

**MARSHALL ISLANDS DEVELOPMENT BANK**

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

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**FINANCIAL STATEMENTS,  
ADDITIONAL INFORMATION AND  
INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2018 AND 2017**

**MARSHALL ISLANDS DEVELOPMENT BANK**  
**(A Component Unit of the Republic of the Marshall Islands)**

Years Ended September 30, 2018 and 2017  
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## **INDEPENDENT AUDITORS' REPORT**

Board of Directors  
Marshall Islands Development Bank:

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Marshall Islands Development Bank (MIDB), a component unit of the Republic of the Marshall Islands, which comprise the statements of net position as of September 30, 2018 and 2017, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of MIDB as of September 30, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## ***Emphasis-of-Matter***

### *Financial Statement Presentation*

As discussed in Note 2 to the financial statements, MIDB elected to present an unclassified statement of net position because current assets are not matched with current liabilities. Presentation of a classified statement of net position for MIDB would be misleading to the extent that the financial statements may be materially misstated. Our opinion is not modified with respect to this matter.

## ***Other Matters***

### *Required Supplementary Information*

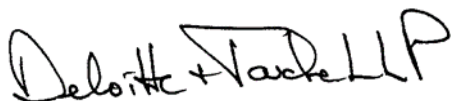
Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 7 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### *Other Information*

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Other Supplementary Information on pages 23 and 24 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

## ***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated January 7, 2019, on our consideration of MIDB'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 purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of MIDB's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering MIDB's internal control over financial reporting and compliance.



January 7, 2019

**MARSHALL ISLANDS DEVELOPMENT BANK**  
**(A Component Unit of the Republic of the Marshall Islands)**

Management's Discussion and Analysis  
 Years Ended September 30, 2018 and 2017

Fiscal year October 1, 2017 to September 30, 2018 has been a productive year for the Marshall Islands Development Bank (MIDB). During the fiscal year, the Bank's resources were utilized to prioritize Consumer, Housing, and Small to Medium Business Loan Programs with the goal and purpose of improving the living standards and conditions of the people of the Republic of the Marshall Islands.

Management's Discussion and Analysis will give you an overview of the Bank's financial highlights and activities for the fiscal year ended September 30, 2018.

**FINANCIAL HIGHLIGHTS**

- MIDB's total assets increased by \$2M or 5.5% from \$36.14M in 2017 to \$38.14M in 2018.
- MIDB's total net position increased by \$2.35M or 7.0% over the course of this year's operations. Net position represents funds from the RMI Government and the USDA Self-Help Housing Project.
- Operating revenues increased by \$0.11M from \$4.03M in 2017 to \$4.14M in 2018, \$2.93M of which was generated through interest on loans. Operating and general and administrative expenses decreased by \$0.04M from \$2.47M in 2017 to \$2.43M in 2018.
- Allowance for loan losses increased by \$1.28M from \$4.71M in 2017 to \$5.99M in 2018. Total non-operating revenues decreased by \$2.58M from \$3.77M in 2017 to \$1.19M in 2018.

**ANALYSIS OF MIDB'S FINANCIAL STATUS**

This analysis serves as an overview to MIDB's basic financial statements. A Summary of Statements of Net Position is shown below that will give insight on MIDB's resources, liabilities and net position, MIDB's priority investments and performance results compared to previous year. At the end of the fiscal year 2018, MIDB's assets of \$38.14M exceeded liabilities of \$2.04M by \$36.10M. However, \$2.03M or 5.6% of the net position is either invested in capital assets or restricted funds that can only be used for the purpose of which the funds were created. The capital assets are resources used by the Bank during the course of its operation to provide services to the people and are assets that are not easily liquidated. As of September 30, 2018 unrestricted net position amounted to \$34.07M, enough to repay all outstanding debts.

Summary of Statements of Net Position

	<u>2018</u>	<u>2017</u>	<u>2016</u>
ASSETS:			
Cash and equivalents	\$ 6,647,034	\$ 6,343,344	\$ 2,652,073
Restricted assets	1,505,822	1,151,965	907,701
Investments in shares of stock	8,189,665	7,196,576	6,440,333
Loans receivable, net	20,317,855	19,128,806	20,100,494
Notes receivable	700,000	-	-
Due from RepMar	-	1,413,600	-
Premises and equipment, net	522,148	618,422	718,937
Other assets	<u>259,767</u>	<u>291,651</u>	<u>278,322</u>
Total assets	<u>\$ 38,142,291</u>	<u>\$ 36,144,364</u>	<u>\$ 31,097,860</u>

**MARSHALL ISLANDS DEVELOPMENT BANK**  
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Management's Discussion and Analysis  
Years Ended September 30, 2018 and 2017

Summary of Statements of Net Position, Continued

	<u>2018</u>	<u>2017</u>	<u>2016</u>
<b>LIABILITIES:</b>			
Long-term debt	\$ 301,955	\$ 603,070	\$ 837,241
RepMar deposit	-	120,301	590,258
Other liabilities	<u>1,738,546</u>	<u>1,668,978</u>	<u>1,859,131</u>
Total liabilities	<u>2,040,501</u>	<u>2,392,349</u>	<u>3,286,630</u>
<b>NET POSITION:</b>			
Net investment in capital assets	522,148	618,422	718,937
Restricted	1,505,822	1,151,965	907,701
Unrestricted	<u>34,073,820</u>	<u>31,981,628</u>	<u>26,184,592</u>
Total net position	<u>36,101,790</u>	<u>33,752,015</u>	<u>27,811,230</u>
	<u>\$ 38,142,291</u>	<u>\$ 36,144,364</u>	<u>\$ 31,097,860</u>

- Loan approvals for the year were approximately \$29.39M, broken down by projects, \$27.63M released under various consumer loans, \$1.57M for small-medium enterprise loans and \$0.19M granted to housing loans. Net loans receivable increased by \$1.79M in 2018 compared with \$0.97M decrease in 2017. Loans released increased from \$27.60M to \$29.39M during the fiscal years 2017 and 2018, respectively.
- The Government of the Marshall Islands invested \$7M in Time Certificate of Deposit at the rate of 4% in May 9, 2003, maturing May 8, 2018. The money received from such TCD was used to finance various loans. As of September 30, 2018, the balance owed for Time Certificate of Deposit to the RMI Government was \$0.
- MIDB obtained \$2M and \$1M of long-term loans from Bank of Marshall Islands (BOMI) in 2012. On September 22, 2015, these loans were restructured for a principal amount of \$1,090,500, interest at 6.5% per annum, due in November 30, 2019. As of September 30, 2018 and 2017, the outstanding principal balance of this loan is \$0.30M and \$0.60M, respectively.

