

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

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**FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT**

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**YEAR ENDED SEPTEMBER 30, 2011**

# ENEWETAK/UJELANG ATOLL LOCAL GOVERNMENT

## Table of Contents Year Ended September 30, 2011

	<u>Page</u>
I. Independent Auditors' Report	1
II. Basic Financial Statements:	
Government-Wide Financial Statements:	
Statement of Net Assets	3
Statement of Activities	4
Governmental Fund Financial Statements:	
Balance Sheet	5
Statement of Revenues, Expenditures, and Changes in Fund Balances	6
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities	7
Notes to the Basic Financial Statements	8
III. Required Supplementary Information - Other than Management's Discussion and Analysis:	
Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund	21
Notes to the Required Supplementary Information - Budgetary Reporting	22
IV. Independent Auditor's Reports on Internal Control and on Compliance:	
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 <i>Government Auditing Standards</i>	24
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	26
Schedule of Expenditures of Federal Awards	28
Notes to Schedule of Expenditures of Federal Awards	29
Schedule of Findings and Questioned Costs	30
Unresolved Prior Year Findings and Questioned Costs	39

## **INDEPENDENT AUDITORS' REPORT**

Mayor Jackson Ading  
Enewetak/Ujelang Local Government  
Republic of the Marshall Islands:

We have audited the accompanying financial statements of the governmental activities and each major fund of the Enewetak/Ujelang Local Government (EULGOV) as of and for the year ended September 30, 2011, which collectively comprise EULGOV's basic financial statements. These financial statements are the responsibility of EULGOV's management. Our responsibility is to express opinions on the respective financial statements based on our audit.

Except as discussed in the following paragraphs, 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of EULGOV's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

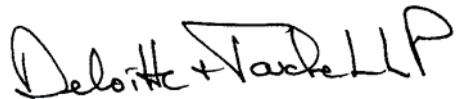
Because of inadequacies in EULGOV's accounting records, we were unable to form an opinion regarding the amounts at which loans receivable are recorded in the accompanying financial statements of the governmental activities and the General Fund at September 30, 2011 (stated at \$2,895,359), or the amount of loan interest income for the year then ended (stated at \$315,554).

As more fully described in Note 6 to the financial statements, EULGOV has not reported derivative instruments in governmental activities. Accounting principles generally accepted in the United States of America require that derivative instruments be recorded at fair value. The amount by which this departure would affect assets, liabilities, net assets, and revenues of the governmental activities has not been determined.

In our opinion, except for the effects of the matters discussed in the preceding paragraphs, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the Enewetak/Ujelang Local Government as of September 30, 2011, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management has omitted the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board (GASB) who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information. The Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund and notes thereto, as set forth in Section III of the foregoing table of contents, is not a required part of the basic financial statements but is supplementary information required by the GASB. This supplementary information is the responsibility of the management of EULGOV. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2019, on our consideration of EULGOV'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 EULGOV'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* and should be considered in assessing the results of our audit.

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

December 20, 2019

ENEWETAK/UJELANG LOCAL GOVERNMENT

Statement of Net Assets  
September 30, 2011

ASSETS

Current assets:	
Cash and cash equivalents	\$ 283,200
Receivables, net	<u>3,078,706</u>
Total current assets	<u>3,361,906</u>
Noncurrent assets:	
Restricted assets:	
Investments	25,348,052
Capital assets, net of accumulated depreciation	<u>1,297,943</u>
Total noncurrent assets	<u>26,645,995</u>
Total assets	<u>\$ 30,007,901</u>

LIABILITIES AND NET ASSETS

Current liabilities:	
Current portion of notes payable	\$ 417,679
Accounts payable	68,474
Withholding taxes payable	37,121
Social security taxes payable	53,194
Interest payable	75,570
Other liabilities and accruals	<u>146,211</u>
Total current liabilities	798,249
Noncurrent liabilities:	
Notes payable, net of current portion	<u>6,225,862</u>
Total liabilities	<u>7,024,111</u>
Commitment and contingency	
Net assets:	
Invested in capital assets	1,297,943
Restricted for:	
Nonexpendable:	
Claims	14,264,590
Resettlement	4,415,696
Unrestricted	<u>3,005,561</u>
Total net assets	<u>22,983,790</u>
Total liabilities and net assets	<u>\$ 30,007,901</u>

See accompanying notes to financial statements.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Statement of Activities  
Year Ended September 30, 2011

	Program Revenues			
Expenses	Charges for Services	Operating Grants and Contributions	Net (Expenses) Revenues and Changes in Net Assets	
<u>Functions/Programs</u>				
Government activities:				
General government	\$ 1,125,457	\$ 378,493	\$ 16,089	\$ (730,875)
Education	76,399	-	-	(76,399)
Public safety	75,263	-	-	(75,263)
Food program	2,010,317	-	1,954,610	(55,707)
Liberation Day	8,025	-	-	(8,025)
Church summer program	6,373	-	-	(6,373)
Nuclear claims related	1,770,692	-	-	(1,770,692)
Unallocated interest - long-term debt	<u>426,597</u>	<u>-</u>	<u>-</u>	<u>(426,597)</u>
	<u>\$ 5,499,123</u>	<u>\$ 378,493</u>	<u>\$ 1,970,699</u>	(3,149,931)
General revenues:				
Investment earnings				315,554
Other				68,350
Contributions to permanent fund				<u>704,401</u>
				<u>1,088,305</u>
				Change in net assets (2,061,626)
				Net assets at the beginning of the year <u>25,045,416</u>
				Net assets at the end of the year <u>\$ 22,983,790</u>

See accompanying notes to financial statements.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Balance Sheet  
Governmental Funds  
September 30, 2011

	General	Special	Permanent		Total
		Revenue	Enjebi	Claims	
<u>ASSETS</u>		Enewetak	Community	Trust	
		Food and	Trust		
		Agricultural			
		Support			
		Program			
Cash and cash equivalents	\$ 283,200	\$ -	\$ -	\$ -	\$ 283,200
Receivables, net	3,027,361	-	8,875	42,470	3,078,706
Restricted assets:					
Investments	<u>-</u>	<u>-</u>	<u>4,406,821</u>	<u>20,941,231</u>	<u>25,348,052</u>
	\$ <u>3,310,561</u>	\$ <u>-</u>	\$ <u>4,415,696</u>	\$ <u>20,983,701</u>	\$ <u>28,709,958</u>
<u>LIABILITIES AND FUND BALANCE</u>					
Liabilities:					
Accounts payable	\$ 68,474	\$ -	\$ -	\$ -	\$ 68,474
Withholding taxes payable	37,121	-	-	-	37,121
Social security taxes payable	53,194	-	-	-	53,194
Other liabilities and accruals	9,588	-	-	-	9,588
Due to other funds	<u>136,623</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>136,623</u>
Total liabilities	<u>305,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>305,000</u>
Commitment and contingency					
Fund balance:					
Restricted:					
Claims	13,796	-	-	20,983,701	20,997,497
Resettlement	-	-	4,415,696	-	4,415,696
Committed:					
Community loan program	2,973,975	-	-	-	2,973,975
Unassigned	<u>17,790</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>17,790</u>
Total fund balance	<u>3,005,561</u>	<u>-</u>	<u>4,415,696</u>	<u>20,983,701</u>	<u>28,404,958</u>
Total liabilities and fund balance	\$ <u>3,310,561</u>	\$ <u>-</u>	\$ <u>4,415,696</u>	\$ <u>20,983,701</u>	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds 1,297,943

