

**MAJURO WATER AND SEWER COMPANY, INC.**

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**FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

## INDEPENDENT AUDITORS' REPORT

Board of Directors  
Majuro Water and Sewer Company, Inc.:

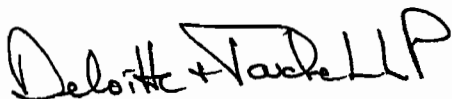
We have audited the accompanying statements of net assets of Majuro Water and Sewer Company, Inc. (MWSC), a component unit of the Republic of the Marshall Islands, as of September 30, 2005 and 2004, and the related statements of revenue, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of MWSC'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 MWSC'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.

In our opinion, such financial statements present fairly, in all material respects, the financial position of MWSC as of September 30, 2005 and 2004, and the changes in net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 2 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 MWSC'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 April 15, 2006, on our consideration of MWSC's internal control over financial reporting and our tests of its compliance with certain 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.



April 15, 2006

# MAJURO WATER AND SEWER COMPANY, INC.

## Management's Discussion and Analysis Year Ended September 30, 2005

This section of the Majuro Water and Sewer Company, Inc. (MWSC) annual financial report presents our discussion and analysis of MWSC's financial performance during the fiscal year that ended on September 30, 2005. It is to be read in conjunction with the financial statements, which follow this section.

### FINANCIAL HIGHLIGHTS

MWSC's net assets decreased by \$174,370 in 2005 compared to a decrease of \$115,175 in 2004. Total revenue decreased by \$78,733 or 7% from \$1,116,213 in 2004 to \$1,037,480 in 2005. Within operating revenues, billings decreased from \$932,414 in 2004 to \$807,567 in 2005. Operating expenses increased slightly from \$1,170,755 in 2004 to \$1,249,182 in 2005. Most of the increase was due to increases in electricity charges. No operating subsidies were received from the General Fund of the Republic of the Marshall Islands (RepMar) for 2005.

### FINANCIAL ANALYSIS OF MWSC

The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets provides an indication of MWSC's financial condition. MWSC's net assets reflects the difference between assets and liabilities. An increase in net assets over time typically indicates an improvement in financial condition.

A summary of MWSC's Statements of Net Assets is presented below:

	<u>2005</u>	<u>2004</u>
Current assets	\$ 228,621	\$ 329,444
Capital assets	<u>75,875</u>	<u>95,980</u>
Total assets	<u>304,496</u>	<u>425,424</u>
Current liabilities	929,792	686,220
Non-current liabilities	<u>-</u>	<u>190,130</u>
Total liabilities	<u>929,792</u>	<u>876,350</u>
Net assets (deficit):		
Invested in capital assets	75,875	95,980
Unrestricted	<u>(701,171)</u>	<u>(546,906)</u>
Total net deficit	<u>\$ (625,296)</u>	<u>\$ (450,926)</u>

As indicated above, total assets decreased by \$120,928 or 28% from \$425,424 in 2004 to \$304,496 in 2005. Most of this decrease is reflected in the decrease in utility receivables of \$132,384 or 10% from \$1,347,165 in 2004 to \$1,214,781 in 2005. Total liabilities reflect an increase of \$53,442 or 6% from \$876,350 in 2004 to \$929,792 in 2005. This is represented by an increase in current liabilities of \$243,572 or 35% to \$929,792 in 2005 compared to \$686,220 in 2004. Most of the increase is attributable to the increase in payables to affiliates. Non-current liabilities decreased by \$190,130 to zero in 2005. This is the result of the liability for social security being transferred to the current liability section in the statement of net assets.

**MAJURO WATER AND SEWER COMPANY, INC.**

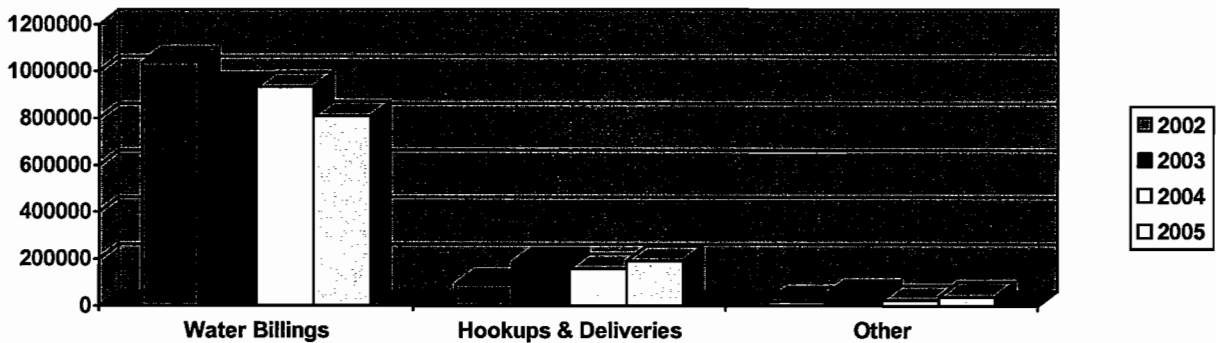
Management's Discussion and Analysis, Continued  
Year Ended September 30, 2005

