

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2001 AND 2000

INDEPENDENT AUDITORS' REPORT

Board of Directors  
Kwajalein Atoll Joint Utilities Resources, Inc.:

We have audited the accompanying balance sheet of the Kwajalein Atoll Joint Utilities Resources, Inc. (KAJUR), a component unit of the Republic of the Marshall Islands, as of September 30, 2001, and the related statements of income and retained earnings and cash flows for the year then ended. We were also engaged to audit the accompanying balance sheet as of September 30, 2000 and the related statements of income and retained earnings and cash flows for the year then ended. These financial statements are the responsibility of KAJUR's management. Our responsibility is to express an opinion on the 2001 financial statements based on our audit.

Except as discussed in the following paragraph, 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Because of inadequacies in KAJUR's accounting records and internal control, we were unable to form an opinion regarding cash, receivables, inventories, plant and equipment, bank overdraft, accounts payable, accrued liabilities, contributed capital, revenues and expenses as of and for the year ended September 30, 2000. Furthermore, in our judgment, the above balances materially affect the determination of results of operations and cash flows for the years ended September 30, 2001 and 2000.

Because of the matter discussed in the preceding paragraph, the scope of our work was not sufficient to express, and we do not express, an opinion on the balance sheet as of September 30, 2000, or on the statements of income and retained earnings and cash flows for the years ended September 30, 2001 and 2000.

In our opinion, the balance sheet as of September 30, 2001 referred to in the first paragraph, presents fairly, in all material respects, the financial position of KAJUR as of September 30, 2001, in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 8 to the financial statements, in 2001 KAJUR changed its method of accounting for contributions in aid to conform with the provisions of Governmental Accounting Standards Board Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transaction* and, retroactively, restated the 2000 financial statements for the change.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 16, 2002, on our consideration of KAJUR's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

*Deloitte & Touche*

May 16, 2002

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Balance Sheets  
September 30, 2001 and 2000

	<u>2001</u>	2000 (As Restated note 8)
<u>ASSETS</u>		
Current assets:		
Cash	\$ 14,852	\$ 30,768
Receivables:		
Utility services, net of allowance for doubtful accounts of \$2,389,393 in 2001 and \$2,530,475 in 2000	564,287	743,069
Due from RepMar	263,842	198,842
Employee receivables	613	-
Other	27,871	278
Inventories	<u>205,682</u>	<u>161,117</u>
Total current assets	1,077,147	1,134,074
Receivable from grantor agency	-	109,336
Plant and equipment, net (note 4)	<u>11,422,700</u>	<u>9,722,394</u>
	<u>\$ 12,499,847</u>	<u>\$ 10,965,804</u>
<u>LIABILITIES AND STOCKHOLDER'S EQUITY</u>		
Current liabilities:		
Bank overdraft	\$ 68,179	\$ -
Accounts payable	260,367	406,260
Due to affiliates (note 5)	379,438	64,799
Accrued liabilities	<u>393,264</u>	<u>196,040</u>
Total current liabilities	<u>1,101,248</u>	<u>667,099</u>
Stockholder's equity:		
Common stock, \$1 par value, 100,000 shares authorized, issued and outstanding	100,000	100,000
Retained earnings	<u>11,298,599</u>	<u>10,198,705</u>
Total stockholder's equity	<u>11,398,599</u>	<u>10,298,705</u>
Contingencies (note 6)	<u>\$ 12,499,847</u>	<u>\$ 10,965,804</u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Statements of Income and Retained Earnings  
Years Ended September 30, 2001 and 2000