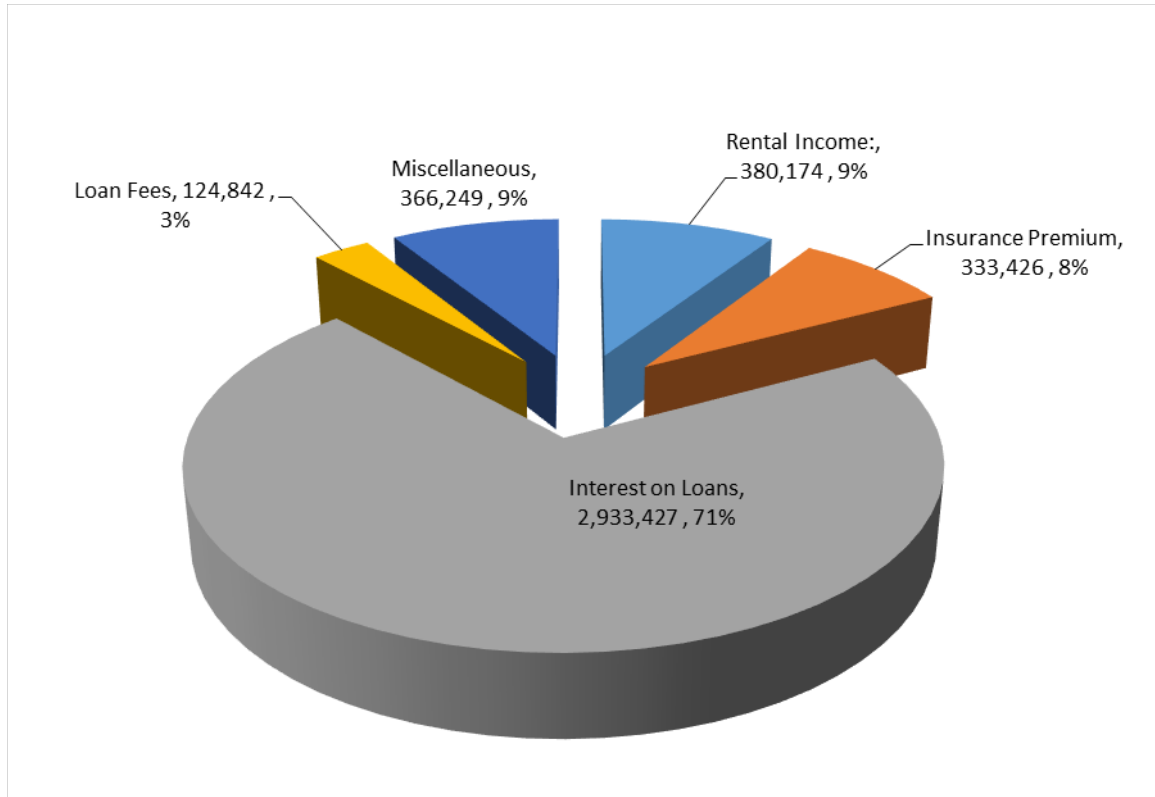
Summary of Statements of Revenues, Expenses and Changes in Net Position

	<u>2018</u>	<u>2017</u>	<u>2016</u>
<b>REVENUES:</b>			
Operating revenues	\$ 4,138,118	\$ 4,029,005	\$ 4,015,810
(Provision for) recovery of loan losses	(545,291)	617,205	-
Nonoperating revenues	<u>1,190,909</u>	<u>3,768,076</u>	<u>711,552</u>
	<u>4,783,736</u>	<u>8,414,286</u>	<u>4,727,362</u>
<b>EXPENSES:</b>			
Operating expenses	49,857	68,624	111,469
General administrative expenses	<u>2,384,104</u>	<u>2,404,877</u>	<u>2,256,702</u>
	<u>2,433,961</u>	<u>2,473,501</u>	<u>2,368,171</u>
Change in net position	2,349,775	5,940,785	2,359,191
Net position at beginning of year	<u>33,752,015</u>	<u>27,811,230</u>	<u>25,452,039</u>
Net position at end of year	<u>\$ 36,101,790</u>	<u>\$ 33,752,015</u>	<u>\$ 27,811,230</u>

**MARSHALL ISLANDS DEVELOPMENT BANK**  
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Management's Discussion and Analysis  
Years Ended September 30, 2018 and 2017

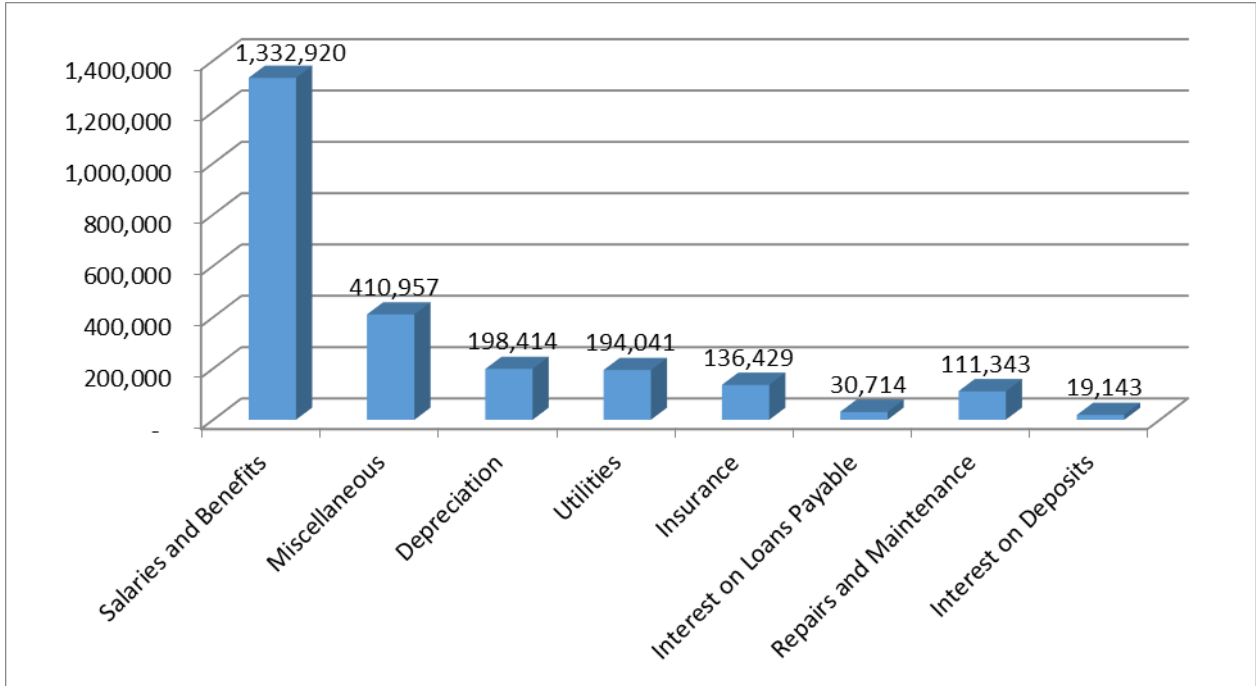
- Total operating revenues for 2018 increased by \$0.11M or 2.6% compared to 2017. About 71% of MIDB's operating revenue comes from interest on loans, 89% of which was generated from consumer loans, 7% from housing loans, and the remaining 4% from business loans. Please see chart below depicting the distribution of the Bank's operating revenues.
- Loan loss expense for 2018 was \$545K primarily the result of restructured loans.



- Total expenses for 2018 decreased by \$0.04M or 2% compared with 2017. MIDB's expenses cover a range of operating, general and administrative expenses.
- Provision for delinquent loans is provided based on the Bank's reasonable estimate, wherein the number of days an account is due, the amount of loan outstanding balance, and the borrower's capability to pay play vital information in the computation of additional allowance to be provided. The graph below shows itemized expenses and provides an over-all picture of the Bank's spending activities.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
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Management's Discussion and Analysis  
 Years Ended September 30, 2018 and 2017



- Interest expense decreased by \$19K or 27% during fiscal year ended September 30, 2018 compared to fiscal year ended September 30, 2017 due to a decrease to both interest on loans payable and interest on deposits. Interest on loans payable pertains to interest payments and accruals for a Bank of Marshall Islands loan while interest on deposits pertains to payments and accruals on the RepMar TCD and various pledged deposits.
- General and administrative expenses in the aggregate decreased by \$21K or 1% from last year's operation due primarily to a decrease in communication by \$13K or 21.2%, printing and advertising by \$16K or 24%, and travel and training by \$15K or 30%.
- Total non-operating revenues for 2018 decreased by \$2.58M from \$3.77M in 2017 to \$1.19M in 2018.