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

	<u>2005</u>	<u>2004</u>
Revenues:		
Operating revenues	\$ <u>1,037,480</u>	\$ <u>1,116,213</u>
Total revenues	<u>1,037,480</u>	<u>1,116,213</u>
Expenses:		
Operating expenses	1,249,182	1,170,755
Non-operating expenses	<u>(37,332)</u>	<u>60,633</u>
Total expenses	<u>1,211,850</u>	<u>1,231,388</u>
Change in net assets	\$ <u>(174,370)</u>	\$ <u>(115,175)</u>

The Statement of Revenue, Expenses and Changes in Net Assets identifies the various revenue and expense items that impacted on the change in net assets. As indicated above, MWSC's total revenues decreased by \$78,733 or 7% from \$1,116,213 in 2004 to \$1,037,480 in 2005. Utility billings decreased by \$124,847 or 13% from \$932,414 in 2004 to \$807,567 in 2005. This decrease in revenue was partially offset by increases in hookups and other revenue of \$46,114. Non-Operating expenses were reduced to a credit balance of \$37,332 through reductions in interest charges of \$143,013 which had been overcharged by MISSA in prior years. No subsidy was received from RepMar in 2005 and 2004.

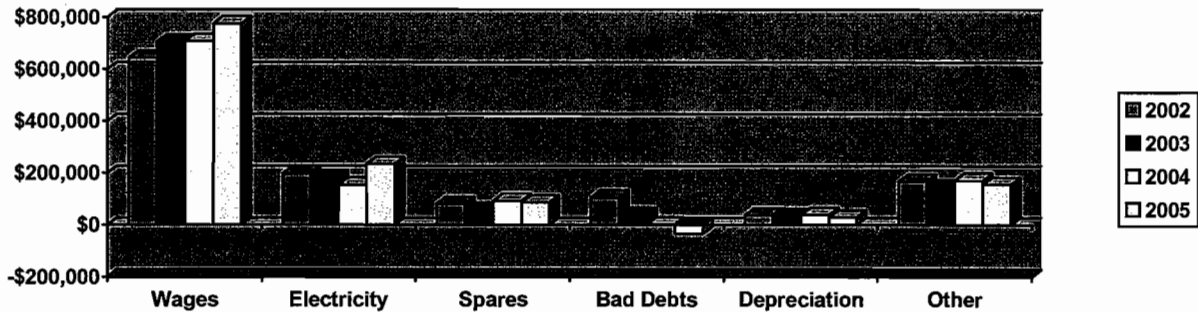
The graph below shows the major components of operating revenues for 2005 compared with 2002, 2003 and 2004:



**MAJURO WATER AND SEWER COMPANY, INC.**

Management's Discussion and Analysis, Continued  
Year Ended September 30, 2005

Total expenses decreased by \$19,538 from \$1,231,388 in 2004 to \$1,211,850 in 2005. The graph below shows the major components of operating expenses for 2005 compared with 2002, 2003 and 2004:



The allowance for doubtful debts has been reduced by \$34,267 which reflects the increased efforts being exerted in debt collection at MWSC.

**CAPITAL ASSETS**

Net capital assets decreased by \$20,105 in 2005 as a result of the acquisition of miscellaneous machinery and office equipment totaling \$10,295, less depreciation for the year of \$30,414, and the retirement of old computer equipment with a cost of \$45,530 and accumulated depreciation of \$45,544. A summary of MWSC's capital assets is presented below:

	<u>2005</u>	<u>2004</u>
Motor vehicles	\$ 168,654	\$ 168,653
Machinery and equipment	119,077	114,395
Office equipment	55,974	95,892
Buildings and leasehold improvements	<u>54,317</u>	<u>54,317</u>
	398,022	433,257
Less accumulated depreciation	<u>(322,147)</u>	<u>(337,277)</u>
	<u>\$ 75,875</u>	<u>\$ 95,980</u>

**ECONOMIC FACTORS**

MWSC 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 MWSC as a going concern will continue to be dependent upon future financial support of RepMar in the form of:

- a) Timely payment by RepMar for the cost of actual utility service provided,
- b) Collection of long outstanding utility receivables, and
- c) Continuing improvements in operations.

