

*Financial Statements and Report on Internal Control and
Compliance*

Majuro Atoll Local Government

*Year ended September 30, 2017
with Report of Independent Auditors*



Majuro Atoll Local Government

Financial Statements and Report on Internal Control and Compliance

Year ended September 30, 2017

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Report of Independent Auditors

Mayor Ladie Jack
Majuro Atoll Local Government
Republic of the Marshall Islands

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and the general fund of Majuro Atoll Local Government (MALGOV) as of and for the year ended September 30, 2017, and the related notes to the financial statements, which collectively comprise MALGOV's basic financial statements as set forth in Section II of the foregoing table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the general fund of MALGOV as of September 30, 2017, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Management has omitted the Management's Discussion and Analysis and the budgetary comparison schedule that accounting principles generally accepted in the United States of America requires to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinions on the basic financial statements is not affected by this missing information.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated July 24, 2026, on our consideration of MALGOV'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 purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Ernst + Young LLP

July 24, 2026

Majuro Atoll Local Government

Governmental Funds Balance Sheet/Statement of Net Position

September 30, 2017

	<u>General Fund</u>	<u>Adjustments (Note 2)</u>	<u>Statement of Net Position</u>
<u>ASSETS</u>			
Cash	\$ 298,897	\$ ---	\$ 298,897
Receivables:			
Taxes	213,443	---	213,443
Due from RepMar	124,000	---	124,000
Due from MIMRA	57,200	---	57,200
Employees	286,617	---	286,617
Other	5,222	---	5,222
Capital assets, net of accumulated depreciation	---	1,318,763	1,318,763
Total assets	<u>\$ 985,379</u>	<u>1,318,763</u>	<u>2,304,142</u>
<u>LIABILITIES</u>			
Short-term loan payable	\$ 130,209	---	130,209
Accounts payable	105,433	---	105,433
Accrued penalties payable	233,912	---	233,912
Accrued interest payable	116,956	---	116,956
Social security tax payable	123,948	---	123,948
Withholding taxes payable	974,635	---	974,635
Other liabilities and accruals	84,666	---	84,666
Long-term liabilities:			
Due within one year	---	125,782	125,782
Total liabilities	<u>1,769,759</u>	<u>125,782</u>	<u>1,895,541</u>
Commitments and contingencies			
Fund balance:			
Unassigned	(784,380)	784,380	---
Total fund balance	(784,380)	784,380	---
Total liabilities and fund balance	<u>\$ 985,379</u>		
Net position:			
Net investment in capital assets		1,318,763	1,318,763
Unrestricted		(910,162)	(910,162)
Total net position		<u>\$ 408,601</u>	<u>\$ 408,601</u>

See accompanying notes.

Majuro Atoll Local Government

Statement of Governmental Fund Revenues, Expenditures and Changes in Fund Balance/Statement of Activities

Year ended September 30, 2017

	General Fund	Adjustments (Note 2)	Statement of Activities
Revenues:			
Taxes:			
Sales tax	\$ 2,282,623	\$ ---	\$ 2,282,623
Gasoline tax	624,387	---	624,387
Beer and liquor tax	533,119	---	533,119
Hotel tax	67,598	---	67,598
Cigarette tax	36,241	---	36,241
RepMar grants	1,400,307	---	1,400,307
Business licenses	308,502	---	308,502
MIMRA transshipment fees	157,200	---	157,200
Land lease	5,000	---	5,000
Other grants	2,000	---	2,000
Interest	963	---	963
Other	151,453	---	151,453
Total revenues	<u>5,569,393</u>	<u>---</u>	<u>5,569,393</u>
Expenditures/expenses:			
Salaries and wages	2,262,574	---	2,262,574
Majuro seawalls and other development projects	856,916	(117,424)	739,492
Unallocated depreciation	---	392,484	392,484
Employee benefits	256,664	---	256,664
Penalties and interest	233,912	---	233,912
Member's compensation	192,000	---	192,000
Gasoline and diesel	163,368	---	163,368
Travel and per diem	161,312	---	161,312
Penalties, interest and bank charges	134,073	---	134,073
Capital improvement projects	97,946	---	97,946
Rent and land leases	96,504	---	96,504
Utilities	76,103	---	76,103
Donations	75,183	---	75,183
Professional fees	53,500	---	53,500
Vehicle maintenance	48,703	---	48,703
Boats	322,413	(276,556)	45,857
Office supplies	100,959	(66,993)	33,966
Entertainment	31,429	---	31,429
Insurance	26,216	---	26,216
Bank charges	3,369	---	3,369
Vehicle rental	1,150	---	1,150
Streetlights	450,510	(450,510)	---
Vehicles	321,311	(321,311)	---
Miscellaneous	308,731	---	308,731
Total expenditures/expenses	<u>6,274,846</u>	<u>(840,310)</u>	<u>5,434,536</u>
Deficiency of revenues under expenditures	(705,453)	705,453	
Change in net position		134,857	134,857
Fund balance/net position:			
Beginning of the year	(78,927)	352,671	273,744
End of the year	<u>\$ (784,380)</u>	<u>\$ 1,192,981</u>	<u>\$ 408,601</u>

See accompanying notes.

Majuro Atoll Local Government

Notes to Financial Statements

Year ended September, 2017

1. Organization

Majuro Atoll Local Government (MALGOV) was established pursuant to Public Law 1981-2, the Local Government Act of the Republic of the Marshall Islands (RepMar) and operates under the Constitution of the Majuro Atoll Local Government. MALGOV is governed by an elected mayor and a fifteen-member council.

2. Summary of Significant Accounting Policies

The accompanying basic financial statements of MALGOV have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of MALGOV's accounting policies are described below.

Government-wide and Fund Financial Statements

Government-wide Financial Statements:

The Statement of Net Position and the Statement of Activities report financial information on all of the non-fiduciary activities of the primary government. For the most part, the effect of interfund activity has been eliminated from these statements.

Primary government activities are defined as governmental activities, which normally are supported by taxes, intergovernmental revenues and other non-exchange revenues.

The Statement of Net Position presents MALGOV's non-fiduciary assets and deferred outflows of resources, and liabilities and deferred inflows of resources, with the difference reported as net position. Net position is reported in three categories:

- Net investment in capital assets consist of capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- Restricted net position results when constraints placed on net position use that are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through enabling legislation. MALGOV has no restricted net position at September 30, 2017.
- Unrestricted net position consists of net position, which does not meet the definition of the two preceding categories. Unrestricted net position often is designated, to indicate that management does not consider them to be available for general operations. They often have restrictions that are imposed by management but can be removed or modified.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Government-wide and Fund Financial Statements, continued

Government-wide Financial Statements, continued:

The Statement of Activities demonstrates the degree to which the direct expenses of given functions or segments are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function or segment. Program revenues include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items not meeting the definition of program revenues are, instead, reported as general revenues.