Long-term liabilities, including notes payable, are not due and payable in the current period and therefore are not reported in the funds. The liabilities include:

Notes payable	(6,643,541)	
Accrued interest payable	<u>(75,570)</u>	
		<u>(6,719,111)</u>
		\$ <u>22,983,790</u>

See accompanying notes to financial statements.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Statement of Revenues, Expenditures, and Changes in Fund Balance  
Governmental Funds  
Year Ended September 30, 2011

		Special Revenue	Permanent		
	General	Enewetak Food and Agricultural Support Program	Enjebi Community Trust	Claims Trust	Total
Revenues:					
Federal grants	\$ -	\$ 1,954,610	\$ -	\$ -	\$ 1,954,610
Other grants	16,089	-	-	-	16,089
Dividends and interest	315,554	-	93,881	445,952	855,387
Net change in fair value of investments	-	-	33,124	243,630	276,754
Fares and freight	65,638	-	-	-	65,638
Boat charter	273,984	-	-	-	273,984
Fuel sales	16,225	-	-	-	16,225
Licenses and fees	22,646	-	-	-	22,646
Other	<u>68,350</u>	<u>-</u>	<u>5,551</u>	<u>20,464</u>	<u>94,365</u>
Total revenues	<u>778,486</u>	<u>1,954,610</u>	<u>132,556</u>	<u>710,046</u>	<u>3,575,698</u>
Expenditures:					
General government	1,017,050	-	-	-	1,017,050
Education	76,399	-	-	-	76,399
Public safety	75,263	-	-	-	75,263
Distributions	1,770,692	-	-	-	1,770,692
Food program	-	1,954,610	-	-	1,954,610
Liberation Day	8,025	-	-	-	8,025
Church summer program	6,373	-	-	-	6,373
Investment management	-	-	30,254	107,947	138,201
Capital projects	109,740	-	-	-	109,740
Debt service:					
Principal	392,563	-	-	-	392,563
Interest	<u>437,170</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>437,170</u>
Total expenditures	<u>3,893,275</u>	<u>1,954,610</u>	<u>30,254</u>	<u>107,947</u>	<u>5,986,086</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(3,114,789)</u>	<u>-</u>	<u>102,302</u>	<u>602,099</u>	<u>(2,410,388)</u>
Other financing sources (uses):					
Operating transfers in	2,994,773	-	-	-	2,994,773
Operating transfers out	<u>-</u>	<u>-</u>	<u>(453,000)</u>	<u>(2,541,773)</u>	<u>(2,994,773)</u>
Total other financing sources (uses), net	<u>2,994,773</u>	<u>-</u>	<u>(453,000)</u>	<u>(2,541,773)</u>	<u>-</u>
Net change in fund balance	(120,016)	-	(350,698)	(1,939,674)	(2,410,388)
Fund balance at the beginning of the year	<u>3,125,577</u>	<u>-</u>	<u>4,766,394</u>	<u>22,923,375</u>	<u>30,815,346</u>
Fund balance at the end of the year	\$ <u>3,005,561</u>	\$ <u>-</u>	\$ <u>4,415,696</u>	\$ <u>20,983,701</u>	\$ <u>28,404,958</u>

See accompanying notes to financial statements -6-



**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Reconciliation of the Statement of Revenues, Expenditures,  
and Changes in Fund Balances of Governmental Funds  
to the Statement of Activities  
Year Ended September 30, 2011

Net change in fund balances - total governmental funds \$ (2,410,388)

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. For the current year, these amounts consist of:

Capital outlays, net of disposals	\$ 195,121	
Depreciation, net	<u>(249,495)</u>	(54,374)

The issuance of long-term debt (e.g. bonds, lease) provides current financial resources to governmental funds, while repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction has any effect on net assets. For the current year, these amounts consist of:

Repayment of notes payable	392,563
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Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds. For the current year, these activities consist of:

Change in accrued interest payable	<u>10,573</u>
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Change in net assets of governmental activities	<u>\$ (2,061,626)</u>
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See accompanying notes to financial statements.

## ENEWETAK/UJELANG LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2011

### (1) Organization

The Enewetak/Ujelang Local Government (EULGOV) was established pursuant to Public Law 1981-2, the Local Government Act of the Republic of the Marshall Islands and operates under the Constitution of the Enewetak/Ujelang Local Government. EULGOV is governed by an elected mayor and a fifteen-member Council.

### (2) Summary of Significant Accounting Policies

The accompanying financial statements of EULGOV have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as applied to government units. The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of EULGOV's accounting policies are described below.

#### A. Government-Wide Financial Statements

The Statement of Net Assets and the Statement of Activities report financial information on all of the non-fiduciary activities of EULGOV. For the most part, the effect of interfund activity has been eliminated from these statements. EULGOV's activities are defined as governmental activities, which are supported by intergovernmental revenues and other non-exchange revenues.

The Statement of Net Assets presents all of EULGOV's non-fiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt that are attributed to the acquisition, construction or improvement of those assets.
- Restricted net assets – nonexpendable consists of permanent funds in which donors or other outside sources have stipulated that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to the principal.
- Unrestricted net assets consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, (for example, internally restricted), to indicate that management does not consider them to be available for general operations.

The Statement of Activities demonstrates the degree to which the direct expenses of given functions or segments are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function or segment. Program revenues include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items not meeting the definition of program revenues are, instead, reported as general revenue.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(2) Summary of Significant Accounting Policies, Continued

B. Fund Financial Statements

The fund financial statements present a balance sheet and a statement of revenues, expenditures, and changes in fund balances for EULGOV's major funds. Major individual governmental funds are reported as separate columns in the fund financial statements pursuant to GASB reporting standards.

EULGOV reports its financial position and results of operations in funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures/expenses. Transactions between funds within a fund type, if any, have not been eliminated.

C. Measurement Focus and Basis of Accounting

Government-Wide Financial Statements:

The government-wide financial statements are reported using the economic resources management focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Amounts reported as program revenue include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as general revenues rather than as program revenues. General revenue is derived from taxation, investment income and other fees that are not allocated to specific programs.

Governmental Fund Financial Statements:

Governmental fund financial statements account for the general governmental activities of EULGOV and are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as they become susceptible to accrual; generally when they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, EULGOV considers revenues to be available if they are collected within 90 days of the end of the current fiscal period.

Miscellaneous revenues from other financing sources are recognized when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available. Investments and related investment earnings are recorded at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Expenditures generally are recorded in the period in which the related fund liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

## ENEWETAK/UJELANG LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2011

### (2) Summary of Significant Accounting Policies, Continued

#### C. Measurement Focus and Basis of Accounting, Continued

Governmental Fund Financial Statements, Continued:

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*, sets forth minimum criteria (percentage of the assets, liabilities, revenues or expenditures/expenses for either fund category or the governmental and enterprise funds combined) for the determination of major funds. Major individual governmental funds are reported as separate columns in the fund financial statements. EULGOV reports the following major funds:

General Fund - This fund is the primary operating fund of EULGOV used to account for all governmental transactions, except those required to be accounted for in another fund.

