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November 3, 2021

Mr. James Bing II
Executive Director
RMI Ports Authority

Dear Mr. Bing:

In planning and performing our audit of the financial statements of RMI Ports Authority (the Authority), a component unit of the Republic of the Marshall Islands, as of and for the year ended September 30, 2020, on which we have issued our report dated November 3, 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 the Authority'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 Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority'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 the Authority'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 November 3, 2021, on our consideration of the Authority'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 the Authority for their cooperation and assistance during the course of this engagement.

Very truly yours,

Deloitte & Touche LLP

SECTION I - DEFICIENCIES

We noted the following deficiencies involving the Authority's internal control over financial reporting as of September 30, 2020 that we wish to bring to your attention.

1) Recording of Financial Transactions

At September 30, 2020, we noted the following unrecorded transactions:

a. Opening of a new $2 bank account and related transactions during the year. As this matter is not considered material to the financial statements, no audit adjustment was proposed.

b. Request for reimbursement from Federal Aviation Administration, which understated both grant receivables and revenues by $178,756. Furthermore, related construction work-in-progress, professional fees and advertising expenses of $128,591, $46,558 and $1,710, respectively, were not recorded timely. Audit adjustments were proposed to correct these misstatements.

We recommend management establish internal control policies and procedures requiring the recording of all financial transactions in the accounting system. Specifically, all requests for grant reimbursement should be supported by journal entries and be processed timely.

2) Cash Collections

Twenty-six daily collections were not deposited timely. We recommend management establish internal control policies and procedures over the timely deposit of cash collections.

3) Receivables

At September 30, 2020, we noted the following observations over receivables:

a. Receivables of $1,174,215 were aged over six years. We recommend management establish internal control policies and procedures relative to timely review and update of aging reports. This matter was discussed in our previous letters to management for fiscal years 2017 through 2019.

b. The Authority's seaport receivable aging schedule is based on the arrival date of vessels, which is normally different from the invoice date. We recommend management establish internal control policies and procedures to: (1) timely process and record invoices; and (2) review the reasonableness of the seaport aging schedule.

4) Reconciliation of Liability Accounts

During the year ended September 30, 2020 test of liabilities, we noted the following:

a. Accounts payable of $22,623 are deemed fully paid but remained outstanding in the Authority's financial statements. After procedures performed, an audit adjustment was proposed to adjust a portion of the accounts payable balance. We recommend management establish internal control policies and procedures requiring reconciliation of account balances with companies to facilitate recordation of year-end accounts payables.

b. One related party payable confirmed $57,700 less than compared to the Authority's recorded amount. We recommend management establish internal control policies and procedures requiring timely reconciliation of balances with related parties.

c. Unearned revenues of $12,335 remains unadjusted from prior year. We recommend management analysis and adjust the stated balance.

SECTION I - DEFICIENCIES, CONTINUED

5) Revenues

During the year ended September 30, 2020 test of revenues, we noted the following:

General

a. We noted usage of invoices and sales receipts without verification of the proper sequence. Twelve invoice numbers and two receipt booklets (100 receipts per booklet) were skipped which could possibly indicate unrecorded revenues and/or collections.

Airport

b. Three items were invoiced 88 days (on average) after the transaction date.

c. Eleven sales receipts aggregating $264 were not recorded. Extrapolation of identified misstatements resulted in a potential misstatement of $13,200. An audit adjustment was proposed to correct this matter.

d. Eighteen missing receipts were not recorded, and related collections were not deposited. It is estimated that the receipts aggregated less than $2,000.

Seaport

e. Five items have inconsistent departure dates in the vessel clearance which differ from that of the invoice, checklist and pilot slips.

f. The Authority bills shipping agents after the vessel departure date, without considering effects on revenue recognitions especially near year-end. Details follow:

   - Nineteen invoices pertain to FY2019 and were not recorded in the correct period. This matter overstated FY2020 revenues by $30,451.

   - Five invoices pertain to FY2020 and were not recorded in the correct period. This matter understated FY2020 revenues by $10,896.

   Audit adjustments were proposed to correct these misstatements.

g. Ebeye office net revenues of $361 were not recorded in the correct period. Extrapolation of the errors resulted in a potential misstatement of $7,220. An audit adjustment was proposed to correct this matter.

h. Ebeye office collections of $1,010 were not timely deposited and reported to the main office.

i. We noted usage of a pre-numbered vessel clearance book without verification of the proper sequence.

We recommend the Authority improve internal control procedures over the (1) usage of pre-numbered vessel clearances, invoices, and the sequential use of sales receipts, (2) preparation of billing and recordation of revenues in the period earned, while focusing on vessels that stay for an extended period in the RMI or arrive in the RMI near year-end, (3) verification that all sales receipts were recorded, (4) verification of the consistency of details in the clearance, supporting invoices, pilot slip and checklist for proper monitoring of vessel movements and avoidance of possible misuse of vessel clearances, and (5) reporting and depositing of collections from the Ebeye office in a timely manner.

SECTION I - DEFICIENCIES, CONTINUED

6) <u>Lease Revenue</u>

The Authority earns and records revenue from leasing a container yard at a rate equal to 1.5% of the lessee's gross receipts, based on lessee submitted reports. We recommend management implement internal control policies and procedures over the review of the pertinent documents to verify the accuracy of recorded and collected lease income.

7) <u>Timely Recording and Verification of Revenues</u>

Marshall Islands Shipping Corporation (MISC) acts as the Authority's agent in collecting wharfage fees for cargo services provided by MISC. MISC submits reports and collections to RMIPA on an annual basis. However, the Authority does not perform an independent verification of such report. As of September 30, 2020, the Authority failed to accrue $10,961 of revenues from MISC. An audit adjustment was proposed to correct this matter. We recommend management establish internal control procedures (1) to timely record wharfage revenues from MISC and (2) to verify the completeness of reports and collections submitted by MISC.

