

December 29, 2017

Mayor James Matayoshi
Rongelap Atoll Local Government
Republic of the Marshall Islands

Dear Mayor Matayoshi:

In planning and performing our audit of the financial statements of the governmental activities and each major fund of the Rongelap Atoll Local Government (RALGOV) for the year ended September 30, 2011, which collectively comprise RALGOV's basic financial statements and on which we have issued our report dated December 29, 2017, 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 RALGOV'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 RALGOV's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of RALGOV'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 RALGOV's internal control over financial reporting and other matters as of September 30, 2011 that we wish to bring to your attention.

We have also issued a separate report to RALGOV, also dated December 29, 2017 on our consideration of RALGOV'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.

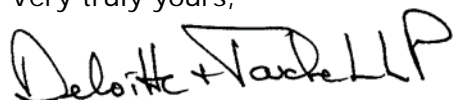
A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal control over financial reporting, is set forth in the attached Appendix II and should be read in conjunction with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

This report is intended solely for the information and use of management, the Council, 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 RALGOV for their cooperation and assistance during the course of this engagement.

Very truly yours,



SECTION I – CONTROL DEFICIENCIES

We identified, and have included below, control deficiencies involving RALGOV's internal control over financial reporting as of September 30, 2011 that we wish to bring to your attention:

(1) Accounts Receivable - Others

As of September 30, 2011, accounts receivable, excluding interest receivable, amounting to \$460,500, which includes an allowance for doubtful accounts of \$365,471 and comprises various receivables from prior fiscal years, including \$132,516 from federal grants and \$131,251 from a contractor, which failed to deliver certain housing projects.

Furthermore, we noted inadequate collection of employee advances. No formal payroll allotment agreements were utilized during the year.

Details of distribution Fund employee advances (GL 1330) and other receivables (GL 1331) beginning balances were not provided. Thus, we were not able to determine and verify the composition of and collections recorded in the referenced accounts.

We recommend that management examine the detail of accounts receivable to determine uncollectible accounts to be written-off and to obtain requisite approval from the Council. Furthermore, management should require timely delivery of billings and invoices to grantors and/or customers. Management should also enforce agreed payroll deductions from employee advances.

(2) Capital Asset Register

As of September 30, 2011, an overstatement of acquisition cost and accumulated depreciation of \$52,554 and \$7,699, respectively occurred. Completed construction-in-progress of \$73,723 was not properly transferred to capital asset accounts and related depreciation expense was not recorded. In addition, details of acquisition date were not provided.

We recommend that the capital asset register be updated for additions and be reconciled to the general ledger.

(3) Interfund Balances

As of September 30, 2011, interfund balances did not reconcile resulting in an unreconciled variance of \$48,968. An audit adjustment was proposed to correct this condition. We recommend that interfund balances be periodically reconciled.

(4) Bank Reconciliation

Bank reconciliations included outstanding checks of \$202,805. Of that amount, 23% or \$46,260 was classified as stale checks.

<u>Fund</u>	<u>Outstanding Checks</u>	<u>Stale Checks</u>
General Fund	\$ 27,388	\$ 10,686
Resettlement Project	17,591	10,059
Distribution	<u>157,826</u>	<u>25,515</u>
Total	\$ <u>202,805</u>	\$ <u>46,260</u>

We recommend management investigate long outstanding checks and determine an appropriate course of action.

SECTION I – CONTROL DEFICIENCIES, CONTINUED

(5) Expenditures

Several disbursements were not supported by vendor invoices and/or check payments. Details follow:

Fund	Check No.	Check \$ Amount
General Fund	42260	\$ 4,880
Distribution Fund	87054	380
Resettlement Project	6888	33,000

We recommend that payments be supported by vendor invoices.

(6) Journal Entries

Unrealized gains from investments of \$37,606 were incorrectly recorded. A reclassification entry was proposed to correct this matter.

Maintenance expenses of \$100 were erroneously recorded as a donation expense. As the amount was not considered material to the financial statements, no audit reclassification was proposed.

JV2011-082 was recorded incorrectly. Our examination of related journal entries appears that the signed JV was incorrect.

A signed copy of JV2011-005a and JV2011-020a and related interfund disbursements were not located. We were not able to validate the interfund borrowing authorization.

We recommend that management properly maintain accounting records and improve its review process.

(7) Travel Expenditures

Of forty-one General Fund expenditures tested, five related to travel and/or per diem which were not supported by travel reports and travel-related receipts. The full amount of per diem was advanced. RALGov’s Travel Policy states that 80% of total per diem should be paid during the time of travel, and 20% will be paid upon returning of the traveler to ensure travelers turn in a travel report along with his/her travel-related receipts to ensure that the traveler does not owe RALGov due to early return or travel cancellation. We recommend compliance occur with RALGOV’s travel policy.