Management's and Discussion and Analysis for the year ended September 30, 2017 is set forth in MIDB's report on the audit of financial statements, which is dated May 10, 2018. That Discussion and Analysis explains the major factors impacting the 2017 financial statements and can be obtained from MIDB's Managing Director at [rmimidb@ntamar.net](mailto:rmimidb@ntamar.net)

Capital Assets and Debt

Capital assets acquisition amounted to \$120K in 2018. For additional information concerning capital assets, please refer to Note 8 to the financial statements. Long term-debt decreased by \$301K in 2018. For additional information concerning debt, please refer to Note 11 to the financial statements.



**MARSHALL ISLANDS DEVELOPMENT BANK**  
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Management's Discussion and Analysis  
Years Ended September 30, 2018 and 2017

**ECONOMIC OUTLOOK**

In the next years to come, MIDB is continuing to expect growth in the demand for housing loans, small to medium business loans and consumer loans, the latter being the major component of MIDB's loan portfolio. MIDB is involved in improving the living conditions of the RMI people through the housing loan projects under Mutual Self Help Housing Projects and USDA Rural Development.

The Bank is currently dependent on income generated from new loans. The net position is just sufficient to pay for MIDB's outstanding debts. MIDB may have to look for other sources of funds to maintain the current portfolio and the rising demand for loans. Starting FY16, MIDB adopted its new Strategic Plan which will guide the operation of MIDB in the next 5 years, to 2020. MIDB is determined to redouble its efforts to make a difference in the economy in the next 5 years.

**ADDITIONAL FINANCIAL INFORMATION**

This discussion and analysis is designed to provide MIDB's customers and other stakeholders with an overview of MIDB's operations and financial condition as at September 30, 2018. Should the reader have questions regarding the information included in this report, or wish to request additional financial information, please contact the Marshall Islands Development Bank Managing Director at the above email address or at P.O Box 1048, Majuro, Marshall Islands, MH 96960.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
**(A Component Unit of the Republic of the Marshall Islands)**

Statements of Net Position  
September 30, 2018 and 2017

<u>ASSETS</u>	<u>2018</u>	<u>2017</u>
Cash and cash equivalents	\$ 6,647,034	\$ 6,343,344
Restricted cash	611,610	594,862
Restricted time certificate of deposit	894,212	557,103
Investment in shares of stock	8,189,665	7,196,576
Receivables, net:		
Loans	20,317,855	19,128,806
Note receivable	700,000	-
Accrued interest	154,429	84,226
Due from RepMar	-	1,413,600
Other	87,188	156,825
Inventory, net	18,150	50,600
Capital assets:		
Non-depreciable capital assets	110,685	83,840
Capital assets, net of accumulated depreciation	<u>411,463</u>	<u>534,582</u>
	<u>\$ 38,142,291</u>	<u>\$ 36,144,364</u>

LIABILITIES AND NET POSITION

Liabilities:		
Notes payable	\$ 301,955	\$ 603,070
RepMar deposit	-	120,301
Accrued interest payable	-	4,245
Accounts payable and accrued expenses	236,605	221,259
Deposits pledged	<u>1,501,941</u>	<u>1,443,474</u>
Total liabilities	<u>2,040,501</u>	<u>2,392,349</u>
Commitments		
Net position:		
Net investment in capital assets	522,148	618,422
Restricted	1,505,822	1,151,965
Unrestricted	<u>34,073,820</u>	<u>31,981,628</u>
Total net position	<u>36,101,790</u>	<u>33,752,015</u>
	<u>\$ 38,142,291</u>	<u>\$ 36,144,364</u>

See accompanying notes to financial statements.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
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Statements of Revenues, Expenses and Changes in Net Position  
September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Operating revenues:		
Interest income on loans	\$ 2,933,427	\$ 2,690,811
Rental income	380,174	367,677
Insurance premiums	333,426	329,293
Federal grants	161,526	172,573
Loan fees	124,842	285,382
Interest income on time certificate of deposit	40,437	24,468
Miscellaneous	<u>164,286</u>	<u>158,801</u>
Total operating revenues	4,138,118	4,029,005
(Provision for) recovery of loan losses	<u>(545,291)</u>	<u>617,205</u>
Net operating revenues	<u>3,592,827</u>	<u>4,646,210</u>
Operating expenses:		
Interest expense:		
Interest on deposits	19,143	25,145
Interest on loans payable	<u>30,714</u>	<u>43,479</u>
Total interest expense	<u>49,857</u>	<u>68,624</u>
General and administrative expenses:		
Salaries and employee benefits	1,332,920	1,332,750
Depreciation	198,414	231,702
Utilities	194,041	182,111
Insurance	136,429	102,109
Repairs and maintenance	111,343	92,778
Professional fees	60,785	23,191
Printing, stationery and advertising	51,889	68,149
Communications	48,551	61,594
Representation	48,353	53,654
Travel and training	33,823	48,323
Impairment loss	29,150	-
Promotion and donation	28,322	34,972
Land lease	26,020	26,636
Office and house rental	21,000	21,000
Fuel	15,656	15,815
Taxes and licenses	1,531	9,804
Bad debts	-	65,365
Miscellaneous	<u>45,877</u>	<u>34,924</u>
Total general and administrative expenses	<u>2,384,104</u>	<u>2,404,877</u>
Income from operations	<u>1,158,866</u>	<u>2,172,709</u>
Nonoperating revenues:		
Contributions from RepMar	-	2,827,200
Investment earnings	<u>1,190,909</u>	<u>940,876</u>
Total nonoperating revenues	<u>1,190,909</u>	<u>3,768,076</u>
Change in net position	2,349,775	5,940,785
Net position at beginning of year	<u>33,752,015</u>	<u>27,811,230</u>
Net position at end of year	<u>\$ 36,101,790</u>	<u>\$ 33,752,015</u>

See accompanying notes to financial statements.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
**(A Component Unit of the Republic of the Marshall Islands)**

Statements of Cash Flows  
September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Cash received from customers	\$ 4,123,380	\$ 3,737,514
Cash payments to suppliers for goods and services	(787,896)	(715,692)
Cash payments to employees for services	(1,349,998)	(1,331,683)
Interest received on time certificate of deposit	40,437	24,468
Interest paid	(54,102)	(75,358)
Operating grants received	<u>161,526</u>	<u>172,573</u>
Net cash provided by operating activities	<u>2,133,347</u>	<u>1,811,822</u>
Cash flows from noncapital financing activities:		
Contributions from RepMar	1,413,600	1,413,600
Net change in pledged deposits	<u>58,467</u>	<u>(242,754)</u>
Net cash provided by noncapital financing activities	<u>1,472,067</u>	<u>1,170,846</u>
Cash flows from capital and related financing activities:		
Additions to premises, equipment and foreclosed assets	(120,043)	(131,187)
Principal repayment of long-term debt	<u>(301,115)</u>	<u>(234,171)</u>
Net cash used for capital and related financing activities	<u>(421,158)</u>	<u>(365,358)</u>
Cash flows from investing activities:		
Loan originations and principal collections, net	(2,724,529)	1,133,592
Net change in restricted assets	(353,857)	(244,264)
Dividends received	<u>197,820</u>	<u>184,633</u>
Net cash provided by (used for) investing activities	<u>(2,880,566)</u>	<u>1,073,961</u>
Net change in cash and cash equivalents	303,690	3,691,271
Cash and cash equivalents at beginning of year	<u>6,343,344</u>	<u>2,652,073</u>
Cash and cash equivalents at end of year	<u>\$ 6,647,034</u>	<u>\$ 6,343,344</u>
Cash flows from operating activities:		
Income from operations	\$ 1,158,866	\$ 2,172,709
Adjustments to reconcile income from operations to net cash provided by operating activities:		
Provision for (recovery of) loan losses	545,291	(617,205)
Provision for bad debts	-	65,365
Impairment loss	29,150	-
Depreciation	198,414	231,702
(Increase) decrease in assets:		
Receivables:		
Accrued interest	(70,203)	(30,681)
Other	69,637	(49,113)
Inventory	3,300	1,100
Increase (decrease) in liabilities:		
Accrued interest payable	(4,245)	(6,734)
Accrued expenses	15,346	59,335
Unearned premiums	(10,107)	(14,656)
Unearned fees	<u>197,898</u>	<u>-</u>
Net cash provided by operating activities	<u>\$ 2,133,347</u>	<u>\$ 1,811,822</u>
Supplemental information of noncash financing activities:		
Related party loan receivable offset:		
Loans receivable	\$ 120,301	\$ 469,957
RepMar deposit	<u>(120,301)</u>	<u>(469,957)</u>
	<u>\$ -</u>	<u>\$ -</u>
Unrealized gain on investment in shares of stock:		
Investment in shares of stock	\$ (993,089)	\$ (756,243)
Investment earnings	<u>993,089</u>	<u>756,243</u>
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
**(A Component Unit of the Republic of the Marshall Islands)**

