

UTRŌK ATOLL LOCAL GOVERNMENT

**INDEPENDENT AUDITORS' REPORTS ON
INTERNAL CONTROL AND ON COMPLIANCE**

YEAR ENDED SEPTEMBER 30, 2009

**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**

Mayor John Kaiko
Utrök Atoll Local Government
Republic of the Marshall Islands:

We have audited the financial statements of the governmental activities and each major fund of the Utrök Atoll Local Government (UALGOV) as of and for the year ended September 30, 2009, which collectively comprise UALGOV's basic financial statements and have issued our report thereon dated October 20, 2011. We conducted our audit 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.

Internal Control Over Financial Reporting

Management of UALGOV is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered UALGOV's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of UALGOV's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of UALGOV's internal control over financial reporting.

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 over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

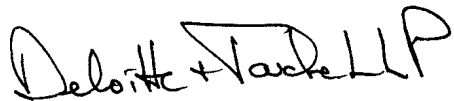
Compliance and Other Matters

As part of obtaining reasonable assurance about whether UALGOV's financial statements are free of 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 Questioned Costs as items 2009-2 and 2009-3.

We noted certain matters that we reported to management of UALGOV in a separate letter dated October 20, 2011.

UALGOV's response to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit UALGOV's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the Council, others within the entity, federal awarding agencies, and the cognizant audit and other federal agencies and is not intended to be and should not be used by anyone other than these specified parties.

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

October 20, 2011

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE
WITH OMB CIRCULAR A-133 AND ON THE SCHEDULE OF EXPENDITURES OF
FEDERAL AWARDS**

Mayor John Kaiko
Utrök Atoll Local Government
Republic of the Marshall Islands:

Compliance

We have audited Utrök Atoll Local Government's (UALGOV) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on its one major federal program for the year ended September 30, 2009. UALGOV's major federal program is identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs (pages 8 through 13). Compliance with the requirements of laws, regulations, contracts, and grants applicable to its one major federal program is the responsibility of UALGOV's management. Our responsibility is to express an opinion on UALGOV's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about UALGOV's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of UALGOV's compliance with those requirements.

In our opinion, UALGOV complied, in all material respects, with the requirements referred to above that are applicable to its one major federal program for the year ended September 30, 2009.

Internal Control Over Compliance

Management of UALGOV is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered UALGOV's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of UALGOV's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

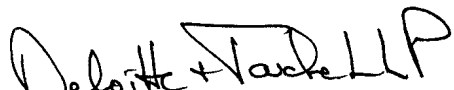
Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying Schedule of Findings and Questioned Costs as item 2009-1. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities and each major fund of the Utrök Atoll Local Government (UALGOV) as of and for the year ended September 30, 2009, and have issued our report thereon dated October 20, 2011. Our audit was performed for the purpose of forming our opinions on the financial statements that collectively comprise UALGOV's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards (page 5) is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of the management of UALGOV. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

UALGOV's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit UALGOV's responses and, accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of management, the Council, others within the entity, federal awarding agencies, and the cognizant audit and other federal agencies and is not intended to be and should not be used by anyone other than these specified parties.


October 20, 2011

UTRÖK ATOLL LOCAL GOVERNMENT

Schedule of Expenditures of Federal Awards
Compact of Free Association, Public Law 99-239
Year Ended September 30, 2009

	Fund Balance Beginning of Year	Net Earnings on Funds	Loan Proceeds	Net Funds Expended	Fund Balance End of Year
<u>U.S. Department of the Interior</u> <u>CFDA #15.875</u>					
Funds passed through the Republic of the Marshall Islands (RepMar):					
The Agreement between the Government of the United States and the Government of the Marshall Islands for the implementation of Section 177 of the Compact of Free Association	<u>\$ 13,878,556</u>	<u>\$ 607,501</u>	<u>\$ 2,440,000</u>	<u>\$ 3,454,468</u>	<u>\$ 13,471,589</u>

Of funds received per the agreement between the Government of the United States and the Government of the Marshall Islands for the implementation of Section 177 of the Compact of Free Association, the cumulative amount of \$13,471,589 remains invested in the Utrök Claims Trust Fund, a permanent fund of UALGOV. Funds expended during the year ended September 30, 2009, are represented by fund manager fees of \$173,246, legal fees of \$151,900, interest expense of \$56,349, a transfer out to the General Fund of \$632,973 for general operations and a transfer out to the Utrök Local Distribution Authority of \$2,440,000 for distribution to the people of Utrök based on an approved distribution scheme.

