

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

**(A COMPONENT UNIT OF THE  
REPUBLIC OF THE MARSHALL ISLANDS)**

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**FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT**

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**YEARS ENDED SEPTEMBER 30, 2008 AND 2007**

## INDEPENDENT AUDITORS' REPORT

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

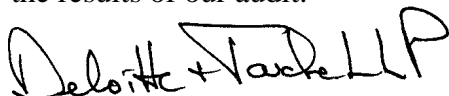
We have audited the accompanying statements of net assets of Majuro Water and Sewer Company, Inc. (MWSC), a component unit of the Republic of the Marshall Islands, as of September 30, 2008 and 2007, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of 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, 2008 and 2007, and the changes in its 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 March 26, 2009, on our consideration of MWSC'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.

  
March 26, 2009

## MAJURO WATER AND SEWER COMPANY, INC.

### Management's Discussion and Analysis Year Ended September 30, 2008

This section of the Majuro Water and Sewer Company, Inc. (MWSC) annual financial report presents management's discussion and analysis of MWSC's financial performance during the fiscal year ended 30<sup>th</sup> September, 2008. It is to be read in conjunction with the financial statements, which follow this section.

#### **FINANCIAL HIGHLIGHTS**

MWSC's net assets increased by \$916,039 in 2008 compared to an increase of \$87,018 in 2007. This was due to the subsidy of \$1,258,763 received in 2008 compared to the subsidy of \$349,404 received in 2007. Total revenue increased by \$77,908 in 2008 compared to a decrease in revenue in 2007 of \$59,188. Within operating revenues, billings increased from \$805,190 in 2007 to \$885,034 (or 9%) in 2008. This was due at least in part to the increase in water tariffs introduced in October 2007. Operating expenses increased by \$149,740 from \$1,272,521 in 2007 to \$1,422,261 mainly because of the increase in electricity costs of \$106,123. An operating subsidy of \$1,258,763 was received from the Republic of the Marshall Islands (RepMar) for fiscal year ended September 2008, of which \$1,159,363 was used to pay the long standing electricity debt owed to Marshalls Energy Company, Inc. (MEC) for past due electricity bills. The Statement of Cash Flows reveals the operating activities of MWSC generated net operating cash inflow of \$40,553 in 2008 compared to a net operating cash inflow of \$11,634 for 2007.

#### **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 reflect 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 Statement of Net Assets is presented below:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Current assets	\$ 356,543	\$ 258,927	\$ 228,294
Capital assets, net	<u>44,880</u>	<u>31,324</u>	<u>53,436</u>
Total assets	<u>401,423</u>	<u>290,251</u>	<u>281,730</u>
Current liabilities	<u>187,092</u>	<u>991,959</u>	<u>1,070,456</u>
Total liabilities	<u>187,092</u>	<u>991,959</u>	<u>1,070,456</u>
Net assets:			
Invested in capital assets	44,880	31,324	53,436
Unrestricted	<u>169,451</u>	<u>(733,032)</u>	<u>(842,162)</u>
Total net assets	<u>\$ 214,331</u>	<u>\$ (701,708)</u>	<u>\$ (788,726)</u>

As indicated above, total assets increased by \$111,172 from \$290,251 in 2007 to \$401,423 in 2008. Total liabilities reflect a decrease of \$804,867 from \$991,959 in 2007 to \$187,092 in 2008. This is represented by a decrease in amount owing to MEC of \$1,159,363 for past due electricity bills. This was achieved through the application of the RepMar subsidy to MWSC's accounts payable debt with Marshalls Energy Company (MEC) for electricity. Total net assets increased by \$916,039 from a deficit of \$(701,708) in 2007 to a surplus of \$214,331 in 2008. There were no non-current liabilities at 30<sup>th</sup> September 2008 or 2007.