Notes to Financial Statements  
September 30, 2018 and 2017

(1) Organization

The Marshall Islands Development Bank (MIDB), a component unit of the Republic of the Marshall Islands (RepMar), was incorporated under the laws of RepMar as a non-stock corporation pursuant to the Marshall Islands Development Bank Act of 1988 (Public Law 1988-1). MIDB was established to promote the development and expansion of the economy of the Marshall Islands in order to improve the standard of living of the people and is governed by a seven-member Board of Directors appointed by the Cabinet of RepMar. The primary activities of MIDB have been designed to strengthen the nation's economic base, increase employment and production, improve the standards of housing, promote exports, and reduce the country's dependence on imports and foreign aid through the approval of viable development loans. MIDB has received funds under Section 211 of the Compact of Free Association (the Compact), direct contributions from RepMar and funds from the U.S. Department of Agriculture (USDA) under the Rural Housing and Community Development Service Housing Preservation and Self-Help Housing Program Grants. MIDB also assumed the assets and liabilities of the former Marshall Islands Economic Development Loan Office, Inc.

MIDB's financial statements are incorporated into the financial statements of RepMar as a component unit.

(2) Summary of Significant Accounting Policies

MIDB follows the pronouncements of the Governmental Accounting Standards Board, which is the nationally accepted standard setting body for establishing accounting principles generally accepted in the United States of America (GAAP) for governmental entities.

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, and GASB Statement No. 61, *The Financial Reporting Entity: Omnibus - an amendment of GASB Statements No. 14 and 34*, establish financial reporting standards for governmental entities, which require that management's discussion and analysis of the financial activities be included with the basic financial statements and notes and modifies certain other financial statement disclosure requirements. In addition, GASB Statement No. 34 requires assets and liabilities of proprietary funds be presented in a classified format to distinguish between current and long-term assets and liabilities. MIDB is a government-owned bank. Banks do not present a classified statement of net position because current assets are not matched with current liabilities. The statements of net position of MIDB present assets and liabilities in order of their relative liquidity, rather than in a classified format.

To conform to these requirements, equity is presented in the following net position categories:

- Net investment in capital assets - capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- Restricted: Nonexpendable - net position subject to externally imposed stipulations that requires MIDB to maintain such permanently. At September 30, 2018 and 2017, MIDB does not have nonexpendable net position. Expendable - net position whose use by MIDB is subject to externally imposed stipulations that can be fulfilled by actions of MIDB pursuant to those stipulations or that expire by the passage of time. As of September 30, 2018 and 2017, MIDB has expendable net position of \$1,505,822 and \$1,151,965, respectively.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
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Notes to Financial Statements  
September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

- Unrestricted - net position that is not subject to externally imposed stipulations. Unrestricted net position may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and deferred outflows of resources, and liabilities and deferred inflows of resources associated with the operation of the fund are included in the statements of net position. Proprietary fund operating statements present increases and decreases in net position. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Classification of Revenues

MIDB has classified its revenues as either operating or nonoperating according to the following criteria:

- *Operating Revenues* - Operating revenues include activities that have the characteristics of exchange transactions, such as (1) insurance premiums, loan fees and interest income on loans and Certificates of Deposit, (2) rental occupancy income associated with MIDB assets, and (3) USDA federal grant revenues.
- *Nonoperating Revenues* - Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement No. 34, such as RepMar appropriations and investment income.

Cash and Cash Equivalents and Time Certificates of Deposit

For purposes of the statements of net position and cash flows, cash and cash equivalents is defined as amounts in demand deposits as well as short-term investments maturing within three months of the date acquired. Deposits maintained in time certificates of deposit with original maturity dates greater than ninety days are separately classified.

Custodial credit risk is the risk that in the event of a bank failure, MIDB's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. MIDB does not have a deposit policy for custodial credit risk.

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(2) Summary of Significant Accounting Policies, Continued

Cash and Cash Equivalents and Time Certificates of Deposit, Continued

As of September 30, 2018 and 2017, the carrying amounts of cash and cash equivalents and time certificates of deposit are \$8,152,856 and \$7,495,309, respectively, and the corresponding bank balances are \$8,483,341 and \$7,674,806, respectively. Of the bank balances, \$830,266 and \$740,273, respectively, are maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. The remaining amounts of \$7,653,075 and \$6,934,533, respectively, are maintained in a financial institution not subject to depository insurance. As of September 30, 2018 and 2017, bank deposits in the amount of \$250,000 were FDIC insured. MIDB does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

Investments

Investments and related investment earnings are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the date as of which the fair value of an asset or liability is determined.

Equity investments in the common stock of Marshall Islands Holdings, Inc. and Marshall Islands Service Corporation (investees) are stated at the Net Asset Value (NAV). The NAV is used as a practical expedient to estimate fair value. The NAV is determined based on the total shareholders' equities reported by the respective investees.

Loans Receivable, Interest Receivable and Allowances for Losses

Loans and interest receivables are due from customers, both individuals and businesses, located within the Republic of the Marshall Islands and are stated at the unpaid principal balances adjusted for charge-offs less the allowances for losses, and unearned loan fees and insurance premiums. Interest on loans is calculated using the simple interest method on daily balances of the principal amount outstanding. Loans are not carried at fair value because they do not meet the definition of an investment under GASB Statement No. 72.

The allowances for loan losses and interest receivable losses are established through a provision for losses charged to expense. Loans and interest receivables are charged against the allowances for losses when management believes that collection is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans and interest receivables that may be uncollectible, based on evaluations of the collectability and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans and current economic conditions that may affect the borrowers' ability to pay.

Other Receivables

Other receivables are due from government agencies, businesses and individuals located within the Republic of the Marshall Islands and are interest-free and uncollateralized. The allowance for uncollectible accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. Management determines the adequacy of the allowance for uncollectible accounts based upon review of the aged accounts receivable. The allowance is established through a provision for bad debts charged to expense.

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Notes to Financial Statements  
September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

Premises and Equipment

Premises and equipment with a cost that equals or exceeds \$500 are capitalized. Such assets are carried at cost less accumulated depreciation. Depreciation is calculated using the straight-line method based on the estimated useful lives of the respective assets. The estimated useful lives of these assets are as follows:

Building and houses	5 - 15 years
Computer systems	5 years
Motor vehicles	3 years
Office furniture	5 years
Office equipment	5 years

Foreclosed Assets

Assets acquired through, or in lieu of, loan foreclosures are held for sale and are initially recorded at the lower of loan carrying amount or fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of the carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (deduction of net position) until then. MIDB has no items that qualify for reporting in this category.

Deferred Inflows of Resources

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (additions to net position) until then. MIDB has no items that qualify for reporting in this category.