See accompanying notes to schedule of expenditures of federal awards.

UTRÖK ATOLL LOCAL GOVERNMENT

Schedule of Expenditures of Federal Awards
Other U.S. Federal Grants
Year Ended September 30, 2009

<u>CFDA#</u>	<u>Agency/Program</u>	Accrued (Deferred) Balance at October 1, 2008	Federal Cash Receipts and Adjustments	Federal Expenditures	Accrued (Deferred) Balance at September 30, 2009
	<u>U.S. Department of Energy</u>				
	Direct award:				
Unknown	Commodity Supplemental Food Program charter cost	\$ -	\$ 10,000	\$ 10,000	\$ -
	Total U.S. Department of Energy	<u>-</u>	<u>10,000</u>	<u>10,000</u>	<u>-</u>
	<u>U.S. Department of Agriculture</u>				
	Fund passed through the Republic of the Marshall Islands:				
10.582	Commodity Supplemental Food Program	\$ 83,386	\$ 158,270	\$ 108,044	\$ 33,160
	Total U.S. Department of Agriculture	<u>83,386</u>	<u>158,270</u>	<u>108,044</u>	<u>33,160</u>
	<u>U.S. Department of Commerce</u>				
	Direct award:				
11.P.L.108-219	Utrök Atoll Radiological Monitoring Support	(32,546)	-	22,656	(9,890)
	Total U.S. Department of Commerce	<u>(32,546)</u>	<u>-</u>	<u>22,656</u>	<u>(9,890)</u>
	<u>U.S. Department of Interior</u>				
	Direct award:				
15.875	Utrök Atoll Radiological Monitoring Support	-	18,808	77,000	58,192
	Total U.S. Department of Commerce	<u>-</u>	<u>18,808</u>	<u>77,000</u>	<u>58,192</u>
		<u>\$ 50,840</u>	<u>\$ 187,078</u>	<u>\$ 217,700</u>	<u>\$ 81,462</u>

The above federal expenditures are included within the expenditures of the general fund of \$812,213.

See accompanying notes to schedule of expenditures of federal awards.

UTRŌK ATOLL LOCAL GOVERNMENT

Notes to Schedule of Expenditures of Federal Awards
Year Ended September 30, 2009

(1) Organization

The Utrōk Atoll Local Government (UALGOV) is a governmental entity governed by its own Constitution. All significant operations of UALGOV are included in the scope of the OMB Circular A-133 audit (the "Single Audit"). The U.S. Department of the Interior has been designated as UALGOV's cognizant agency for the Single Audit. UALGOV is the subrecipient of funds received through Section 177 of the Compact of Free Association from the Republic of the Marshall Islands (RepMar). These funds must be distributed in accordance with the agreement concerning procedures for the implementation of United States economic assistance, programs and services provided in the Compact of Free Association between the Government of the United States and the Government of the Marshall Islands, dated July 31, 1986. It has been determined these funds are not subject to general U.S. federal requirements such as OMB's Circular A-87 and Circular A-102, but rather must be expended in compliance with local laws and regulations and Compact intent.