Enewetak Food and Agricultural Support Program Fund - a special revenue fund that accounts for all financial transactions of direct grants received from the U.S. Department of the Interior related to the provision of water-borne transportation of agricultural products to Enewetak including operations and maintenance of the vessel used for such purposes.

Enjebi Community Trust Fund - a permanent fund that accounts for United States Congress appropriations under United States Public Law 99-239, which was paid and distributed in accordance with an agreement between the Government of the United States, the Government of the Republic of the Marshall Islands and EULGOV to assist in the resettlement of Enjebi Island by the people of Enewetak.

Claims Trust Fund - a permanent that accounts for funds received under Article II, Section 3, of the agreement between the Government of the United States and the Government of the Republic of the Marshall Islands for the implementation of Section 177 of the Compact of Free Association (the Compact). In accordance with Article II, Section 8, of the Compact, EULGOV executed the Enewetak/Ujelang Claims Trust agreement and established the Claims Trust Fund. Pursuant to Section 7.2 of the trust agreement, after the final payment was received on October 27, 2001, the Claims Trust Fund was required to distribute annually to the people of Enewetak between 15% and 35% of its net income. In addition, pursuant to Section 8.1 of the trust agreement, EULGOV may also invade up to 3% of the corpus of the Claims Trust Fund. Such invasion may occur in the event of an unforeseen natural disaster or other similar circumstance, as determined by the sole discretion of EULGOV, in order to prevent hardship to the people of Enewetak. An invasion of the corpus shall not occur more frequently than once every three years.

#### D. Cash and Cash Equivalents

Cash and cash equivalents include cash held in demand deposits as well as short-term investments with a maturity date within three months of the date acquired by EULGOV.

#### E. Investments

Investments are carried at fair value. Fair value is the amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(2) Summary of Significant Accounting Policies, Continued

F. Receivables

Loans receivable are due from individuals located within the Republic of the Marshall Islands and are stated at the unpaid balances less the allowances for losses. Interest on loans is calculated using the simple interest method on daily balances of the principal amount outstanding.

The allowances for loan losses is established through a provision for losses charged to expense. Loans are charged against the allowance 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 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 consist of amounts advanced to individuals, on an unsecured basis, substantially all of whom are situated in the Republic of the Marshall Islands. Receivables are stated net of allowances for uncollectable accounts.

Receivables as of September 30, 2011, for the primary government's individual major governmental funds, including applicable allowance for uncollectible accounts, are as follows:

	<u>General Fund</u>	Enewetak Food and Agricultural Support Program Fund	Enjebi Community Trust Fund	Claims Trust Fund	<u>Total</u>
Receivables:					
Loans	\$ 2,895,359	\$ -	\$ -	\$ -	\$ 2,895,359
Interest and dividends	78,616	-	8,875	42,470	129,961
Employees	97,790	-	-	-	97,790
Other	<u>13,531</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>13,531</u>
	3,085,296	-	8,875	42,470	3,136,641
Less allowance for doubtful debts	<u>(57,935)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(57,935)</u>
	<u>\$ 3,027,361</u>	<u>\$ -</u>	<u>\$ 8,875</u>	<u>\$ 42,470</u>	<u>\$ 3,078,706</u>

G. Interfund Receivables/Payables

During the course of its operations, EULGOV records transactions between individual funds for goods provided or services rendered. Receivables and payables resulting from transactions between funds are classified as "due from other funds" or "due to other funds" on the governmental funds balance sheet.

H. Restricted Assets

Certain assets of EULGOV are classified as restricted assets because their use is completely restricted by trust agreements or loan pledge agreements. Specifically, investments recorded in the Enjebi Community Trust Fund and the Claims Trust Fund of \$4,406,821 and \$20,941,231, respectively, are restricted in that they are not available to be used in current operations.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(2) Summary of Significant Accounting Policies, Continued

I. Capital Assets

Capital assets, which include property, plant and equipment and infrastructure assets (e.g. roads, docks, airports, water catchments, and other similar items), whether purchased or constructed, are recorded at historical cost. Asset acquisitions of \$5,000 and above are capitalized. Depreciation is provided over the estimated useful lives of the assets through use of the straight-line method.

The estimated useful lives of these assets are as follows:

Buildings	10 years
Motor vehicles	4 years
Vessel and marine equipment	4 - 10 years
Machinery and equipment	4 years
Furniture and equipment	4 years

J. Interfund/Intrafund Transactions

As a general rule, the effect of interfund activity has been eliminated in the government-wide statements. Exceptions to this rule are: 1) activities between funds reported as governmental activities and funds reported as business-type activities and 2) activities between funds that are reported in different functional categories in either the governmental or business-type activities column. Elimination of these activities would distort the direct costs and program revenues for the functions concerned.

K. Fund Equity

GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, was implemented, effective for the fiscal year ending September 30, 2011. It establishes fund balance classifications based on the extent to which RepMar is bound to honor constraints on the specific purposes for which amounts in those funds can be spent. As a result of implementing this statement, there were significant changes in RepMar's fund structure. Funds that did not meet the new special revenue fund definition were moved to the General Fund. Amounts previously reported as reserved and unreserved fund balance are now reported under the following fund balance classifications:

- Non-spendable - includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.
- Restricted - includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.
- Committed - includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision making authority and does not lapse at year-end.
- Assigned - includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed.
- Unassigned includes negative fund balances in other governmental funds.

## ENEWETAK/UJELANG LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2011

### (2) Summary of Significant Accounting Policies, Continued

#### K. Fund Equity, Continued

EULGOV has a general policy to first use restricted resources for expenditures incurred for which both restricted and unrestricted (committed, assigned, and unassigned) resources are available. When expenditures are incurred for which only unrestricted resources are available, the general policy of EULGOV is to use committed resources first, followed by assigned, and then unassigned. The use of restricted/committed resources may be deferred based on a review of the specific transaction.

A formal minimum fund balance policy has not been adopted.

#### L. Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the general purpose financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

#### M. New Accounting Standards

During fiscal year 2011, EULGOV implemented the following pronouncements:

- GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The implementation of this statement did not have a material effect on the financial statements of EULGOV.
- GASB Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools. The implementation of this statement did not have a material effect on the financial statements of EULGOV.

In December 2009, GASB issued Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which addresses issues related to the use of the alternative measurement method and the frequency and timing of measurements by employers that participate in agent multiple-employer other postemployment benefit (OPEB) plans. The provisions of this Statement are effective for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of EULGOV.

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of EULGOV.

## ENEWETAK/UJELANG LOCAL GOVERNMENT

Notes to Financial Statements  
September 30, 2011

### (2) Summary of Significant Accounting Policies, Continued

#### M. New Accounting Standards, Continued

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*, which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity*, and No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of EULGOV.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of EULGOV.

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of EULGOV.

In July 2011, GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions (an amendment of GASB Statement No. 53)*, which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The provisions of this statement are effective for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of EULGOV.

### (3) Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposit and investment risks.

EULGOV does not have formal deposit and investment policies. Investments in the Enjebi Community Trust Fund and the Claims Trust Fund are governed by their respective trust agreements.



**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(3) Deposits and Investments, Continued

A. Deposits

Custodial credit risk is the risk that in the event of a bank failure, EULGOV'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. EULGOV does not have a deposit policy for custodial credit risk.