Taxes

Corporate profits are not subject to income tax in the Republic of the Marshall Islands. The Government of the Republic of the Marshall Islands imposes a gross revenue tax of 3% on revenues. MIDB is specifically exempt from gross revenue tax pursuant to Section 817 of Public Law 1988-1.

Recognition of Loan Premium and Loan Processing Revenues

Loan insurance premiums and loan processing fees are generally recognized as revenue on a pro rata basis up to a maximum of three-year term. The portion of premiums and loan processing fees that will be earned in the future is deferred and reported as unearned premiums and unearned loan processing fees.



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Notes to Financial Statements  
September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended September 30, 2018, MIDB implemented the following pronouncements:

- GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments.
- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement.
- GASB Statement No. 85, *Omnibus 2017*, which address practice issues that have been identified during implementation and application of certain GASB Statements including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits).
- GASB Statement No. 86, *Certain Debt Extinguishment Issues*, which improves consistency in accounting and financial reporting for in-substance defeasance of debt.

The implementation of these statements did not have a material effect on the accompanying financial statements.

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which addresses accounting and financial reporting for certain asset retirement obligations (AROs) associated with the retirement of a tangible capital asset. The provisions in Statement No. 83 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*, which establishes criteria for identifying fiduciary activities of all state and local governments. The provisions in Statement No. 84 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2017, GASB issued Statement No. 87, *Leases*, which establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. The provisions in Statement No. 87 are effective for fiscal years beginning after December 15, 2019. Management has yet to determine whether the implementation of this statement will have a material effect on the financial statements.

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(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In April 2018, GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*, which improves the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. The provisions in Statement No. 88 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2018, GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, which requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. The provisions in Statement No. 89 are effective for fiscal years beginning after December 15, 2019. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In August 2018, GASB issued Statement No. 90, *Majority Equity Interests – an Amendment of GASB Statements No. 14 and No. 61*, which improves the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and the relevance of financial statement information for certain component units. The provisions in Statement No. 90 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

Estimates

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and deferred outflows of resources, liabilities and deferred inflows of resources, and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and valuation of foreclosed assets.

(3) Investments

A summary of MIDB's investments as of September 30, 2018 and 2017 that are valued using the Net Asset Value (NAV) per share is as follows:

	<u>2018</u>	<u>2017</u>
Marshall Islands Holdings, Inc.	\$ 8,142,535	\$ 7,152,116
Marshall Islands Service Corporation	<u>47,130</u>	<u>44,460</u>
	\$ <u>8,189,665</u>	\$ <u>7,196,576</u>

The investment in Marshall Islands Holdings, Inc. (MIHI) comprises of 16% and 15%, respectively, of the outstanding shares as of September 30, 2018 and 2017. MIHI engages in all aspects of holding company activities in the Marshall Islands and is the sole shareholder of Bank of Marshall Islands (BOMI). In addition, the investment in Marshall Islands Service Corporation (MISC), an affiliate of BOMI, comprises of less than 1% of the outstanding shares as of September 30, 2018 and 2017. During the years ended September 30, 2018 and 2017, related dividend income was \$197,820 and \$184,632, respectively.

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Notes to Financial Statements  
September 30, 2018 and 2017

(4) Loans Receivable

Loans receivable as of September 30, 2018 and 2017 are summarized as follows:

	<u>2018</u>	<u>2017</u>
Loans receivable	\$ 26,823,177	\$ 24,166,207
Less: unearned premiums	(317,477)	(327,584)
unearned loan processing fees	(197,898)	-
allowance for loan losses	<u>(5,989,947)</u>	<u>(4,709,817)</u>
	<u>\$ 20,317,855</u>	<u>\$ 19,128,806</u>

An analysis of the change in the allowance for loan losses during the years ended September 30, 2018 and 2017 is as follows:

	<u>2018</u>	<u>2017</u>
Beginning balance	\$ 4,709,817	\$ 4,090,835
Reinstated loans which were subsequently collected	738,978	1,237,047
Provision for (recovery of) loan losses	545,291	(617,205)
Charge-offs	<u>(4,139)</u>	<u>(860)</u>
Ending balance	<u>\$ 5,989,947</u>	<u>\$ 4,709,817</u>

The loan portfolio is comprised of consumer, housing and business loans. The majority of the 2018 and 2017 loan portfolio is unsecured, while the remaining portion is secured by various forms of collateral. Additionally, these loans are normally cosigned by third parties. The basis for expected repayment of a majority of the consumer loans and housing loans is the continued employment of the borrower and allotment agreements between MIDB and the borrower's employer. All loans are at fixed rates ranging from 4% - 7% for business loans, 6% - 7% for housing loans, and 7% - 14% for consumer loans.

(5) Accrued Interest Receivable

Accrued interest receivable as of September 30, 2018 and 2017 is summarized as follows:

	<u>2018</u>	<u>2017</u>
Republic of the Marshall Islands	\$ 165,696	\$ 92,340
Investment Development Fund	<u>-</u>	<u>37,161</u>
Gross accrued interest receivable	165,696	129,501
Less: allowance for doubtful interest	<u>(11,267)</u>	<u>(45,275)</u>
	<u>\$ 154,429</u>	<u>\$ 84,226</u>

An analysis of the change in the allowance for interest receivable during the years ended September 30, 2018 and 2017 is as follows:

	<u>2018</u>	<u>2017</u>
Beginning balance	\$ 45,275	\$ 73,044
Charge-offs	<u>(34,008)</u>	<u>(27,769)</u>
Ending balance	<u>\$ 11,267</u>	<u>\$ 45,275</u>

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Notes to Financial Statements  
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(6) Other Receivables

Other receivables as of September 30, 2018 and 2017, are as follows:

	<u>2018</u>	<u>2017</u>
Rental	\$ 423,855	\$ 499,684
Other	<u>30,168</u>	<u>123,751</u>
	454,023	623,435
Allowance for uncollectible accounts	<u>(366,835)</u>	<u>(466,610)</u>
	\$ <u>87,188</u>	\$ <u>156,825</u>

(7) Restricted Deposits

MIDB maintains a savings deposit as of September 30, 2018 and 2017 in the amount of \$611,610 and \$594,862, respectively, which is restricted to collateralize loans funded by Rural Housing Service (RHS). The Memorandum of Understanding signed with the RHS requires MIDB to create and maintain an escrow account with an initial deposit of \$500,000. If the account falls below \$500,000, MIDB shall deposit in the escrow account 5% of all RHS loans issued until such time that the account has reached \$500,000. MIDB also maintains a time certificate of deposit as of September 30, 2018 and 2017 with an affiliated bank in the amount of \$894,212 and \$557,103, respectively, which is restricted to collateralize a loan payable by Tobolar Copra Processing Authority.

