

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2004 AND 2003

INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying statements of net assets of Kwajalein Atoll Joint Utilities Resources, Inc. (KAJUR), a component unit of the Republic of the Marshall Islands, as of September 30, 2004 and 2003, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of KAJUR's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of KAJUR's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide 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 inventories and operating expenses as of September 30, 2004. Furthermore, in our judgement, the above balances materially affect the determination of results of operations and cash flows for the year ended September 30, 2004.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had the accounting records and internal control over financial reporting related to inventories and operating expenses been adequate, as discussed in the third paragraph above, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of KAJUR as of September 30, 2004 and 2003, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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 the Governmental Accounting Standards Board. This supplementary information is the responsibility of KAJUR'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 the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 14, 2007, on our consideration of KAJUR'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 the 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.

A handwritten signature in black ink, appearing to read "Deloitte + Touche LLP". The signature is stylized and written in a cursive-like font.

May 14, 2007

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Management's Discussion and Analysis Year Ended September 30, 2004

This section of the Kwajalein Atoll Joint Utility Resources, Inc. (KAJUR) annual financial report presents our discussion and analysis of KAJUR's financial performance during the fiscal year that ended on September 30, 2004. It is to be read in conjunction with the financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

KAJUR's net assets decreased by \$3,765,904 compared to an increase of \$454,500 in 2003. Total operating revenues have increased by \$667,064 or 29% from \$2,299,899 in 2003 to \$2,966,963 in 2004. Total operating expenses, likewise, have increased by \$215,142 or 4% from \$4,895,243 in 2003 to \$5,110,385 in 2004.

FINANCIAL ANALYSIS OF KAJUR

The Statement of Net Assets (page 6) and the Statement of Revenues, Expenses and Changes in Net Assets (page 7) provide an indication of KAJUR's financial condition. KAJUR's net assets reflect the difference between assets and liabilities. An increase in net assets over time typically indicates an improvement in financial condition.

A summary of KAJUR's Statement of Net Assets is presented below:

	<u>2004</u>	<u>2003</u>
Current and other assets	\$ 123,305	\$ 526,998
Capital assets	<u>7,307,850</u>	<u>10,790,548</u>
Total assets	<u>7,431,155</u>	<u>11,317,546</u>
Current liabilities	1,739,305	1,879,843
Non-current liabilities	<u>20,051</u>	<u>-</u>
Total liabilities	<u>1,759,356</u>	<u>1,879,843</u>
Net assets:		
Invested in capital assets	\$ 7,307,850	\$ 10,790,548
Unrestricted	<u>(1,636,051)</u>	<u>(1,352,845)</u>
Total net assets	<u>\$ 5,671,799</u>	<u>\$ 9,437,703</u>

As indicated above, total assets have decreased by \$3,886,391 or 34% from \$11,317,546 in 2003 to \$7,431,155 in 2004. Most of this decrease is reflected in the decrease in capital assets of \$3,482,698 from \$10,790,548 in 2003 to \$7,307,850 in 2004. This is mainly a result of retirement of the Enterprise generators that are no longer in use in the total cost of \$6,316,030, and the capitalization of the new 4 units of Cummins engines and other projects for \$1,613,759, and construction still in progress for electric, water and sewer in the total amount of \$522,376 plus a decrease in current assets of \$403,693 from \$526,998 in 2003 to \$123,305 in 2004.

Total liabilities reflect decrease of \$120,487 or 6% from \$1,879,843 in 2003 to \$1,759,356 in 2004. This decrease is represented by a decrease in current liabilities of \$140,538 or 7% from \$1,879,843 in 2003 to \$1,739,305 in 2004 and the recognition of a long-term obligation for sick leave to employees in the amount of \$20,051 as of 2004, which is treated as a non-current liability.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