As of September 30, 2011, the carrying amount of EULGOV's total cash and cash equivalents was \$283,200 and the corresponding bank balances were \$379,309, which are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2011, bank deposits in the amount of \$266,607 were FDIC insured. EULGOV 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.

B. Investments

As of September 30, 2011, investments at fair value are as follows:

	Enjebi Community <u>Trust</u>	Claims <u>Trust</u>	<u>Total</u>
Cash management	\$ 170,370	\$ 367,163	\$ 537,533
Fixed income	634,779	3,156,042	3,790,821
Mutual funds	80,972	403,197	484,169
Common equities	1,913,001	9,361,041	11,274,042
Real Estate	108,065	870,727	978,792
Hedge funds	935,944	4,270,034	5,205,978
Other	<u>563,690</u>	<u>2,513,027</u>	<u>3,076,717</u>
	<u>\$ 4,406,821</u>	<u>\$ 20,941,231</u>	<u>\$ 25,348,052</u>

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, EULGOV will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. EULGOV's investments are held and administered by trustees in accordance with various trustee agreements. Based on negotiated trust and custody contracts, all of these investments were held in EULGOV's name by EULGOV's custodial financial institutions at September 30, 2011.

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. EULGOV does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for EULGOV. As of September 30, 2011, there were no investments in any one issuer that exceeded 5% of total investments.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(3) Deposits and Investments, Continued

B. Investments, Continued

As of September 30, 2011, maturities of investments in fixed income securities is as follows:

<u>Maturity</u>	<u>Enjebi Community Trust</u>	<u>Claims Trust</u>	<u>Total</u>
Less than 1 year	\$ 10,000	\$ 51,000	\$ 61,000
1 - 5 years	200,000	995,000	1,195,000
6 - 10 years	108,159	598,847	707,006
11 - 15 years	53,927	408,019	461,946
Over 15 years	<u>214,682</u>	<u>857,031</u>	<u>1,071,713</u>
	<u>\$ 586,768</u>	<u>\$ 2,909,897</u>	<u>\$ 3,496,665</u>

The above maturity schedule includes cash equivalents maturing within six months and excludes preferred stocks and fixed income funds.

As of September 30, 2011, credit ratings of investments in fixed income securities is as follows:

<u>Moody's Rating</u>	<u>Enjebi Community Trust</u>	<u>Claims Trust</u>	<u>Total</u>
Aaa	\$ 291,313	\$ 1,454,594	\$ 1,745,907
Aa	46,645	249,097	295,742
A	128,265	647,089	775,354
Other rated	152,956	763,190	916,146
Non-Rated	<u>15,600</u>	<u>42,072</u>	<u>57,672</u>
	<u>\$ 634,779</u>	<u>\$ 3,156,042</u>	<u>\$ 3,790,821</u>

(4) Capital Assets

Capital asset activities for the year ended September 30, 2011, is as follows:

	<u>Balance October 1, 2010</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance September 30, 2011</u>
Buildings	\$ 154,582	\$ 125,631	\$ -	\$ 280,213
Motor vehicles	244,935	69,490	-	314,425
Vessel and marine equipment	1,428,200	-	-	1,428,200
Machinery and equipment	163,418	-	-	163,418
Furniture and equipment	<u>10,433</u>	<u>-</u>	<u>-</u>	<u>10,433</u>
	2,001,568	195,121	-	2,196,689
Less accumulated depreciation	<u>(649,251)</u>	<u>(249,495)</u>	<u>-</u>	<u>(898,746)</u>
	<u>\$ 1,352,317</u>	<u>\$ (54,374)</u>	<u>\$ -</u>	<u>\$ 1,297,943</u>

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(4) Capital Assets, Continued

Depreciation expense was charged to the following functions:

General government	\$ 159,793
Food program	<u>89,702</u>
	\$ <u>249,495</u>

(5) Loan Payable

In 2001 and 2003, EULGOV obtained bank loans of \$2,585,000 and \$2,000,000, respectively, to fund distributions to the people of Enewetak. In 2004, the principal sums owing on these loan facilities were consolidated into one credit facility with an outstanding principal balance of \$3,700,000. In addition, EULGOV obtained a \$3,000,000 bank loan to fund distributions to the people of Enewetak. In 2007, the principal sums owing on these loan facilities were consolidated into one credit facility with an outstanding principal balance of \$8,000,000, interest at 3-Month LIBOR plus 1% (1.25% at September 30, 2011). Simultaneously, EULGOV entered into an interest rate swap agreement with a fixed rate of 6.3% per annum with a termination date of October 27, 2022. Quarterly principal payments to be paid on the 27th day of October, January, April, and July commence January 27, 2008 in the amount of \$82,723 increasing to \$197,104 on January 27, 2022. The loan is collateralized by the assignment and pledge of certain investment holdings held by EULGOV in the Claims Trust Fund together with investment earnings to be received by EULGOV from the Claims Trust Fund. The term of the loan is for fifteen years and matures on October 27, 2022. As of September 30, 2011, the amount outstanding and payable on this loan totaled \$6,643,541.

The change in loans payable during the year ended September 30, 2011, is as follows:

<u>Balance</u> <u>October 1, 2010</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance</u> <u>September 30, 2011</u>	<u>Due Within</u> <u>12 months</u>
\$ <u>7,036,104</u>	\$ _____ -	\$ <u>(392,563)</u>	\$ <u>6,643,541</u>	\$ <u>417,679</u>

Future debt interest payments are calculated using rates applicable to the scheduled payment nearest to September 30, 2011 for variable rate debt. The net swap payments are calculated by subtracting the projected future variable rate interest payment per the swap agreement from the projected future fixed rate payment per the swap agreement. Projected future variable rate payments on the swap agreement are based on variable rates applicable to the scheduled payment nearest to September 30, 2011.

Annual debt service requirements to maturity for variable-rate debt hedged by an interest rate swap agreement are as follows:

<u>Year ending</u> <u>September 30,</u>	<u>Variable-Rate Debt</u>			
	<u>Principal</u>	<u>Interest</u>	<u>Interest</u> <u>Rate</u> <u>Swap, Net</u>	<u>Total</u>
2012	\$ 417,679	\$ 88,845	\$ 323,813	\$ 830,337
2013	444,402	82,993	303,333	830,728
2014	472,835	76,766	281,423	831,024
2015	503,087	70,141	257,136	830,364
2016	535,275	63,092	231,294	829,661
2017 - 2021	3,236,058	192,891	707,135	4,136,084
2022 - 2023	<u>1,034,205</u>	<u>11,139</u>	<u>40,836</u>	<u>1,086,180</u>
	\$ <u>6,643,541</u>	\$ <u>585,867</u>	\$ <u>2,144,970</u>	\$ <u>9,374,378</u>

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(6) Derivative Instruments

Derivative instruments such as interest rate and commodity swaps, interest rate locks, options (caps, floors, and collars), swaptions, forward contracts, and futures contracts are entered into by governments as investments; as hedges of identified financial risks associated with assets or liabilities, or expected transactions (i.e., hedgeable items); to lower the costs of borrowings; to effectively fix cash flows or synthetically fix prices; or to offset the changes in fair value of hedgeable items. GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, requires derivative instruments to be reported at fair value in the government-wide financial statements. The changes in fair value of hedging derivative instruments do not affect investment revenue but are required to be reported as deferred outflows of resources or deferred inflows of resources. Alternatively, the changes in fair value of investment derivative instruments (which include ineffective hedging derivative instruments) are required to be reported as part of investment revenue in the current reporting period. As of September 30, 2011, EULGOV was unable to ascertain the fair value of the derivative instrument associated with the interest rate swap agreement discussed in Note 5.