Fund Financial Statements

MALGOV uses one governmental fund to report on its financial position and results of operations. The operations of this fund are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures.

Separate financial statements are provided for governmental funds. MALGOV presents a balance sheet and a statement of revenues, expenditures and changes in fund balances for its governmental fund. The ending fund balance on the balance sheet is then reconciled to the ending governmental net position.

Adjustments required to reconcile total governmental fund balance to net position of governmental activities in the Statement of Net Position are as follows:

Total fund balance - governmental funds		\$(784,380)
Add:		
Depreciable capital assets	2,722,154	
Accumulated depreciation	(1,403,391)	
		1,318,763
Less:		
Loan payable		(125,782)
Total net position - governmental activities		\$ <u>408,601</u>

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Government-wide and Fund Financial Statements, continued

Fund Financial Statements, continued

Adjustments required to reconcile net change in total governmental fund balance to change in net position of governmental activities in the Statement of Activities are as follows:

Net change in fund balance - governmental funds	\$(705,453)
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Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. For the current year, these amounts consist of:

Capital outlays	1,232,794	
Depreciation expense	(392,484)	
		<u>840,310</u>

Change in net position - governmental activities	\$ <u>134,857</u>
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Measurement Focus and Basis of Accounting

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows. Grants and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements account for the general governmental activities of MALGOV and are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as they become susceptible to accrual; generally, when they are both measurable and available. Revenues are available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, MALGOV considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

Amounts reported as program revenues include (1) charges to customers or applicants for goods, services, or privileges provided, (2) operating grants and contributions, and (3) capital grants and contributions. Internally dedicated resources are reported as general revenues rather than as program revenues. General revenues are derived from taxation and other items that are not allocated to specific programs.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Measurement Focus and Basis of Accounting, continued

Unrestricted contributions and grants are recorded as revenue in the statement of revenues, expenditures, and changes in fund balances when received (in the case of contributions) or when approved by the grantor agency (in the case of grants).

Cash and Cash Equivalents

Custodial credit risk is the risk that in the event of a bank failure, MALGOV's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. MALGOV does not have a deposit policy for custodial credit risk.

For purposes of the balance sheet/statement of net position, cash and cash equivalents is defined as cash on hand and cash held in demand accounts. As of September 30, 2017, the carrying amount of the primary government's total cash and cash equivalents was \$298,897 and the corresponding bank balances were \$397,219. Of the bank balances, \$309,435 is maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2017, bank deposits in the amount of \$250,000 were FDIC insured. The remaining bank deposits of \$87,784 are maintained in financial institutions not subject to depository insurance. MALGOV does not require collateralization of its cash deposits; therefore, deposit levels more than FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

Receivables

In general, tax revenues are recognized on the government-wide financial statements, when assessed or levied, and on the governmental fund financial statements to the extent that it is both measurable and available. Tax receivables are primarily due from businesses and individuals residing on islands within the Majuro Atoll.

In accordance with Executive Committee Minute 01-2016, MALGOV executed certain uncollateralized and interest-free financing arrangements with employees for the purpose of purchasing vehicles. MALGOV financed 35% of the purchase price with the remaining 65% of the purchase price due from the employee. Repayment of amounts due from employees occurs through bi-weekly payroll deductions. As of September 30, 2017, the amount of \$286,617 is due from employees under these arrangements.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Capital Assets

Capital assets, which consist of vehicles, furniture and fixtures, and other equipment, are reported in the government-wide financial statements. Such assets, whether purchased or constructed, are recorded at historical cost or estimated historical cost. Contributed capital assets are recorded at estimated fair market value at the date of donation. Title to the land on which MALGOV's facilities are located is held in the name of the landowner. Fair market rental value related to this property has not been assessed or recorded.

MALGOV has not developed a capitalization policy. The costs of normal maintenance and repairs that do not add to the value of assets or materially extend asset lives are not capitalized. Capital assets are depreciated using the straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded in the statement of activities. Estimated useful lives for depreciable assets are as follows:

Vehicles and heavy equipment	3 to 7 years
Furniture and fixtures	2 to 5 years
Other equipment	6 years

Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to a future period and will not be recognized as an outflow of resources (deduction of net position) until then. MALGOV has no items that qualify for reporting in this category.

Compensated Absences

It is MALGOV's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. There is no liability for unpaid accumulated sick leave since MALGOV does not have a policy to pay any amounts when employees separate from service with MALGOV. All vacation pay is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, because of employee resignations or retirements.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Deferred Inflows of Resources

In addition to liabilities, the statement of financial position reports a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net assets that applies to a future period and so will not be recognized as an inflow of resources until then. MALGOV has no items that qualify for reporting in this category.

Fund Balance

Governmental fund balances are classified as follows:

Non-spendable - includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.

Restricted - includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.

Committed - includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision-making authority and does not lapse at year-end.

Assigned - includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed.

Unassigned - includes negative fund balances in other governmental funds.

Restricted/committed amounts are spent first when both restricted and unrestricted fund balance is available unless there are legal documents/contracts that prohibit doing this. In addition, committed, then assigned, and lastly unassigned amounts of unrestricted fund balance are expended in that order.

MALGOV has a general policy to first use restricted resources for expenditures incurred for which both restricted and unrestricted (committed, assigned, and unassigned) resources are available. When expenditures are incurred for which only unrestricted resources are available, the general policy of MALGOV is to use committed resources first, followed by assigned, and then unassigned. The use of restricted/committed resources may be deferred based on a review of the specific transaction.

A formal minimum fund balance policy has not been adopted.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts assets and liabilities and disclosure of contingent assets and liabilities at the date of financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results may differ from those estimates.

Recently Adopted Accounting Pronouncements

During the year ended September 30, 2017, MALGOV implemented the following pronouncements:

- GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement No. 68, and Amendments to Certain Provisions of GASB Statements No. 67 and No. 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements No. 67 and No. 68 with the reporting requirements in Statement No. 68.
- GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, as amended*, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which addresses financial reporting requirements for governments whose employees are provided with postemployment benefits other than pensions (other postemployment benefits or OPEB).
- GASB Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements.
- GASB Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*, which addresses a practice issue regarding the scope and applicability of Statement No. 68, *Accounting and Financial Reporting for Pensions*.
- GASB Statement No. 80, *Blending Requirements for Certain Component Units - an amendment of GASB Statement No. 14*, which improves financial reporting by clarifying the financial statement presentation requirements for certain component units.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Recently Adopted Accounting Pronouncements, continued

- GASB Statement No. 82, *Pension Issues - an amendment of GASB Statements No. 67, No. 68, and No. 73*, which addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

The implementation of these statements did not have a material effect on the accompanying financial statements.

