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September 10, 2021

Mr. Albon Jelke
General Manager
Air Marshall Islands, Inc.
P.O. Box 1319
Majuro MH 96960

Dear Mr. Jelke:

In planning and performing our audit of the financial statements of Air Marshall Islands, Inc. (AMI) as of and for the year ended September 30, 2020 (on which we have issued our report dated September 10, 2021), 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 AMI'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 AMI's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of AMI'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 AMI's internal control over financial reporting and other matters as of September 30, 2020 that we wish to bring to your attention.

We have also issued a separate report to the Board of Directors, also dated September 10, 2021, on our consideration of AMI'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 AMI for their cooperation and assistance during the course of this engagement.

Very truly yours,

Deloitte + Touche LLP

SECTION I - CONTROL DEFICIENCIES

We identified, and have included below, control deficiencies involving AMI's internal control over financial reporting as of September 30, 2020 that we wish to bring to your attention:

1) Cash

   The September 2020 bank reconciliation included the following exceptions:

   - $19,623 of long outstanding checks were not timely reconciled.
   - $5,511 of unreleased checks were recorded as outstanding checks.
   - $7,140 of collections were incorrectly recorded as deposits-in-transit

   Audit adjustments were proposed to correct these exceptions. We recommend management establish policies over the processing, reconciliation, monitoring and disposition of unreleased checks and deposits-in-transit.

2) Collection of Receivables

   At September 30, 2020, receivables included the following exceptions:

   - Returned checks receivable increased by $1,110 from $35,613 in FY2019 to $36,723 in FY2020, of which, $35,675 originated in FY2017 and prior.
   - Employee receivables amounted to $30,555, of which $22,266 were aged over 90 days.
   - Trade receivables included $29,527 aged over six years.

   We recommend management increase collection efforts. Collection of receivables was discussed in our previous letters to management for fiscal years 2006 through 2019.

3) Allowance for Doubtful Accounts

   At September 30, 2020, trade and other receivables, net of subsequent collections, aged over 90 days of $117,563 were not provided for within the allowance for doubtful accounts. AMI has a policy of specifically identifying receivables that are doubtful as to collection. An audit adjustment was proposed to correct this matter. We recommend management revisit its current policy in determining the allowance for doubtful accounts. Through available historical data, management may consider implementing an allowance percentage for each receivable age bracket.

4) Prepaid Expense and Long-Term Deposits

   At September 30, 2020, long-term deposits included the following exceptions:

   - $297,875 of construction in progress was erroneously recorded as a long-term deposit.
   - A $274,918 deposit was not reclassified to capital assets when the asset was received.
   - An unknown $14,000 prepaid expense has been outstanding since 2009.

   Audit adjustments were proposed to correct these exceptions. We recommend management perform regular analysis and monitoring of prepaid expense and long-term deposit accounts.

5) Capital Assets

   For 8 of 10 capital asset additions tested, acquisition dates, which AMI uses as the start of the depreciation period, differ from actual asset receipt dates. An audit adjustment was proposed to correct this matter. We recommend management implement internal control procedures to monitor assets receiving date through examination and filing of receiving and shipping documents.

SECTION I - CONTROL DEFICIENCIES, CONTINUED

6) Expendable Parts

At September 30, 2020, expendable parts included the following exceptions:

- Expendable part issuances during 2020 of $921,307 were recorded at year-end as part of the financial closing process.

- Of forty samples tested, twelve in an aggregate amount of $58,120 increased in quantity compared to prior year, with no current year purchases noted. These expendable parts might arise from the following:

  - uninstalled aircraft parts put back in storage
  - parts erroneously excluded from prior year physical count
  - parts erroneously included in another inventory item with similar features but a different serial number in the prior year physical count

- Expendable parts recorded as an expense are not monitored to avoid inclusion in the physical count and/or capital assets upon installation.

- Uninstalled aircraft parts for repair are not monitored as to recordation.

We recommend management improve internal control procedures over physical counts. Management may consider physical segregation of expendable parts into new purchases, uninstalled parts, and expensed items. Moreover, parts are expected to be arranged in an orderly manner that facilitates accurate physical counts per part/serial number, by trained counters. Lastly, we recommend management implement formal procedures to correctly record transactions involving (1) expendable parts that do not meet capitalization policy or expendable part recognition, and (2) uninstalled aircraft parts, to avoid double recording.

7) Revenues

Of twenty-six passenger revenue items tested, four have a student, senior citizen or child rate without a documented basis. We recommend management establish policies and procedures relating to documenting discounted fares.

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) Reconciliation Reports

For the year ended September 30, 2020, we noted the following reconciliation exceptions:

- Review of daily cash and sales reconciliation reports occurs in two weeks to one month on average. We recommend management perform more timely review of reconciliation reports to detect errors or shortages and take corrective action.

- For outer island collections, the pilot verifies the actual number of passengers onboard against the sales report submitted by the Agent. However, there is no formal documentation that such verification by the pilot is performed. We recommend management formalize and document the reconciliation of actual passenger information, sales report and cash collection report to verify completeness of outer islands recorded revenues. Such reconciliation should be subjected to review by an appropriate level of management and if possible, be verified against other documents, such as the completed "Status" sheet upon arrival of the aircraft.

SECTION II - OTHER MATTERS, CONTINUED

2) Adequacy of Documents

   A lease for certain office space could not be provided. Documentation should be on file to support all financial statement transactions.

3) Local Noncompliance - RMI Procurement Code

   An operating expense of $1,700 was not adequately documented to evidence compliance with the RMI Procurement Code. We recommend management require policies and procedures be established to demonstrate compliance with the RMI Procurement Code.

4) Board Sitting Fees

   During the year ended September 30, 2020, AMI paid sitting fees of $5,600 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 AMI. 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.

5) Review of Non-Routine Journal Entries

   For four journal entries tested, a formal process of approval or review was not adequately documented. We recommend management revisit internal control procedures over documentation, review and filing of non-routine journal entries to adjust or correct account balances.

6) Annual Leave Hours

   AMI has no written policy indicating that employees are entitled to an accrual of no more than 160 annual leave hours. We recommend management formalize policies over employee leave entitlements.

7) Prepayment

   During the year ended September 30, 2020, we noted a prepayment of fuel to be used in the subsequent period amounting to $28,038. Section 146 (Subsection 1) of Financial Management Act of 1990 states that for vendors located in Republic of Marshall Islands, checks for bills of materials, supplies and incidentals of every kind and character, shall be made payable to the order of each individual person to whom the Republic is indebted, except for assignment of monies approved by the Secretary of Finance per Section 148 of the same Act, but only after an invoice arid purchase order have been presented and certified that the materials, supplies, and incidentals have been received. AMI appears non-compliant with the Act as the transaction does not represent payment of indebtedness. We recommend management comply with the Financial Management Act.

SECTION III - DEFINITIONS

The definition of a deficiency is as follows:

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.

APPENDIX II

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

AMI'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.