(8) Premises and Equipment

Capital asset activity for the years ended September 30, 2018 and 2017 is as follows:

	<u>2018</u>			
	<u>October 1, 2017</u>	<u>Additions</u>	<u>Deletions/ Transfers</u>	<u>September 30, 2018</u>
Building and houses	\$ 2,722,943	\$ 38,120	\$ -	\$ 2,761,063
Computer systems	284,668	8,262	-	292,930
Motor vehicles	354,671	33,300	(147,990)	239,981
Office furniture	62,499	595	-	63,094
Office equipment	<u>434,470</u>	<u>12,921</u>	<u>-</u>	<u>447,391</u>
	3,859,251	93,198	(147,990)	3,804,459
Less accumulated depreciation	<u>(3,324,669)</u>	<u>(198,414)</u>	<u>130,087</u>	<u>(3,392,996)</u>
	534,582	(105,216)	(17,903)	411,463
Construction materials	<u>83,840</u>	<u>74,908</u>	<u>(48,063)</u>	<u>110,685</u>
	\$ <u>618,422</u>	\$ <u>(30,308)</u>	\$ <u>(65,966)</u>	\$ <u>522,148</u>

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Notes to Financial Statements  
September 30, 2018 and 2017

(8) Premises and Equipment, Continued

	2017			September 30, 2017
	October 1, 2016	Additions	Deletions/ Transfers	
Building and houses	\$ 2,691,595	\$ 31,348	\$ -	\$ 2,722,943
Computer systems	281,858	2,810	-	284,668
Motor vehicles	302,826	51,845	-	354,671
Office furniture	59,194	3,305	-	62,499
Office equipment	<u>428,321</u>	<u>6,149</u>	<u>-</u>	<u>434,470</u>
	3,763,794	95,457	-	3,859,251
Less accumulated depreciation	<u>(3,092,967)</u>	<u>(231,702)</u>	<u>-</u>	<u>(3,324,669)</u>
	670,827	(136,245)	-	534,582
Construction materials	<u>48,110</u>	<u>55,020</u>	<u>(19,290)</u>	<u>83,840</u>
	<u>\$ 718,937</u>	<u>\$ (81,225)</u>	<u>\$ (19,290)</u>	<u>\$ 618,422</u>

(9) Foreclosed Assets

Foreclosed assets are presented net of an allowance for losses. Foreclosed assets as of September 30, 2018 and 2017 are summarized as follows:

	<u>2018</u>	<u>2017</u>
Foreclosed assets	\$ 350,000	\$ 350,000
Allowance for losses	<u>(350,000)</u>	<u>(350,000)</u>
	<u>\$ -</u>	<u>\$ -</u>

(10) Investment in Property

In April 2005, MIDB purchased property for \$139,000, with the ultimate intention of selling the property. The property is currently being leased to tenants. Depreciation is recognized by use of an estimated 10-year life and by the straight line method. As of September 30, 2018 and 2017, the property has been fully depreciated and is presented net of accumulated depreciation of \$139,000.

(11) Note Payable

MIDB has a note payable to an affiliate bank in the amount of \$1,090,500, dated September 22, 2015, interest at 6.5% per annum, due in monthly installments of principal and interest of \$25,265 through November 30, 2019, collateralized by a time certificate of deposit and an assignment of loans receivable. This loan was a restructure of the \$2,000,000 and \$1,000,000 prior year loans. As of September 30, 2018 and 2017, the balance outstanding is \$301,955 and \$603,070, respectively.

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Notes to Financial Statements  
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(11) Note Payable, Continued

Annual debt service requirements to maturity for principal and interest are as follows:

<u>Year ending</u> <u>September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2019	\$ 292,018	\$ 11,162	\$ 303,180
2020	<u>9,937</u>	<u>53</u>	<u>9,990</u>
	<u>\$ 301,955</u>	<u>\$ 11,215</u>	<u>\$ 313,170</u>

Long-term debt changes during the years ended September 30, 2018 and 2017 are as follows:

	<u>Balance</u> <u>October 1,</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>September 30,</u>	<u>Due Within</u> <u>One Year</u>
2018:					
Note payable	\$ <u>603,070</u>	\$ <u>-----</u>	\$ <u>(301,115)</u>	\$ <u>301,955</u>	\$ <u>292,018</u>
2017:					
Note payable	\$ <u>837,241</u>	\$ <u>-----</u>	\$ <u>(234,171)</u>	\$ <u>603,070</u>	\$ <u>295,449</u>

(12) Related Party Transactions

MIDB is a component unit of RepMar and is therefore affiliated with all RepMar-owned and affiliated entities, including Air Marshall Islands, Inc. (AMI) and Tobolar Copra Processing Authority (TCPA).

In 2013, MIDB entered into a loan with AMI whereby MIDB loaned AMI \$2,500,000 for the purpose of funding operations. In 2015, the Board approved the charge-off of the entire loan in the amount of \$2,376,134. Accordingly, pursuant to Cabinet Minute C.M. 064 (2015), MIDB commenced withdrawal of funds from the RepMar deposit as a partial settlement. Total related payments through withdrawals during the years ended September 30, 2018 and 2017 were \$125,501 and \$493,153, respectively.

On July 3, 2018, MIDB entered into a short-term loan with TCPA whereby MIDB loaned TCPA \$805,480 for the purpose of funding the operations, secured by the assignment of fund allocated to TCPA under Cabinet Minute C.M. 133 (2018). Such loan was paid in full on August 21, 2018 by RepMar. On August 22, 2018, MIDB entered into another short-term loan with TCPA amounting to \$700,000 secured by the agreement of funds allocated to TCPA under Cabinet Minute C.M. 168 (2018) and as guaranteed by RepMar. As at September 30, 2018, the outstanding balance is \$700,000.

As of September 30, 2018 and 2017, MIDB has deposits with an affiliate bank of \$7,653,075 and \$6,934,533, respectively. The deposits accrue interest at rates of 0.25% to 2% per annum. Interest earned for the years ended September 30, 2018 and 2017 was \$40,437 and \$24,468, respectively.

As of September 30, 2018 and 2017, MIDB employees have outstanding loans of \$965,462 and \$807,640, respectively. In addition, the directors of MIDB have outstanding loans as of September 30, 2018 and 2017, of \$316,019 and \$323,546, respectively. All loans were made at normal commercial terms and conditions.

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Notes to Financial Statements  
September 30, 2018 and 2017

(12) Related Party Transactions, Continued

As of September 30, 2018 and 2017, MIDB has an outstanding certificate of deposit of \$0 and \$120,301, respectively, payable to RepMar. The deposit is for a fifteen-year term and accrues interest at 4% per annum. This deposit is withdrawable in full or in part before maturity date with the consent of MIDB. As of September 30, 2018 and 2017, interest payable relating to this deposit amounted to \$0 and \$4,245, respectively, and is included within the statements of net position as accrued interest payable.

Movements in the outstanding RepMar certificate of deposit during the years ended September 30, 2018 and 2017 are as follows:

	Balance <u>October 1,</u>	<u>Additions</u>	<u>Reductions</u>	Balance <u>September 30,</u>
2018:				
RepMar deposit	\$ <u>120,301</u>	\$ <u>5,200</u>	\$ <u>(125,501)</u>	\$ <u>      -</u>
2017:				
RepMar deposit	\$ <u>590,258</u>	\$ <u>23,196</u>	\$ <u>(493,153)</u>	\$ <u>120,301</u>

During the year ended September 30, 2017, the operations of MIDB were funded by an appropriation of \$2,827,200 from the RepMar Nitijela for the purpose of funding the Small and Medium-sized Enterprises Business and Housing Loan Program, of which \$1,721,356 and \$1,234,809 remains unexpended as of September 30, 2018 and 2017, respectively. MIDB has recorded a receivable from RepMar at September 30, 2018 and 2017 of \$0 and \$1,413,600, respectively, associated with this appropriation.

(13) Risk Management

MIDB is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. MIDB has elected to purchase insurance covering a 5-story commercial building in Delap Village and 10 residential units in Rairok Village against fire, lightning and typhoon. MIDB has also purchased commercial automobile insurance and fire, lightning and typhoon insurance covering office contents from independent third parties for the risks of losses to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. MIDB management believes that the policies purchased are sufficient to cover any loss, if any, to which it is exposed.

(14) Commitments

MIDB committed to guarantee a loan payable to an affiliate bank by Tobolar Copra Processing Authority with a principal balance totaling \$928,164 and \$976,103 as of September 30, 2018 and 2017, respectively.

Further, certain loans recorded in the books of USDA are subject to a MIDB guarantee, the balance of which amounted to \$11,466,905 and \$11,087,474 as of September 30, 2018 and 2017, respectively. During the years ended September 30, 2018 and 2017, MIDB made payments to USDA in the amount of \$7,079 and \$0, respectively for related delinquent loans.