Upcoming Accounting Pronouncements

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, as amended*, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 75 will be effective for fiscal year ending September 30, 2018.

In March 2016, GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements*, which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 81 will be effective for fiscal year ending September 30, 2018.

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which addresses accounting and financial reporting for certain asset retirement obligations (AROs) associated with the retirement of a tangible capital asset. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 84 will be effective for the fiscal year ending September 30, 2020.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*, which establishes criteria for identifying fiduciary activities of all state and local governments. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 84 will be effective for the fiscal year ending September 30, 2021.

In March 2017, GASB issued Statement No. 85, *Omnibus 2017*, which address practice issues that have been identified during implementation and application of certain GASB Statements including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits). MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 85 will be effective for fiscal year ending September 30, 2018.

In May 2017, GASB issued Statement No. 86, *Certain Debt Extinguishment Issues*, which improves consistency in accounting and financial reporting for in-substance defeasance of debt. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 86 will be effective for fiscal year ending September 30, 2018.

In June 2017, GASB issued Statement No. 87, *Leases*, which establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 87 will be effective for the fiscal year ending September 30, 2022.

In April 2018, GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*, which improves the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 88 will be effective for fiscal year ending September 30, 2019.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In June 2018, GASB issued Statement No. 89, *Accounting for Interest Cost Incurred Before the End of a Construction Period*, which (1) enhances the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and (2) simplifies accounting for interest cost incurred before the end of a construction period. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 89 will be effective for the fiscal year ending September 30, 2022.

In August 2018, GASB issued Statement No. 90, *Majority Equity Interest - an Amendment of GASB Statements No. 14 and No. 61*, which improves the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and the relevance of financial statement information for certain component units. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 90 will be effective for fiscal year ending September 30, 2020.

In May 2019, GASB issued Statement No. 91, *Conduit Debt Obligations*, which provides a single method of reporting conduit debt obligations by issuers and eliminates diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. In accordance with GASB Statement No. 95, GASB Statement No. 91 will be effective for the fiscal year ending September 30, 2023.

In January 2020, GASB issued Statement No. 92, *Omnibus 2020*, which enhances comparability in accounting and financial reporting and improves the consistency of authoritative literature by addressing practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about the effective date of Statement No. 87, *Leases*, and Implementation Guide No. 2019-3, *Leases*, for interim financial reports, the terminology used to refer to derivative instruments and the applicability of certain requirements of Statement No. 84, *Fiduciary Activities*, to postemployment benefits. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. The requirements related to the effective date of GASB Statement No. 87 and Implementation Guide 2019-3, reissuance recoveries and terminology used to refer to derivative instruments are effective upon issuance. In accordance with GASB Statement No. 95, the remaining requirements of GASB Statement No. 92 are effective for the fiscal year ending September 30, 2022.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In March 2020, GASB issued Statement No. 93, *Replacement of Interbank Offered Rates (IBORs)*, which establishes accounting and financial reporting requirements related to the replacement of IBORs, most notably, the London Interbank Offered Rate (LIBOR), in hedging derivative instruments and leases. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. In accordance with GASB Statement No. 95, the requirements of GASB Statement No. 93 are effective for the fiscal year ending September 30, 2022. In accordance with GASB Statement No. 95, the requirements of GASB Statement No. 93 relative to the removal of LIBOR as an appropriate benchmark interest rate is effective for the fiscal year ending September 30, 2023. All other requirements of GASB Statement No. are effective for the fiscal year ending September 30, 2022.

In March 2020, GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The primary objective of this Statement is to improve financial reporting by addressing issues related to public-private and public-public partnership arrangements. This Statement also provides guidance for accounting and financial reporting for availability payment arrangements. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 94 will be effective for the fiscal year ending September 30, 2023.

In May 2020, GASB issued Statement No. 95, *Postponement of the Effective Dates of Certain Authoritative Guidance*, which postpones the effective dates of GASB Statement No. 84, 89, 90, 91, 92 and 93 by one year and GASB Statement No. 87 by 18 months; however, earlier application of the provisions addressed in GASB Statement No. 95 is encouraged and permitted to the extent specified in each pronouncement as originally issued. In accordance with GASB Statement No. 95, MALGOV has elected to postpone implementation of these statements.

In May 2020, GASB issued Statement No. 96, *Subscription-Based Information Technology Arrangements*. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset - an intangible asset - and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 96 will be effective for the fiscal year ending September 30, 2023.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In June 2020, GASB issued Statement No. 97, *Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans - an amendment of GASB Statements No. 14 and No. 84, and a supersession of GASB Statement No. 32*. The primary objectives of this Statement are to (1) increase consistency and comparability related to the reporting of fiduciary component units in circumstances in which a potential component unit does not have a governing board and the primary government performs the duties that a governing board typically would perform; (2) mitigate costs associated with the reporting of certain defined contribution pension plans, defined contribution other postemployment benefit (OPEB) plans, and employee benefit plans other than pension plans or OPEB plans (other employee benefit plans) as fiduciary component units in fiduciary fund financial statements; and (3) enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 97 will be effective for the fiscal year ending September 30, 2022.

In October 2021, GASB issued Statement No. 98, *The Annual Comprehensive Financial Report*, which establishes the term annual comprehensive financial report and its acronym ACFR. That new term and acronym replace instances of comprehensive annual financial report and its acronym in generally accepted accounting principles for state and local governments. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 98 will be effective for the fiscal year ending September 30, 2022.

In April 2022, GASB issued Statement No. 99, *Omnibus 2022*, which contains guidance whose effective dates are in future periods. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 99:

- 1) Modifies guidance in GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, to bring all guarantees under the same financial reporting requirements and disclosures effective for fiscal year ending September 30, 2024.
- 2) Provides guidance on classification and reporting of derivative instruments within the scope of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, effective for fiscal year ending September 30, 2024.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

- 3) Provides clarification of provisions in GASB Statement No. 87 related to the determination of the lease term, classification of a lease as a short-term lease, recognition and measurement of a lease liability and a lease asset, and identification of lease incentives effective for fiscal year ending September 30, 2023.
- 4) Provides clarification of provisions in GASB Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*, related to (a) the determination of the public-private and public-public partnership (PPP) term and (b) recognition and measurement of installment payments and the transfer of the underlying PPP asset. Effective for fiscal year ending September 30, 2023.
- 5) Provides clarification of provisions in GASB Statement No. 96, *Subscription-Based Information Technology Arrangements*, related to the subscription-based information technology arrangement (SBITA) term, classification of a SBITA as a short-term SBITA, and recognition and measurement of a subscription liability. Effective for fiscal year ending September 30, 2023.
- 6) Modifies accounting and reporting guidance in GASB Statement No. 53 related to termination of hedge. Guidance is effective for fiscal year ending September 30, 2023.