(8) Account Reconciliation

Proceeds of a \$30,227 time certificate of deposit were redeposited two months after withdrawal. It appears that RALGOV failed to timely follow up on this matter and lost two months of interest income.

GL 2007 (Allotments Payable) of General Fund resulted in a \$3,209 difference from the audited beginning balance. In addition, the Resettlement Project’s interfund receivable was overstated by \$15,000. These matters were corrected through a proposed audit adjustment.

A General Fund outstanding liability (GL 2010 Accounts payable – Others) of \$1,479 appears to have been paid on October 30, 2009 and does not appear to be valid.

We recommend management timely reconcile and update accounting records.

SECTION I – CONTROL DEFICIENCIES, CONTINUED

(9) Documentation

Our examination of bidding documents for various heavy equipment and vehicle acquisitions noted an absence of an approver's signature that evidences independent review and concurrence of the evaluation performed. Further, bid quotations from one of four vendors were not on file.

One \$5,000 donation was not supported by a death certificate.

Minutes of an Executive Council meeting documenting approval of the sale of 425,000 Acionmobile shares were not available. Stock certificates of the remaining \$750 investment balance were not available.

Several names or number of share(s) on distribution checks differed from information indicated on the Distribution List. However, no application of transfer/name change, birth certificate, and death certificate was on file to verify/confirm the changes.

Approval for the decrease from \$500 to \$250 per semester of scholarship assistance to Rongelapese students was not documented.

Approval of the selection of the insurance company that handles the local government employees' retirement trust was not provided. No documentation was provided regarding the designation of the two employees insured per the policy.

We recommend management adopt policies and procedures requiring adequate documentation supporting the validity, correctness, and authorization of transactions.

(10) Payroll

Timesheets are not kept for employees. We recommend that management adopt a policy of requiring timesheets to monitor employee attendance.

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) Segregation of Duties

RALGOV's current level of staffing limits the number of personnel available for accounting duties. Accordingly, appropriate segregation of duties is not always possible which may result in a weakness in internal controls, specifically in the role of the City Manager who has access to assets, has approving authority for disbursements, and also has full access to accounting records. To mitigate this weakness, a critical element in RALGOV's internal control system is the involvement of management in the day-to-day operations and review of accounting activities and financial reports.

Furthermore, certain duties of the Chief Accountant are incompatible such as processing checks for claims payments and distribution of such to payees. We recommend that management establish controls to require rotation of the check distribution function among RALGOV staff.

We encourage involvement of management on a continuing basis and a thorough review of accounting activities and financial reports as a means to maintain effective internal controls until a more structured control environment becomes cost effective.

(2) Sick Leave and Annual Leave Policy

There are currently no policies and procedures governing employee absences including sick leave and vacation leave. Employee paid time off is usually allowed by management. However, no policies are in place that establish limits and authorizations. Furthermore, mandatory vacation policy may be especially beneficial to RALGOV, being a small entity where certain employees may be handling incompatible duties. This would allow management to observe if there is any noticeable change while another person is performing the duties. We recommend that management establish vacation and sick leave policies.

(3) Amendments to Claims Trust Agreement

The original Trust Agreement was approved by the Government of the Marshall Islands (RepMar) through the Ministry of Finance and the Attorney General, consistent with the Rongelap Agreed Minute, pursuant to Section 8 of the Article II of the Compact Section 177 Agreement. However, it appears that such approval was not obtained for the Amended Claims Trust Agreement. We recommend that management consult with legal counsel as to the need to obtain approval of the Amended Trust from RepMar.

(4) Scholarship Assistance

Guidelines on Scholarship Grants indicate that a student shall receive scholarship funds "...provided the student meets the minimum grade requirement of 2.0 average [in the prior semester]". For one \$500 scholarship payment (check # 41048), the student achieved a 1.5 average for the prior semester and per policy, should have not received scholarship funds. However, the Mayor and Council decided to allow students one extra semester to raise their grade average. We recommend that guidelines associated with scholarship assistance be amended to reflect this amendment.

SECTION II - OTHER MATTERS, CONTINUED

(5) Reporting

Management reports were not available. We recommend management consider preparing management reports that assist management and executive officers to monitor financial transactions and that support a relevant and well-informed decision making process.

A trust Fund Summary report noted a \$118,567 understatement of management fees and an overstatement of drawdowns. We recommend that management improve its review process and timely reconcile trust fund reports.

SECTION III – DEFINITIONS

The definition of a deficiency that is established in AU 325, *Communicating Internal Control Related Matters Identified in an Audit*, 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

RALGOV'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.