(7) Social Security Taxes Payable

At September 30, 2011, EULGOV was liable for social security taxes in the amount of \$53,194, including certain delinquent social security taxes of \$26,484, payable to the Marshall Islands Social Security Administration (MISSA). In 2010, EULGOV and MISSA entered into a promissory note agreement for delinquent taxes. The terms of the agreement includes monthly payments of \$2,000, inclusive of interest at 12% per annum, commencing February 10, 2010 increasing to \$3,000 commencing February 10, 2011 with final payment due on July 10, 2012.

The change in delinquent social security taxes payable during the year ended September 30, 2011, is as follows:

<u>Balance</u> <u>October 1, 2010</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance</u> <u>September 30, 2011</u>	<u>Due Within</u> <u>12 months</u>
<u>\$ 53,356</u>	<u>\$ -</u>	<u>\$ (26,872)</u>	<u>\$ 26,484</u>	<u>\$ 26,484</u>

(8) Commitment

EULGOV entered into an office lease agreement for a term of five years commencing February 1, 2011. Annual rent payments amount to \$12,000.

(9) Contingency

It is EULGOV's policy to record the cost of sick leave when leave is actually taken and a liability is actually incurred. The accumulated estimated amount of unused sick leave at September 30, 2011 is not available.

(10) Risk Management

EULGOV 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. EULGOV has elected to purchase commercial insurance from independent third parties for the risks of loss to which it believes it to be exposed. Settled claims have not exceeded this commercial coverage in any of the past three years.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Notes to Financial Statements  
September 30, 2011

(11) Subsequent Event

On March 31, 2016, EULGOV entered into a settlement agreement with Bank of America whereby Bank of America agreed to forgive the outstanding principal balance of \$4,541,985 associated with the \$8,000,000 loan.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

**REQUIRED SUPPLEMENTARY INFORMATION  
- BUDGETARY REPORTING**

**YEAR ENDED SEPTEMBER 30, 2011**

## ENEWETAK/UJELANG LOCAL GOVERNMENT

### Schedule of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual - General Fund Year Ended September 30, 2011

	Budgeted Amounts		Actual	Variance with
	Original	Final		Final Budget - Positive (Negative)
<b>Revenues:</b>				
Other grants	\$ 16,000	\$ 16,000	\$ 16,089	\$ 89
Dividends and interest	450,000	450,000	315,554	(134,446)
Fares and freight	100,000	100,000	65,638	(34,362)
Boat charter	-	-	273,984	273,984
Fuel sales	-	-	16,225	16,225
Licenses and fees	40,000	40,000	22,646	(17,354)
Other	-	-	68,350	68,350
<b>Total revenues</b>	<b><u>606,000</u></b>	<b><u>606,000</u></b>	<b><u>778,486</u></b>	<b><u>172,486</u></b>
<b>Expenditures:</b>				
General government	764,490	764,490	1,017,050	(252,560)
Education	122,100	122,100	76,399	45,701
Public safety	92,450	92,450	75,263	17,187
Distributions	2,080,000	2,080,000	1,770,692	309,308
Liberation Day	10,000	10,000	8,025	1,975
Church summer program	12,000	12,000	6,373	5,627
Capital projects	-	-	109,740	(109,740)
Debt service	829,117	829,117	829,733	(616)
<b>Total expenditures</b>	<b><u>3,910,157</u></b>	<b><u>3,910,157</u></b>	<b><u>3,893,275</u></b>	<b><u>16,882</u></b>
<b>Deficiency of revenues under expenditures</b>	<b><u>(3,304,157)</u></b>	<b><u>(3,304,157)</u></b>	<b><u>(3,114,789)</u></b>	<b><u>189,368</u></b>
<b>Other financing sources:</b>				
Loan proceeds	1,000,000	1,000,000	-	(1,000,000)
Operating transfers in from the Enjebi Trust Fund	453,000	453,000	453,000	-
Operating transfers in from the Claims Trust Fund	1,851,157	1,851,157	2,541,773	690,616
<b>Total other financing sources</b>	<b><u>3,304,157</u></b>	<b><u>3,304,157</u></b>	<b><u>2,994,773</u></b>	<b><u>(309,384)</u></b>
<b>Deficiency of revenues and other financing sources under expenditures</b>	<b>-</b>	<b>-</b>	<b>(120,016)</b>	<b>(120,016)</b>
<b>Fund balance at beginning of year</b>	<b><u>3,125,577</u></b>	<b><u>3,125,577</u></b>	<b><u>3,125,577</u></b>	<b><u>-</u></b>
<b>Fund balance at end of year</b>	<b><u>\$ 3,125,577</u></b>	<b><u>\$ 3,125,577</u></b>	<b><u>\$ 3,005,561</u></b>	<b><u>\$ (120,016)</u></b>

See accompanying notes to required supplementary information - budgetary reporting

## ENEWETAK/UJELANG LOCAL GOVERNMENT

Notes to Required Supplementary Information - Budgetary Information  
September 30, 2011

### Budgetary Information

The EULGOV Constitution provides for the Executive Committee to introduce into the Council, the proposed budget for the Fiscal Year effective October 1. The budget includes estimates of the proposed expenditures for all the funds and the sources of funds. The Executive members of the EULGOV Council review and recommend changes to the proposed budget during the budget deliberation prior to presentation to the Council. EULGOV council meeting holds public hearing/s during which the Council presents to the constituents the proposed budget for the coming fiscal year. After all of the feedbacks are heard, the Council en banc amends, if necessary, and then approves the budget through an ordinance duly enacted by the EULGOV Council.

The Appropriation Ordinance for fiscal year 2011 was passed by the Council on August 26, 2010. Formal budget integration is employed as a management control device during the year for all funds. The Executive Council has the authority to reprogram budgeted estimates in accordance with the EULGOV Constitution. All annual appropriations lapse at the end of the fiscal year unless otherwise specified in the Ordinance. Supplemental appropriations may occur throughout the year. Unexpended encumbrances at each fiscal year end are carried forward until they are expended or canceled without further ordinance for the matter.

Encumbrance accounting has not been utilized by the General Fund.



**ENEWETAK/UJELANG LOCAL GOVERNMENT**

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

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**YEAR ENDED SEPTEMBER 30, 2011**

**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 Jackson Ading  
Enewetak/Ujelang Local Government  
Republic of the Marshall Islands:

We have audited the financial statements of the governmental activities and each major fund of the Enewetak/Ujelang Local Government (EULGOV) as of and for the year ended September 30, 2011, which collectively comprise EULGOV's basic financial statements and have issued our report thereon dated December 20, 2019. Our report was modified to include qualifications due to the inadequacies of accounting records for loans receivable and the lack of recording derivative instruments at fair value. Except as discussed in the preceding sentence, 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 EULGOV is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered EULGOV's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of EULGOV's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of EULGOV's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

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. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 2011-001, 2011-002, 2011-003, 2011-004 and 2011-006 to be material weaknesses.

