

**NATIONAL ENVIRONMENTAL
PROTECTION AUTHORITY FUND**

**FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT**

YEAR ENDED SEPTEMBER 30, 2003



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INDEPENDENT AUDITORS' REPORT

Board of Directors
Republic of the Marshall Islands
National Environmental Protection Authority Fund:

We were engaged to audit the accompanying statement of net assets of the National Environmental Protection Authority Fund (EPA), a component unit of the Republic of the Marshall Islands (RepMar), as of September 30, 2003, and the related statements of revenues, expenses and changes in net assets and of cash flows for the year then ended. These financial statements are the responsibility of EPA's management.

Because of inadequacies in EPA's accounting records and internal control over financial reporting, we were unable to form an opinion regarding the amounts recorded as advances and net assets in the accompanying statement of net assets (stated at \$25,790 and \$311,075, respectively), or the amounts recorded as grant revenues in the accompanying statement of revenues, expenses and changes in net assets (stated at \$304,960).

As discussed in notes 1 and 4 to the accompanying financial statements, the financial statements of EPA relates solely to those accounting records maintained by EPA and do not incorporate any accounts related to its operations that may be accounted for by RepMar's Treasury or any of RepMar's other branches, departmental units or component units.


Since advances and grant revenues materially affect the determination of financial position, results of operations, and cash flows, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements referred to in the first paragraph.

As described in note 2 to the accompanying financial statements, EPA adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*.

The Management's Discussion and Analysis on pages 3 through 5 is not a required part of the basic financial statements but is supplementary information required by GASB. This information is the responsibility of EPA's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 21, 2005, on our consideration of EPA's internal control over financial reporting and 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 the internal control over financial reporting or on compliance. That report is an integral part of an engagement to audit in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our engagement.

July 21, 2005



Jean M. Tenyokwe
Auditor-General

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Management's Discussion and Analysis
September 30, 2003

This section of Environmental Protection Authority (EPA) Fund's annual financial report presents our discussion and analysis for EPA's financial performance during the fiscal year that ended on September 30, 2003. Please read it in conjunction with the financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

EPA's net assets increased by \$260,073 or 510% from \$51,002 in 2002 to \$311,075 in 2003. Operating revenues also increased by \$278,156 or 226% from \$123,342 in 2002 to \$401,498 in 2003. Operating expenses had decreased by \$19,163 or 11% from \$160,588 in 2002 to \$141,425 in 2003.

FINANCIAL ANALYSIS OF EPA

The statement of Net Assets (page 6) and the Statement of Revenues, Expenses and Changes in Net Assets (page 7) provide an indication of EPA's financial condition. EPA's net assets reflect the difference between assets and liabilities. Any change in net assets over time typically indicates either an improvement or a problem in the financial condition of the organization.

A summary of EPA's net assets is presented below:

	<u>2003</u>	<u>2002</u>
Current assets	\$ 282,095	\$ 69,395
Capital assets	<u>43,373</u>	<u>622</u>
Total assets	\$ 325,468	\$ 70,017
Current liabilities	<u>\$ 14,393</u>	<u>\$ 19,015</u>
Investment in capital assets	43,373	622
Unrestricted	<u>267,702</u>	<u>50,380</u>
Total net assets	<u>311,075</u>	<u>51,002</u>
Total liabilities and net assets	<u>\$ 325,468</u>	<u>\$ 70,017</u>

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As indicated above, total assets increased by \$255,451 or 365% from \$70,017 in 2002 to \$325,468 in 2003. This increase is comprised of an increase of \$212,452 in current and other assets and increase in project grants received from foreign funding sources such as the UNEP and SPREP. The increase in capital assets was due to the purchase of a new motor vehicle and various office furniture and equipments.

Total liabilities reflect a decrease of \$4,622 or 24% from \$19,015 in 2002 to \$14,393 in 2003. The decrease reflects improved settlement of the outstanding delinquent liabilities owed to both the Republic of the Marshall Islands (RepMar) and the Marshall Islands Social Security Administration (MISSA) from prior administrations.

A summary of EPA's Statement of Revenues, Expenses, and Change in Net Assets is presented below:

	<u>2003</u>	<u>2002</u>
Operating revenue	\$ 401,498	\$ 123,342
Operating expenses	<u>141,425</u>	<u>160,588</u>
Change in net assets	260,073	(37,246)
Net assets in beginning of year	<u>51,002</u>	<u>87,626</u>
Net assets at end of year	<u>\$ 311,075</u>	<u>\$ 50,380</u>

The Statement of Revenues, Expenses and Changes in Net Assets identifies the various revenue and expense items that implicit the change in net assets. As indicated above, EPA's total revenue increased by \$278,563 or 227% from \$123,342 to \$401,498 in 2003. This increase was mainly due to the increase in funding from foreign sources for project grants and the improvement in the enforcement and management of collection of fines.

