Deloitte & Touche LLP
361 South Marine Corps Drive
Tamuning, GU 96913-3973
USA

Tel: +1 (671) 646-3884
Fax: +1 (671) 649-4265

www.deloitte.com

June 16, 2020

Mr. Dwight Heine
Managing Director
Marshall Islands Development Bank

Dear Mr. Heine:

In planning and performing our audit of the financial statements of the Marshall Islands Development Bank (MIDB) as of and for the year ended September 30, 2019 (on which we have issued our report dated June 16, 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 MIDB'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 MIDB's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of MIDB'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. However, in connection with our audit, we identified, and included in the attached Appendix I, deficiencies related to MIDB'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 16, 2020, on our consideration of MIDB's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters.

The 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 Office of the Auditor-General, management, others within the organization, 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 MIDB for their cooperation and assistance during the course of this engagement.

Very truly yours,

Deloitte & Touche LLP

SECTION I – 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 are as follows:

1. Late payment of Withholding and Social Security Taxes

Comment:

MIDB paid employee income taxes withheld in a manner inconsistent with 48 MIRC Chapter 1, Income Tax Act of 1989, Section 105.

Scrutiny of withholding tax payments (Form 1178) indicated the following exceptions:

Payroll period	Date Paid	Payroll period	Date Paid
11/10/18 - 12/07/18	01/22/2019	03/30/19 - 04/26/19	05/31/2019
12/08/18 - 01/04/19	01/22/2019	05/25/19 - 06/21/19	08/30/2019
02/02/19 - 03/01/19	03/28/2019	06/22/19 - 07/19/19	09/26/2019
03/02/19 - 03/29/19	05/09/2019	07/20/19 - 08/16/19	09/26/2019

Form 1178 is due within two weeks following the preceding four week pay period. MIDB was noncompliant with this requirement.

Scrutiny of the employer's quarterly Social Security tax returns indicated that the quarter ending 12/31/2018 return was not timely remitted. MISSA tax deadline is the 10th of the first month of the following quarter. MIDB was noncompliant with this requirement.

Recommendation: We recommend management timely remit MISSA taxes and RMI withholding tax payments in accordance with established requirements.

2. Noncompliance with Income Tax Act

Comment: 48 MIRC Chapter 1, Income Tax Act of 1989 states that:

(a) Section 117 - There shall be assessed, levied, collected and paid a non-resident tax of ten percent (10%) on the gross income earned by every non-resident person in respect of services provided or performed by such person relating to any client in the Marshall Islands;

(b) Section 118.1 - It shall be the duty of every client to deduct or withhold the tax referred to in Section 117 of this Chapter from such person at the time the fee is paid to him. The tax so deducted shall be paid by him on or before the last day of the month following each quarter, to wit, on or before April 30, July 31, October 31, and January 31. Every such client shall, on or before the date provided for the payment of tax, make a full, true and correct return showing all such fees paid by him; and

(c) Section 118.2 - Where any client fails to deduct or withhold or pay the tax referred to in subsection (1) of this Section, he shall be personally liable to pay the said tax referred to in Section 117 of this Chapter.

MIDB paid professional service fees of $26,962 to a non-resident company; however, the non-resident tax was not withheld and paid.

Recommendation: We recommend management establish policies and procedures to comply with the RepMar Income Tax Act of 1989, as amended.

SECTION I – OTHER MATTERS, CONTINUED

3. Negative Balances in Deposit Accounts

Comment: As of September 30, 2019, there were 188 savings deposit accounts with negative balances totaling $40,629. Savings deposits generally pertain to loan overpayments resulting from dated records and withdrawals made through customer refunds. Therefore, it appears that the Bank refunded certain customers in excess of related deposit balances or this matter could be attributed to dated records.

Recommendation: Management should continue to pursue this matter and consider adding these amounts to existing loans. Otherwise, management should decide whether these balances should be charged-off or an applicable allowance for doubtful accounts be provided as appropriate.

4. Loan Overpayment

Comment: MIDB receives loan payments from borrowers through payroll deductions or allotments remitted by borrower employers. Payments received in excess of loan balances are deposited to the MIDB borrower's savings account.

Recommendation: We recommend that management establish policies and procedures to timely monitor loan accounts with excess payments. Further, management should consider designating a person responsible for informing related borrowers of the excess payments.

5. Employee Pension Plan

Comment: MIDB has a retirement plan for employees wherein MIDB employees who elect to be members of the plan contribute $30/pay period and MIDB will match the full amount of the employee contribution.

Recommendation: We recommend that management establish an employee pension plan outside of MIDB to be administered by a pension plan trustee to clearly segregate pension plan assets and liabilities for the security of its plan members.

6. Board Sitting Fees

Comment: During the year ended September 30, 2019, MIDB paid sitting fees of $36,900 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 MIDB.

Recommendation: 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 II – DEFINITION

A *deficiency* 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

MIDB'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 effected 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.