

June 19, 2020

Mr. Jack Chong Gum  
Chief Executive Officer  
Marshalls Energy Company, Inc.  
P.O. Box 1439  
Majuro, Marshall Islands 96960

Dear Mr. Chong Gum:

In planning and performing our audit of the financial statements of Marshalls Energy Company (MEC) as of and for the year ended September 30, 2019 (on which we have issued our report dated June 19, 2020), 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 MEC'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 MEC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of MEC'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 the attached Appendix I, deficiencies related to MEC's internal control over financial reporting and other matters as of September 30, 2019, that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated June 19, 2020, on our consideration of MEC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters.

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

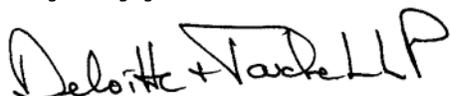
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with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

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

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

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

Very truly yours,

A handwritten signature in black ink that reads "Deloitte + Touche LLP". The signature is stylized and appears to be written in a cursive or semi-cursive font.

**SECTION I - DEFICIENCIES**

We identified, and have included below, certain deficiencies involving MEC's internal control over financial reporting as of September 30, 2019, that we wish to bring to your attention:

(1) Receivables

Collection of outer island solar electricity billings:

Outer island solar electricity customers are billed \$5 per month; however, collection follow-up does not appear to occur. MEC does not enforce the 30-day disconnection policy. We recommend management establish and enforce policies and procedures governing outer island collections. This matter was discussed in our previous letters to management for the audits of fiscal years 2007 through 2018.

Returned checks receivable:

At September 30, 2019, MEC recorded \$65,967 of returned checks receivable and this amount was fully reserved. We recommend management establish related collection policies and procedures. This matter was discussed in our previous letters to management for the audits of fiscal years 2009 through 2018.

(2) Inventory

Fuel inventory:

Inventory reconciliation variances appear to exist throughout the year but do not appear to be investigated. While there may be an acceptable industry variance rate, the noted variances exceeded the acceptable or normal rate. We recommend management strengthen internal control policies over monitoring, reconciliation, and review of fuel inventory.

Also, fuel dipping sheets appear to be unorganized and some are missing. Further, we noted several errors in the recorded number of gallons (converted based on actual fuel dipping sheets) per Monthly Statistical Fuel Report. Also, there are inconsistencies between the recorded reading per actual fuel dipping sheets and Monthly Statistical Fuel Report. We recommend management implement appropriate internal controls over inventory management. This matter was discussed in our previous letters to management for the audits of fiscal years 2013 through 2018.

(3) Property, Plant and Equipment

Updating of fixed asset register:

Asset tags are not reflected in the fixed asset register. We recommend management update fixed asset register reflecting asset tag numbers.

Monitoring the outer island fixed asset register:

A fixed asset register as of September 30, 2019 for outer island residential solar projects was not provided. We recommend management support fixed asset costs, accumulated depreciation, and depreciation expense through a reconciled fixed asset register. This matter was discussed in our previous letters to management for the audits of fiscal years 2013 through 2018.

## SECTION I - DEFICIENCIES, CONTINUED

### (4) Electric Revenue

Rotation of meter readers:

Meter readers are not periodically rotated. To improve internal controls, we recommend meter reader schedules be rotated.

Monitor and review line losses:

Line losses are a function of kilowatt hours generated and billed. A generation analysis for fiscal year 2019 could not be provided. Thus, line loss percentages could not be calculated. We recommend management implement a process to monitor and review line losses.

### (5) Daily collection receipts

For 3 of 22 daily cash collections tested, deposits occurred on an average of 2 to 3 banking days after receipt. Although this might be acceptable per MEC's policy, we recommend management revisit established policies and procedures requiring that cash collections be deposited on the next banking day.

## SECTION II - OTHER MATTERS

Our observations concerning other matters related to operations, compliance with laws and regulations, and best practices involving internal control over financial reporting that we wish to bring to your attention at this time are as follows:

### (1) Information Technology

MEC has not adopted formal policies and procedures governing information technology and data security. We recommend management adopt formal policies and procedures governing information technology and data security. This matter was discussed in our previous letters to management for the audits of fiscal years 2008 through 2018.

### (2) Depreciation Rates

MEC is required to apply RUS-approved depreciation rates to all capital assets. The list of approved depreciation rates could not be located. We recommend this list be located and copies be provided to accounting staff responsible for recording and depreciating fixed assets. This matter was discussed in our letters to management for the audits of fiscal years 2003 through 2018.

### (3) Retirement Savings Plan

Taxes are currently not withheld on MEC's matching of employee contributions to the retirement plan. We recommend management require applicable taxes be withheld on employer matching of retirement plan contributions and be remitted to taxing authorities. This matter was discussed in our previous letters to management for the audits of fiscal years 2010 through 2018.

### (4) Adequacy of Documents

Settlement agreements should be retained on file; however, an executed agreement with one customer could not be located. Further, approved leave form of one employee for pay periods ending 03/31/2019 and 06/23/2019 could not be provided to us. We recommend documentation be on file to support all recorded financial statement transactions. This matter was discussed in our previous letters to management for the audit of fiscal year 2018.

**SECTION II - OTHER MATTERS, CONTINUED**

(5) Propane issuances

We were unable to test the completeness of Product Delivery Reports (PDR forms) issued due to issuance not being in sequence. We recommend management improve internal controls over approved PDRs. This matter was discussed in our previous letters to management for the audit of fiscal year 2018.

(6) Board Sitting Fees

During the year ended September 30, 2019, MEC paid sitting fees of \$12,900 to Board members. These fees may constitute wages under the Income Tax Act 1989 and thus be subject to withholding taxes. No withholding taxes were withheld by MEC. We recommend management obtain an interpretation from the Ministry of Finance, Banking and Postal Services Chief of Revenue and Taxation concerning the applicability of withholding taxes on sitting fees paid to Board members.

**SECTION III - 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**

MEC'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.