## **MAJURO WATER AND SEWER COMPANY, INC.**

Management's Discussion and Analysis, Continued  
Year Ended September 30, 2005

### **ADDITIONAL FINANCIAL INFORMATION**

This discussion and analysis is designed to provide MWSC's customers and other stake holders with an overview of MWSC'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 Majuro Water and Sewer Company, Inc. General Manager at P.O. Box 1751, Majuro MH 96960.

**MAJURO WATER AND SEWER COMPANY, INC.**

Statements of Net Assets  
September 30, 2005 and 2004

<u>ASSETS</u>	<u>2005</u>	<u>2004</u>
Current assets:		
Cash	\$ 16,776	\$ 49,141
Receivables:		
Utility	1,214,781	1,347,165
Affiliates	239,790	205,004
Other	20,626	9,926
	<u>1,475,197</u>	<u>1,562,095</u>
Less allowance for doubtful accounts	<u>(1,391,070)</u>	<u>(1,425,337)</u>
	<u>84,127</u>	<u>136,758</u>
Inventory	124,335	130,691
Prepaid expenses	3,383	12,854
Total current assets	<u>228,621</u>	<u>329,444</u>
Capital assets	398,022	433,257
Accumulated depreciation	<u>(322,147)</u>	<u>(337,277)</u>
Net capital assets	<u>75,875</u>	<u>95,980</u>
	<u>\$ 304,496</u>	<u>\$ 425,424</u>

LIABILITIES AND NET ASSETS (DEFICIT)

Current liabilities:		
Accounts payable	\$ 14,384	\$ 24,660
Social security taxes payable	191,237	128,135
Withholding taxes payable	175,201	198,073
Payable to affiliates	525,472	286,680
Other accrued liabilities	23,498	48,672
Total current liabilities	<u>929,792</u>	<u>686,220</u>
Social security taxes payable, net of current portion	<u>-</u>	<u>190,130</u>
Total liabilities	<u>929,792</u>	<u>876,350</u>
Commitment and contingency		
Net assets (deficit):		
Invested in capital assets	75,875	95,980
Unrestricted	<u>(701,171)</u>	<u>(546,906)</u>
Total net deficit	<u>(625,296)</u>	<u>(450,926)</u>
	<u>\$ 304,496</u>	<u>\$ 425,424</u>

See accompanying notes to financial statements.

**MAJURO WATER AND SEWER COMPANY, INC.**

Statements of Revenues, Expenses and Changes in Net Deficit  
Years Ended September 30, 2005 and 2004

	2005	2004
Operating revenues:		
Utility billings	\$ 807,567	\$ 932,414
Hook-up and deliveries	192,126	159,749
Other	37,787	24,050
Total operating revenues	1,037,480	1,116,213
Operating expenses:		
Salaries, wages and benefits	775,380	708,336
Electricity	235,265	154,572
Spare parts	86,419	92,680
Petroleum, oil and lubricants	36,191	26,838
Depreciation and amortization	30,402	40,272
Insurance	29,370	21,908
Communications	19,865	21,173
Office supplies	13,231	17,547
Contractual services	7,510	16,100
Travel	3,738	11,417
Repairs and maintenance	2,641	11,454
Uniforms	-	8,307
Bad debts (recoveries)	(34,267)	2,657
Miscellaneous	43,437	37,494
Total operating expenses	1,249,182	1,170,755
Operating loss	(211,702)	(54,542)
Nonoperating revenues (expenses):		
Income tax, penalties and interest	37,332	(58,984)
Interest expense	-	(1,649)
Total nonoperating revenues (expenses), net	37,332	(60,633)
Change in net deficit	(174,370)	(115,175)
Net deficit at beginning of year	(450,926)	(335,751)
Net deficit at end of year	\$ (625,296)	\$ (450,926)

See accompanying notes to financial statements.