	<u>2001</u>	2000 (As Restated note 8)
Operating revenues:		
Electric and service billings	\$ 1,863,077	\$ 1,717,643
Water	243,100	48,676
Other	<u>1,889</u>	<u>127,324</u>
Total operating revenues	<u>2,108,066</u>	<u>1,893,643</u>
Operating expenses:		
Fuel and lubricants	1,669,812	1,415,564
Depreciation	740,400	849,212
Salaries, wages and benefits	640,623	612,201
Supplies and materials	197,415	86,194
Operations and maintenance	178,350	23,303
Travel and transportation	163,914	43,434
Bad debts	109,336	-
Communications	74,726	34,911
Contractual services	69,423	14,092
Rental	62,154	277,500
Equipment	4,014	13,506
Miscellaneous	<u>71,712</u>	<u>12,299</u>
Total operating expenses	<u>3,981,879</u>	<u>3,382,216</u>
Operating loss	<u>(1,873,813)</u>	<u>(1,488,573)</u>
Nonoperating revenues (expenses):		
Capital grants (note 5)	2,423,707	1,125,943
Operating subsidies (note 5)	550,000	2,029,965
Interest expense	<u>-</u>	<u>(9,266)</u>
Total nonoperating revenues (expenses), net	<u>2,973,707</u>	<u>3,146,642</u>
Net income	1,099,894	1,658,069
Retained earnings at beginning of year	<u>10,198,705</u>	<u>8,540,636</u>
Retained earnings at end of year	<u>\$ 11,298,599</u>	<u>\$ 10,198,705</u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Statements of Cash Flows  
Years Ended September 30, 2001 and 2000

	2001	2000 (As Restated note 8)
Cash flows from operating activities:		
Operating loss	\$ (1,873,813)	\$ (1,488,573)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	740,400	849,212
Bad debts	109,336	-
(Increase) decrease in assets:		
Utility services receivables	178,782	(38,730)
Due from RepMar	(65,000)	(198,842)
Employee receivables	(613)	-
Other receivables	(27,593)	(278)
Inventories	(44,565)	(160,256)
Increase (decrease) in liabilities:		
Accounts payable	(145,893)	224,488
Due to affiliates	314,639	-
Accrued liabilities	<u>197,224</u>	<u>51,151</u>
Net cash used for operating activities	<u>(617,096)</u>	<u>(761,828)</u>
Cash flows from noncapital financing activities:		
Operating subsidies (note 5)	550,000	896,632
Increase (decrease) in bank overdraft	68,179	(9,685)
Interest payments	<u>-</u>	<u>(9,266)</u>
Net cash provided by noncapital financing activities	<u>618,179</u>	<u>877,681</u>
Cash flows from capital and related financing activities:		
Principal payments of long-term debt	-	(50,734)
Acquisition and construction of capital assets	(2,440,706)	(1,182,426)
Capital grants (note 5)	<u>2,423,707</u>	<u>1,125,943</u>
Net cash used for capital and related financing activities	<u>(16,999)</u>	<u>(107,217)</u>
Net (decrease) increase in cash	(15,916)	8,636
Cash at beginning of year	<u>30,768</u>	<u>22,132</u>
Cash at end of year	<u>\$ 14,852</u>	<u>\$ 30,768</u>
Supplemental schedule of noncash noncapital financing activities:		
Forgiveness of liabilities under management contract (note 5):		
Noncash increase in operating subsidies	\$ -	\$ 1,133,333
Noncash decrease in note payable	-	(581,418)
Noncash decrease in accrued liabilities	<u>-</u>	<u>(551,915)</u>
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

## KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements  
September 30, 2001 and 2000

### (1) Organization

The Kwajalein Atoll Joint Utilities Resources, Inc. (KAJUR), a component unit of the Republic of the Marshall Islands, was incorporated under the laws of the Republic of the Marshall Islands (RepMar) on September 1, 1990, to generate and distribute utilities on the island of Ebeye. On October 19, 1990, the Board of Directors of the Kwajalein Atoll Development Authority (KADA) authorized the transfer of \$14,075,046 in utility plant and equipment to KAJUR. KAJUR has sold 100,000 shares of \$1 par value common stock to KADA, which is the sole owner of common stock of KAJUR. KAJUR's financial statements are incorporated into the general purpose financial statements of RepMar as a component unit.

On October 28, 1999, RepMar and KADA awarded a twenty-four month management contract to the American Samoa Power Authority (ASPA) to assume operational control of KAJUR. The term of the contract is from November 2, 1999 to October 31, 2001 and conditions of the contract are included in the management contract between RepMar, KADA and ASPA (see note 7).

