

*Management Letter*

**Air Marshall Islands, Inc.**

(A Component Unit of the Republic of the Marshall Islands)

*Year ended September 30, 2023*





Ernst & Young LLP  
231 Ypao Road  
Suite 201 Ernst & Young  
Building  
Tamuning, Guam 96913

Tel: +1 671 649 3700  
Fax: +1 671 649 3920  
ey.com

January 13, 2025

Management and the Board of Directors  
Air Marshall Islands, Inc.

In planning and performing our audit of the financial statements of the business-type activities of Air Marshall Islands, Inc. (AMI) as of and for the year ended September 30, 2023, in accordance with auditing standards generally accepted in the United States, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, we considered its internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of AMI's internal control. Accordingly, we do not express an opinion on the effectiveness of AMI's internal control.

A deficiency in internal control 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 material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

During our audit, we noted the following deficiencies in internal control (as described above) and other matters:

### **Inventory**

Condition: During our review of the inventory obsolescence calculation, we noted that the methodology and underlying assumptions were not adequately documented or supported by reliable data. Specifically, we observed the following issues: (1) The calculation did not leverage historical trends or usage patterns to substantiate the assumptions used to estimate inventory obsolescence; (2) There is no formal policy or procedure in place to define how inventory obsolescence should be evaluated, increasing the risk of inconsistency or oversight; (3) The supporting documentation for obsolescence adjustments, such as aging reports, forecasted demand, or market analysis, was incomplete or missing. This lack of support creates a risk of inaccurate financial reporting and may result in misstated inventory balances. It also reduces the ability to assess whether obsolescence reserves are sufficient or excessive.

### **Inventory, continued**

Recommendation: We recommend management implement the following steps: (1) Establish a clear policy for evaluating inventory obsolescence, including the criteria for identifying obsolete or slow-moving inventory and the methodology for calculating reserves; (2) Ensure all obsolescence calculations are supported by comprehensive data, such as usage patterns and inventory aging reports; (3) Regularly review the obsolescence reserve methodology to ensure it remains relevant and incorporates the latest business and market trends. By addressing these areas, AMI can enhance the reliability of its financial reporting and ensure compliance with applicable accounting standards.

### **Lease Contract**

Condition: An office lease on Kwajalein was not supported by a lease agreement duly signed by all parties.

Recommendation: We recommend management establish internal control policies and procedures requiring contractual arrangements be supported by executed agreements between the respective parties.

### **TakeFlite Revenue System**

Condition: During our audit, we noted that there is no formal process in place to reconcile revenue recorded in the TakeFlite Revenue System (TRS) with the related accounts in the general ledger. The lack of reconciliation increases the risk of discrepancies between the two systems going undetected. During the year ended September 30, 2023, the following exceptions were noted:

| <u>GL Account</u> | <u>Revenue Source</u> | <u>TRS Balance</u> | <u>GL Balance</u>  | <u>Variance</u> |
|-------------------|-----------------------|--------------------|--------------------|-----------------|
| 40000             | Passenger             | \$4,407,127        | \$4,412,273        | \$( 5,146)      |
| 40100             | Freight               | 716,484            | 717,005            | ( 521)          |
| 40200             | Excess Baggage        | 296,233            | 296,233            | ---             |
| 40370             | Fuel Surcharge        | 513,894            | 496,149            | 17,745          |
| 45100             | No Show/Reissue       | 87,367             | 87,367             | ---             |
| 45150             | PTA service charge    | <u>28,380</u>      | <u>28,380</u>      | <u>---</u>      |
|                   |                       | <u>\$6,049,485</u> | <u>\$6,037,407</u> | <u>\$12,078</u> |

No explanation was provided with respect to the noted variances between the TRS and the GL.

Recommendation: We recommend management establish a formal process to reconcile revenue between the TRS and the general ledger on a regular basis.

## **Revenue Recognition - Fuel Surcharge and Re-issuance Tickets**

Condition: During our audit, we noted that fuel surcharge and ticket re-issuance revenues are not consistently recorded when earned, as required under the accrual basis of accounting. Instead, fuel surcharge and re-issuance tickets revenues are recorded at year end to the MIP accounting system through journal voucher entry based on transactions extracted from the Takeflite system. This practice results in inaccurate financial reporting, including misstatement of revenue and net income in certain periods.

Recommendation: We recommend that management implement policies and procedures to ensure fuel surcharge and ticket re-issuance revenues are recorded when earned, and that periodic reconciliation of revenues between the Takeflite revenue system and the MIP accounting system occurs.

## **Board Sitting Fees**

Condition: During the year ended September 30, 2023, AMI paid sitting fees of \$6,800 to Board members. These fees may constitute wages under the Income Tax Act 1989 and thus may be subject to withholding taxes. No withholding taxes were withheld by AMI.

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.

## **Retirement Savings Plan**

Condition: During the year ended September 30, 2023, AMI made employer contributions, totaling \$78,443 to employee retirement savings plans. Taxes are not currently withheld and paid on the employer contributions.

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 employer contributions to employee retirement savings plan.

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This communication is intended solely for the information and use of management, the Board of Directors, 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. However, this report is also a matter of public record.

January 13, 2025

At this time, we would like to thank all the staff and management of AMI for their cooperation extended to us during the course of our audit. We would be pleased to discuss the above matters or to respond to any questions, at your convenience.

Sincerely,

*Ernst + Young LLP*