## MAJURO WATER AND SEWER COMPANY, INC.

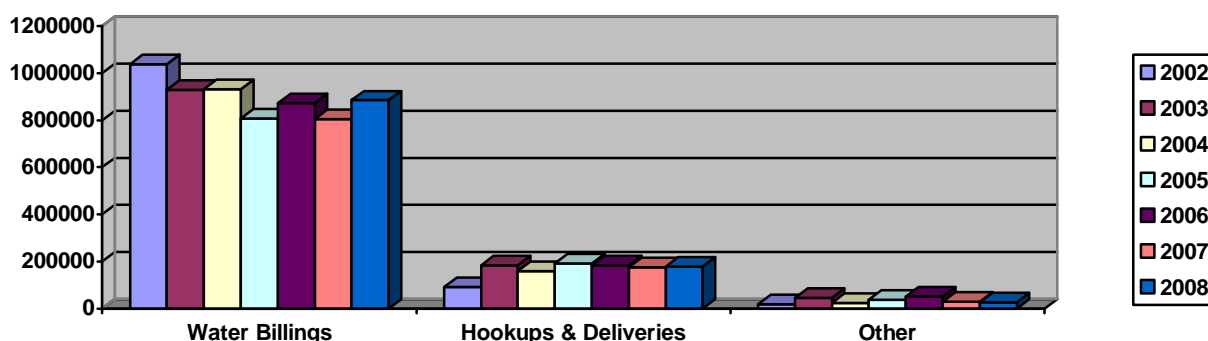
### Management's Discussion and Analysis, Continued Year Ended September 30, 2008

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

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Revenues:			
Operating revenues, net	\$ 1,088,043	\$ 1,010,135	\$ 1,069,323
Non-operating revenues	<u>1,258,763</u>	<u>349,404</u>	-
Total revenues	<u>2,346,806</u>	<u>1,359,539</u>	<u>1,069,323</u>
Expenses:			
Operating expenses	1,422,261	1,272,521	1,191,047
Non-operating expenses	<u>8,506</u>	-	<u>41,706</u>
Total expenses	<u>1,430,767</u>	<u>1,272,521</u>	<u>1,232,753</u>
Change in net assets	<u>\$ 916,039</u>	<u>\$ 87,018</u>	<u>\$ (163,430)</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 operating revenue increased by \$77,908 or 7% from \$1,010,135 in 2007 to \$1,088,043 in 2008. Utility billings also increased by a similar amount, \$79,844 or 9% over 2007. No subsidy was received from RepMar in either 2005 or 2006. The subsidy received in 2007 was in two parts. There was a subsidy of \$250,000 received, which was used to pay a portion of the long standing debt to MEC for past due electricity accounts. The remainder, \$99,404 was utilized as an operating subsidy. Of the subsidy received in 2008 of \$1,258,763, \$1,159,363 was applied in its entirety to the overdue electricity bills owed to MEC.

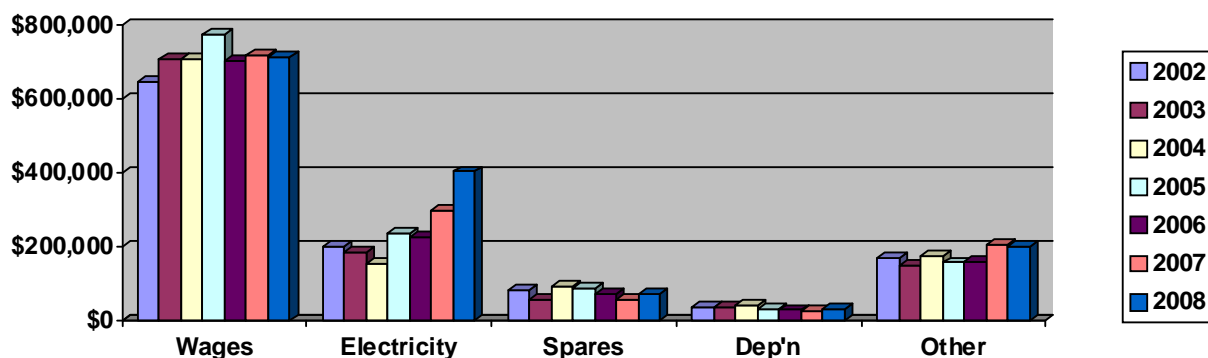
The graph below shows the major components of operating revenue for 2008 compared with the years 2002 through to 2008:



## MAJURO WATER AND SEWER COMPANY, INC.

### Management's Discussion and Analysis, Continued Year Ended September 30, 2008

Operating expenses increased by \$149,740 or 12% to \$1,422,261 in 2008 from \$1,272,521 in 2007. The operating loss increased by \$71,832 from \$262,386 in 2007 to \$334,218 in 2008. This was largely due to the increases in electricity bills amounting to \$106,123. The graph below shows the major components of operating expenses for 2008 compared with the years 2002 through to 2008:



Management's Discussion and Analysis for the year ended September 30, 2007 is set forth in the report on the audit of MWSC's financial statements, which is dated May 16, 2008. That Discussion and Analysis explains the major factors impacting the 2007 financial statements.

### **CAPITAL ASSETS AND DEBT**

Net capital assets increased by \$13,556 in 2008 as a result of the acquisition of motor vehicles costing \$38,750 and miscellaneous office and other equipment costing \$7,726 less total depreciation for the year of \$32,850, and the retirement of old machinery and office equipment with a total cost of \$75,903 and related accumulated depreciation of \$75,833. A summary of MWSC's capital assets is presented below:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Motor vehicles	\$ 116,582	\$ 130,985	\$ 130,185
Machinery and equipment	94,318	101,632	103,115
Office equipment	34,580	42,290	42,873
Buildings and leasehold improvements	<u>54,317</u>	<u>54,317</u>	<u>54,317</u>
	299,797	329,224	330,490
Less accumulated depreciation	<u>(254,917)</u>	<u>(297,900)</u>	<u>(277,054)</u>
	<u>\$ 44,880</u>	<u>\$ 31,324</u>	<u>\$ 53,436</u>

For additional information on capital assets, please refer to note 4 in the accompanying financial statements. MWSC has no long-term debt as of September 30, 2008, 2007 and 2006.

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

Management's Discussion and Analysis, Continued  
Year Ended September 30, 2008

### **ECONOMIC OUTLOOK**

MWSC will continue to monitor operating expenses and maintain tight fiscal constraints and control over cash and will continue to endeavor to improve 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 services provided,
- b) Collection of long outstanding utility receivables,
- c) Continuing improvements in operations.

### **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, 2008 and 2007

<u>ASSETS</u>	<u>2008</u>	<u>2007</u>
Current assets:		
Cash	\$ 55,272	\$ 24,999
Receivables:		
Utility	1,391,569	1,335,450
Affiliates	193,432	68,612
Other	3,238	4,447
	<u>1,588,239</u>	<u>1,408,509</u>
Less allowance for doubtful accounts	<u>(1,411,974)</u>	<u>(1,305,018)</u>
	<u>176,265</u>	<u>103,491</u>
Inventory	125,006	122,204
Prepaid expenses	-	8,233
Total current assets	<u>356,543</u>	<u>258,927</u>
Capital assets, net	<u>44,880</u>	<u>31,324</u>
	<u>\$ 401,423</u>	<u>\$ 290,251</u>
 <u>LIABILITIES AND NET ASSETS</u> 		
Current liabilities:		
Accounts payable	\$ 32,066	\$ 22,615
Social security taxes payable	35,754	47,592
Withholding taxes payable	61,777	84,960
Payable to affiliates	17,850	777,334
Other accrued liabilities	39,645	59,458
Total current liabilities	<u>187,092</u>	<u>991,959</u>
Commitment and contingency		
Net assets:		
Invested in capital assets	44,880	31,324
Unrestricted	<u>169,451</u>	<u>(733,032)</u>
Total net assets	<u>214,331</u>	<u>(701,708)</u>
	<u>\$ 401,423</u>	<u>\$ 290,251</u>

See accompanying notes to financial statements.

