

June 25, 2008

CONFIDENTIAL

Mr. Jefferson Barton
Secretary, Ministry of Finance
Republic of the Marshall Islands
P.O. Box D
Majuro, MH 96960

Dear Secretary Barton:

We have audited the financial statements of the Republic of the Marshall Islands (RepMar) as of and for the year ended September 30, 2007, and have issued our report thereon dated June 25, 2008. In planning and performing our audit of the governmental activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information, which collectively comprise the basic financial statements of RepMar, we considered its internal control as a basis for designing our auditing procedures for the purpose of expressing our opinions on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of RepMar's internal control.

During our audit, we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations are intended to improve internal control or result in other operating efficiencies and are summarized below.

1. Embassy Consultant Contracts

Of \$78,116 in direct payments for two Embassy employees made by the Washington Embassy, we noted one item in the amount of \$1,731 relating to the bi-weekly salary for one employee that was not supported by a valid employment contract. Instead, the payment was supported by a contract that expired in September 1997. Additionally, of \$19,598 in direct payments for one Embassy employee made by the Tokyo Embassy, we noted one item in the amount of \$10,720 relating to reimbursement for the bi-weekly salary of the employee that was not supported by a valid employment contract. Instead, the payment was supported by a contract that expired in June 27, 2006. We recommend that the Ministry of Foreign Affairs ensure that salaries for Embassy employees are supported by valid employment contracts.

2. Revenues

Of 116 General Fund revenue items tested, we noted two items in the amounts of \$32,889 (customer # 3140-04) and \$1,244 (customer # 4863-04) that were not supported by underlying tax returns. We recommend that the Ministry of Finance ensure that all tax revenues recorded are supported by filed tax returns.

3. Unclaimed Property

On November 28, 2002, the Secretary of Finance received \$93,737 from the Bank of Hawaii representing unclaimed customer accounts when the bank closed its branch, and recorded such as a liability within G/L Acct # 300430-50080. In accordance with Public Law No. 1999-89, any unclaimed property, which escheats to RepMar under the provisions of the law, shall be deposited into an Abandoned Business Interests account within the Unclaimed Business Property Fund. The Secretary of Finance is required to publish the existence of such property within one year after receipt. As of September 30, 2007, the Secretary of Finance has not published the existence of such property in the local newspaper. We recommend that the Ministry of Finance publish the existence of escheated property in accordance with the enabling legislation.

4. Petty Cash Imprest Accounts

At September 30, 2007, the Ministry of Finance recorded twenty-seven petty cash imprest accounts, aggregating \$23,306. We selected one item for testing (G/L Acct # 950000-11044, Ebeye Thyroid Petty Cash) in the amount of \$7,585; however, it was determined that this petty cash account no longer existed. As the amount of \$7,585 was not considered material to the basic financial statements, no audit adjustment was proposed. We recommend that the Ministry of Finance examine all recorded petty cash imprest accounts and determine whether such represent valid petty cash accounts.

5. Embassy Imprest Accounts

Three months subsequent to September 30, 2007 (December 31, 2007), the imprest accounts for the Tokyo Embassy (G/L Acct # 950000-12020) and the Honolulu Consulate (G/L Acct # 950000-12070) in the amounts of \$100,000 and \$10,000, respectively, were not supported by completed imprest account reconciliations or bank statement reconciliations. We recommend that the Ministry of Finance ensure that imprest account and bank statement reconciliations are performed for all Embassy accounts on a monthly basis.

6. Payroll Clearing Account

At September 30, 2007, the Ministry of Finance recorded a credit balance within the payroll clearing account (G/L Acct # 100100-13025) in the amount of \$2,330 representing a payroll bank account with Bank of Marshall Islands that was closed in fiscal year 2004. We recommend that that Ministry of Finance determine the validity of this account balance and correct the general ledger for amounts no longer considered valid.

7. Bank Errors

The bank reconciliation for the General Fund General Account (G/L Acct # 950000-13010) and Payroll Account (G/L Acct # 950000-13020) included bank errors in the amounts of \$5,333 and \$9,878, respectively, that date back as far as fiscal year 2003 without apparent follow-up with the financial institution. Given the aging of these balances, collectibility from the financial institution may be doubtful. We recommend that the Ministry of Finance follow-up on all bank errors with the financial institution in a more timely manner.

8. Unrecorded Transactions

At September 30, 2007, the Ministry of Finance recorded a savings account (G/L Acct # 950000-15040) in the amount of \$62,427. We obtained confirmation of this account balance from Bank of Marshall Islands, which indicated an account balance of \$61,204, with the variance of \$1,223 representing unrecorded transactions. As the amount of \$1,223 was not considered material to the basic financial statements, no audit adjustment was proposed. We recommend that the Ministry of Finance ensure transactions on all bank accounts are recorded.

9. Accounts Payable – Landowners

At September 30, 2007, the Ministry of Finance recorded an amount payable to landowners (G/L Acct # 100100-55040) in the amount of \$16,499, which represented amounts received from Mobil Oil Micronesia, Inc. (MOMI) for a land lease at the airport not yet paid to the landowners. However, all payments for fiscal year 2007 were paid to the landowners thus the recorded liability may no longer be valid. As the amount of \$16,499 was not considered material to the basic financial statements, no audit adjustment was proposed. We recommend that the Ministry of Finance determine the validity of amounts payable to landowners for the MOMI land lease at the airport.

10. Payroll-related Liabilities

At September 30, 2007, the Ministry of Finance recorded accrued payroll (G/L Acct # 960000-60460) in the amount of \$4,921 relating to direct deposits for PPE 9/29/07 whereas actual direct deposits amounted to \$27,686. In addition, the Ministry of Finance recorded accruals for various allotments in the amount of \$951,914 whereas actual allotments payable amounted to \$949,719. As the net variance of \$20,570 was not considered material to the basic financial statements, no audit adjustment was proposed. We recommend that the Ministry of Finance ensure that recorded payroll-related liabilities represent actual amounts payable to employees.

