

Management Letter

Marshall Islands Development Bank

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

Year ended September 30, 2023



November 8, 2024

The Board of Directors and Management
Marshall Islands Development Bank

In planning and performing our audit of the financial statements of the business-type activities of Marshall Islands Development Bank (MIDB) 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 the MIDB's internal control. Accordingly, we do not express an opinion on the effectiveness of the MIDB'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:

Loans Receivable

Condition: Tests of a representative sample of twenty-eight (28) loans revealed certain matters in the design, implementation and adherence to internal controls over the lending and credit administration area. These matters are as follows:

- a. For eight loans, the loan number was not documented or reflected on the promissory note or the loan agreement.
- b. For four loans, information such as loan amount, maturity date, payment frequency, total payments, and interest rate was not consistent throughout the loan file, i.e. promissory note, loan agreement, amortization table, and loan trial balance.
- c. For one loan, the signed amendment to loan agreement was not on file.

Loans Receivable, continued

Recommendation: We recommend management perform a comprehensive review of its policies and procedures and strengthen internal controls over lending and credit administration and monitoring of such controls.

Allowance for Loans Losses

Condition: Management uses loss reserve ratios that are not directly related to the level of credit losses and not supported by a loss migration analysis. Furthermore, management does not have a robust system to determine allowance for loan losses based on a migration of historical losses or individual evaluation of loan impairment and related losses.

Recommendation: We recommend management establish internal control policies and procedures requiring comprehensive analysis of historical losses and other qualitative factors in determining the adequacy of the allowance.

Customer Refunds Payable

Condition: 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 borrower's deposit account. Examination of the schedule of customer refunds payable indicated 3,326 accounts aggregating \$1,041,948 that have been non-moving/ inactive for more than 1 year, which were not timely assessed and monitored.

Recommendation: We recommend management establish internal control policies and procedures to timely monitor loan accounts with excess payments. Furthermore, we recommend management consider designating a person responsible for informing related borrowers of excess payments.

Undrawn Loan Funds

Condition: At September 30, 2023, undrawn loan funds amounted to \$397,037, which included 343 non-moving/inactive accounts aggregating \$277,498 that have been outstanding for more than 1 year, which were not timely assessed and monitored.

Recommendation: We recommend management establish internal control policies and procedures to timely monitor long outstanding undrawn loan fund.

Related Party Loans

Condition: Related party loans are compiled manually resulting in errors and incomplete capture of these loans.

Recommendation: We recommend management tag related party loans at the time of origination and perform regular review to identify change in their status. Timely and accurate loan tagging will facilitate accurate identification and reporting.

Board Sitting Fees and Management Allowances

Condition: During the year ended September 30, 2023, MIDB paid sitting fees of \$64,400 to Board members and paid allowances of \$25,000 to senior management. These fees and allowances may constitute wages under the Income Tax Act 1989 and thus may be subject to withholding taxes. No withholding taxes were withheld by MIDB.

Recommendation: We recommend management obtain an interpretation and/or official documentation from the Ministry of Finance, Banking and Postal Services Chief of Revenue and Taxation concerning the applicability of withholding taxes on sitting fees and allowances paid to Board members and senior management.

Retirement Savings Plans

Condition: During the year ended September 30, 2023, MIDB made employer contributions, totaling \$71,816, to employee retirement savings plan. 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.

RMI Withholding Tax

Condition: MIDB filed and paid income taxes withheld in a manner inconsistent with 48 MIRC Chapter 1, Income Tax Act of 1989, Section 105. Specifically, examination of employer's Withholding tax return (Form 1178) indicated that payroll period 05/04/2023 through 05/31/2023 was filed and paid on 06/19/2023. Form 1178 is due within two weeks following the preceding four-week pay period. MIDB was noncompliant with this requirement.

Recommendation: We recommend MIDB file and remit RMI withholding tax payment in accordance with the established requirement.

Lease Agreements

Condition: Examination of lease agreements indicated the following:

- a. Revised lease arrangements for one of MIDB's land leases was not formally documented.
- b. Revised lease arrangements for one of MIDB's rental spaces was not formally documented.

Recommendation: We recommend management require lease agreements with counterparties be formally documented to memorialize revised contractual arrangements.

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.

At this time, we would like to thank all the staff and management of MIDB 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.

Ernst + Young LLP