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

Statements of Revenues, Expenses and Changes in Net Assets  
Years Ended September 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Operating revenues:		
Utility billings	\$ 991,990	\$ 820,425
Hook-up and deliveries	177,244	175,820
Other	<u>25,765</u>	<u>29,125</u>
	1,194,999	1,025,370
Less uncollectable accounts	<u>(106,956)</u>	<u>(15,235)</u>
Total operating revenues	<u>1,088,043</u>	<u>1,010,135</u>
Operating expenses:		
Salaries, wages and benefits	713,737	715,881
Electricity	401,844	295,721
Spare parts	73,731	56,272
Petroleum, oil and lubricants	65,651	52,919
Depreciation and amortization	32,850	27,047
Contractual services	28,104	14,240
Communications	24,210	30,508
Insurance	19,305	19,788
Office supplies	12,871	14,084
Repairs and maintenance	2,457	7,405
Travel	-	5,263
Miscellaneous	<u>47,501</u>	<u>33,393</u>
Total operating expenses	<u>1,422,261</u>	<u>1,272,521</u>
Operating loss	<u>(334,218)</u>	<u>(262,386)</u>
Nonoperating revenues (expenses):		
RepMar subsidy	1,258,763	349,404
Penalties and interest	<u>(8,506)</u>	<u>-</u>
Total nonoperating revenues (expenses), net	<u>1,250,257</u>	<u>349,404</u>
Change in net assets	916,039	87,018
Net assets at beginning of year	<u>(701,708)</u>	<u>(788,726)</u>
Net assets at end of year	<u>\$ 214,331</u>	<u>\$ (701,708)</u>

See accompanying notes to financial statements.

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

Statements of Cash Flows  
Years Ended September 30, 2008 and 2007

	2008	2007
Cash flows from operating activities:		
Cash received from customers	\$ 1,039,669	\$ 960,119
Cash payments to suppliers for goods and services	(278,762)	(257,447)
Cash payments to employees for services	(720,354)	(691,038)
Net cash provided by operating activities	40,553	11,634
Cash flows from noncapital financing activities:		
RepMar subsidy	75,000	99,404
Principal payments on RepMar promissory note	(27,200)	(40,800)
Principal payments on MISSA promissory note	-	(30,800)
Penalties and interest paid	(11,604)	(65,515)
Net cash provided by (used for) noncapital financing activities	36,196	(37,711)
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(46,476)	(4,935)
Net change in cash	30,273	(31,012)
Cash at beginning of year	24,999	56,011
Cash at end of year	\$ 55,272	\$ 24,999
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (334,218)	\$ (262,386)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	32,850	27,047
Bad debts	106,956	15,235
Loss on disposal of fixed assets	70	-
(Increase) decrease in assets:		
Receivables:		
Utility	(56,119)	(106,640)
Affiliates	(100,420)	28,688
Other	1,209	12,701
Inventory	(2,802)	(3,396)
Prepaid expenses	8,233	(8,233)
Increase (decrease) in liabilities:		
Accounts payable	9,451	11,185
Social security taxes payable	(11,838)	10,002
Payable to affiliates	399,879	252,114
Other accrued liabilities	(12,698)	35,317
Net cash provided by operating activities	\$ 40,553	\$ 11,634
Summary of noncash financing activities:		
RepMar subsidy	\$ 1,159,363	\$ 250,000
Decrease in payables to affiliates	(1,159,363)	(250,000)
	\$ -	\$ -

See accompanying notes to financial statements.

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2008 and 2007

### (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 terms of both the lease and the franchise were for a ten year period commencing on March 9, 1989, and 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 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 GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and modified by GASB Statement No. 38, *Certain Financial Statement Note 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, 2008 and 2007

## (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. MWSC 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

Custodial credit risk is the risk that in the event of a bank failure, MWSC's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name. MWSC does not have a deposit policy for custodial credit risk.

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, 2008 and 2007, cash was \$55,272 and \$24,999, respectively, and the corresponding bank balances were \$59,724 and \$30,813, respectively, which are maintained in one financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2008 and 2007, bank deposits were fully FDIC insured.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2008 and 2007

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

### 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 collectability 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).

### 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.

### Revenue Recognition

Sales of water are recorded as billed to customers on a monthly billing cycle basis with customer water meters being read at the end of each month. Revenue is recognized in the period that meters are read. Wastewater treatment is billed at a flat rate of \$12 per month for residential accounts (\$10 per month in 2007) and \$9 per pan for commercial and government accounts (\$7.50 per month in 2007). Water delivery sales and hook-up fees are recorded when the services are provided to the customers.