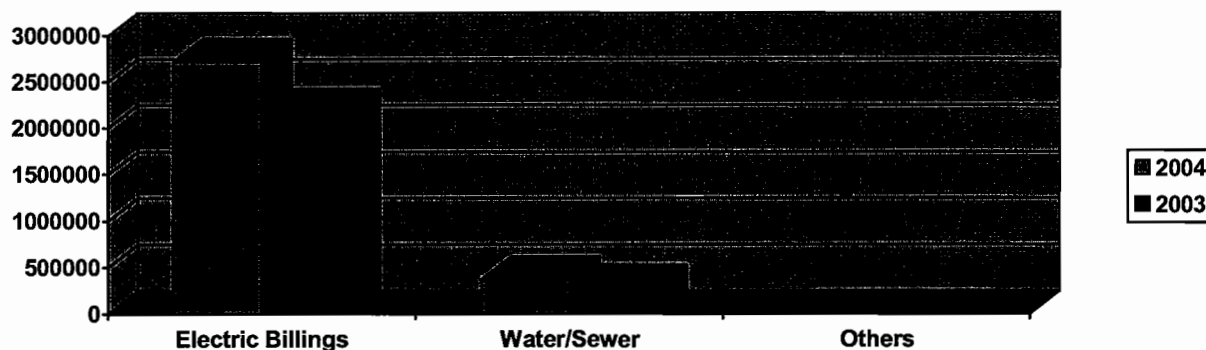
Management's Discussion and Analysis, Continued
Year Ended September 30, 2004

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

	<u>2004</u>	<u>2003</u>
Revenues:		
Operating revenues	\$ 2,966,963	\$ 2,299,899
Non-operating revenues	<u>326,895</u>	<u>199,004</u>
Total revenues	<u>3,293,858</u>	<u>2,498,903</u>
Expenses:		
Operating expenses	5,110,385	4,895,243
Non-operating expenses	<u>2,875,669</u>	<u>54,072</u>
Total expenses	<u>7,986,054</u>	<u>4,949,315</u>
Income (loss) before capital contributions	(4,692,196)	(2,450,412)
Capital contributions	<u>926,292</u>	<u>2,904,912</u>
Change in net assets	\$ <u>(3,765,904)</u>	\$ <u>454,500</u>

The Statement of Revenue, Expenses and Changes in Net Assets identifies the various revenue and expense items that impacted the change in net assets. As indicated above, KAJUR's total revenues have increased by \$794,955 or 32% from \$2,498,903 in 2003 to \$3,293,858 in 2004. Within operating revenues, electric billings have increased by \$578,194 or 29% from \$2,017,773 in 2003 to \$2,595,967 in 2004, while water and sewer billings likewise have increased by \$88,905 or 32% from \$280,843 in 2003 to \$369,748 in 2004.

The graph below shows the major components of operating revenues for 2004 compared with 2003 and 2002:

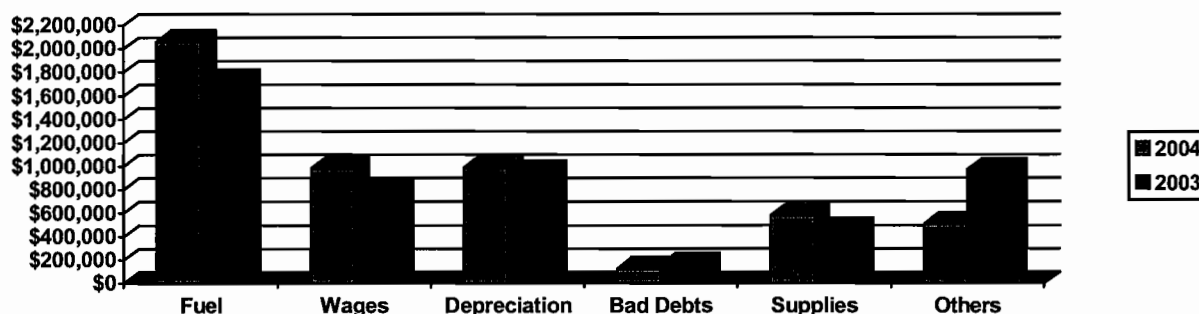


KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Management's Discussion and Analysis, Continued
Year Ended September 30, 2004

Total expenses have increased by \$3,036,739 or 61% from \$4,949,315 in 2003 to \$7,986,054 in 2004. This increase was due to the effect of a loss in plant asset retirement of \$2,830,625 calculated between acquisition cost and applied depreciation. Operating expenses have a slight increase of \$215,142 or 4% only. This reflects management's commitment to maintain tight and effective control over both expenses and cash flow.