**MAJURO WATER AND SEWER COMPANY, INC.**

Statements of Cash Flows  
Years Ended September 30, 2005 and 2004

	2005	2004
Cash flows from operating activities:		
Cash received from customers	\$ 1,124,378	\$ 1,292,485
Cash payments to suppliers for goods and services	(345,892)	(467,945)
Cash payments to employees for services	(800,554)	(715,434)
Net cash (used for) provided by operating activities	(22,068)	109,106
Cash flows from noncapital financing activities:		
Interest and penalties paid	-	(60,633)
Net cash used for noncapital financing activities	-	(60,633)
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(10,297)	(43,303)
Net cash used for capital and related financing activities	(10,297)	(43,303)
Net change in cash	(32,365)	5,170
Cash at beginning of year	49,141	43,971
Cash at end of year	\$ 16,776	\$ 49,141
Reconciliation of operating loss to net cash (used for) provided by operating activities:		
Operating loss	\$ (211,702)	\$ (54,542)
Adjustments to reconcile operating loss to net cash (used for) provided by operating activities:		
Depreciation and amortization	30,402	40,272
Bad debts	(34,267)	2,657
(Increase) decrease in assets:		
Receivables:		
Utility	132,384	(52,583)
Affiliates	(34,786)	227,339
Other	(10,700)	1,516
Inventory	6,356	7,547
Prepaid expenses	9,471	(10,814)
Increase (decrease) in liabilities:		
Accounts payable	(10,276)	(11,939)
Payable to affiliates	126,224	(33,249)
Other accrued liabilities	(25,174)	(7,098)
Net cash (used for) provided by operating activities	\$ (22,068)	\$ 109,106

See accompanying notes to financial statements.

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2005 and 2004

### (1) Organization

Majuro Water and Sewer Company, Inc. (MWSC) was granted a corporate charter by the Cabinet of the Republic of the Marshall Islands (RepMar) on January 26, 1989. MWSC's principal lines of business are predominantly the collection and distribution of fresh water and wastewater. The principal markets for the collection and distribution of fresh water and wastewater are government agencies, businesses and residential customers located on the atoll of Majuro.

An exclusive franchise to construct, maintain and operate the fresh water, waste water and sewer system within Majuro Atoll was granted to MWSC by RepMar on March 9, 1989. Simultaneously, RepMar leased to MWSC, at no cost, the Majuro Atoll fresh water, waste water and sewer system. The term of both the lease and the franchise was for a ten year period commencing on March 9, 1989, and was to continue thereafter unless terminated by either party six months after written notice to the other.

On February 19, 2003, RepMar and MWSC entered into a Water and Sewer Franchise Agreement (the Agreement) to provide water and sewer service to the atoll of Majuro. The Agreement incorporates a lease agreement for MWSC to lease from RepMar the water and sewer system for a period of ten years at a rate of \$100,000 per annum, commencing three years after the lease is in effect (February 19, 2006). The Agreement also forgave loans related to the construction of the water and sewer system and transferred the water system infrastructure to RepMar. RepMar and MWSC elected to record the forgiveness of these loans, and the related transfer of the water and sewer system asset from MWSC to RepMar, during the year ended September 30, 2002.

MWSC's financial statements are incorporated into the general purpose financial statements of RepMar as a component unit.

### (2) Summary of Significant Accounting Policies

The accounting policies of MWSC 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. MWSC 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 modifies certain other financial statement disclosure requirements.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2005 and 2004

## (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.

### 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, 2005 and 2004, cash was \$16,776 and \$49,141, respectively, and the corresponding bank balances were \$42,483 and \$78,092, respectively, which are maintained in one financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2005 and 2004, bank deposits were fully FDIC insured.

### Receivables

All receivables are due from government agencies, businesses and individuals located within the Republic of the Marshall Islands and are interest free and uncollateralized. 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.

### Inventory

Inventory is valued at the lower of cost (first-in, first-out) or market (net realizable value).

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2005 and 2004

## (2) Summary of Significant Accounting Policies, Continued

### Plant and Equipment

Plant and equipment are stated at cost. Depreciation of plant and equipment and amortization of leasehold improvements are calculated on the straight-line method based on the estimated useful lives of the respective assets. Individual items with a cost of \$500 and an expected useful life of three years or longer are capitalized. The estimated useful lives of these assets are as follows:

Vehicles	2 - 4 years
Office equipment	3 - 8 years
Buildings and leasehold improvements	4 years
Machinery and equipment	5 - 10 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 water and sewer services by public utility companies are exempt from gross revenue tax. Accordingly, MWSC is exempt from this tax relating to gross revenue from sales of water and sewer services.