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2008 and 2007

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

#### New Accounting Standards

During fiscal year 2008, MWSC implemented GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues*, and GASB Statement No. 50, *Pension Disclosures an amendment of GASB Statements No. 25 and 27*. GASB Statement No. 43 establishes uniform financial reporting for other postemployment benefit plans by state and local governments and GASB Statement No. 50 more closely aligns the financial reporting requirements for pensions with those for other post-employment benefits. GASB Statement No. 48 establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing, and includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment 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, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB Statement No. 49 provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In June 2007, GASB issued statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. GASB Statement No. 51 addresses whether and when intangible assets should be considered capital assets for financial reporting purposes. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In November 2007, GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. GASB Statement No. 52 improves the quality of financial reporting by requiring endowments to report their land and other real estate investments at fair value, creating consistency in reporting among similar entities that exist to invest resources for the purpose of generating income. The provisions of this statement are effective for periods beginning after June 15, 2008. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2008 and 2007

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

### New Accounting Standards, Continued

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. GASB Statement No. 53 is intended to improve how state and local governments report information about derivative instruments - financial arrangements used by governments to manage specific risks or make investments - in their financial statements. The provisions of this statement are effective for periods beginning after June 15, 2009. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

## (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, 2008 and 2007, was as follows:

	2008			
	October 1, <u>2007</u>	<u>Additions</u>	<u>Retirements</u>	September 30, <u>2008</u>
Vehicles	\$ 130,985	\$ 38,750	\$ (53,153)	\$ 116,582
Machinery and equipment	101,632	887	(8,201)	94,318
Office equipment	42,290	6,839	(14,549)	34,580
Buildings and leasehold improvements	<u>54,317</u>	-	-	<u>54,317</u>
	329,224	46,476	(75,903)	299,797
Less accumulated depreciation and amortization	<u>(297,900)</u>	<u>(32,850)</u>	<u>75,833</u>	<u>(254,917)</u>
	<u>\$ 31,324</u>	<u>\$ 13,626</u>	<u>\$ (70)</u>	<u>\$ 44,880</u>
	2007			
	October 1, <u>2006</u>	<u>Additions</u>	<u>Retirements</u>	September 30, <u>2007</u>
Vehicles	\$ 130,185	\$ 800	\$ -	\$ 130,985
Machinery and equipment	103,115	-	(1,483)	101,632
Office equipment	42,873	4,135	(4,718)	42,290
Buildings and leasehold improvements	<u>54,317</u>	-	-	<u>54,317</u>
	330,490	4,935	(6,201)	329,224
Less accumulated depreciation and amortization	<u>(277,054)</u>	<u>(27,047)</u>	<u>6,201</u>	<u>(297,900)</u>
	<u>\$ 53,436</u>	<u>\$ (22,112)</u>	<u>\$ -</u>	<u>\$ 31,324</u>

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2008 and 2007

### (5) Social Security Taxes Payable

At September 30, 2008 and 2007, MWSC was liable for taxes payable to the Marshall Islands Social Security Administration (MISSA) in the amount of \$35,754 and \$47,592, respectively. In addition, MWSC was liable for certain delinquent taxes payable. In addition, MWSC was liable for certain delinquent taxes payable. On February 7, 2003, MWSC and MISSA entered into a promissory note for the repayment of these delinquent taxes payable in the original 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. The promissory note was paid off during fiscal year 2007. Changes in MWSC's promissory note payable to MISSA for the year ended September 30, 2007, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Repayments</u>	<u>Ending Balance</u>
2007	\$ <u>30,800</u>	\$ <u>-</u>	\$ <u>(30,800)</u>	\$ <u>-</u>

