amount
93792	172210	$ 5,106
96918	183284	$ 100,000
99815	185120	$ 2,728
Unknown	187168	$ 3,302
100306/ 100483	191011	$ 2,970

- A $2,528 representation expenditure was incorrectly referenced with wire transfer payment # 09000988; the correct # is 09000884.

- Variances between recorded expenditures and underlying vendor invoices provided were noted for the following expenditures:

Account #	APV #	Recorded Expenditure	Invoice Amount	Variance
02115	09000899	18,624	17,433	1,191
02605	09000918	2,822	2,850	(27)
02750	167081	143,325	139,656	3,669
02021	171630	920	900	20
02215	176009	3,483	3,573	(90)
02330	176692	112,578	112,758	(180)
01520	177813	2,728	2,813	(84)
02021	186843	3,302	3,287	15
02021	191011	2,970	2,870	100

No explanation was provided for the above variances.

- We were unable to ascertain whether check # 93792 had cleared the bank as we were unable to trace the check to a bank statement and the associated September 2012 bank account reconciliation did not include the aforementioned check as a reconciling item.

We recommend that the Ministry of Finance establish policies and procedures requiring that payments to vendors are adequately supported by vendor invoices, contracts, and other appropriate documentation. This matter was discussed in our previous letters to management for the audits of fiscal years 2010 and 2011. We further recommend that document references are verified.

Grants Fund Non-payroll Expenditures

A $15,887 item (check # 99140, APV # 183541) was supported only by a proforma sales invoice or quote. We recommend that final invoices are obtained and filed to support expenditures.

Encumbrances

Of twenty-four (24) outstanding encumbrances tested for the Grants Assistance Fund, we noted the following exceptions:

- For one item (contract # C0337201), the recorded encumbrance did not agree with the underlying contract.

- The following encumbrances were not adjusted for gross receipts taxes associated with payments to contractors:

Fund	Contract#	Outstanding Encumbrance	Gross Receipts Tax
510100	C0789201	$ 607,377	$ 2,525
510100	C0305701	$ 65,006	$ 1,899
510100	C0807801	$ 129,928	$ 4,616
510100	C0841901	$ 372,076	$ 1,696
510100	M0738501	$ 168,388	$ 6,003

  Additionally, for contract # C0841901, the gross receipts tax noted above was included in the payment (check # 100778) to the contractor instead of being withheld and paid into Treasury.

We recommend that the Ministry of Finance periodically examine the encumbrance subsidiary ledger and de-obligate amounts no longer considered valid. Furthermore, we recommend that encumbrances are de-obligated for taxes withheld from contractor payments. This matter was discussed in our previous letters to management for the audits of fiscal years 2010 and 2011.

Subsequent Disbursements

Of sixty-three subsequent disbursements tested, the following exceptions were noted:

- $108,936 in unrecorded liabilities as of September 30, 2012, as follows:

Fund	Check #	Unrecorded Liability
General	101699	$ 42,661
General	101951	2,355
General	102446	1,249
Grants Assistance	102536	917
General	102667	1,168
General	103108	19,944
Grants Assistance	103209	38,602
General	9000972	2,041
		$ 108,936

  No audit adjustment was proposed as the above amounts were not considered material to the financial statements.

- For one disbursement (check # 101699, dated 10/12/2012), the withheld gross receipts tax had yet to be paid into Treasury eight months later.

Subsequent Disbursements, Continued

We recommend that the Ministry of Finance implement appropriate cut-off procedures including establishing policies and procedures to record liabilities in the correct period. We further recommend that the Ministry of Finance verify that withheld taxes are paid into Treasury.

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, 2012 that we wish to bring to your attention:

Unclaimed Property

On November 28, 2002, the Secretary of Finance received $93,737, representing unclaimed customer accounts, from Bank of Hawaii due to closure of its Majuro branch. Such is recorded as a liability within G/L Acct # 300430-50080. In accordance with Marshall Islands Revised Code, Title 30 Chapter 5, *Disposition of Unclaimed Business Interests*, 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, 2012, the Secretary of Finance had 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. This matter was discussed in our previous letters to management for the audits of fiscal years 2003 through 2011.

General Ledger Accounts

There is a lack of control over creation of new general ledger accounts. Supervisory approval of a new GL A/c # 950000-12055 created by accounting department personnel was not evident. We recommend that the Ministry of Finance establish policies and procedures relative to creation of new general ledger accounts. This matter was discussed in our previous letter to management for the audit of fiscal year 2011.

QuickBooks Disbursements

During the year, the Ministry of Finance utilized the QuickBooks accounting software to disburse non-federal funds from a checking account that was separate from RepMar's General Fund bank account. Disbursements from this account were recorded in the 4gov DILOG accounting system through a manual journal entry at year end. We were informed that the intent of such practice was to expedite payments on critical purchases such as those for the recent dengue fever outbreak and drought relief efforts.

We examined the check register for the above account and noted that the same check # (141) was used for two separate payments and that check # 145 was not recorded. This account was closed in April 2012; however, we were informed that similar accounts were opened in fiscal year 2013.

We recommend that management ensure that disbursements from such accounts are in compliance with RepMar's Procurement Code and that such are accurately captured in the 4gov DILOG accounting system.

Receiving Reports

Based on discussions with the Chief Procurement Officer, formal receiving reports are not consistently prepared and filed upon receipt of goods from vendors. A log is maintained by the Procurement & Supply office which only documents when goods are picked up by RepMar's ministries and agencies. We recommend that the Ministry of Finance prepare and maintain receiving reports upon receipt of goods from vendors. This matter discussed in our previous letter to management for the audit of fiscal years 2011.

Voided Checks

Check # 90689, dated 10/14/2011, was voided; however, the original voided check could not be located. We recommend that original voided checks be retained on file.

Gross Receipts Taxes Offset

The Ministry of Finance offset gross receipts taxes amounting to $154,077 against certain fees claimed by a tax payer from RepMar. No Cabinet Minute was made available to support approval of this offset.

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. This matter discussed in our previous letters to management for the audits of fiscal years 2009 through 2011.

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 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. This matter discussed in our previous letters to management for the audits of fiscal years 2009 through 2011.

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.