

MAJURO RESORT, INC.

INDEPENDENT AUDITORS' REPORT ON
INTERNAL CONTROL AND ON COMPLIANCE

FIFTEEN MONTHS ENDED DECEMBER 31, 2001



INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
BASED UPON THE AUDIT PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS

Board of Directors
Majuro Resort, Inc.:

We have audited the financial statements of Majuro Resort, Inc. (MRI) for the fifteen months ended December 31, 2001, and have issued our report thereon dated March 26, 2002. 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.

Compliance

As part of obtaining reasonable assurance about whether MRI's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. 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 that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings (pages 3 through 5) as items 2001-1 through 2001-3.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered MRI's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting, which we have reported to management of MRI in a separate letter dated March 26, 2002.

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

Deloitte & Touche

March 26, 2002

MAJURO RESORT, INC.

Schedule of Findings
Fifteen Months Ended December 31, 2001

Local Noncompliance

Finding No. 2001-1

Criteria: Section 5 of the Republic of the Marshall Islands (RepMar) Income Tax Act of 1989, as amended, states that the employer shall, once every four weeks or thirteen times per year, pay taxes withheld under Section 4 of the Act.

Condition: At December 31, 2001, MRI owed RepMar \$94,064 in income tax withholdings from employee wages. This amount is represented by income tax withheld from employee wages for the period July 1, 1999 through July 31, 2001.

Cause: The cause of the above condition is unknown.

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

Recommendation: We recommend that management comply with the Income Tax Act of 1989, as amended.

Prior Year Status: Noncompliance with the Income Tax Act of 1989, as amended, was reported as a finding in the audits of MRI for fiscal years 1998 through 2000.

Auditee Response and Corrective Action Plan: As in past years, MRI has not generated sufficient business levels to meet all of its financial obligations. When operating cash shortfalls occur, ownership needs to issue a subsidy to MRI in order for it to pay off these obligations. Requests for subsidies have been presented, but due to the economic hardships facing RepMar, funding has not been available. MRI anticipates FY 2002 business levels to increase, which may allow additional operating cash to be used for the payment of the delinquent payroll withholding income taxes.

MAJURO RESORT, INC.

Schedule of Findings, Continued
Fifteen Months Ended December 31, 2001

Local Noncompliance

Finding No. 2001-2

Criteria: Section 153 of the Republic of the Marshall Islands (RepMar) Income Tax Act of 1989, as amended, states that there shall be assessed a tax of eight percent of the daily room rate on hotel and resort facilities in the Marshall Islands. The tax shall be collected by the owner of the room and forwarded to RepMar on a monthly basis.

Condition: At December 31, 2001, MRI owed RepMar \$227,373 in hotel tax. This amount is represented by unpaid RepMar hotel tax for the months of July 1999 through December 31, 2001.

Cause: The cause of the above condition is unknown.

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

Recommendation: We recommend that management comply with the Income Tax Act of 1989, as amended.

Prior Year Status: Noncompliance with the Income Tax Act of 1989, as amended, was reported as a finding in the audits of MRI for fiscal years 1998 through 2000.

Auditee Response and Corrective Action Plan: As in past years, MRI has not generated sufficient business levels to meet all of its financial obligations. When operating cash shortfalls occur, ownership needs to issue a subsidy to MRI in order for it to pay off these obligations. Requests for subsidies have been presented, but due to the economic hardships facing RepMar, funding has not been available. A possible resolution presented by the MRI Board of Directors is for RepMar to forgive the \$227,373 national hotel tax and treat it as a subsidy without transferring funds between the entities. This requires a budget appropriation for the subsidy by the national government.

MAJURO RESORT, INC.

Schedule of Findings, Continued
Fifteen Months Ended December 31, 2001

Local Noncompliance

Finding No. 2001-3

Criteria: Sections 2 and 6 of the Majuro Atoll Local Government (Malgov) General Revenue Tax Ordinance of 1992 states that there shall be assessed: 1) a sales tax of four percent on retail sales; and 2) a room tax of three dollars per room per day on hotel accommodation. The taxes shall be collected and forwarded to Malgov on the fourteenth of each month.

Condition: At December 31, 2001, MRI owed Malgov sales tax and room tax, totaling \$11,071 and \$18,257, respectively. This amount is represented by unpaid taxes for the months of September 2001 through December 31, 2001.

Cause: The cause of the above condition is unknown.

Effect: The effect of the above condition is noncompliance with the Malgov General Revenue Tax Ordinance of 1992.

Recommendation: We recommend that management comply with the Malgov General Revenue Tax Ordinance of 1992.

Prior Year Status: Noncompliance with the Malgov General Revenue Tax Ordinance of 1992 was reported as a finding in the audits of MRI for fiscal years 1998 through 2000.

Auditee Response and Corrective Action Plan: Payments to Malgov for sales tax and room tax have been withheld due to outstanding accounts receivable from Malgov to MRI. An informal agreement was reached with Malgov that payments for the taxes would be made as the accounts receivable balance was reduced. The amounts paid by MRI would be equal to the amount of payment received by MRI. Currently, Malgov has \$7,364 due to MRI. This arrangement will be discontinued in FY 2002 and MRI will pay its delinquent taxes to Malgov. The amount owed MRI will be obtained through normal credit and collection procedures.

MAJURO RESORT, INC.

Unresolved Prior Year Comments
Fifteen Months Ended December 31, 2001

The status of unresolved prior year findings are disclosed within the Schedule of Findings section (pages 3 through 5) of this report.