

June 30, 2007

CONFIDENTIAL

Mr. William F. Roberts  
General Manager  
Marshalls Energy Company, Inc.  
P.O. Box 1439  
Majuro, Marshall Islands 96960

Dear Mr. Roberts:

In planning and performing our audit of the financial statements of Marshalls Energy Company, Inc. (MEC) for the year ended September 30, 2006, on which we have issued our report dated June 30, 2007, we developed the following recommendations concerning certain matters related to MEC's internal control and certain observations and recommendations on other accounting, administrative and operating matters. Our principal recommendations are summarized below:

(1) Billings - Electricity

Of twenty-five invoices tested, we noted one (invoice#551028) where the manual meter reading was missing. We recommend that management ensure that meter reading logs are maintained to support the accuracy and validity of customer billings.

(2) Purchases/Disbursements

Of twenty-five nonpayroll purchases/disbursements tested, we noted one instance paid through check #16024 that was an overpayment. We recommend that management establish adequate policies and procedures for the review of supporting invoices/contracts and computations to ensure accuracy of payments.

(3) Payroll

Of twenty-five payroll disbursements tested, we noted the following:

- Approved hours differed from hours paid for the following employees:

<u>Employee #</u>	<u>PPE</u>	<u>Approved Hours</u>	<u>Paid Hours</u>
G085	01/22/06	98	80
A021	01/22/06	80	85

(3) Payroll, Continued

- Certain authorized allotment forms were not located for the following employees:

<u>Employee #</u>	<u>PPE</u>
D004	11/13/05
A021	01/22/06
GO81	01/22/06
JG02	07/09/06
D006	10/16/05

We recommend that management ensure that employees are paid approved hours and that authorized allotment forms are retained. We recommended the same in our letter to management dated May 8, 2006.

(4) Electric Receivables

It is the policy of MEC to disconnect customer balances that have been overdue for over 60 days. However, a customer who signs a promissory note to make specific monthly payments or allotments is not disconnected, even though the monthly payments are lower than average monthly consumption. We noted two instances of allotments or monthly promissory note payments lower than monthly consumption. As a result, overdue balances do not decrease but instead increase by the amount of unpaid current consumption. We recommend that management review its policies and procedures and establish necessary changes to ensure that allotments or monthly payments of overdue accounts are sufficient to pay off overdue balances within a reasonable time period.

(5) Other Receivables

Reconciliation of subsidiary and general ledger balances is not performed on a regular basis. As a result, several adjustments were required at year end including an adjustment to correct a duplicate entry to sales. Management should ensure that accounts receivable subsidiary and general ledger balances are reconciled on a regular basis. We also recommend a thorough review of detail balances, including credit balances, to ensure their validity.

(6) Review of Suspect Report – Electricity Receivables

As a control measure to ensure that meter readings are input correctly, the billing system generates a suspect transaction report. This report highlights all transactions with a variance of 2% or more over the prior month. However, we did not see any evidence of review of these reports. We recommend that management implement policies and procedures to document reviews of the suspect report to ensure that meter readings are input accurately.

(7) Materials and Supplies

Of twenty-four materials and supplies items tested, the recorded unit cost for one item (part # PO90A, valued at \$33,485, per unit) varied from the actual unit cost of \$3,450. We also noted that the quantity in the valuation report for the following items varied from actual counts:

<u>Part#</u>	<u>Quantity Per Valuation Report</u>	<u>Quantity Per Count Sheet</u>
DZ034	128	0
NE0460	2	1

We recommend that management ensure that materials and supplies are accurately valued. This matter was discussed in our previous letters dated May 8, 2006 and January 11, 2005.

(8) Materials and Supplies Management

The inventory custodian in the Distribution Department also records issuances, receipts and adjustments to inventory. The annual physical count is also performed by the same individual. We recommend that appropriate internal control policies and procedures be established to ensure that responsibility for the following activities in relation to inventory management are segregated: (1) custody of inventory, (2) counting inventory periodically and comparing the counts to inventory records, and (3) processing inventory transactions (e.g., receipt, shipping) and/or adjustments. If one individual has responsibility for more than one of these functions, that individual could misappropriate assets and conceal the misappropriation.

(9) Fixed Asset

We were unable to verify existence of fixed asset #s 000005 and 000214 due to lack of sufficient information on the fixed asset register. Further, fixed assets are not tagged; thus, identification of assets could not be performed. We recommend that management ensure that relevant information on each fixed asset is entered in the fixed asset system to enable identification of assets. We also recommend attaching pre-numbered identification tags to fixed assets to facilitate the identification of fixed assets.

(10) Depreciation Rates

MEC is required to apply RUS approved depreciation rates on all fixed assets. The list of approved depreciation rates could not be located. We recommend that this list be located and copies provided to relevant accounting staff who are responsible for recording and depreciating fixed assets. This matter was discussed in our previous letters dated May 8, 2006, January 11, 2005 and December 18, 2003.

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(11) Insurance

The franchise agreement with RepMar governing solar and other renewable alternative energy systems effective April 15, 2003, requires that MEC maintain general comprehensive liability insurance covering the grantor (RepMar) and MEC, and their respective employees against liability claims for bodily injuries, death and property damages occasioned by franchise activities. The franchise covers the entire Republic of the Marshall Islands. The renewed insurance policy covers only MEC and its employees for incidents occurring within the Company's compound in Delap Village and Rong Rong Village in Majuro, Jebwor, Namdrik, Jaluit and Wotje Atolls. We recommend that management comply with the franchise requirements. This matter was discussed in our previous letters dated May 8, 2006 and January 11, 2005.

(12) General Ledger Account Reconciliations

We noted errors in recording accounts receivable, inventory, loan payments, and cost of goods sold. Errors were corrected through proposed adjusting journal entries. We recommend that management establish procedures to ensure that monthly reconciliations of general ledger balances are performed and reconciling items are identified and addressed in a timely manner.

(13) Maintenance of System Back-ups

MEC does not currently have a policy on maintenance of system back-ups. In the event of an emergency or other unplanned interruptions, such as a computer crash, since each system is maintained in a single computer, MEC is likely to incur unnecessary expenses due to the need to reconstruct data. We recommend that management establish policies and procedures to ensure that system file back-ups are maintained for its accounting systems (General Ledger, Billings, Inventory and Fixed Assets Systems). The policies and procedures should include daily schedules and off-site storage of back-ups, among others.

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This report is intended solely for the information and use of management and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

We would like to thank the accounting staff and management for their assistance during the course of our audit. Should you have any questions regarding the matters discussed herein, please contact our office at your convenience.

Very truly yours,