In June 2022, GASB issued Statement No. 100, *Accounting Changes and Error Corrections - An Amendment of GASB Statement No. 62*, which enhances accounting and financial reporting requirements for accounting changes and error corrections and requires that (a) changes in accounting principles and error corrections be reported retroactively by restating prior periods, (b) changes to or within the financial reporting entity be reported by adjusting beginning balances of the current period, and (c) changes in accounting estimates be reported prospectively by recognizing the change in the current period. Requirements applicable to changes in accounting principles apply to the implementation of a new pronouncement if there is no specific transition guidance in the new pronouncement. The Statement also requires that aggregate amounts of adjustments to, and restatements of, beginning net position, fund balance, or fund net position, as applicable, be displayed by reporting unit in the financial statements. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 100 will be effective for fiscal year ending September 30, 2024.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In June 2022, GASB issued Statement No. 101, *Compensated Absences*, which better meets the information needs of financial statement users by updating the recognition and measurement guidance for compensated absences. This Statement requires that liabilities for compensated absences be recognized for leave that has not been used and leave that has been used but not yet paid, provided the services have occurred, the leave accumulates, and the leave is more likely than not to be used for time off or otherwise paid in cash or noncash means. In estimating the leave that is more likely than not to be used or otherwise paid or settled, a government should consider relevant factors such as employment policies related to compensated absences and historical information about the use or payment of compensated absences. Leave that is more likely than not to be settled through conversion to defined benefit postemployment benefits should not be included in a liability for compensated absences. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 101 will be effective for fiscal year ending September 30, 2025.

In December 2023, GASB issued Statement No. 102, *Certain Risk Disclosures*, which provides users of the government financial statements with essential information about risks related to a government's vulnerabilities due to ascertain concentrations or constraints. This Statement requires a government to assess whether a concentration or constraint makes the primary government reporting unit or other reporting units that report a liability for revenue debt vulnerable to the risk of a substantial impact. Additionally, this Statement requires a government to assess whether an event or events associated with a concentration or constraint that could cause the substantial impact to have occurred, have begun to occur, or are more likely than not to begin to occur within 12 months of the date the financial statements are issued. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 102 will be effective for fiscal year ending September 30, 2025.

In April 2024, GASB issued Statement No. 103, *Financial Reporting Model Improvements*, which improves key components of the financial reporting model to enhance its effectiveness in providing information that is essential for decision making and assessing a government's accountability. This Statement also addresses certain application issues identified through agenda research conducted by the GASB. This Statement establishes new accounting and financial reporting requirements - or modifies existing requirements - related to the following: a) management's discussion and analysis (MD&A); b) unusual or infrequent items; c) presentation of the proprietary fund statement of revenues, expenses, and changes in fund net position; d) information about major component units in basic financial statements; e) budgetary comparison information; and f) financial trends information in the statistical section. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 103 will be effective for fiscal year ending September 30, 2026.

Majuro Atoll Local Government

Notes to Financial Statements, continued

2. Summary of Significant Accounting Policies, continued

Upcoming Accounting Pronouncements, continued

In September 2024, GASB issued Statement No. 104, *Disclosure of Certain Capital Assets*, which provides users of government financial statements with essential information about certain types of capital assets. This Statement requires certain types of capital assets to be disclosed separately in the capital assets note disclosures required by Statement 34. Lease assets recognized in accordance with Statement No. 87, *Leases*, and intangible right-to-use assets recognized in accordance with Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*, should be disclosed separately by major class of underlying asset in the capital assets note disclosures. Subscription assets recognized in accordance with Statement No. 96, *Subscription-Based Information Technology Arrangements*, also should be separately disclosed. In addition, this Statement requires intangible assets other than those three types to be disclosed separately by major class. This Statement also requires additional disclosures for capital assets held for sale. A capital asset is a capital asset held for sale if (a) the government has decided to pursue the sale of the capital asset and (b) it is probable that the sale will be finalized within one year of the financial statement date. Governments should consider relevant factors to evaluate the likelihood of the capital asset being sold within the established time frame. This Statement requires that capital assets held for sale be evaluated each reporting period. Governments should disclose (1) the ending balance of capital assets held for sale, with separate disclosure for historical cost and accumulated depreciation by major class of asset, and (2) the carrying amount of debt for which the capital assets held for sale are pledged as collateral for each major class of asset. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 104 will be effective for the fiscal year ending September 30, 2026.

In December 2025, GASB issued Statement No. 105, *Subsequent Events*, which improves the financial reporting requirements for subsequent events, thereby enhancing consistency in their application and better meeting the information needs of financial statement users. MALGOV is evaluating the effect that this Statement, upon implementation, will have on the financial statements. GASB Statement No. 105 will be effective for the fiscal year ending September 30, 2027.

Majuro Atoll Local Government

Notes to Financial Statements, continued

3. Capital Assets

Capital asset activity for the year ended September 30, 2017, was as follows:

	October 1, 2016	Additions	Transfers and Disposals	September 30, 2017
Vehicles	\$ 1,227,848	\$ 667,948	\$ ---	\$ 1,895,796
Furniture and fixtures	41,193	516,559	---	557,752
Other equipment	<u>220,319</u>	<u>48,287</u>	<u>---</u>	<u>268,606</u>
	1,489,360	1,232,794	---	2,722,154
Less accumulated depreciation	(<u>1,010,907</u>)	<u>(392,484)</u>	<u>---</u>	<u>(1,403,391)</u>
	\$ <u>478,453</u>	\$ <u>840,310</u>	\$ <u>---</u>	\$ <u>1,318,763</u>

4. Withholding Taxes Payable

As of September 30, 2017, MALGOV was liable for withholding taxes payable to the Republic of the Marshall Islands (RepMar) in the aggregate amount of \$1,208,547, which includes related penalties and interest of \$233,912. No repayment schedule with RepMar exists and thus the entire amount has been reflected as a current liability in the accompanying financial statements.

5. Short-term Borrowings

On February 17, 2017, MALGOV executed a \$300,000 loan with a bank, interest at 12% per annum, due in monthly installments of \$26,097 plus interest, commencing March 17, 2017 through February 17, 2018, collateralized by an assignment of quarterly allotments from RepMar and an assignment of sales taxes. Loan proceeds were used to finance certain operational activities. As of September 30, 2017, loan payable to bank amounted to \$130,209.

6. Note Payable

Note payable to the Marshall Islands Development Bank (MIDB) in the original amount of \$208,524, interest at 6.5% per annum, collateralized by certain motor vehicles, an assignment of quarterly allotments from RepMar and an assignment of sales taxes. The note payable was originally due on July 15, 1998. Management of MALGOV subsequently agreed with MIDB for repayment to commence in January 2002; however, the terms of this agreement have not been documented. No changes occurred during the year ended September 30, 2017 in liabilities reported as part of MALGOV's long-term liabilities in the statement of net position. As of September 30, 2017, note payable to MIDB amounted to \$125,782.