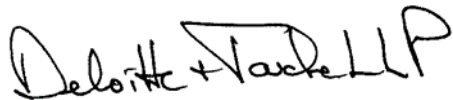
A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 2011-001, 2011-002, 2011-003, 2011-004 and 2011-006 to be significant deficiencies.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether EULGOV's basic 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 2011-004 and 2011-005.

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

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



December 20, 2019

**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 Jackson Ading  
Enewetak/Ujelang Local Government  
Republic of the Marshall Islands:

## **Compliance**

We have audited the Enewetak/Ujelang Local Government's (EULGOV) 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 each of its major federal programs for the year ended September 30, 2011. EULGOV's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of EULGOV's management. Our responsibility is to express an opinion on EULGOV'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 EULGOV'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 EULGOV's compliance with those requirements.

In our opinion, EULGOV complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2011.

## **Internal Control Over Compliance**

Management of EULGOV 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 EULGOV'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 EULGOV'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 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 weakness, as defined above.

### **Schedule of Expenditures of Federal Awards**

We have audited the financial statements of the governmental activities and each major fund of EULGOV as of and for the year ended September 30, 2011, and have issued our report thereon dated December 20, 2019, which report was qualified due to the inadequacies of accounting records for loans receivable and the lack of recording derivative instruments at fair value. Our audit was performed for the purpose of forming our opinions on the financial statements that collectively comprise EULGOV's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards 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 EULGOV. 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.

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

December 20, 2019

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Expenditures of Federal Awards  
Year Ended September 30, 2011

<u>CFDA#</u>	<u>Agency/Program</u>	<u>Federal Expenditures</u>
	<u>U.S. Department of the Interior</u>	
	Funds received in a direct capacity:	
15.875	Operation of the Enewetak Food and Agricultural Support Program	<u>\$ 1,954,610</u>

See accompanying notes to schedule of expenditures of federal awards.

## ENEWETAK/UJELANG LOCAL GOVERNMENT

### Notes to Schedule of Expenditures of Federal Awards Year Ended September 30, 2011

#### (1) Scope of Review

The Enewetak/Ujelang Local Government (EULGOV) is a governmental entity governed by its own Constitution. All significant operations of EULGOV 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 EULGOV's cognizant agency for the Single Audit. EULGOV 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.

EULGOV is also the recipient of non-Compact funds received from the U.S. Department of the Interior. These funds must be expended in accordance with grant awards and are subject to general U.S. federal requirements, including OMB's Circular A-87 and Circular A-102.

#### (2) Summary of Significant Accounting Policies

##### a. Basis of Accounting

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of EULGOV 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. For federal direct assistance grants, authorizations represent the total allotment or grant award received. For Compact of Free Association programs, authorizations represent total current year allotments plus any prior year excess over program expenditures. All expenses and capital outlays are reported as expenditures.

##### b. Indirect Cost Allocation

EULGOV has not entered into an approved indirect cost negotiation agreement covering fiscal year 2011. EULGOV did not charge federal programs for indirect costs during fiscal year 2011.

##### c. CFDA # 15.875

CFDA # 15.875 represents the Office of Insular Affairs (OIA), U. S. Department of the Interior. Funding from this source is subject to varying rules and regulations since OIA administers the Compact of Free Association (the Compact), which is a treaty, and is not a federal program. The Compact is comprised of various funded programs, each with separate compliance requirements. To maximize audit coverage of OIA funding, the OIG has recommended that programs administered under CFDA # 15.875 be grouped by like compliance requirements and such groupings be separately evaluated as major programs.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Findings and Questioned Costs  
Year Ended September 30, 2011

**Section I - Summary of Auditor's Results**

*Financial Statements*

- |    |   |                          |
|----|---|--------------------------|
| 1. | Type of auditors' report issued:  | Unmodified and Qualified |
|    | Internal control over financial reporting:  |                          |
| 2. | Material weakness(es) identified?   | Yes                      |
| 3. | Significant deficiency(ies) identified that are not considered to be material weakness(es)? | None reported            |
| 4. | Noncompliance material to the financial statements noted?                                   | Yes                      |

*Federal Awards*

- |               |  |               |                                |        |   |  |
|---------------|--|---------------|--------------------------------|--------|---|--|
|               | Internal control over major programs:  |               |                                |        |   |  |
| 5.            | Material weakness(es) identified?  | No            |                                |        |   |  |
| 6.            | Significant deficiency(ies) identified that are not considered to be material weakness(es)?  | None reported |                                |        |   |  |
| 7.            | Type of auditors' report issued on compliance for major programs:  | Unmodified    |                                |        |   |  |
| 8.            | Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?   | No            |                                |        |   |  |
| 9.            | EULGOV's major programs were as follows:   |               |                                |        |   |  |
|               | <table border="0"> <tr> <td style="text-align: center;"><u>CFDA #</u></td> <td style="text-align: center;"><u>Name of Federal Program</u></td> </tr> <tr> <td style="text-align: center;">15.875</td> <td style="text-align: center;">Economic, Social and Political Development of the Territories and the Freely Associated States:<br/>Enewetak Food and Agricultural Support Program</td> </tr> </table> | <u>CFDA #</u> | <u>Name of Federal Program</u> | 15.875 | Economic, Social and Political Development of the Territories and the Freely Associated States:<br>Enewetak Food and Agricultural Support Program |  |
| <u>CFDA #</u> | <u>Name of Federal Program</u>   |               |                                |        |   |  |
| 15.875        | Economic, Social and Political Development of the Territories and the Freely Associated States:<br>Enewetak Food and Agricultural Support Program  |               |                                |        |   |  |
| 10.           | Dollar threshold used to distinguish between Type A and Type B Programs, as those terms are defined in OMB Circular A-133:   | \$300,000     |                                |        |   |  |
| 11.           | EULGOV qualified as a low-risk auditee, as that term is defined in OMB Circular A-133?   | No            |                                |        |   |  |



**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2011

**Section II - Financial Statement Findings**

<u>Reference Number</u>	<u>Findings</u>
2011-001	Distribution Payments
2011-002	Loans Receivable
2011-003	Derivative Instruments
2011-004	Expenditures/RMI Procurement
2011-005	Loans Payable
2011-006	Employee Receivables/Credit Card Usage

**Section III - Federal Award Findings and Questioned Costs**

No matters are reportable.

## ENEWETAK/UJELANG LOCAL GOVERNMENT

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2011

Finding No.: 2011-001  
Area: Distribution Payments

Criteria: Disbursements from the Enewetak Distribution Authority (EDA) should be made to the designated payee based on the number of eligible household members per the Quarterly Distribution Listing.

Condition: We tested thirty-three distribution payments made to the people of Enewetak and noted the following exceptions:

1. Eleven disbursements (check #s 6353, 6551, 7129, 7865, 7972, 10038, 10880, 10991, 11682, 11793 and 11993) showed no indication of the recipients signing as evidence of the check receipt.
2. Two disbursements (check #s 7609 and 10662) lacked evidence of authorization of check receipt by representatives of recipients.
3. Three disbursements (check #s 6709, 6919 and 11124) were not evidenced by the underlying check payment and corresponding check register.

Cause: The cause of the above condition is the lack of adequate controls over distribution payments.

Effect: The effect of the above condition is the inability to determine whether the designated payees received distribution payments.