### New Accounting Standards

In fiscal year 2005, MWSC implemented GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3) and GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. Implementation of GASB Statement Nos. 40 and 42 is reflected in the accompanying financial statements.

For fiscal year 2006, MWSC will be implementing the following:

Statement No. 42 "*Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries.*"

Statement No. 44 "*Economic Condition Reporting: The Statistical Section, an amendment of NCGA Statement 1.*"

Statement No. 46 "*Net Assets Restricted by Enabling Legislation.*"

Statement No. 47 "*Accounting for Termination Benefits.*"

Statements 44 and 46, are anticipated to have no financial impact. MWSC has not evaluated the financial impact of implementing Statements 42 and 47.

In fiscal year 2007, MWSC will be implementing Statement No. 45 "*Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions.*" MWSC has not evaluated the financial impact of implementing this Statement.

**MAJURO WATER AND SEWER COMPANY, INC.**

Notes to Financial Statements  
September 30, 2005 and 2004

**(3) Risk Management**

MWSC 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. MWSC has elected not to purchase commercial insurance for the risks of loss to which it is exposed. Instead, MWSC 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 in any of the past three years.

**(4) Capital Assets**

Capital asset activity for the years ended September 30, 2005 and 2004, was as follows:

	2005			
	October 1, <u>2004</u>	<u>Additions</u>	<u>Retirements</u>	September 30, <u>2005</u>
Vehicles	\$ 168,653	\$ -	\$ -	\$ 168,654
Machinery and equipment	114,395	4,682	-	119,077
Office equipment	95,892	5,615	(45,532)	55,974
Buildings and leasehold improvements	<u>54,317</u>	<u>-</u>	<u>-</u>	<u>54,317</u>
	433,257	10,297	(45,532)	398,022
Less accumulated depreciation and amortization	<u>(337,277)</u>	<u>(30,402)</u>	<u>45,532</u>	<u>(322,147)</u>
	<u>\$ 95,980</u>	<u>\$ (20,105)</u>	<u>\$ -</u>	<u>\$ 75,875</u>
	2004			
	October 1, <u>2003</u>	<u>Additions</u>	<u>Retirements</u>	September 30, <u>2004</u>
Vehicles	\$ 137,904	\$ 30,749	\$ -	\$ 168,653
Machinery and equipment	103,387	11,008	-	114,395
Office equipment	94,346	1,546	-	95,892
Buildings and leasehold improvements	<u>54,317</u>	<u>-</u>	<u>-</u>	<u>54,317</u>
	389,954	43,303	-	433,257
Less accumulated depreciation and amortization	<u>(297,005)</u>	<u>(40,272)</u>	<u>-</u>	<u>(337,277)</u>
	<u>\$ 92,949</u>	<u>\$ 3,031</u>	<u>\$ -</u>	<u>\$ 95,980</u>

**(5) Social Security Taxes Payable**

At September 30, 2005 and 2004, MWSC was liable for taxes payable to the Marshall Islands Social Security Administration (MISSA) in the amount of \$191,237 and \$318,265, respectively. On February 7, 2003, MWSC and MISSA entered into a promissory note for the repayment of certain delinquent taxes payable in the amount of \$427,774. The terms of the agreement include monthly payments of \$10,000, inclusive of interest at 12% per annum, commencing March 30, 2003. As of September 30, 2005, the balance of the note is \$95,007 and interest payable is \$66,811.

**MAJURO WATER AND SEWER COMPANY, INC.**

Notes to Financial Statements  
September 30, 2005 and 2004

(5) Social Security Taxes Payable, Continued

Long-term liability activity during the years ended September 30, 2005 and 2004 is as follows:

2005				
<u>Balance at</u> <u>October 1, 2004</u>	<u>Payments</u>	<u>Additions</u>	<u>Balance at</u> <u>September 30, 2005</u>	<u>Amount due</u> <u>within one year</u>
\$ 318,265	\$ 127,028	\$ -	\$ 191,237	\$ 191,237
2004				
<u>Balance at</u> <u>October 1, 2003</u>	<u>Payments</u>	<u>Additions</u>	<u>Balance at</u> <u>September 30, 2004</u>	<u>Amount due</u> <u>Within one year</u>
\$ 403,089	\$ 84,824	\$ -	\$ 318,265	\$ 128,135