### (2) Summary of Significant Accounting Policies

The accounting policies of KAJUR 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. KAJUR 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

All 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 this fund are included in the balance sheets.

Stockholder's equity (i.e., net assets) is segregated into common stock and retained earnings components. Proprietary fund operating statements present increases and decreases in net total assets.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements  
September 30, 2001 and 2000

(2) Summary of Significant Accounting Policies, Continued

Basis of Accounting, Continued

The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses recorded at the time liabilities are incurred. Revenues are recorded as billed to customers on a monthly cycle billing basis. At the end of each month, unbilled revenues are accrued for each cycle based on the most recent cycle billing.

Cash

For purposes of the balance sheets and statements of cash flows, cash is defined as cash on hand and cash in checking accounts. At September 30, 2001 and 2000, substantially all of KAJUR'S cash is with a non-federally insured bank.

Receivables and Allowance for Doubtful Accounts

KAJUR provides electric services to government agencies, businesses and individuals located on the island of Ebeye and bills for these services on a monthly basis. The allowance for doubtful 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 operating expenses. Receivables are not collateralized.

Inventories

Inventories of fuel and supplies are stated at the lower of cost (first-in, first-out) or market (net realizable value) at September 30, 2001 and 2000. Bulk fuel inventories are held for power plant use.

Plant and Equipment

Plant and equipment are stated at cost. Depreciation of plant and equipment is calculated on the straight-line method based on the estimated useful lives of the respective assets.

Compensated Absences

Vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. The liability as of September 30, 2001 and 2000, is \$112,668 and \$-0-, respectively, and is included within the balance sheets as accrued liabilities. Sick pay benefits vest at 50% and are recorded as an expense and liability as the benefits accrue to employees. The liability as of September 30, 2001 and 2000, is \$40,875 and \$-0-, respectively, and is included within the balance sheets as accrued liabilities.

Reclassifications

Certain reclassifications have been made to the 2000 financial statements in order to conform with the 2001 presentation.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements  
September 30, 2001 and 2000

(3) Risk Management

KAJUR 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. KAJUR has elected not to purchase commercial insurance for the risks of loss to which it is exposed. Instead, KAJUR 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 as a result of these risks have occurred for the past three years.

(4) Plant and Equipment

A summary of plant and equipment as of September 30, 2001 and 2000, is as follows:

	<u>Estimated Useful Lives</u>	<u>2001</u>	<u>2000</u>
Plant and machinery	20 - 25 years	\$ 10,537,921	\$ 12,495,388
Distribution system	20 - 25 years	1,307,541	1,965,156
Water system	20 - 25 years	2,665,082	-
Other equipment	5 years	<u>404,843</u>	<u>439,069</u>
Plant and equipment in service		14,915,387	14,899,613
Less accumulated depreciation		<u>(6,960,019)</u>	<u>(6,264,618)</u>
Net plant and equipment in service		7,955,368	8,634,995
Construction-in-progress		<u>3,467,332</u>	<u>1,087,399</u>
Total plant and equipment, net		\$ <u>11,422,700</u>	\$ <u>9,722,394</u>

(5) Related Party Transactions

KAJUR is wholly owned by KADA, which was created on September 1, 1990, by a public law of RepMar. KADA is operated by a Board of Directors, who are appointed by the Cabinet of RepMar. KAJUR is therefore affiliated with all RepMar owned and affiliated entities.

KAJUR is affiliated with ASPA, a company with whom RepMar and KADA have contracted to manage its operations. Related management fee expense is incurred by RepMar.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements  
September 30, 2001 and 2000

(5) Related Party Transactions, Continued

KAJUR utilizes services from certain affiliated entities at substantially the same terms and conditions as those incurred from third parties. A summary of related party transactions for the years ended September 30, 2001 and 2000 and the related payable balances as of September 30, 2001 and 2000, are as follows:

	2001	
	Expenses	Payable
American Samoa Power Authority (ASPA)	\$ -	\$ 49,521
Marshall Islands Social Security Administration	51,765	203,585
Marshall Islands National Telecommunications Authority	74,726	35,526
RepMar	-	90,806
	\$ 126,491	\$ 379,438
	2000	
	Expenses	Payable
American Samoa Power Authority (ASPA)	\$ -	\$ 2,781
Marshall Islands Social Security Administration	42,700	8,819
Marshall Islands National Telecommunications Authority	34,911	8,318
RepMar	-	44,881
	\$ 77,611	\$ 64,799

In accordance with the management contract between RepMar, KADA and ASPA (see note 1), RepMar is responsible for all liabilities, actual and contingent, relating to KAJUR's operations prior to commencement of the management contract. As such, during the year ended September 30, 2000, RepMar paid in full KAJUR's note to bank in the amount of \$581,418. Additionally, RepMar assumed KAJUR's liability to the Marshall Islands Social Security Administration and RepMar's withholding taxes in the amount of \$410,519 and \$141,396, respectively. These amounts were recorded as operating subsidies in the accompanying financial statements.

Additionally, the management contract between RepMar, KADA and ASPA, RepMar and KADA are required to make working capital available for KAJUR's operations. During the years ended September 30, 2001 and 2000, RepMar made \$550,000 and \$896,632, respectively, available for this purpose. These amounts are recorded as operating subsidies in the accompanying financial statements.

As of September 30, 2001 and 2000, KAJUR maintained demand deposit accounts with a related financial institution in the amount of \$14,852 and \$30,251, respectively.

On October 8, 1999, RepMar entered into a loan agreement with the Asian Development Bank for the Ebeye Health and Infrastructure Project. Under the terms of the loan agreement, loan funds are to be made available for the rehabilitation and expansion of the existing water supply and sewerage systems on Ebeye Island, and the upgrading of Ebeye's power generation and distribution system. During the years ended September 30, 2001 and 2000, RepMar made available to KAJUR loan funds in the amount of \$2,189,600 and \$817,244, respectively, as capital grants in accordance with the terms and conditions of the loan agreement. KAJUR is under no obligation to repay these amounts to RepMar.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements  
September 30, 2001 and 2000

(5) Related Party Transactions, Continued

KAJUR received additional capital grants from ASPA through a grant award from the U.S. Department of the Interior (DOI). During the years ended September 30, 2001 and 2000, \$34,107 and \$179,699, respectively, were received by KAJUR for the funding of equipment and repairs related to this grant. Additionally, during the years ended September 30, 2001 and 2000, KAJUR received \$-0- and \$129,000, respectively, in matching funds related to this grant from RepMar.

KAJUR received additional capital grants from RepMar during the years ended September 30, 2001 and 2000 in the amounts of \$200,000 and \$-0-, respectively.

(6) Contingencies

KAJUR has incurred significant net operating losses since inception. KAJUR depends on KADA and RepMar for cash and noncash funding to continue its operations. Although KADA and RepMar have provided funding in the past, no formal agreement exists to provide funds in the future, except as described in note 6. The continuation of KAJUR's operations is dependent upon future financial support from KADA and RepMar and/or significant improvements in operations.

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

(7) Subsequent Event

On November 9, 2001, the Cabinet of RepMar approved the extension of the management contract with ASPA to manage the operations of KAJUR for an additional two years ( see note 1).

(8) Restatement

Effective October 1, 2000, KAJUR implemented GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*. The provisions of this standard require capital grants and contributions to be recognized as non-operating revenue on the Statements of Income and Retained Earnings. In prior periods, capital grants and contributions had been recorded as a direct increase to contributions in aid in the equity section of the Balance Sheet. As a result, contributed capital and retained earnings as of October 1, 1999, and capital grants for the year ended September 30, 2000, have been restated from the amounts previously reported as follows:

	<u>As Previously Reported</u>	<u>As Restated</u>
At October 1, 1999:		
Contributed capital	\$ <u>9,193,930</u>	\$ <u>          -</u>
Retained earnings (deficit)	\$ <u>(653,294)</u>	\$ <u>8,540,636</u>
For the year ended September 30, 2000:		
Capital grants	\$ <u>          -</u>	\$ <u>1,125,943</u>