Recommendation: We recommend that management obtain written authorization and that such be kept on file before distribution checks are released to anyone other than the designated payee. In addition, we recommend that the designated payee, upon receipt, acknowledge all disbursements received in writing. Furthermore, we recommend that management require that birth certificates are maintained on file supporting the recipient's share of distribution.

Prior Year Status: The lack of adequate controls over distribution payments was reported as a finding in the Single Audits of EULGOV for fiscal years 2006 through 2010.

Auditee Response and Corrective Action Plan: Authorization is to be obtained prior to the release of checks and the payee or authorized representative acknowledge receipt of check by signing the check stub.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2011

Finding No.: 2011-002  
Area: Loans Receivable

Criteria: An adequate system of internal control requires that accounting records be maintained over loans receivable whereby a subsidiary loan ledger be maintained showing transaction and payment history separately for each customer to whom credit has been extended.

Condition: At September 30, 2011, loans receivable of \$2,895,359 were not reconciled to and supported by a subsidiary loan ledger together with loan interest income and processing fees of \$315,554 that was recognized for the year then ended.

Cause: The cause of the above condition is the lack of adequate controls over backup procedures to allow for recovery of the subsidiary loan ledger from the computerized loan management system.

Effect: The effect of the above condition is the inability to determine that loans receivable are included in the financial statements at appropriate amounts and the accuracy of recorded loan interest income resulting in an audit opinion qualification.

Recommendation: We recommend that management establish internal controls over backup and recovery of computerized loan management system data to facilitate the maintenance and periodic reconciliation of the subsidiary loan ledger with the loans receivable balance in the general ledger.

Prior Year Status: The lack of adequate controls over backup procedures to allow for recovery of the subsidiary loan ledger from the computerized loan management system was reported as a finding in the Single Audits of EULGOV for fiscal years 2006 through 2010.

Auditee Response and Corrective Action Plan: A new in-house loan system is to be installed to properly account for the loan receivables and maintain the subsidiary ledgers.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2011

Finding No.: 2011-003  
Area: Derivative Instruments

Criteria: Generally accepted accounting principles requires that investment derivative instruments be reported at fair value on the statement of net position. The changes in fair value of investment derivative instruments are required to be reported as part of investment revenue in the current reporting period.

Condition: Management entered into an interest rate swap agreement, dated November 20, 2007, as an investment in anticipation of lowering the costs of borrowing associated with an outstanding bank loan. As of September 30, 2011, the outstanding bank loan amounted to \$6,643,541; however, management was unable to ascertain the fair value of the interest rate swap agreement associated with this debt.

Cause: The cause of the above condition is the lack of determining the fair value of the interest rate swap agreement at the end of the reporting period.

Effect: The effect of the above condition is nonconformity with generally accepted accounting principles associated with derivative instruments resulting in an audit opinion qualification.

Recommendation: We recommend that management determine the fair value of the interest rate swap agreement at the end of each reporting period. Such will facilitate reporting at fair value on the statement of net position and whether a gain or loss related to this derivative instrument is required to be recognized.

Prior Year Status: The lack of recording derivative instruments at fair value was reported as a finding in the Single Audits of EULGOV for fiscal years 2008 through 2010.

Auditee Response and Corrective Action Plan: The interest rate swap agreement in question was not entered into as an investment; it was entered into with our lender, at our lender's behest, for the purpose of limiting our exposure to interest rate increases on our variable rate loan. The swap agreement was terminated, and the entire outstanding balance of the underlying loan was forgiven by the lender, as of March 31, 2016. The auditee nonetheless accepts the auditor's recommendation and, in the unlikely event that auditee enters into an investment derivative instrument in the future, auditee will take steps to determine the fair value of such instrument as of the end of each reporting period.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2011

Finding No.: 2011-004  
Area: Expenditures/RMI Procurement

Criteria: Expenditures should be supported by vendor invoices, contracts, or other attendant documentation evidencing the nature, validity and reasonableness of the expenditures incurred. In addition, procurement of goods and services should be in accordance with the RMI Procurement Code, which 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 emergency and for the selection of the particular contractor shall be included in the contract file.

Condition: Of \$690,115 in non-payroll expenditures for the General Fund, thirteen items totaling \$167,097 were tested and the following exceptions were noted:

For the following item, attendant documentation supporting the procurement process was not available for examination:

<u>Date</u>	<u>Document #</u>	<u>Amount</u>
07/20/2011	17507	\$ 2,096

Furthermore, the EULGOV Council has established a small purchases policy for purchases less than \$2,500; however, the policy does not stipulate the method of related procurement to be adopted.

Cause: The cause of the above condition is the lack of adequate internal control policies and procedures requiring documentation of purpose of expenditures and procurement procedures to satisfy compliance with RMI procurement guidelines.

Effect: The effect of the above condition is potential unauthorized expenditures and noncompliance with the RMI Procurement Code.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2011

Finding No.: 2011-004, Continued  
Area: Expenditures/RMI Procurement

Recommendation: We recommend that management require that expenditures be supported by vendor invoices, contracts, or other attendant documentation evidencing the nature, validity and reasonableness of the expenditures incurred. Furthermore, we recommend that EULGOV comply with the RMI procurement guidelines.

Prior Year Status: The lack of adequate controls requiring documentation of purpose of expenditures and procurement procedures to satisfy compliance with RMI procurement guidelines was reported as a finding in the Single Audits of EULGOV for fiscal years 2006 through 2010.

Auditee Response and Corrective Action Plan: Compliance with the RMI Procurement Code will be strictly implemented and all expenditures shall be supported by invoice and other supporting documents.

## ENEWETAK/UJELANG LOCAL GOVERNMENT

### Schedule of Findings and Questioned Costs, Continued Year Ended September 30, 2011

Finding No.: 2011-005  
Area: Loans Payable

Criteria: Section 150 (2) of 4 MIRC Chapter 1 of the Local Government Act states that unless authorized by the Minister a local government shall not incur indebtedness chargeable to future revenue which extends beyond the next five (5) full financial years, and a local government shall not in any financial year incur any indebtedness or grant any charge against future revenue such that the total liability of the local government in that year for debt services exceeds fifteen percent (15%) of the estimated revenue for that year.

Condition: At September 30, 2011, EULGOV was indebted to a financial institution for a \$6,643,541 loan. The loan was executed on November 20, 2007 for a period of fifteen years. No approval to exceed the five year period was provided by EULGOV to indicate that loan indebtedness was approved by the Minister of Internal Affairs. In addition, debt service of \$829,733 represented 23% of estimated 2011 revenues.

Cause: The cause of the above condition is the lack of adequate controls over the incurrence of loan indebtedness in accordance with the Local Government Act.

Effect: The effect of the above condition is potential noncompliance with the Local Government Act regarding loan indebtedness and debt service coverage.

Recommendation: We recommend that management comply with the Local Government Act and obtain written approval of the Minister of Internal Affairs for loan indebtedness exceeding the five year term limit. Furthermore, we recommend that management comply with debt service coverage requirements.

Prior Year Status: The lack of adequate controls over the incurrence of loan indebtedness in accordance with the Local Government Act was reported as a finding in the Single Audits of EULGOV for fiscal years 2006 through 2010.