8) <u>Timely Recording of Expenses</u>

During the year ended September 30, 2020, the following expenses were not timely recorded:

a. Utilities- $36,314
b. Pilotage expenses- $22,680
c. Pilot boat expenses- $3,695
d. Gas, oil, fuel expenses- $1,536

Audit adjustments were proposed to correct these misstatements. We recommend management establish internal control policies and procedures over the accuracy and timely recording of expenses.

9) <u>Fixed Assets</u>

During the year ended September 30, 2020, we noted the following fixed asset observations.

a. The Authority does not implement periodic inspection and inventory of capital assets.

b. Some fixed asset register amounts do not agree with trial balance amounts. This is caused by asset disposals not removed from the register and prior year adjustments not reflected in the register.

c. Of twenty-three assets sighted for existence, six tags were not updated in the fixed asset register and one asset was not physically tagged.

d. Two assets were disposed of in the previous years but were not removed from the fixed assets register.

e. The fixed asset register does not completely include the percentage of Federal participation in the project costs for the Federal award for the property acquired, the location, use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property, in accordance with the applicable equipment management requirements. Further, there is no control system to ensure adequate safeguards to prevent loss, damage, or theft of the property.

We recommend management establish internal control policies and procedures over fixed assets and strengthen asset monitoring, maintenance procedures and disposals. Furthermore, we recommend management consider tagging all applicable property and equipment to facilitate accurate record keeping and accountability. Lastly, we recommend management update the fixed asset register based on the inventory of fixed assets in accordance with applicable property rules and regulations, and trial balance amounts.

SECTION I - DEFICIENCIES, CONTINUED

10) Annual Leave Hours

Per the Authority's contracts with employees and employee handbook, annual/vacation leave entitlements in excess of 208 hours outstanding at the end of the payroll year shall not be carried forward to the subsequent year. Accrued annual leave was overstated by $18,296, due to accruals in excess of 208 hours. An audit adjustment was proposed to correct this matter. We recommend management establish internal control policies and procedures over employee leave entitlements.

11) General Journals and Bank Reconciliation

Various year-end general journals and monthly bank reconciliation statements prepared reflected no evidence of review and approval by an appropriate level of management. Furthermore, the majority of year-end general journals were not supported by supporting calculations, attachments and description of the entry. We recommend management establish internal control policies and procedures requiring the review of documents by an appropriate level of management and document that such review was performed.

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) Prepayments

The Authority's practice is to prepay $5,000 to a vendor for future fuel consumption. 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. We recommend management establish internal control policies and procedures over advance payments to vendors and comply with the Financial Management Act.

2) Retirement Savings Plan Taxation

Taxes are currently not withheld on the Authority's matching of employee contributions to the retirement plan. We recommend management require applicable taxes be withheld on employer matching of retirement plan contributions. This matter was discussed in our previous audits for fiscal years 2018 and 2019.

3) Board Sitting Fees

During the year ended September 30, 2020, the Authority paid sitting fees of $13,600 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 the Authority. 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. This matter was discussed in our previous audit for fiscal year 2019.

4) Withholding Taxes

As of September 30, 2020, RMIPA has unpaid withholding taxes from contractors of $45,019, that originated from prior and current years (GL codes 22011 and 22010). Per Section 110 of Income Tax Act of 1989, every business, on or before the last day of the month following the close of each quarter, shall pay the amount of tax imposed to the Secretary of Finance. We recommend management comply with the provisions of the tax law.

SECTION II - OTHER MATTERS, CONTINUED

5) Pilotage Fees

During the year ended September 30, 2020, the Authority paid pilotage fees of $292,125 to qualified pilots, which included pilots who were employees of the Authority and other RepMar Ministries and Agencies. On April 9, 2019, RepMar's Government Ethics Board issued a directive to the Authority, which stated that the Authority's arrangement with the pilots constitutes a violation of Ethics in Government Act, terms of employment by which these government employees must comply and RepMar taxation laws and regulations. As of September 30, 2020, the Authority has yet to comply with the recommended action plans of the Government Ethics Board. We recommend management comply with the recommended action plan of the Government Ethics Board and obtain an interpretation from the Ministry of Finance, Banking and Postal Services Chief of Revenue and Taxation concerning the applicability of withholding taxes on pilotage fees. This matter was discussed in our previous audit for fiscal year 2019.

6) Compliance with Shipping Pilotage Regulations (2007)

RMI Shipping Pilotage Regulations (2007) requires the Authority pay 10% quarterly of its pilot related revenues to the General Fund or any other Fund established, for the sole purpose of creating a Training Fund for Marshallese pilots. As of September 30, 2020, the payable to Ministry of Transportation, Communications and Information Technology amounted to $491,611 and no payments have been made for the past several fiscal years. We recommend management comply with regulations over payments of pilot related fees.

7) Financial Consultant

In 2020, the Authority entered into a contract and paid $55,361 to a foreign national Financial Consultant as an independent contractor, which may not comply with local labor laws and regulations. The Office of the Attorney General subsequently issued a memorandum prohibiting foreign nationals from contracting with government agencies unless applicable labor laws and regulations are adhered to. Furthermore, the Authority obtained supplemental financial services from the Financial Consultant for which no formal contractual agreement was executed. We recommend management comply with local labor laws and regulations in contracting with foreign nationals. Furthermore, we recommend management require financial services be supported by an executed contractual agreement.

SECTION III - DEFINITION

The definition of a deficiency that 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.

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 Authority'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 is 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.