The graph below shows the major components of operating expenses for 2004 compared with 2003:



CAPITAL ASSET ADMINISTRATION

KAJUR's investment in capital assets as of September 30, 2004 amounted to \$10,816,381, net of accumulated depreciation of \$3,508,531, leaving a net book value of \$7,307,850. KAJUR's capital assets include plant and machinery, electrical and water distribution systems, and other equipment. Major capital asset additions during the year related to the acquisition of new Cummins generators to replace the Enterprise generators that were written off during the year.

Additional information on KAJUR's capital assets can be found in note 4 to the financial statements.

ECONOMIC FACTORS

KAJUR will continue to monitor operating expenses and maintain tight fiscal constraints and control over utility receivables in order to improve cash collections. The ongoing viability of KAJUR as a going concern will continue to be dependent upon future financial support of RepMar in the form of:

- a) Subsidies and grants,
- b) the collection of long outstanding utility receivables, and
- c) continuing improvements in operations.

ADDITIONAL FINANCIAL INFORMATION

This discussion and analysis is designed to provide KAJUR's customers and other interested parties with an overview of KAJUR's financial operations and financial condition. Should the reader have questions regarding the information included in this report or wish to request additional financial information, please contact the Kwajalein Atoll Joint Utility Resources, Inc. General Manager at P.O. Box 5819, Ebeye MH 96960.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Statements of Net Assets
September 30, 2004 and 2003