(6) Withholding Taxes Payable

At September 30, 2005 and 2004, MWSC was liable for withholding taxes payable to RepMar in the amount of \$175,201 and \$198,073, respectively. On October 5, 2003, MWSC entered into a promissory note agreement for the repayment of certain delinquent taxes payable in the amount of \$138,601. The terms of the agreement include interest at 6% per annum to be repaid over a period of twenty-four months commencing October 30, 2003. As of September 30, 2005, the balance of the note was \$141,041, for which a total of \$16,542 was paid during the year. On January 30, 2006, the above promissory note was refinanced whereby MWSC agreed to repay the sum of \$164,048 plus penalties and interest of \$29,336 over a period of twenty-seven months. The terms of the agreement include interest at 12% per annum commencing January 30, 2006. In accordance with Financial Accounting Standards Board Statement No. 6, MWSC has elected to reflect the impact of this transaction in subsequent periods.

(7) Related Party Transactions

MWSC is wholly-owned by the Marshall Islands Development Authority (MIDA), a component unit of RepMar, and is therefore affiliated with all RepMar-owned and affiliated entities.

MWSC's utility service is provided to RepMar and all RepMar-owned and affiliated entities. Services are extended to these entities at more favorable terms and conditions than those provided to third parties.

MWSC utilizes services from certain affiliated entities at substantially more favorable terms and conditions than those incurred from third parties.

**MAJURO WATER AND SEWER COMPANY, INC.**

Notes to Financial Statements  
September 30, 2005 and 2004

(7) Related Party Transactions, Continued

A summary of related party transactions for the years ended September 30, 2005 and 2004, and related receivable and payable balances as of September 30, 2005 and 2004, is as follows:

	2005			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 260,057	\$ 96,974	\$ 169,329	\$ 175,201
Marshall's Energy Company, Inc.	8,301	235,265	5,514	524,646
Marshall Islands National Telecommunications Authority	8,670	10,227	4,788	826
Marshall Islands Social Security Administration	55,055	222,966	775	191,237
Majuro Resort, Inc.	4,221	1,932	45,922	-
Other	<u>42,252</u>	<u>11,310</u>	<u>13,462</u>	<u>-</u>
	<u>\$ 378,556</u>	<u>\$ 578,674</u>	<u>\$ 239,790</u>	<u>\$ 891,910</u>
	2004			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 197,018	\$ 64,817	\$ 130,280	\$ 198,073
Marshall's Energy Company, Inc.	41,026	154,572	-	286,680
Marshall Islands National Telecommunications Authority	20,152	13,773	14,044	-
Marshall Islands Social Security Administration	51,455	247,584	-	318,265
Majuro Resort, Inc.	12,985	1,893	41,650	-
Other	<u>37,900</u>	<u>10,395</u>	<u>19,030</u>	<u>-</u>
	<u>\$ 360,536</u>	<u>\$ 493,034</u>	<u>\$ 205,004</u>	<u>\$ 803,018</u>

Receivables from and payables to affiliates are uncollateralized, interest free and have no set repayment terms except as disclosed in notes 5 and 6.

(8) Commitment

On February 19, 2003, RepMar and MWSC entered into a franchise agreement to provide water and sewer service to the atoll of Majuro. The agreement incorporates a lease agreement for MWSC to lease from RepMar the water and sewer system for a period of ten years at a rate of \$100,000 per annum, commencing three years after the lease is in effect (February 19, 2006).

Total future minimum lease payments for subsequent years ending September 30, are as follows:

Year ending September 30,	
2006	\$ 66,667
2007	100,000
2008	100,000
2009	100,000
2010	100,000
2011 - 2015	500,000
2016	<u>33,333</u>
	<u>\$ 1,000,000</u>

**MAJURO WATER AND SEWER COMPANY, INC.**

Notes to Financial Statements  
September 30, 2005 and 2004

(9) Contingency

MWSC has incurred losses from operations of \$211,702 and \$54,542 during the years ended September 30, 2005 and 2004, respectively, and as of those dates, has working capital deficiencies of \$701,171 and \$356,776, respectively, and deficits of \$625,296 and \$450,926, respectively. Management believes that the continuation of MWSC's operations is dependent upon the future financial support of RepMar, compensation by RepMar for the cost of actual utility service provided, the collection of long outstanding utility receivables, and/or significant improvements in operations.