Majuro Atoll Local Government

Notes to Financial Statements, continued

7. RepMar Appropriations

During the year ended September 30, 2017, MALGOV was the recipient of appropriations from RepMar's Nitijela. A summary of RepMar appropriations by funding source received by MALGOV for the year ended September 30, 2017 is as follows:

ROC Capital Projects Fund:	
Majuro Development Projects	\$ 595,200
Majuro Seawall Project	309,107
General Fund:	
Majuro Seawall Project	<u>496,000</u>
	<u>\$1,400,307</u>

As of September 30, 2017, \$124,000 relating to these appropriations is due from RepMar.

8. Commitments and Contingencies

Commitments

On January 6, 2017, MALGOV executed a 2-year memorandum of agreement with the Marshall Islands Marine Resources Authority (MIMRA) with respect to the joint monitoring of transshipment and other enforcement activities related to such transshipments. In accordance with the terms of the agreement, MIMRA is required to collect and remit to MALGOV the amount of \$400 per vessel calling into Majuro Port for transshipment purposes. The total amount collected by MIMRA is payable to MALGOV on a quarterly basis. During the year ended September 30, 2017, MIMRA remitted \$157,200 to MALGOV in accordance with this agreement with \$57,200 due and receivable at September 30, 2017.

MALGOV has entered into various land lease agreements with landowners for periods ending up to July 1, 2047. Under the terms of the lease agreements, MALGOV is obligated to pay annual instalments in advance of amounts ranging from \$1,000 to \$9,518.

Majuro Atoll Local Government

Notes to Financial Statements, continued

8. Commitments and Contingencies, continued

Commitments, continued

Future minimum lease payments under these lease agreements are as follows:

<u>Year ending</u> <u>September 30,</u>	
2018	\$ 13,518
2019	13,518
2020	18,974
2021	30,946
2022	34,145
2023 - 2027	170,725
2028 - 2032	170,725
2033 - 2037	170,725
2038 - 2042	162,753
2043 - 2047	<u>52,363</u>
	<u>\$838,932</u>

Contingencies

MALGOV is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. MALGOV has elected not to purchase commercial insurance coverage from independent third parties for the risks of loss to which it is exposed. Instead, MALGOV believes it is more economical to manage its risks internally. Claims expenses and liabilities are reported when it is probable that a loss has occurred, and the amount of that loss can be reasonably estimated. No losses because of these risks have occurred for the past three years.

Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Honorable Mayor Ladie Jack
Majuro Atoll Local Government

We have audited, 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 (*Government Auditing Standards*), the financial statements of the governmental activities and the general fund of the Majuro Atoll Local Government (MALGOV) as of and for the year ended September 30, 2017, and the related notes to the financial statements, which collectively comprise MALGOV's basic financial statements, and have issued our report thereon dated July 24, 2026.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered MALGOV's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of MALGOV's internal control. Accordingly, we do not express an opinion on the effectiveness of MALGOV'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 MALGOV'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 the attention of those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. We identified certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as items 2017-001 through 2017-009, that we consider to be material weaknesses.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether MALGOV's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*, which are described in the accompanying Schedule of Findings and Responses as items 2017-010 through 2017-012.

MALGOV's Response to Findings

Government Auditing Standards requires the auditor to perform limited procedures on MALGOV's response to the findings identified in our audit and described in the accompanying Schedule of Findings and Responses. MALGOV's response was not subjected to the other auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Ernst + Young LLP

July 24, 2026

Majuro Atoll Local Government
Schedule of Findings and Responses

Year ended September 30, 2017

Finding No. 2017-001

Area: Financial Reporting

Criteria: Government-wide financial statements prepared in accordance with Governmental Accounting Standards Board (GASB) standards require governments to report expenses by function in the statement of activities. At a minimum, direct expenses should be reported for each governmental function or program.

Condition: During our audit, we noted the government did not present expenses by functional classification in the statement of activities. Expenses were aggregated without appropriate functional allocation and presented in a manner inconsistent with GASB reporting requirements.

Cause: The condition appears to result from inadequate financial statement preparation and review procedures to ensure compliance with applicable governmental accounting standards related to government-wide financial statement presentation.

Effect: Failure to properly report expenses by function reduces the transparency and usefulness of the financial statements to users and may result in noncompliance with generally accepted accounting principles applicable to governmental entities. Users of the financial statements may be unable to adequately evaluate the cost of governmental functions and programs.

Recommendation: We recommend management implement procedures to ensure expenses are properly classified and reported by function in the statement of activities in accordance with applicable GASB requirements. This process should include a detailed review of expense classifications and supporting allocations during the financial statement preparation process.

Views of responsible officials: Management appreciates the auditor's recommendation. The finding relates to the financial reporting process in place during the fiscal year ended September 30, 2017. Since that time, management has strengthened the financial statement preparation and review process to ensure expenditures are appropriately classified and presented in accordance with applicable GASB reporting requirements.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-002

Area: Bank Accounts

Criteria: Sound internal control practices and generally accepted accounting principles require that bank accounts be reconciled timely and accurately to the accounting records to ensure that recorded cash balances are complete, accurate, and properly supported. In addition, effective internal controls over financial reporting require supervisory review and resolution of reconciling items.

Condition: During our audit, we noted the following recorded cash account balances reflected in the general ledger that were not supported by completed and accurate bank reconciliations:

<u>GL Acct #</u>	<u>GL Acct Name</u>	<u>Unadjusted Balance</u>	<u>Adjusting Entry</u>
1010	General Fund	\$(20,896)	\$20,896
1011	Grant Fund	\$5,873	\$(5,873)
1012	Payroll Account	\$10,316	\$(13,041)
1021	General Account	\$(151)	\$151
1023	Special Education Fund	\$15	\$(15)
1030	Copra Fund	\$10,026	\$(10,026)
1032	Pilot School Fund	\$150	\$(150)
1033	Payroll Pilot School	\$246	\$(246)
1034	Majuro Day	\$10,663	\$(10,663)
1035	TCD Account	\$45,000	\$(45,000)
1036	Savings Account	\$42,443	\$(42,443)
1038	MALGOV Reserve Account	\$1,000	\$(1,000)
1039	Majuro Day	\$(2,348)	\$2,348
1040	RECD Grant	\$1,500	\$(1,500)
1041	Japanese Grant – Woja Project	\$90,000	\$(90,000)
1042	India Grant	\$100,000	\$(100,000)
1046	Majuro Day 2013	\$(605)	\$605
1048	Majuro Day 2015	\$495	\$(90)
1050	Ajeltake Too Ook Aetok Project	\$(1,414)	\$1,414
1051	Majuro Day 2017	\$19,780	---
1052	Ajeltake Community Development Fund	\$1,000	---

Management subsequently provided adjusting entries to correct recorded account balances.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-002, continued

Area: Bank Accounts

Cause: The condition appears to have resulted from inadequate monitoring and review of the bank reconciliation process, insufficient staffing resources, and a lack of internal control policies and procedures to ensure reconciliations are completed and reviewed on a timely basis.