Below is a summary of the major components of operating revenues for EPA in 2003 compared to 2002:

<u>Operating revenues</u>	<u>2003</u>	<u>2002</u>
Grants	\$ 304,960	\$ 66,390
Fines	65,000	27,542
Fees	18,740	22,094
Interest	-0-	223
Other	12,798	7,093
Totals	<u>\$ 401,498</u>	<u>\$ 123,342</u>

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Total expenses decreased by \$19,022 or 12% from \$160,588 in 2002 to \$141,425 in 2003 resulting in an increase of \$260,073 or 510% in Change of Net Assets. The decrease in operational expenses reflects fewer travel, and less spending on maintenance and other miscellaneous office expenses.

Below is a summary of other major components of operating expenses for EPA in 2003 compared to 2002:

<u>Operating Expenses</u>	<u>2003</u>	<u>2002</u>
Salaries and Wages	\$ 49,861	\$ 39,191
Supplies and materials	20,393	19,208
Travel	16,493	38,028
Communications	12,742	7,600
Other	41,936	56,561
Total	<u>\$ 141,425</u>	<u>\$ 160,588</u>

CAPITAL ASSETS

Net Capital Assets increased by \$42,751 primarily as a result of the acquisition of a new motor vehicle and various office furniture and equipment. A summary of EPA's current Investment in Capital Assets is presented below:

	<u>2003</u>	<u>2002</u>
Motor Vehicles	\$ 19,995	\$ -0-
Office furniture and Equipment	26,347	1,288
Accumulated depreciation	<u>(2,969)</u>	<u>(666)</u>
Total	<u>\$ 43,373</u>	<u>\$ 622</u>

ADDITIONAL FINANCIAL INFORMATION

This discussion and analysis is designed to provide EPA's counterparts with an overview of EPA's financial operations and financial condition. Should the reader have questions regarding the information included in this report or wish to request for additional information, please contact the National Environmental Protection Authority, General Manager, at P.O. Box 1322, Majuro, MH 96960.

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Statement of Net Assets
September 30, 2003

ASSETS

Current assets:	
Cash	\$ 256,295
Receivables, net	10
Advances	25,790
Total current assets	<u>282,095</u>
Capital assets, net	<u>43,373</u>
	<u>\$ 325,468</u>

LIABILITIES AND NET ASSETS

Current liabilities:	
Accounts payable	\$ 1,858
Other liabilities and accruals	12,535
Total liabilities	<u>14,393</u>
Commitments and contingencies	
Net assets:	
Invested in capital assets	43,373
Restricted	-
Unrestricted	267,702
Total net assets	<u>311,075</u>
	<u>\$ 325,468</u>

See accompanying notes to financial statements.

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Statement of Revenues, Expenses and Changes in Net Assets
Year Ended September 30, 2003

Operating revenues:	
Grants	\$ 304,960
Fines	65,000
Fees and charges	18,740
Other	12,798
	<u>401,498</u>
Total operating revenues	401,498
Operating expenses:	
Salaries and wages	49,861
Supplies and materials	20,393
Travel	16,493
Communications	12,742
Rentals	8,111
Utilities	5,000
Printing and reproduction	2,713
Freight	2,475
Depreciation	2,303
Miscellaneous	21,334
	<u>141,425</u>
Total operating expenses	141,425
Operating income	260,073
Net assets at beginning of year	<u>51,002</u>
Net assets at end of year	<u>\$ 311,075</u>

See accompanying notes to financial statements.

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Statement of Cash Flows
Year Ended September 30, 2003

Cash flows from operating activities:	
Operating grants received	\$ 304,960
Cash received from customers	86,340
Cash payments to suppliers for goods and services	(122,320)
Cash payments to employees for services	(45,300)
Other operating revenues	12,798
	<u>236,478</u>
Net cash used in operating activities	236,478
Cash flows from capital and related financing activities:	
Acquisition of capital assets	(45,054)
	<u>(45,054)</u>
Net cash used in capital and related financing activities	(45,054)
Net increase in cash	191,424
Cash at beginning of year	64,863
	<u>64,863</u>
Cash at end of year	\$ <u><u>256,287</u></u>
Reconciliation of operating income to net cash used in operating activities:	
Operating income	\$ 260,073
Adjustments to reconcile operating income to net cash used in operating activities:	
Depreciation	2,303
(Increase) decrease in assets:	
Receivables	2,600
Advances	(23,876)
Increase (decrease) in liabilities:	
Accounts payable	(9,183)
Other liabilities and accruals	4,561
	<u>4,561</u>
Net cash used in operating activities	\$ <u><u>236,478</u></u>

See accompanying notes to financial statements.