<u>ASSETS</u>	<u>2004</u>	<u>2003</u>
Current assets:		
Cash	\$ -	\$ 6,041
Receivables:		
Utility	2,719,968	2,711,799
Employee receivables	1,948	1,784
Other	140,300	140,375
	<u>2,862,216</u>	<u>2,853,958</u>
Less allowance for doubtful accounts	<u>(2,673,325)</u>	<u>(2,549,269)</u>
Total receivables, net	<u>188,891</u>	<u>304,689</u>
Inventories	<u>(65,586)</u>	<u>216,268</u>
Total current assets	123,305	526,998
Capital assets, net	<u>7,307,850</u>	<u>10,790,548</u>
	<u>\$ 7,431,155</u>	<u>\$ 11,317,546</u>
 <u>LIABILITIES AND NET ASSETS</u> 		
Current liabilities:		
Bank overdraft	\$ 24,872	\$ 29,227
Accounts payable	763,350	944,885
Due to affiliates	521,314	508,358
Accrued liabilities	316,969	284,573
Deferred revenue	112,800	112,800
Total current liabilities	<u>1,739,305</u>	<u>1,879,843</u>
Accrued sick leave - long-term	<u>20,051</u>	<u>-</u>
	<u>1,759,356</u>	<u>1,879,843</u>
Contingencies		
Net assets:		
Invested in capital assets	7,307,850	10,790,548
Unrestricted	<u>(1,636,051)</u>	<u>(1,352,845)</u>
Total net assets	<u>5,671,799</u>	<u>9,437,703</u>
	<u>\$ 7,431,155</u>	<u>\$ 11,317,546</u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Statements of Revenues, Expenses and Changes in Net Assets
Years Ended September 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Operating revenues:		
Electric and service billings	\$ 2,595,967	\$ 2,017,773
Water	369,748	280,843
Other	1,248	1,283
	<u>2,966,963</u>	<u>2,459,775</u>
Operating expenses:		
Fuel and lubricants	2,061,756	1,728,340
Depreciation	986,097	947,053
Salaries, wages and benefits	980,495	786,640
Supplies and materials	576,698	461,197
Operations and maintenance	177,109	360,266
Contractual services	121,782	127,578
Travel and transportation	94,884	159,853
Rental	56,689	100,035
Communications	27,744	39,226
Equipment	1,101	3,440
Training	-	132,520
Miscellaneous	26,030	49,095
	<u>5,110,385</u>	<u>5,055,119</u>
Total operating expenses		
Operating loss	<u>(2,143,422)</u>	<u>(2,595,344)</u>
Nonoperating revenues (expenses):		
Operating subsidy	326,895	199,004
Interest expense	(750)	(3,065)
Capital related outlays	(44,294)	(51,007)
Loss on write-off of fixed assets	<u>(2,830,625)</u>	<u>-</u>
	<u>(2,548,774)</u>	<u>144,932</u>
Total nonoperating revenues (expenses), net		
Capital grants	<u>926,292</u>	<u>2,904,912</u>
Change in net assets	(3,765,904)	454,500
Net assets at beginning of year	<u>9,437,703</u>	<u>8,983,203</u>
Net assets at end of year	<u>\$ 5,671,799</u>	<u>\$ 9,437,703</u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Statements of Cash Flows
Years Ended September 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Cash flows from operating activities:		
Cash received from customers	\$ 3,036,736	\$ 2,589,549
Cash payments to suppliers for goods and services	(2,932,046)	(2,911,766)
Cash payments to employees for services	<u>(980,495)</u>	<u>(844,185)</u>
Net cash used for operating activities	<u>(875,805)</u>	<u>(1,166,402)</u>
Cash flows from noncapital financing activities:		
Operating subsidy received	326,895	405,254
Change in bank overdraft	(4,355)	(12,858)
Insurance claim recovery	<u>150,000</u>	<u>-</u>
Net cash provided by noncapital financing activities	<u>472,540</u>	<u>392,396</u>
Cash flows from capital and related financing activities:		
Capital grants received	926,292	3,185,212
Acquisition of capital assets	(484,024)	(2,360,470)
Other capital related outlays	(44,294)	(51,007)
Interest expense	<u>(750)</u>	<u>(3,065)</u>
Net cash provided by capital and related financing activities	<u>397,224</u>	<u>770,670</u>
Net decrease in cash	(6,041)	(3,336)
Cash at beginning of year	<u>6,041</u>	<u>9,377</u>
Cash at end of year	\$ <u><u>-</u></u>	\$ <u><u>6,041</u></u>
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (2,143,422)	\$ (2,595,344)
Adjustments to reconcile loss from operations to net cash used for operating activities:		
Depreciation	986,097	947,053
Provision for uncollectible accounts receivable	124,056	159,876
(Increase) decrease in assets:		
Accounts receivables:		
Utility	(8,169)	229,163
Employees	(164)	(1,784)
Other	75	(99,389)
Inventories	281,854	(28,009)
Increase (decrease) in liabilities:		
Accounts payable	(181,535)	185,592
Payable to affiliates	12,956	92,201
Other current and accrued liabilities	<u>52,447</u>	<u>(55,761)</u>
Net cash used for operating activities	\$ <u><u>(875,805)</u></u>	\$ <u><u>(1,166,402)</u></u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2004 and 2003

(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.

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 was from November 2, 1999 to October 31, 2001 and conditions of the contract were included in the management contract between RepMar, KADA and ASPA. On November 9, 2001, the Cabinet of RepMar approved the extension of the management contract for an additional two years with the same conditions. On April 30, 2003, the ASPA management contract ended and three ASPA employees were retained by KAJUR on a contractual basis to continue the management and operations, however, there was no formal contract approved by the Cabinet of RepMar.

On May 2, 2006, the Cabinet of RepMar approved the transfer of all management responsibilities of KAJUR to the Board of Directors of the Marshalls Energy Company, Inc., a component unit of RepMar. On July 24, 2006, the Cabinet of RepMar approved the introduction of legislation to the Nitijela (RepMar's legislature) to repeal the enabling legislation that created KADA.

KAJUR'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 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.

GASB issued 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 modify certain other financial statement disclosure requirements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2004 and 2003

(2) Summary of Significant Accounting Policies, Continued

To conform to the requirements of GASB Statement 34, retained earnings are presented in the following net asset categories:

- Investment in capital assets; capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- 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.

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 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. KAJUR considers utility revenues and costs that are directly related to utility operations to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

Cash

For purposes of the statements of net assets and cash flows, cash is defined as cash on hand and cash in checking accounts. At September 30, 2004 and 2003, substantially all of KAJUR's cash is with a non-federally insured bank.