Effect: Failure to prepare and maintain accurate bank reconciliations increases the risk that errors, omissions, unauthorized transactions, or misappropriation of assets may not be detected timely. In addition, unsupported cash balances may result in material misstatements to the financial statements.

Recommendation: We recommend management implement procedures to ensure all bank reconciliations are prepared completely and accurately each month, reviewed by appropriate supervisory personnel, and resolved timely for all outstanding reconciling items. Management should also ensure that the reconciled cash balances agree to the general ledger and supporting bank documentation.

Views of responsible officials: Management appreciates the auditor's recommendation. During the audit, management reviewed the historical bank reconciliations and accepted the proposed audit adjustments where appropriate to ensure the financial statements were fairly presented. Management has since implemented monthly bank reconciliations for all active bank accounts, with supervisory review and timely resolution of reconciling items to strengthen internal controls over cash management.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-003

Area: Accounts Receivable

Criteria: Effective internal controls over financial reporting require that subsidiary ledgers be maintained accurately and reconciled regularly to the general ledger. In addition, generally accepted accounting principles require that accounts receivable balances reported in the financial statements be supported by detailed underlying records that are complete and accurate.

Condition: During our audit, we noted that the following recorded accounts receivable balances reflected in the general ledger were either not reconciled to or supported by detailed subsidiary ledger records:

<u>GL Acct #</u>	<u>GL Acct Name</u>	<u>Unadjusted Balance</u>	<u>Adjusting Entry</u>
1111	Accounts Receivable – Customers	\$494,718	\$(100,075)
1112	Accounts Receivable – Employees	\$167,187	\$(295)
1115	Accounts Receivable – Returned Checks	\$5,222	---
1420	Due From MADF	\$108,794	\$(108,794)

Specifically, subsidiary ledger balances did not reconcile to the general ledger, and management was unable to provide sufficient documentation supporting certain receivable amounts recorded at year-end. Such was resolved through alternative audit procedures and management subsequently provided adjusting entries to correct recorded account balances.

Furthermore, alternative audit procedures over employee accounts receivable indicated unrecorded balances associated with financing arrangements with employees for the purpose of purchasing vehicles aggregating \$83,318 were not correctly recorded as receivables due from employees. Audit adjustments were proposed to correct this misstatement.

Cause: The condition appears to have resulted from inadequate reconciliation procedures, insufficient review of receivable activity, and a lack of formal processes to ensure that subsidiary ledger balances agree to the general ledger on a timely basis.

Effect: Failure to maintain accurate and reconciled subsidiary ledger records increases the risk that errors, omissions, or unsupported receivable balances may occur and remain undetected. As a result, accounts receivable and related revenue balances may be materially misstated.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-003, continued

Area: Accounts Receivable

Recommendation: We recommend management establish and implement procedures to ensure accounts receivable subsidiary ledgers are maintained completely and accurately and reconciled to the general ledger on a regular basis. Reconciling differences should be investigated and resolved timely, and supervisory review of reconciliations should be documented.

Views of responsible officials: Management concurs with the auditor's recommendation. During the audit, management reviewed the historical accounts receivable balances and accepted the proposed audit adjustments where appropriate to ensure the financial statements were fairly presented. Management has implemented routine reconciliations between subsidiary ledgers and the general ledger, strengthened supporting documentation, and enhanced monitoring of outstanding receivable balances.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-004

Area: Allowance for Doubtful Accounts

Criteria: Generally accepted accounting principles require that accounts receivable be reported at their net realizable value, including an appropriate allowance for doubtful accounts. Effective internal controls over financial reporting require management to periodically evaluate receivable balances and estimate potential uncollectible amounts based on available information and reasonable assumptions.

Condition: During our audit, we noted the recorded allowance for doubtful accounts totaling \$91,818 was not supported by an underlying evaluation of the collectability of outstanding receivable balances. Management subsequently represented that no allowance for doubtful accounts was required and subsequently provided an adjusting entry to correct the recorded account balance.

Cause: The condition appears to have resulted from the lack of formal policies and procedures requiring periodic review and analysis of outstanding receivable balances and related collection experience.

Effect: Failure to perform a periodic analysis of the allowance for doubtful accounts increases the risk that accounts receivable and bad debt expense may be materially misstated. In addition, financial statements may not accurately reflect the estimated amount expected to be collected.

Recommendation: We recommend management establish formal procedures to perform and document periodic analyses of the allowance for doubtful accounts. The analysis should consider factors such as the aging of receivables, historical collection experience, current economic conditions, specific account reviews, and other relevant information affecting collectability. The allowance should be adjusted as necessary to ensure receivables are reported at net realizable value.

Views of responsible officials: Management appreciates the auditor's recommendation. During the audit, management reviewed the allowance for doubtful accounts and recorded the necessary adjustment to ensure the financial statements were fairly presented. Management now performs periodic assessments of outstanding receivables based on aging reports, collection history, and other relevant information to ensure receivables are reported at their estimated net realizable value.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-005

Area: Capital Assets

Criteria: Effective internal controls over capital assets require management to maintain accurate and complete fixed asset records and periodically assess whether recorded assets continue to exist and provide service utility. Generally accepted accounting principles require capital assets to be properly recorded, depreciated, and removed from the accounting records upon disposal or when no longer in service.

Condition: During our audit, we noted that the fixed asset ledger included capital assets that were fully depreciated and no longer in use by the local government. These assets remained recorded in the underlying fixed asset records without evidence of periodic review to determine whether such assets should be removed from the accounting records. Management subsequently provided adjusting entries to correct recorded account balances to reduce asset cost and related accumulated depreciation by \$1,716,328 and \$1,730,361, respectively.

Cause: The condition appears to have resulted from the lack of periodic physical inventories and management review of the fixed asset ledger to identify assets that are obsolete, disposed of, or no longer in use.

Effect: Failure to periodically review the fixed asset ledger may result in inaccurate capital asset records, including the continued reporting of assets that no longer exist or provide value to the entity. In addition, the lack of accurate asset records may impair management's ability to safeguard assets and monitor capital asset activity effectively.

Recommendation: We recommend management establish procedures to periodically review the fixed asset ledger and perform physical inventories of capital assets to identify assets that are obsolete, disposed of, or no longer in use. Assets identified as no longer in service should be evaluated for removal from the accounting records in accordance with applicable accounting policies.