Auditee Response and Corrective Action Plan: Compliance with the Local Government Act will be enforced. Written approval from the Minister of Internal Affairs shall be obtained when incurring indebtedness.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Schedule of Findings and Questioned Costs, Continued  
Year Ended September 30, 2011

Finding No.: 2011-006  
Area: Employee Receivables/Credit Card Usage

Criteria: Receivables due from employees should be collected in a timely manner. Furthermore, credit card usage should be limited to official local government business.

Condition: At September 30, 2011, EULGOV recorded \$97,790 due from employees, which included \$92,321 from personal use of the Corporate credit card. During the year ended September 30, 2011, charges associated with personal use amounted to \$19,022 less payroll deductions of \$16,512. A corresponding allowance for doubtful debts of \$57,935 has been recognized; however, management has not updated such allowance as management believes that the employee has the intent and the ability to repay the amount in full. As the amount was not considered material to the financial statements, no audit adjustment was proposed.

Cause: The cause of the above condition is the lack of adequate controls associated with employee receivables and policies and procedures over Corporate credit card usage.

Effect: The effect of the above condition is potential bad debts associated with employee receivables and expenditures lacking clear public purpose or benefit served.

Recommendation: We recommend that management timely collect employee receivables. Furthermore, we recommend that the Council establish policies and procedures associated with the Corporate credit card limiting such usage for official local government business.

Prior Year Status: The lack of adequate controls associated with employee receivables and policies and procedures over Corporate credit card usage was reported as a finding in the Single Audits of EULGOV for fiscal years 2006 through 2010.

Auditee Response and Corrective Action Plan: Employee receivables are collected every payroll through payroll deductions.



**ENEWETAK/UJELANG LOCAL GOVERNMENT**

Unresolved Prior Year Findings and Questioned Costs  
Year Ended September 30, 2011

Questioned Costs

There were no unresolved questioned costs for EULGOV as at September 30, 2011.

Unresolved Prior Year Findings

The status of unresolved prior year findings is discussed in the Schedule of Findings and Questioned Costs section of this report.

<u>Finding Number</u>	<u>CFDA Number</u>	<u>Questioned Costs</u>	<u>Status</u>
2004-007	15.875	\$ -	Refer Note 1.
2004-008	15.875	\$ -	Refer Note 1.
2004-009	15.875	\$ -	Refer Note 1.
2005-003	15.875	\$ -	Refer Note 1.
2005-004	15.875	\$ -	Refer Note 1.
2006-005	15.875	\$ -	Refer Note 1.
2006-006	15.875	\$ -	Refer Note 1.
2007-005	15.875	\$ -	Refer Note 1.
2008-009	15.875	\$ -	Refer Note 1.
2009-009	15.875	\$ -	Refer Note 1.
2010-007	15.875	\$ -	Refer Note 1.
2010-008	15.875	\$ -	Refer Note 1.

Note 1: Resolved through a grantor agency determination dated July 9, 2014.

**ENEWETAK/UJELANG LOCAL GOVERNMENT**  
**INDEPENDENT AUDITORS' MANAGEMENT LETTER REPORT**  
**YEAR ENDED SEPTEMBER 30, 2011**

December 20, 2019

Mr. Neil Flores  
City Manager  
Enewetak/Ujelang Local Government  
P.O. Box 1199  
Majuro, MH 96960

Dear Mr. Flores:

In planning and performing our audit of the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Enewetak/Ujelang Local Government (the "Government"), as of and for the year ended September 30, 2011, which collectively comprise the Government's basic financial statements, (on which we have issued our report dated December 20, 2019), in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, we considered the Government's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Government's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Government's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, in connection with our audit, we identified, and included in Attachment I, deficiencies related to the Government's internal control over financial reporting as of September 30, 2011 that we wish to bring to your attention.

We have also issued a separate report to the Honorable Mayor Jackson Ading, also dated December 20, 2019, on our consideration of the Government's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters.

The definition of a deficiency is also set forth in Attachment I.

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

This report is intended solely for the information and use of the Council, management, others within the organization, and the Office of the Auditor General and is not intended to be and should not be used by anyone other than these specified parties.



We will be pleased to discuss the attached comments with you and, if desired, to assist you in implementing any of the suggestions.

We wish to thank the staff and management of the Government for their cooperation and assistance during the course of this engagement.

Very truly yours,

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

## SECTION I – DEFICIENCIES

We identified the following deficiencies involving the Government's internal control over financial reporting as of September 30, 2011 that we wish to bring to your attention.

### Accrued Expenditures

Comment: At September 30, 2011, liabilities of \$9,374 and \$12,500, respectively, were not recorded for payroll expenditures and legal services incurred during the year and paid subsequent to year end. As these amounts were not considered material to the financial statements, no audit adjustments were proposed.

Recommendation: We recommend that management establish internal control procedures requiring expenditures be recorded in the period in which the related fund liability is incurred.

### Employee Withholding Tax Liability

Comment: At September 30, 2011, the Government recorded a \$37,121 withholding tax liability representing unremitted employee income taxes, which included withholdings relating to pre-April 2006. During the year ended September 30, 2011, the Government timely withheld and remitted employee income taxes to the RMI Division of Taxation in accordance with enabling legislation; however, the Government has not reconciled this liability account in order to identify whether the balance represents a valid obligation.

Recommendation: We recommend that management communicate with the RMI Division of Taxation for the purpose of reconciling the employee withholding tax liability account and remit unpaid income taxes in a timely manner.

### Boat Charter Revenue

Comment: During the year ended September 30, 2011, the Government recorded boat charter revenue from voyage charters whereby charter rates were not formally adopted by the Government. Instead, informal rates of \$7,800 per steaming day, \$5,000 per sailing day and \$3,000 per for standby day were utilized. In addition, charter party agreements were not negotiated to formalize the respective responsibilities of the Government and the charterer.

Recommendation: We recommend that the Government require that boat charters be supported by charter party agreements outlining terms and conditions of the charter, including negligence clauses, so as to limit the liability of the Government in the event of a catastrophe. In addition, we recommend that the Government formalize daily charter rates and require that rates charged be sufficient to cover boat charter costs.

## SECTION II – DEFINITION

The definition of a deficiency is as follows:

A *deficiency* in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when (a) a properly designed control does not operate as designed, or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.

## **MANAGEMENT'S RESPONSIBILITY FOR, AND THE OBJECTIVES AND LIMITATIONS OF, INTERNAL CONTROL OVER FINANCIAL REPORTING**

The following comments concerning management's responsibility for internal control over financial reporting and the objectives and inherent limitations of internal control over financial reporting are adapted from auditing standards generally accepted in the United States of America.

### **Management's Responsibility**

The Government's management is responsible for the overall accuracy of the financial statements and their conformity with generally accepted accounting principles. In this regard, management is also responsible for establishing and maintaining effective internal control over financial reporting.

### **Objectives of Internal Control over Financial Reporting**

Internal control over financial reporting is a process affected by those charged with governance, management, and other personnel and designed to provide reasonable assurance about the achievement of the entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. Internal control over the safeguarding of assets against unauthorized acquisition, use, or disposition may include controls related to financial reporting and operations objectives. Generally, controls that are relevant to an audit of financial statements are those that pertain to the entity's objective of reliable financial reporting (i.e., the preparation of reliable financial statements that are fairly presented in conformity with generally accepted accounting principles).

### **Inherent Limitations of Internal Control over Financial Reporting**

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.