11. Payroll Expenditures – Group Life Insurance Premiums

Of \$207,091 in payroll expenditures relating to the employer share for group life insurance premiums, four items, totaling \$96, were tested and the following exceptions were noted:

<u>Employee #</u>	<u>Actual Employer Share</u>	<u>Expected Employer Share</u>	<u>Variance</u>	<u>Actual Employee Share</u>	<u>Expected Employee Share</u>	<u>Variance</u>
20819	\$ 39.00	\$ 39.60	\$ (0.60)	\$ 27.00	\$ 27.00	\$ -
41519	\$ 11.88	\$ 13.86	\$ (1.98)	\$ 8.10	\$ 9.45	\$ (1.35)

Based on discussions with payroll department personnel, the item relating to employee # 20819 appears to be an input error whereas the item relating to employee # 41519 appears to be the failure of updating insurance premiums subsequent to the employee receiving a pay increment. We recommend that management establish internal control policies and procedures to ensure that changes made to the payroll master file are independently verified and that group life insurance premiums paid represent accurate amounts based on authorized employee pay rates.

12. Miscellaneous Receivables

At September 30, 2007, the Ministry of Finance recorded the following receivable balances that were not supported by underlying subledgers:

<u>G/L Acct #</u>	<u>G/L Balance</u>	<u>G/L Acct #</u>	<u>G/L Balance</u>	<u>G/L Acct #</u>	<u>G/L Balance</u>
100100-20200	\$ 39,700	100100-24012	\$ 2,367	100100-24060	\$ 13,875
100100-22005	\$ 33,419	100100-24020	\$ 12,053	100100-24090	\$ 84,295
100100-22020	\$ 18,956	100100-24027	\$ 1,298	100100-24100	\$ 193,995
				950000-24100	\$ (1,566)

No audit adjustments were proposed for the above items as these receivable balances were offset by an allowance for uncollectible accounts in the amount of \$398,392. We recommend that the Ministry of Finance reconcile these receivable accounts and determine their ultimate collectibility.

13. Loan Drawdowns

At September 30, 2007, we obtained a confirmation from the Asian Development Bank, which included a balance outstanding for Loan Number 1948 RMI (SF) – Outer Island Transport Infrastructure Project in the amount of \$507,517. This loan account was closed on September 15, 2006 yet additional loan drawdowns occurred during fiscal year 2007 in the amount of \$58,612. No documentation was made available supporting these drawdowns. We recommend that the Ministry of Finance determine the validity of these drawdowns against this loan account.

14. Loans Payable

During the year ended September 30, 2007, the Ministry of Finance remitted \$2,685,133 to the Asian Development Bank (ADB) as debt service payments on certain outstanding loan balances. We obtained confirmation from ADB for debt service payments made during the year ended September 30, 2007, and noted the following variances:

	<u>Balance per RepMar</u>	<u>Balance per ADB</u>	<u>Variance</u>
Principal repayment	\$ 1,345,970	\$ 1,404,555	\$ (58,585)
Interest payments	<u>1,339,163</u>	<u>1,260,474</u>	<u>78,689</u>
	<u>\$ 2,685,133</u>	<u>\$ 2,665,029</u>	<u>\$ 20,104</u>

In addition, we obtained confirmation from ADB of outstanding loans payable at September 30, 2007, and agreed such to the corresponding balances recorded by the Ministry of Finance. The following variances were noted:

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<u>Loan #</u>	<u>Balance per RepMar</u>	<u>Balance per ADB</u>	<u>Variance</u>
1102	\$ 3,039,780	\$ 3,099,560	\$ (59,780)
1218	452,166	462,645	(10,479)
1249	7,161,764	7,252,028	(90,264)
1250	651,540	664,201	(12,661)
1316	4,882,110	4,909,565	(27,455)
1389	8,109,176	7,971,482	137,694
1513	11,290,181	11,177,293	112,888
1694	8,953,626	8,953,626	-
1791	4,923,345	4,923,345	-
1828	3,397,242	3,388,600	8,642
1829	8,388,966	8,388,966	-
1948	507,517	507,517	-
	<u>\$ 61,757,413</u>	<u>\$ 61,698,828</u>	<u>\$ 58,585</u>

We recommend that management establish internal control policies and procedures to ensure that reconciliations of loans payable balances are prepared and independently reviewed on a periodic basis and in a timely fashion.

15. Credit Card Payable

At September 30, 2007, the outstanding balance payable on RepMar's credit card amounted to \$49,959, of which only \$4,505 was recorded as a liability at year end. No reconciliation of the September 2007 credit card statement to the general ledger balance was made available. Furthermore, based on discussions with Finance personnel, no reconciliations were performed for the entire fiscal year. As the unrecorded liability of \$45,454 was not considered material to the basic financial statements, no audit adjustment was proposed. We recommend that management establish internal control policies and procedures to ensure that credit card statement reconciliations are prepared and independently reviewed on a monthly basis and in a timely fashion.

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In addition, we identified certain deficiencies in internal control that we consider to be significant deficiencies, and in accordance with *Government Auditing Standards* communicated them in writing to RepMar in a separate report dated June 25, 2008.

Our audit procedures are designed primarily to enable us to form opinions on the basic financial statements, and therefore, may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of RepMar's organization gained during our work to make comments and suggestions that we hope will be useful to you. We would be pleased to discuss these comments and recommendations with you at your convenience.

This report is intended solely for the information and use of the members of the management of RepMar and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