In 2001, MIDB assumed payment obligations under a fifteen-year ground lease, expiring on January 14, 2003, with an option to renew for an additional five years. In 2005, MIDB entered into an amended lease agreement with the landowners. The term of the amended lease is twenty years, expiring on January 13, 2023.

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Notes to Financial Statements  
September 30, 2018 and 2017

(14) Commitments, Continued

In 2003, MIDB assumed payment obligations under a thirty-year ground lease, expiring on December 31, 2028, with an option to renew for two additional terms of thirty years each.

In 2010, MIDB entered into a fifty-year ground lease agreement for a portion of Awao Weto property expiring on January 14, 2060.

In 2010, MIDB entered into a fifty-year ground lease agreement for a portion of Kabilwe Weto property expiring on May 31, 2060.

MIDB has entered into other lease agreements expiring over various years through September 30, 2063.

Future minimum lease payments under these leases are as follows:

Year ending <u>September 30,</u>	
2019	\$ 26,930
2020	27,027
2021	27,027
2022	27,027
2023	24,194
2024 - 2028	116,988
2029 - 2033	81,048
2034 - 2038	42,835
2039 - 2043	38,725
2044 - 2048	25,421
2049 - 2053	25,421
2054 - 2058	25,421
2059 - 2063	<u>20,091</u>
	 \$ <u>508,155</u>

MIDB has entered into several leases as lessor expiring over various years through December 31, 2029. Future minimum lease income for subsequent years ending September 30 is as follows:

Years ending <u>September 30,</u>	
2019	\$ 395,754
2020	321,870
2021	219,192
2022	154,640
2023	38,610
2024 - 2028	151,800
2029	<u>37,950</u>
	 \$ <u>1,319,816</u>



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Combining Statement of Net Position  
September 30, 2018

<u>ASSETS</u>	Marshall Islands Development Bank	RMI Small- Medium Enterprise Project	USDA Self-Help Housing Project	Total
Cash and cash equivalents	\$ 4,961,824	\$ 1,721,356	\$ (36,146)	\$ 6,647,034
Restricted cash	611,610	-	-	611,610
Restricted time certificate of deposit	894,212	-	-	894,212
Investments	8,189,665	-	-	8,189,665
Receivables, net:				
Loans	18,878,987	1,438,868	-	20,317,855
Notes receivable	700,000	-	-	700,000
Accrued interest	150,619	3,810	-	154,429
Other	74,111	-	13,077	87,188
Inventory, net	18,150	-	-	18,150
Capital assets:				
Nondepreciable capital assets	33,052	-	77,633	110,685
Depreciable capital assets, net	408,657	-	2,806	411,463
	<u>\$ 34,920,887</u>	<u>\$ 3,164,034</u>	<u>\$ 57,370</u>	<u>\$ 38,142,291</u>

LIABILITIES AND NET POSITION

Liabilities:				
Notes payable	\$ 301,955	\$ -	\$ -	\$ 301,955
Accounts payable and accrued expenses	80,631	79,929	76,045	236,605
Deposits pledged	<u>1,335,649</u>	<u>158,816</u>	<u>7,476</u>	<u>1,501,941</u>
Total liabilities	<u>1,718,235</u>	<u>238,745</u>	<u>83,521</u>	<u>2,040,501</u>
Net position:				
Net investment in capital assets	441,709	-	80,439	522,148
Restricted	1,505,822	-	-	1,505,822
Unrestricted	<u>31,255,121</u>	<u>2,925,289</u>	<u>(106,590)</u>	<u>34,073,820</u>
Total net position	<u>33,202,652</u>	<u>2,925,289</u>	<u>(26,151)</u>	<u>36,101,790</u>
	<u>\$ 34,920,887</u>	<u>\$ 3,164,034</u>	<u>\$ 57,370</u>	<u>\$ 38,142,291</u>

See accompanying independent auditors' report.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
**(A Component Unit of the Republic of the Marshall Islands)**

Combining Statement of Revenues, Expenses and Changes in Net Position  
September 30, 2018

	Marshall Islands Development Bank	RMI Small- Medium Enterprises Project	USDA Self-Help Housing Project	Total
Operating revenues:				
Interest income on loans	\$ 2,851,961	\$ 81,466	\$ -	\$ 2,933,427
Rental income	380,174	-	-	380,174
Insurance premiums	333,426	-	-	333,426
Federal grants	-	-	161,526	161,526
Loan fees	114,883	9,959	-	124,842
Interest income on time certificate of deposit	40,371	-	66	40,437
Miscellaneous	164,286	-	-	164,286
Total operating revenues	3,885,101	91,425	161,592	4,138,118
Provision for loan losses	(547,337)	2,046	-	(545,291)
Net operating revenues	3,337,764	93,471	161,592	3,592,827
Operating expenses:				
Interest expense:				
Interest on deposits	19,143	-	-	19,143
Interest on loans payable	30,714	-	-	30,714
Total interest expense	49,857	-	-	49,857
General and administrative expenses:				
Salaries and employee benefits	1,183,359	-	149,561	1,332,920
Depreciation	196,650	-	1,764	198,414
Utilities	194,041	-	-	194,041
Insurance	120,481	-	15,948	136,429
Repairs and maintenance	107,611	-	3,732	111,343
Professional fees	57,785	-	3,000	60,785
Printing, stationery and advertising	51,318	-	571	51,889
Communications	48,027	-	524	48,551
Representation	48,353	-	-	48,353
Travel and training	30,258	-	3,565	33,823
Impairment loss	29,150	-	-	29,150
Promotion and donation	28,322	-	-	28,322
Land lease	26,020	-	-	26,020
Office and house rental	21,000	-	-	21,000
Fuel	10,427	-	5,229	15,656
Taxes and licenses	1,486	-	45	1,531
Miscellaneous	44,099	440	1,338	45,877
Total general and administrative expenses	2,198,387	440	185,277	2,384,104
Income (loss) from operations	1,089,520	93,031	(23,685)	1,158,866
Nonoperating revenues:				
Investment earnings	1,190,909	-	-	1,190,909
Change in net position	2,280,429	93,031	(23,685)	2,349,775
Net position at beginning of year	30,922,223	2,832,258	(2,466)	33,752,015
Net position at end of year	\$ 33,202,652	\$ 2,925,289	\$ (26,151)	\$ 36,101,790

See accompanying independent auditors' report.

**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**

The Board of Directors  
Marshall Islands Development Bank:

We have audited, 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, the financial statements of the Marshall Islands Development Bank (MIDB), which comprise the statement of net position as of September 30, 2018, and the related statements of revenues, expenses and changes in net position and of cash flows for the year then ended and the related notes to the financial statements, and have issued our report thereon dated January 7, 2019.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered MIDB's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of MIDB's internal control. Accordingly, we do not express an opinion on the effectiveness of MIDB's internal control.

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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as items 2018-001 through 2018-003 that we consider to be material weaknesses.

### **Compliance and Other Matters**

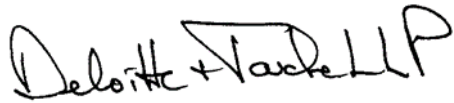
As part of obtaining reasonable assurance about whether MIDB's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect 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 item 2018-004.

## MIDB's Response to Findings

MIDB's response to the findings identified in to our audit are described in the accompanying Schedule of Findings and Responses. MIDB's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

## Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

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

January 7, 2019

**MARSHALL ISLANDS DEVELOPMENT BANK**  
(A Component Unit of the Republic of the Marshall Islands)

Schedule of Findings and Responses  
Year Ended September 30, 2018

Finding No. 2018-001

Loans Receivable

Criteria: A comprehensive set of policies and procedures should be in place to govern the lending and credit administration processes, which should include, at a minimum, internal control procedures over processing loan approvals, loan boarding, completeness and accuracy of loan documentation, safeguarding pertinent loan documents and monitoring loan covenant requirements.