### (6) Withholding Taxes Payable

At September 30, 2008 and 2007, MWSC was liable for withholding taxes payable to RepMar in the amount of \$58,358 and \$78,443, respectively, and related penalties and interest in the amount of \$3,419 and \$6,517, respectively. In addition, MWSC was liable for certain delinquent taxes payable. On January 30, 2006, a 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. Changes in MWSC's promissory note payable to RepMar for the years ended September 30, 2008 and 2007, follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Repayments</u>	<u>Ending Balance</u>
2008	\$ <u>68,848</u>	\$ <u>-</u>	\$ <u>(27,200)</u>	\$ <u>41,648</u>
2007	\$ <u>109,848</u>	\$ <u>-</u>	\$ <u>(40,800)</u>	\$ <u>68,848</u>

MWSC did not comply with the repayment terms of this promissory note. Accordingly, this promissory note payable along with related penalties and interest payable is reflected as a current liability in the accompanying financial statements and is presented within the current withholding taxes payable balance.

### (7) Related Party Transactions

MWSC is a component unit of RepMar, and is therefore affiliated with all RepMar-owned and affiliated entities.

During the years ended September 30, 2008 and 2007, MWSC received operating subsidies from RepMar in the amount of \$1,258,763 and \$349,404, respectively, of which \$1,159,363 and \$250,000, respectively, was paid directly to the Marshalls Energy Company, Inc. as partial payment on outstanding electricity billings owed by MWSC. At September 30, 2008 and 2007, operating subsidies due from RepMar amounted to \$24,400 and \$0, respectively.

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2008 and 2007

### (7) Related Party Transactions, Continued

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 afforded to third parties.

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

A summary of related party transactions for the years ended September 30, 2008 and 2007, and related receivable and payable balances as of September 30, 2008 and 2007, is as follows:

	2008			
	Revenues	Expenses	Receivables	Payables
RepMar	\$ 198,369	\$ 92,926	\$ 134,436	\$ 61,777
Marshalls Energy Company, Inc.	19,635	401,844	25,832	16,711
Marshall Islands National Telecommunications Authority	8,577	14,428	1,239	1,139
Marshall Islands Social Security Administration	856	61,921	83	35,754
Majuro Resort, Inc.	58,435	-	13,385	-
Other	<u>45,206</u>	<u>11,043</u>	<u>18,457</u>	<u>-</u>
	<u>\$ 331,078</u>	<u>\$ 582,162</u>	<u>\$ 193,432</u>	<u>\$ 115,381</u>
	2007			
	Revenues	Expenses	Receivables	Payables
RepMar	\$ 76,844	\$ 2,459	\$ 22,062	\$ 84,960
Marshalls Energy Company, Inc.	6,187	295,721	17,773	775,589
Marshall Islands National Telecommunications Authority	5,428	21,263	1,569	1,745
Marshall Islands Social Security Administration	644	-	124	47,592
Majuro Resort, Inc.	31,030	-	14,933	-
Other	<u>25,987</u>	<u>12,143</u>	<u>12,151</u>	<u>-</u>
	<u>\$ 146,120</u>	<u>\$ 331,586</u>	<u>\$ 68,612</u>	<u>\$ 909,886</u>

Receivables from and payables to affiliates are uncollateralized, are 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).

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2008 and 2007

### (8) Commitment, Continued

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

<u>Year ending</u> <u>September 30,</u>	
2009	\$ 366,667
2010	100,000
2011	100,000
2012	100,000
2013	100,000
2014-2017	<u>233,333</u>
	<u>\$ 1,000,000</u>

During the years ended September 30, 2008 and 2007, MWSC did not record the liability per the franchise agreement due to lack of capacity to make the payments in the foreseeable future. MWSC essentially depends on financing from RepMar and MEC to be able to continue as a going concern. Thus, management will negotiate the franchise terms with RepMar. If negotiations fail, MWSC may become liable for the above amounts but management does not believe that it will possess the ability to liquidate that liability.

### (9) Going Concern

MWSC has incurred losses from operations of \$334,218 and \$262,386 during the years ended September 30, 2008 and 2007, respectively, and as of those dates working capital were of \$169,451 and (\$733,032), 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, among other matters. Additionally, in order for MWSC to continue as a going concern, it may need to delay payments to the Marshalls Energy Company, Inc. for electric usage or to delay payments to RepMar for delinquent employee withholding taxes.