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Notes to Financial Statements
September 30, 2003

(1) Organization

The National Environmental Protection Authority Fund (EPA), a component unit of the Republic of the Marshall Islands (RepMar), was created by the National Environmental Protection Authority Act of 1984 (Public Law No. 1984-31, the Act). EPA began operations as a statutory corporation on December 19, 1984, in accordance with the Act. The objectives of EPA are to preserve and improve the quality of the environment of the Republic of the Marshall Islands.

The operations of EPA were accounted for as a separate fund within RepMar's Ministry of Finance. In April 1997, EPA established a separate bank account outside of RepMar's Treasury for the purpose of receiving and disbursing funds in accordance with Public Law No. 1984-31. Accordingly, the accompanying financial statements relate solely to those accounting records maintained by EPA and do not incorporate any accounts related to EPA's operations that may be accounted for by RepMar's Treasury or any of RepMar's other branches, departmental units or component units.

EPA is governed by a Chairman and four other members, all of whom are appointed by the President of RepMar.

EPA's financial statements are incorporated into the financial statements of RepMar as a component unit.

(2) Summary of Significant Accounting Policies

The accounting policies of EPA conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds. Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, requires that proprietary activities apply all applicable GASB pronouncements as well as Statements and Interpretations issued by the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989. EPA has implemented GASB 20 and elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of the fund are included in the statements of net assets. Proprietary fund operating statements present increases and decreases in net total assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

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Notes to Financial Statements
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(2) Summary of Significant Accounting Policies, Continued

Basis of Accounting, Continued

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All other revenues are reported as nonoperating. Operating expenses includes the cost of sales and services, administrative expenses, and depreciation on capital assets. Expenses not meeting this definition are reported as nonoperating expenses.

Cash

For purposes of the statements of net assets and cash flows, cash is defined as cash on hand and cash held in demand accounts. As of September 30, 2003, the carrying amount of cash was \$256,295 and the corresponding bank balance was \$285,955. Of the bank balance amount, \$282,418 was maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2003, bank deposits in the amount of \$100,000 are FDIC insured. EPA does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized.

Receivables

All receivables are due from businesses and individuals located within the Republic of the Marshall Islands and are interest free and uncollateralized. The allowance for uncollectible accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectibility of these accounts and prior collection experience. The allowance is established through a provision for bad debts charged to expense. As of September 30, 2003, EPA recorded an allowance for uncollectible accounts in the amount of \$3,042.

Fixed Assets

EPA does not have a capitalization policy for fixed assets; however, items with a cost that equals or exceeds \$100 are generally capitalized at the time of acquisition. Depreciation is calculated using the straight-line method based on the estimated useful lives of the respective assets. The estimated useful lives of these assets are as follows:

Motor vehicles	3 years
Other furniture and equipment	5 years

Taxes

Corporate profits are not subject to income tax in the Republic of the Marshall Islands. The Government of the Republic of the Marshall Islands imposes a gross receipts tax of 3% on revenues. EPA is specifically exempt from this tax.

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September 30, 2003

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During fiscal year 2003, EPA implemented GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, and modified by Statement No. 38, *Certain Financial Statement Disclosures*. These statements establish financial reporting standards for governmental entities which require that management's discussion and analysis of the financial activities be included with the basic financial statements and notes and modifies certain other financial statement disclosure requirements.

To conform to the requirements of GASB 34, the following changes have been made to EPA's financial statements for fiscal year 2003:

- Fund balance has been reclassified into the following net assets categories:
 - Invested in capital assets; capital assets, net of accumulated depreciation and related debt, plus construction or improvement of those assets.
 - Restricted; net assets that are subject to constraints placed on net asset use either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through enabling legislation.
 - Unrestricted; net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.
- The statement of cash flows has been presented using the direct method.

Due to the implementation of GASB Statement No. 34, the beginning net assets have been restated as follows:

Fund balance reported as of September 30, 2002	\$ <u>50,380</u>
Capital assets	1,288
Accumulated depreciation	<u>(666)</u>
	<u>622</u>
Beginning net assets as of October 1, 2002	\$ <u>51,002</u>

For fiscal year 2004, EPA will be implementing GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units* (an amendment of GASB Statement 14), which provides additional guidance on GASB Statement No. 14, in determining whether an entity should be reported as a component unit based on the nature and significance of its relationship with a primary government. Management does not believe that the implementation of this statement will have a material effect on the financial statements of EPA.

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(5) Related Party Transactions, Continued

EPA occupies certain office space belonging to RepMar at no cost. No lease agreement has been executed to formalize this arrangement. However, management is of the opinion that no rental payments for the use of the office space are anticipated. The fair value of this contribution is presently not determinable. Accordingly, the contributed use of facilities has not been recognized as revenue and expenditures in the accompanying financial statements.

(6) Contingency

EPA does not maintain general liability insurance coverage on its operations. In the event of a loss, EPA may be self-insured to a material extent.