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Mr. Drauna Aisake Waqasokolala
General Manager
Air Marshall Islands, Inc.
P.O. Box 1319
Majuro MH 96960

Dear Mr. Waqasokolala:

In planning and performing our audit of the financial statements of Air Marshall Islands, Inc. (AMI) as of and for the year ended September 30, 2014 (on which we have issued our report dated July 10, 2015), 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 AMI'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 AMI's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of AMI'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 AMI's internal control over financial reporting and other matters as of September 30, 2014 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated July 10, 2015, on our consideration of AMI's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters.

The definition of a deficiency is also set forth in the attached Appendix I.

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

This report is intended solely for the information and use of the Board of Directors, management, 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 AMI 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 AMI's internal control over financial reporting as of September 30, 2014 that we wish to bring to your attention:

1) Collections

- No significant movement occurred in returned checks receivable as almost 100% pertain to balances dated 2013 and prior. We recommend management increase its collection efforts. This matter was discussed in our previous letters to management in fiscal years 2009 to 2013.
- Employee receivables as of September 30, 2014 amounted to \$171,691. Only 9% of FY13 balances were collected in FY14. Furthermore, 86% of the total is due from employees who have resigned. This matter was discussed in our previous letters to management during the 2006 to 2013 audits.
- \$289,831 of receivables are aged over six years. We recommend management enhance internal control policies over cash sales and collection reconciliations. Also, we recommend management establish internal control policies relative to timely reviewing and updating aging report.

2) Unearned Revenues

Several tickets expired based on AMI policy. As of September 30, 2014, \$6,872 of domestic flights were aged 12 months and beyond. We recommend management establish internal control policies relative to monitoring and updating unearned revenue.

3) Disbursements

Lease agreements were not available supporting recorded lease expense. We recommend management implement appropriate control policies that assist in filing documents validating transactions and that leases be updated. This matter has been discussed in our previous letter to management for the audit of fiscal years 2011 and 2013.

4) Travel Advances and Expenses

We noted long outstanding travel advances and expenses were not timely reported and liquidated. Per Company policy, employees are required to submit a travel expense report after travel. However, there is no formal policy as to when the liquidation of expenses is to occur. We recommend management establish a formal policy related to liquidation of advances and implement appropriate action encouraging compliance with Company policies.

5) Reconciliation of Accounts

Insurance prepayments were recorded although the prepayment already expired. Timely posting and reconciliation of accounts is not practiced. We recommend that management establish policies and procedures requiring timely posting and reconciliation of accounts.

6) Accruals and Prepayments

As of September 30, 2014, one purchase transaction was recorded after payment. The expense pertains to prior year. Also, we noted that timely reconciliation of prepayments/deposits is not performed. Parts received in prior years were recorded as expenses of the current year. We recommend that management establish policies and procedures requiring the timely recording of transactions and timely reconciliation of prepayments/deposits.

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

Management believes that there is a minimal risk regarding segregation of duties due to the size of AMI as well as the simplicity of transactions; however, most systems of internal control rely on assigning responsibilities to different individuals or segregating incompatible functions. However, the person responsible for inventory custody also has access to inventory records and master files. Furthermore, year-end actual counts evidenced by inventory sheets were not reflected in the inventory valuation report. This matter may be mitigated by records maintained at accounting and the performance of periodic cut-off procedures. This matter was discussed in our previous letters to management in the audits of fiscal years 2006 through 2013.

2) Information Technology Policies

Systems back up procedures are not frequently performed. The Company does not have documented IT policies. We recommend management implement frequent system backups to minimize opportunity for data loss. Management may also consider the adoption of formal IT policies. This matter was discussed in our previous letter to management in the audit of fiscal years 2011 and 2013.

3) Employee Manual and Permanent Files

The last revision of the AMI employee manual occurred more than ten years ago. An annual employee assessment and review is not conducted to assess employee performance. AMI has not consistently provided an Employee Code of Conduct to its employees, which may result in employee actions outside of AMI's vision, mission, policies and procedures, and governing laws and regulations. We recommend management consider revisiting and updating the employee manual and provide an employee code of conduct to address updates on employee related matters and to guide personnel on Company policies, employee code of conduct and ethics. Management may also consider conducting annual employee performance assessments to address manpower efficiency and effectiveness. This matter was discussed in our previous letter to management in the audit of fiscal years 2011 and 2013.

4) Cancellation Fees

Expenses associated with aircraft acquisition should be supported by an underlying purchase agreement. During the year ended September 30, 2014, AMI incurred expenses in the amount of \$82,000 as cancellation fees for a prior commitment to purchase a Dornier 228-200 for which provision of cancellation fees was not evidenced in the underlying purchase agreement. We recommend that expenses incurred be supported by underlying agreements or other authoritative documentation.

SECTION III – DEFINITIONS

The definition of a deficiency 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 Company 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

AMI'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.