Views of responsible officials: Management concurs with the auditor's recommendation. During the audit, management reviewed the historical fixed asset records and accepted the proposed audit adjustments to remove assets that were no longer in service. Management has since enhanced capital asset procedures by maintaining an updated fixed asset register and ensuring obsolete or disposed assets are identified and removed on a timely basis.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-006

Area: Capital Assets

Criteria: Effective internal controls over capital assets require periodic physical inventories to verify the existence and condition of assets and to ensure that fixed asset records are accurate and complete. Sound business practices also require entities to maintain adequate accountability over capital assets to safeguard public resources.

Condition: During our audit, we noted that the local government did not perform periodic physical inventories of capital assets. As a result, management could not verify the existence, condition, or location of certain capital assets recorded in the fixed asset ledger.

Cause: The condition appears to have resulted from the lack of formal policies and procedures requiring periodic physical inventories and reconciliation of capital assets to the fixed asset ledger.

Effect: Failure to conduct periodic inventories of capital assets increases the risk that lost, stolen, obsolete, or disposed assets may not be identified timely. In addition, inaccuracies in the fixed asset records may occur and remain undetected, potentially resulting in misstatements to the financial statements.

Recommendation: We recommend management establish and implement procedures requiring periodic physical inventories of capital assets. Inventory results should be reconciled to the fixed asset ledger, discrepancies should be investigated and resolved timely, and supporting documentation of the inventory process should be maintained.

Views of responsible officials: Management recognizes the importance of maintaining accurate capital asset records and appreciates the auditor's recommendation. Periodic physical verification of capital assets has since been implemented, with inventory results reconciled to the fixed asset register and discrepancies investigated and resolved in a timely manner.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-007

Area: Payroll Accruals

Criteria: Generally accepted accounting principles require expenditures and liabilities to be recognized in the period in which they are incurred. Effective internal controls over financial reporting require procedures to ensure payroll-related accruals are identified, calculated, reviewed, and recorded accurately at period-end.

Condition: During our audit, we noted that payroll-related expenditures and liabilities were not consistently accrued in the proper accounting period. Specifically, payroll costs incurred prior to September 30, 2017 in the amount of \$86,761 were not recorded as accrued liabilities and expenditures until the subsequent fiscal period. Furthermore, payroll costs incurred in the prior year in the amount of \$90,336 were not accrued in the prior year but recorded as expenditures in the current year. Audit adjustments were proposed to correct these misstatements.

Cause: The condition appears to have resulted from inadequate period-end closing procedures and the lack of formal processes to identify and record payroll accruals for services rendered prior to year-end.

Effect: Failure to record payroll accruals in the correct accounting period may result in an understatement or overstatement of expenditures, liabilities, and related fund balances or net position in the financial statements.

Recommendation: We recommend management establish and implement procedures to ensure payroll expenditures and related liabilities are accrued in the proper accounting period. Procedures should include identifying payroll earned but unpaid at year-end, calculating the related accruals accurately, and performing supervisory review of period-end payroll entries.

Views of responsible officials: Management appreciates the auditor's recommendation. During the audit, management reviewed the payroll accrual balances and accepted the proposed audit adjustments where appropriate to ensure payroll expenditures and liabilities were fairly presented. Management has strengthened year-end closing procedures to ensure payroll expenditures and related liabilities are recognized in the appropriate accounting period.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-008

Area: Accounts Payable

Criteria: Effective internal controls over financial reporting require that subsidiary ledgers be maintained accurately and reconciled regularly to the general ledger. In addition, generally accepted accounting principles require that accounts payable balances reported in the financial statements be supported by detailed underlying records that are complete and accurate.

Condition: During our audit, we noted that the following recorded accounts payable balances reflected in the general ledger were either not reconciled to or supported by detailed subsidiary ledger records:

<u>GL Acct #</u>	<u>GL Acct Name</u>	<u>Unadjusted Balance</u>	<u>Adjusting Entry</u>
2000	Accounts Payable	\$679,342	\$(573,909)
2002	Accrued Interest Payable	\$37,905	\$(37,905)
2004	Accounts Payable Adjustments	\$(19,000)	\$19,000
2015	Allotment Payable	\$255,294	\$(255,294)
2025	Bank of Hawaii	\$200	\$(200)
2027	Marshall Islands Service Corp	\$(301,501)	\$301,501
2029	G&L Enterprises	\$419	\$(419)
2038	MJCC	\$4,538	\$(4,538)
2049	Triple O Store	\$1,369	\$(1,369)
2064	Jenny Capelle	\$100	\$(100)
2510	Due to General Fund	\$108,794	\$(108,794)

Specifically, subsidiary ledger balances did not reconcile to the general ledger, and management was unable to provide sufficient documentation supporting certain payable amounts recorded at year-end. Such was resolved through alternative audit procedures and management subsequently provided adjusting entries to correct recorded account balances.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-008, continued

Area: Accounts Payable

Condition, continued: In addition, the following recorded liability account balances were not reconciled to underlying supporting documentation:

<u>GL Acct #</u>	<u>GL Acct Name</u>	<u>Unadjusted Balance</u>	<u>Adjusting Entry</u>
2005	Notes Payable	\$185,782	\$(60,000)
2006	Short-term Loan Payable	\$127,131	\$3,078
2010	Social Security Payable	\$68,134	\$55,814
2011	Income Tax Payable	\$1,586,523	\$(611,888)
2020	Accrued Salaries	\$7,588	\$18,811
2031	Individual Assurance Company-IAC	\$47,111	\$(47,111)

Audit adjustments were proposed to correct these misstatements.

Cause: The condition appears to have resulted from inadequate reconciliation procedures, insufficient review of payable activity, and a lack of formal processes to ensure that subsidiary ledger balances agree to the general ledger on a timely basis.

Effect: Failure to maintain accurate and reconciled subsidiary ledger records increases the risk that errors, omissions, or unsupported payable balances may occur and remain undetected. As a result, accounts payable and related expenditure balances may be materially misstated.

Recommendation: We recommend management establish and implement procedures to ensure accounts payable subsidiary ledgers are maintained completely and accurately and reconciled to the general ledger on a regular basis. Reconciling differences should be investigated and resolved timely, and supervisory review of reconciliations should be documented.

Views of responsible officials: Management concurs with the auditor's recommendation. During the audit, management reviewed the historical accounts payable balances and accepted the proposed audit adjustments where appropriate to ensure the financial statements were fairly presented. Management has implemented regular reconciliations between the accounts payable subsidiary ledger and the general ledger, strengthened supporting documentation requirements, and enhanced supervisory review procedures.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-009

Area: Accounts Payable

Criteria: Generally accepted accounting principles require expenditures and liabilities to be recognized in the period in which the underlying obligation is incurred, regardless of when payment is made. Effective internal controls over financial reporting require procedures to identify and record accounts payable and accrued liabilities timely and accurately at period-end.