(2) Summary of Significant Accounting Policies

Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of UALGOV and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

UTRÖK ATOLL LOCAL GOVERNMENT

Schedule of Findings and Questioned Costs Year Ended September 30, 2009

Section I - Summary of Auditor's Results

Financial Statements

- | | |
|--|---------------|
| 1. Type of auditors' report issued: | Unqualified |
| Internal control over financial reporting: | |
| 2. Material weakness(es) identified? | No |
| 3. Significant deficiency(ies) identified? | None reported |
| 4. Noncompliance material to financial statements noted? | Yes |

Federal Awards

- | | |
|---|-------------|
| Internal control over major programs: | |
| 5. Material weakness(es) identified? | No |
| 6. Significant deficiency(ies) identified? | Yes |
| 7. Type of auditors' report issued on compliance for major programs: | Unqualified |
| 8. Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? | Yes |
| 9. UALGOV's major programs were as follows: | |
| <u>CFDA #</u> <u>Name of Federal Program</u> | |
| 15.875 Economic, Social and Political Development of the Territories and the Freely Associated States:
Section 177 of the Compact of Free Association | |
| 10. Dollar threshold used to distinguish between Type A and Type B programs: | \$300,000 |
| 11. Auditee qualified as a low-risk auditee? | No |

Section II - Financial Statement Findings

<u>Reference Number</u>	<u>Findings</u>	<u>Refer Page #</u>
2009-2	Local Noncompliance	12
2009-3	Local Noncompliance	13

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Schedule of Findings and Questioned Costs, Continued
Year Ended September 30, 2009

Section III - Federal Award Findings and Questioned Costs

<u>Reference Number</u>	<u>Findings</u>	<u>Questioned Costs</u>	<u>Refer Page #</u>
2009-1	Procurement and Suspension and Debarment	\$ 46,914	10 - 11

UTRÖK ATOLL LOCAL GOVERNMENT

Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2009

Finding No.: 2009-1
 Program/Area: Procurement and Suspension and Debarment
 Agency/Program Name: U.S. Department of Agriculture - CFDA # 10.582: Commodity Assistance Program
 U.S. Department of Commerce - CFDA # 11.P.L. 108-219: Utrök Atoll
 Radiological Monitoring Support
 U.S. Department of Energy: Charter Costs for Commodity Assistance Program
 Questioned Costs: \$46,914

Criteria: Purchases of goods and services by recipients of Federal grant funding are constrained by the concept of “fair procurement practices”. Section 3016.36 of 7 CFR 3016, Section 600.236 of 10 CFR 600, and Section 24.36 of 15 CFR 24, *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*, states that grantees and subgrantees will use their own procurement procedures, which reflect applicable State and local laws and regulations, provided that the procurements conform to applicable Federal law and the standards identified in this section. Thus, the following guidelines shall be observed based on RepMar’s Procurement Code:

(a) Section 124 - unless otherwise authorized by law, all Government contracts (including local government Councils) 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. 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 three 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.

Condition: Of \$217,700 in Federal Grants expenditures, we tested four (4) items totaling \$122,118 and noted the following that did not evidence adequate compliance with either formal or informal procurement procedures:

<u>Grantor Agency</u>	<u>CFDA No.</u>	<u>Amount</u>	<u>Questioned Costs</u>	<u>Check#</u>
U.S. Department of Agriculture	10.582	\$ 21,000	\$ 8,000	4473
U.S. Department of Agriculture	10.582	\$ 15,914	15,914	4150
U.S. Department of Energy	Unknown	\$ 21,000	10,000	4473
U.S. Department of Commerce	11.P.L. 108-219	\$ 13,000	<u>13,000</u>	5112
			<u>\$46,914</u>	

Cause: The cause of the above condition is the lack of adequate internal control policies and procedures requiring the documentation of procurement procedures to establish compliance with procurement requirements.

Effect: The effect of the above condition is noncompliance with procurement procedures and questioned costs result.

UTRÖK ATOLL LOCAL GOVERNMENT

Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2009

Finding No.: 2009-1, Continued
Program/Area: Procurement and Suspension and Debarment
Agency/Program Name: U.S. Department of Agriculture - CFDA # 10.582: Commodity Assistance Program
U.S. Department of Commerce - CFDA # 11.P.L. 108-219: Utrök Atoll
Radiological Monitoring Support
U.S. Department of Energy: Charter Costs for Commodity Assistance Program
Questioned Costs: \$46,914

Recommendation: We recommend that UALGOV comply with requisite procurement standards. Specifically, supporting documentation should indicate the history of procurement, including the rationale for and method of procurement, the contractor selection or rejection, and the basis for the contract price.