Conditions:

Tests of a representative sample of 40 loans revealed several matters in the design, implementation and adherence to internal controls in the lending and credit administration areas that we recommend be considered by management.

- a. One loan folder (Note no. 68496) was not provided.
- b. Five loans tested (Note nos. 47145, 57526, 67158, 79086, 59225) either do not have a completed loan document checklist in file or were not signed by the validating and verifying officer.
- c. Eight loans tested (Note nos. 25602, 77510, 79339, 80972, 47145, 57526, 67158, 75502) contain information, such as % paid off of old loan, maturity date, and loan date opening, that is not consistent throughout the loan files, i.e. loan document checklist, loan drawdown form, promissory note, loan agreement, loan disclosure form, loan trial balance and loan transaction history.
- d. One loan tested (Note no. 57526) has blank application form for the co-borrower.
- e. Two loans tested (Note nos. 47145 and 57526) have no credit checks for the co-borrower.
- f. One loan tested (Note no. 47145) has a co-borrower who also serves as the guarantor for the loan.
- g. One loan tested (Note no. 79086) has no guarantor and no guarantor pay check stubs in file.
- h. For one commercial loan tested (Note no. 77510), the guarantor signed as a co-borrower in the promissory note.
- i. One refinanced delinquent loan tested (Note no. 80080) was not tagged based on the status of the loan paid off.
- j. One loan tested (Note no. 67158) was erroneously waived the interest in the system, thus all payments made were applied to principal.
- k. Two loans out of 6119 loans (Note nos. 83589 and 78441) in the loans trial balance has maturity date different from maturity date in the loan folders due to typographical error in encoding in the system.

Cause: The cause of the above condition appears to be potential noncompliance with the criteria.

Effect: The effect of the above is the potential occurrence of errors in the loan portfolio. This condition also gives rise to potential losses due to insufficient safeguarding of legal documents.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
(A Component Unit of the Republic of the Marshall Islands)

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2018

Finding No. 2018-001, Continued

Loans Receivable, Continued

Recommendation: MIDB should perform a comprehensive review of its policies and procedures and strengthen controls and monitoring of those controls.

Prior Year Status: Similar issues concerning loan documentation have been reported as a finding in the audits of MIDB for fiscal years 2007 through 2017.

Auditee Response and Corrective Action Plan:

- a. Loan officer who processes the loan will try to locate the folder. The bank is already scanning all loan files on a daily basis to avoid misplaced folders.
- b. Although loans were not signed by verification officer, all the required loan documents were met and complete. The Bank does not normally utilize a checklist form for housing loans. However, the Bank will make sure that such is utilized in the coming year.
- c. The Bank will ensure all required loan documents will be met, completed and consistent throughout the loan files.
- d. The error has been corrected already. There is no co-borrower for the loan.
- e. There is no co-borrower for Note no. 57526. As for Note no. 47145, Management will thoroughly review each loan file to ensure all applicants have credit checks.
- f. The Bank will ensure that such is not repeated again.
- g. Guarantor's pay check stub has already been provided to file and available for revision.
- h. As indicated above, the Bank will ensure that such is not repeated again.
- i. Management will thoroughly review refinanced delinquent loans to ensure all are properly tagged based on status of loans paid off.
- j. The error has been corrected in the system already. Payments are now made to both interest and principal.
- k. The Bank will ensure that such is not repeated in the future.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
(A Component Unit of the Republic of the Marshall Islands)

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2018

Finding No.: 2018-002

Allowance for Loans Losses

Criteria: Adequate accounting controls necessitate that allowance for loan losses be appropriately reviewed and monitored.

Condition: On September 3, 2018, MIDB revised the interest rate for housing and commercial loans from 8.5% to 7%, as approved by the Board of Directors on July 25, 2018. Upon revision of the system rates, the open dates of the loans were also revised from the original release date to 09/03/2018. Thus, past due days were altered to zero (0) days. This resulted in an understatement of the allowance for loan losses of \$654,185 and an overstatement of accrued interest receivable of \$90,519 as of September 30, 2018. Adjustments have been proposed for both misstatements but MIDB agreed to record only the \$654,185 adjustment for the allowance for loan losses. The \$90,519 adjustment was not recorded by MIDB due to its immaterial nature.

Cause: The cause of the above condition is the lack of adequate review and monitoring procedures on assessing allowance for loan losses.

Effect: The effect of the above condition is potential misstatement of allowance for loan losses.

Recommendation: We recommend that management implement appropriate internal control policies over reviewing and monitoring the allowance for loan losses.

Auditee Response and Corrective Action Plan: Management will ensure that allowance for loan losses is properly reviewed and monitored.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
(A Component Unit of the Republic of the Marshall Islands)

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2018

Finding No. 2018-003

Principal payments on delinquent loans

Criteria: GAAP allows recognition and accrual of interest for loans with less than 90 days past due. However, upon discontinuance of the accrual of interest, all unpaid accrued interest is reversed and subsequent collections are applied to principal and interest is only recognized after principal is fully recovered.

Condition: MIDB's application of payments for delinquent loans is not in accordance with GAAP. Upon discontinuance of the accrual of interest on delinquent loans receivables, all unpaid accrued interest is not reversed and subsequent collections are first applied to interest and then to principal. In FY2018, payments received from delinquent loans applied to interest amounted to \$347,777. As this amount was not considered material, no audit adjustment was recorded.

Cause: The cause of the above condition is the lack of adequate review and monitoring procedures of repayments made by delinquent borrowers.

Effect: The effect of the above condition is potential misstatement of loans receivable and loan interest income.

Recommendation: We recommend that management address the application of payments for delinquent loans in accordance with GAAP.

Auditee Response and Corrective Action Plan: Management will ensure that delinquent loans are monitored manually on a quarterly basis so that the loans receivable are properly stated.



**MARSHALL ISLANDS DEVELOPMENT BANK**  
(A Component Unit of the Republic of the Marshall Islands)

Schedule of Findings and Responses, Continued  
Year Ended September 30, 2018

Finding No. 2018-004

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; provided, however, that procurement requirements shall not be artificially divided so as to constitute a small purchase under this Section. 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 a supply, service, or construction item without competition when it is determined in writing that there is only one source for the required supply, service, or construction item.
- (d) Section 129 - notwithstanding any other provision of this Act, emergency procurement may be made when there exists a threat to public health, welfare, or safety under emergency conditions as defined in regulations promulgated by the Policy Office; provided, that such emergency procurement shall be made with such competition as is practicable under the circumstances. A written determination of the basis for the emergence and for the selection of the particular contractor shall be included in the contract file.

Condition: The following payments were not adequately documented to evidence compliance with the procurement process set forth in the criteria:

- 1) Purchase of a vehicle for \$23,500, check #117274
- 2) Repairs and maintenance of \$500, check #123831

Cause: The cause of the above condition may be a lack of adequate internal control policies and procedures requiring documentation of compliance with RepMar's Procurement Code.

Effect: The effect of the above condition may result in noncompliance with RepMar's Procurement Code.

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

Prior Year Status: Similar issues concerning noncompliance with RepMar's Procurement Code have been reported as a finding in the audit of MIDB for fiscal years 2016 and 2017.

Auditee Response and Corrective Action Plan: The management of Marshall Islands Development Bank will ensure that price quotations are obtained in order to comply with RepMar's Procurement Code.

**MARSHALL ISLANDS DEVELOPMENT BANK**  
**(A Component Unit of the Republic of the Marshall Islands)**

Unresolved Prior Year Findings  
Year Ended September 30, 2018

The status of unresolved prior year findings is disclosed within the Schedule of Findings and Responses section of this report.