Receivables

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 expense. 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, 2004 and 2003. Bulk fuel inventories are held for power plant use.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2004 and 2003

(2) Summary of Significant Accounting Policies, Continued

Plant and Equipment

KAJUR does not have a formal capitalization policy for plant and equipment; however, items with a cost that equals or exceeds \$500 are generally capitalized at the time of acquisition. Depreciation of plant and equipment is calculated on the straight-line method based on the estimated useful lives of the respective assets, which are as follows:

Plant and machinery	20 - 25 years
Distribution system	20 - 25 years
Water system	20 - 25 years
Other 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 revenue tax of 3% on revenues. Pursuant to the Income Tax Act of 1989, as amended, sales of electricity services by public utility companies are exempt from gross revenue tax. Accordingly, KAJUR is exempt from this tax relating to gross revenue from sales of electric services.

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, 2004 and 2003, is \$39,907 and \$43,902, respectively, and is included within the statements of net assets as accrued liabilities. Sick pay benefits vest at 50% and are recorded as an expense and a liability as the benefits accrue to employees. The liability as of September 30, 2004 and 2003, is \$40,108 and \$41,180, respectively, and is included within the statements of net assets as accrued liabilities.

New Accounting Standards

During fiscal year 2004, KAJUR implemented GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units* (an amendment of GASB Statement 14) and GASB Technical Bulletin No. 2003-1, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets*. GASB Statement No. 39 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. GASB Technical Bulletin No. 2003-1 clarifies guidance on derivative disclosures pending the results of the GASB's project on reporting and measurement of derivatives and hedging activities. The implementation of these pronouncements did not have a material impact on the financial statements of KAJUR.

For fiscal year 2005, KAJUR will be implementing GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3), which addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, GASB Statement No. 40 requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Management does not believe that the implementation of this statement will have a material effect on the financial statements of KAJUR.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2004 and 2003

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In November 2003, GASB issued Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which establishes standards for impairment of capital assets when its service utility has declined significantly or unexpectedly. The provisions of this Statement are effective for periods beginning after December 15, 2004. Management does not believe that the implementation of this statement will have a material effect on the financial statements of KAJUR.

In April 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which establishes uniform reporting standards for other postemployment benefits and supercedes the interim guidance included in GASB Statement No. 26. The provisions of this Statement are effective for periods beginning after December 15, 2005. Management does not believe that the implementation of this statement will have a material effect on the financial statements of KAJUR.

In May 2004, GASB issued Statement No. 44, *Economic Condition Reporting: The Statistical Section, an amendment to NCGA Statement 1*. GASB Statement No. 44 improves the understandability and usefulness of statistical section information and adds information from the new financial reporting model for state and local governments required by GASB Statement No. 34. The provisions of this Statement are effective for periods beginning after June 15, 2005. Management does not believe that the implementation of this statement will have a material effect on the financial statements of KAJUR.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Post employment Benefits Other Than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other post employment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this Statement are effective for periods beginning after December 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of KAJUR.

Reclassifications

Certain reclassifications have been made to the 2003 financial statements to conform with the 2004 presentation.

(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.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2004 and 2003

(4) Capital Assets

Capital assets activity for the years ended September 30, 2004 and 2003, was as follows:

	2004			
	October 1, 2003	Additions	Retirements	September 30, 2004
Plant and machinery	\$ 9,743,342	\$ 1,554,785	\$ (6,316,030)	\$ 4,982,097
Distribution system	2,401,283	53,281	-	2,454,564
Water system	748,873	-	(186,564)	562,309
Other equipment	<u>985,570</u>	<u>5,694</u>	<u>-</u>	<u>991,264</u>
	13,879,068	1,613,760	(6,502,594)	8,990,234
Less accumulated depreciation	<u>(6,044,403)</u>	<u>(986,097)</u>	<u>3,521,969</u>	<u>(3,508,531)</u>
	7,834,655	627,663	(2,980,625)	5,481,703
Construction work-in-progress	<u>2,955,883</u>	<u>522,376</u>	<u>(1,652,112)</u>	<u>1,826,147</u>
	<u>\$ 10,790,548</u>	<u>\$ 1,150,039</u>	<u>\$ (4,632,737)</u>	<u>\$ 7,307,850</u>
	2003			
	October 1, 2002	Additions	Retirements	September 30, 2003
Plant and machinery	\$ 9,727,293	\$ 16,049	\$ -	\$ 9,743,342
Distribution system	2,387,708	13,575	-	2,401,283
Water system	748,873	-	-	748,873
Other equipment	<u>907,171</u>	<u>78,399</u>	<u>-</u>	<u>985,570</u>
	13,771,045	108,023	-	13,879,068
Less accumulated depreciation	<u>(5,097,350)</u>	<u>(947,053)</u>	<u>-</u>	<u>(6,044,403)</u>
	8,673,695	(839,030)	-	7,834,665
Construction work-in-progress	<u>703,436</u>	<u>2,252,447</u>	<u>-</u>	<u>2,955,883</u>
	<u>\$ 9,377,131</u>	<u>\$ 1,413,417</u>	<u>\$ -</u>	<u>\$ 10,790,548</u>

(5) Related Party Transactions

KAJUR is a component unit of 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.

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(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, 2004 and 2003 and the related receivable and payable balances as of September 30, 2004 and 2003, are as follows:

	2004		
	<u>Expenses</u>	<u>Receivable</u>	<u>Payable</u>
American Samoa Power Authority (ASPA)	\$ 56,768	\$ -	\$ 381,871
Marshall Islands Social Security Administration	27,744	-	35,364
Marshall Islands National Telecommunications Authority	-	32,887	-
RepMar	-	297,708	75,909
Other	-	4,175	28,170
	<u>\$ 84,512</u>	<u>\$ 334,770</u>	<u>\$ 521,314</u>
	2003		
	<u>Expenses</u>	<u>Receivable</u>	<u>Payable</u>
American Samoa Power Authority (ASPA)	\$ 336,933	\$ -	\$ 87,373
Marshall Islands Social Security Administration	-	-	340,119
Marshall Islands National Telecommunications Authority	39,226	-	9,552
RepMar	-	-	71,314
	<u>\$ 376,159</u>	<u>\$ -</u>	<u>\$ 508,358</u>

In accordance with 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, 2004 and 2003, RepMar made \$0 and \$199,004, respectively, available for this purpose. The management contract ended in 2003; however, KAJUR received \$326,895 as an operating subsidy from RepMar during the year ended September 30, 2004.

As of September 30, 2004 and 2003, KAJUR maintained demand deposit accounts with a related financial institution in the amount of \$0 and \$6,041, respectively.

KAJUR received additional capital grants from ASPA through grant awards from the U.S. Department of the Interior (DOI). During the years ended September 30, 2004 and 2003, \$0 and \$1,242,612, respectively, were received by KAJUR for the funding of equipment and infrastructure projects related to these grants. Additionally, during the years ended September 30, 2004 and 2003, KAJUR received \$926,292 and \$1,775,100, respectively, in matching funds related to these grants from RepMar. As of September 30, 2004 and 2003, KAJUR recorded deferred revenue of \$112,800 and \$112,800, respectively, representing unexpended capital grants. During the years ended September 30, 2004 and 2003, KAJUR refurbished a school building funded by a DOI grant amounting to \$0 and \$51,007, respectively, which was transferred to RepMar.

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(6) Going Concern

KAJUR has incurred significant net operating losses since inception. KAJUR depends on RepMar for cash and noncash funding to continue its operations. Although RepMar have provided funding in the past, no formal agreement exists to provide funds in the future, except as described in note 5. The continuation of KAJUR's operations is dependent upon future financial support from RepMar in the form of operating subsidies and/or significant improvements in operations through the collection of long outstanding utility receivables and other matters.

Litigation

In the ordinary course of business, claims have been filed against KAJUR. Management does not believe that the plaintiffs will prevail and the ultimate outcome is currently not determinable. Therefore, no provision has been recorded in the accompanying financial statements for losses, if any, that may result.