Auditee Response and Corrective Action Plan: Management recognizes the need to fully comply with the procurement standards. It will ensure that future purchases be properly supported and documented in accordance to the standards.

UTRŌK ATOLL LOCAL GOVERNMENT

Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2009

Local Noncompliance

Finding No. 2009-2

Criteria: RepMar's Procurement Code states the following:

- (a) Section 124 - unless otherwise authorized by law, all Government contracts (including local government Councils) 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. 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 three 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.

Condition: UALGOV's purchase of a \$25,097 bumbum boat and \$72,183 purchase/installation costs of a reverse osmosis desalination unit from non-federal sources did not undergo competitive bidding processes. In addition, total charter costs of \$21,000 (of which \$18,000 was reported under Finding No. 2009-1) did not evidence adequate support of informal procurement procedures. Following are the expenditure details.

<u>Date</u>	<u>Check#/Invoice#</u>	<u>Amount</u>
9/3/2009	Ck. # 5068	\$ 25,097
6/8/2009	Inv. # 10032	63,440
9/3/2009	Inv. # 10034	8,743
4/14/2009	Ck. # 4473	<u>3,000</u>
		<u>\$100,280</u>

Cause: The cause of the above condition is the lack of adequate policies and procedures requiring the documentation of procurement procedures to ensure compliance with procurement requirements.

Effect: The effect of the above condition is noncompliance with procurement procedures.

Recommendation: We recommend that UALGOV comply with requisite procurement standards. Specifically, supporting documentation should indicate the history of procurement, including the rationale for and method of procurement, the contractor selection or rejection, and the basis for the contract price.

Auditee Response and Corrective Action Plan: Management recognizes the need to fully comply with the procurement standards. It will ensure that future purchases be properly supported and documented in accordance to the standards.

UTRŌK ATOLL LOCAL GOVERNMENT

Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2009

Local Noncompliance

Finding No. 2009-3

Criteria: Distribution from the Claims Trust Fund should be made in accordance with the underlying trust agreement. Specifically, section 4.2 (b) of the Claims Trust Fund agreement states that UALGOV shall retain not less than 30% but no more than 85% of the net income arising from the corpus of the Trust. Furthermore, section 5.2 of the Claims Trust Fund agreement states that an invasion of corpus shall not occur more frequently every than once every three years.

Condition: During the year ended September 30, 2009, net income of the Trust Fund was \$434,255, 70% of which amounts to \$303,978 (maximum amount available to be withdrawn from net income). However, total drawdowns for fiscal year 2009 amounted to \$632,973, which exceeded the allowable amount that may be withdrawn by \$328,995.

Cause: The cause of the above condition is distribution of funds from the Claims Trust Fund in excess of the maximum amount allowed per trust agreement.

Effect: The effect of the above condition is the possibility of noncompliance with Claims Trust Fund agreement.

Recommendation: We recommend that UALGOV comply with the trust agreement concerning distributions made from the Claims Trust Fund.

Auditee Response and Corrective Action Plan: Fiscal Year 2009 was a difficult year for Utrik Claims Trust Fund. Although it posted a net income of \$434,255 at the end of the year, it struggled through the instability of the US stock market during the year. As a response to this, the management is looking for ways to minimize the drawdown from UCTF by applying and acquiring grants to help in the operations and reduce the actual expenses to possible level.

UTRŌK ATOLL LOCAL GOVERNMENT

Unresolved Prior Year Findings and Questioned Costs Year Ended September 30, 2009

Questioned Costs

The prior year Single Audit report on compliance with laws and regulations noted the following questioned costs and comments that were unresolved at September 30, 2009:

Questioned costs previously reported	\$ -
Questioned costs of fiscal year 2009 Single Audit	<u>46,914</u>
Unresolved questioned costs at September 30, 2009	\$ <u>46,914</u>

Unresolved Findings

There are no unresolved prior year findings from prior year Single Audits of UALGOV.