Condition: During our audit, we noted that payments associated with delinquent accounts payable in the amount of \$105,000 were recorded as expenditures when paid rather than when the related goods or services were received. As a result, certain liabilities and expenditures were not recognized in the proper accounting period in accordance with the modified accrual basis of accounting. An audit adjustment was proposed to correct this misstatement.

Cause: The condition appears to have resulted from inadequate understanding and application of accrual basis accounting principles, as well as insufficient procedures for identifying and recording outstanding liabilities at year-end.

Effect: Failure to record delinquent accounts payable on the accrual basis may result in the understatement of liabilities and expenditures in one accounting period and the overstatement of expenditures in the subsequent period when payment is made. This condition may lead to inaccurate financial reporting and reduced comparability between reporting periods.

Recommendation: We recommend management establish and implement procedures to ensure liabilities are recorded in the period in which goods or services are received, regardless of payment date. Procedures should include timely review of unpaid invoices, identification of delinquent obligations, and recording of appropriate accounts payable and accrual entries at period-end.

Views of responsible officials: Management appreciates the auditor's recommendation. During the audit, management reviewed the accounting treatment of outstanding liabilities and accepted the proposed audit adjustment to ensure liabilities were recognized in the appropriate reporting period. Management has strengthened year-end closing procedures to ensure liabilities are recorded in the period in which goods or services are received in accordance with the applicable accounting standards.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-010

Area: Purpose Restricted Grants

Criteria: Generally accepted accounting principles and applicable grant agreements require grant revenues with purpose restrictions to be accounted for in accordance with the terms and conditions of the award. Effective internal controls require management to establish procedures to identify, monitor, and document compliance with grant restrictions and related expenditures.

Condition: During our audit, we noted the following grants with purpose restrictions received from RepMar's Nitijela, that were not consistently recorded and monitored in a manner that ensured expenditures were aligned with the specific grant requirements:

ROC Capital Projects Fund:	
Majuro Development Projects	\$ 595,200
Majuro Seawall Project	309,107
General Fund:	
Majuro Seawall Project	<u>496,000</u>
	<u>\$1,400,307</u>

Restricted grant revenues were recognized without adequate documentation demonstrating compliance with the related purpose restrictions.

Cause: The condition appears to have resulted from inadequate policies and procedures for tracking restricted grant activity and insufficient review of grant agreements to ensure compliance with applicable restrictions.

Effect: Failure to properly account for and monitor grants with purpose restrictions increases the risk of noncompliance with grant requirements, improper recognition of revenue, and misstatement of restricted balances, revenues, or expenditures in the financial statements.

Recommendation: We recommend management establish formal procedures to review grant agreements, identify applicable purpose restrictions, and maintain detailed records of grant revenues and related expenditures. Management should periodically monitor grant activity to ensure expenditures are allowable, properly documented, and incurred in accordance with the terms of the grant agreement.

Views of responsible officials: Management concurs with the auditor's recommendation. The finding relates to historical grant administration procedures for the fiscal year ended September 30, 2017. Management has strengthened grant management procedures by maintaining detailed grant records, monitoring expenditures against approved grant purposes, and periodically reviewing compliance with grant agreements.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-011

Area: Local Noncompliance

Criteria: 48 MIRC Chapter 1, Income Tax Act of 1989, Section 105, states that the employer shall once every four (4) weeks or thirteen times per year, pay taxes withheld under Section 104 under Chapter 1. The employer shall, along with the taxes, within two (2) weeks following the preceding four (4) week period make a full, true and correct return showing all wages and salaries paid by the employer to the employees during the preceding four (4) week period and showing the tax due and withheld thereon as provided in Section 104 of the Chapter.

Condition: MALGOV filed and paid income taxes withheld for the year ended September 30, 2017 in a manner inconsistent with the criteria. As of September 30, 2017, MALGOV was liable for income taxes withheld in the amount of \$974,635, which included unremitted income taxes withheld from prior years. Unrecorded penalties and interest associated with unremitted income taxes amounted to \$233,912 and \$116,956, respectively. Audit adjustments were proposed to correct these misstatements.

Cause: The cause of the above condition is the lack of policies and procedures to monitor timely filing of returns and payment of withheld income taxes.

Effect: The effect of the above condition is noncompliance with the RepMar Income Tax Act of 1989, as amended.

Recommendation: We recommend that management establish policies and procedures to comply with the RepMar Income Tax Act of 1989, as amended.

Views of responsible officials: Management appreciates the auditor's recommendation. During the audit, management reviewed the outstanding statutory payroll obligations and accepted the proposed audit adjustments where appropriate to ensure the financial statements were fairly presented. Management has strengthened procedures for the timely filing and remittance of statutory payroll obligations through regular reconciliations, periodic management review, and ongoing monitoring of outstanding tax liabilities to improve compliance with applicable legislation.

Majuro Atoll Local Government

Schedule of Findings and Responses, continued

Finding No. 2017-012

Area: Procurement

Criteria: Applicable procurement laws, regulations, and organizational policies require procurements to be conducted in a fair, transparent, and competitive manner. Effective internal controls over procurement activities require adequate documentation, appropriate approvals, and compliance with established purchasing thresholds and bidding requirements.

Condition: During our audit, we noted instances in which procurements were not conducted in accordance with applicable procurement laws, regulations, and established policies. Specifically, certain purchases lacked required competitive quotations or bids, supporting procurement documentation, or evidence of appropriate approvals as required by governing procurement requirements.

Cause: The condition appears to have resulted from inadequate understanding of procurement requirements, insufficient oversight of procurement activities, and the lack of formal policies and procedures to ensure compliance with applicable laws and regulations.

Effect: Failure to comply with procurement laws and regulations increases the risk of unauthorized purchases, favoritism, waste of public resources, and noncompliance with applicable legal and grant requirements. In addition, inadequate procurement practices may reduce transparency and public accountability.

Recommendation: We recommend management strengthen procurement procedures to ensure compliance with applicable procurement laws, regulations, and internal policies. Procedures should include adequate training for personnel involved in procurement activities, maintenance of complete procurement documentation, supervisory review of procurements, and periodic monitoring for compliance with purchasing requirements.

Views of responsible officials: Management concurs with the auditor's recommendation. The finding relates to procurement practices that existed during the fiscal year ended September 30, 2017. Management has strengthened procurement controls by implementing formal procurement procedures, requiring competitive quotations in accordance with established thresholds, maintaining complete supporting documentation, and enhancing management oversight to ensure compliance with applicable procurement policies and regulations.