

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

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

**FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT**

YEARS ENDED SEPTEMBER 30, 2009 AND 2008

INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying statements of net assets of the Kwajalein Atoll Joint Utilities Resources, Inc. (KAJUR), a component unit of the Republic of the Marshall Islands, as of September 30, 2009 and 2008, 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.

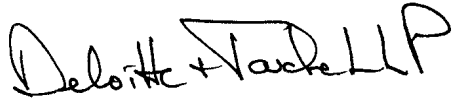
Except as discussed in the following paragraph, we conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United 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 the inadequacy of accounting records, we were unable to form an opinion regarding the amounts at which receivables, net of allowance for uncollectible accounts, are recorded in the accompanying statement of net assets at September 30, 2008.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had the accounting records been adequate for us to satisfy ourselves about receivables, as discussed in the third paragraph above, the financial statements present fairly, in all material respects, the financial position of KAJUR as of September 30, 2009 and 2008, and its 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 3 through 7 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 June 30, 2010, 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 that reads "Deloitte + Tuckers LLP". The signature is written in a cursive, stylized font.

June 30, 2010

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Management's Discussion and Analysis Year Ended September 30, 2009

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 ended on September 30, 2009. It is to be read in conjunction with the financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

KAJUR's net assets decreased by \$580,235 in 2009 compared to an increase of \$172,009 in 2008. The significant decrease in net assets was mainly due to \$750,199 capital contributions received in 2008. In 2008, KAJUR was the recipient of capital grants from the Republic of the Marshall Islands (RepMar), of which \$466,419 was paid directly by RepMar to vendors for the acquisition and construction of capital assets. In 2009, KAJUR did not receive capital contributions.

Total net operating revenue decreased from \$3,248,558 in 2008 to \$3,140,598 in 2009. Electric and Service, Water and Other billings decreased by \$531,060 from 2008 to 2009. The provision for doubtful account decreased from \$781,401 in 2008 to \$358,301 in 2009, resulting in a decrease of \$423,100. The decreasing trend for both the billings and provision for doubtful accounts is attributed to the debit meter installation for residential customers which was completed in 2008. As a result, the final net impact for total operating revenue decreased slightly by \$107,960 from 2008 to 2009.

Total operating expenses decreased from \$6,341,298 in 2008 to \$6,268,292 in 2009. Although fuel and lubricant expenses decreased significantly by \$821,733 from 2008 to 2009, other costs to include but not limited to depreciation, operations and maintenance expenses increased by \$748,727. Overall, the net impact of the total operating expenses decreased slightly by \$73,006 from 2008 to 2009.

FINANCIAL ANALYSIS OF KAJUR

The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets 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>2009</u>	<u>2008</u>	<u>2007</u>
Current and other assets	\$ 1,829,698	\$ 1,623,068	\$ 1,917,468
Capital assets	<u>4,241,345</u>	<u>5,060,129</u>	<u>4,690,962</u>
Total assets	\$ <u>6,071,043</u>	\$ <u>6,683,197</u>	\$ <u>6,608,430</u>
Current liabilities	\$ 979,205	\$ 1,015,358	\$ 1,093,611
Non-current liabilities	<u>834,431</u>	<u>830,197</u>	<u>849,186</u>
Total liabilities	<u>1,813,636</u>	<u>1,845,555</u>	<u>1,942,797</u>
Net assets:			
Invested in capital assets	4,241,345	5,060,129	4,690,962
Unrestricted	<u>16,062</u>	<u>(222,487)</u>	<u>(25,329)</u>
Total net assets	\$ <u>4,257,407</u>	\$ <u>4,837,642</u>	\$ <u>4,665,633</u>

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Management's Discussion and Analysis, Continued Year Ended September 30, 2009

As indicated above, total assets have increased from \$6,608,430 in 2007 to \$6,683,197 in 2008 but have decreased significantly in 2009 to \$6,071,043. Most of the change is explained by a decrease in net capital assets by \$818,784 from 2008 to 2009 and an increase in the allowance for bad debts by \$234,451 from 2008 to 2009.

There has been a trending decrease in total liabilities from \$1,942,797 in 2007 to \$1,845,555 in 2008 and \$1,813,636 in 2009.

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

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Revenues:			
Net operating revenues	\$ 3,140,598	\$ 3,248,558	\$ 2,885,729
Non-operating revenues	<u>3,075,712</u>	<u>3,005,611</u>	<u>3,779,894</u>
Total revenues	<u>6,216,310</u>	<u>6,254,169</u>	<u>6,665,623</u>
Expenses:			
Operating expenses	6,268,292	6,341,298	5,696,856
Non-operating expenses	<u>528,253</u>	<u>491,061</u>	<u>852,225</u>
Total expenses	6,796,545	6,832,359	6,549,081
Income (loss) before capital contributions	(580,235)	(578,190)	116,542
Capital contributions	<u>-</u>	<u>750,199</u>	<u>354,804</u>
Change in net assets	\$ <u>(580,235)</u>	\$ <u>172,009</u>	\$ <u>471,346</u>

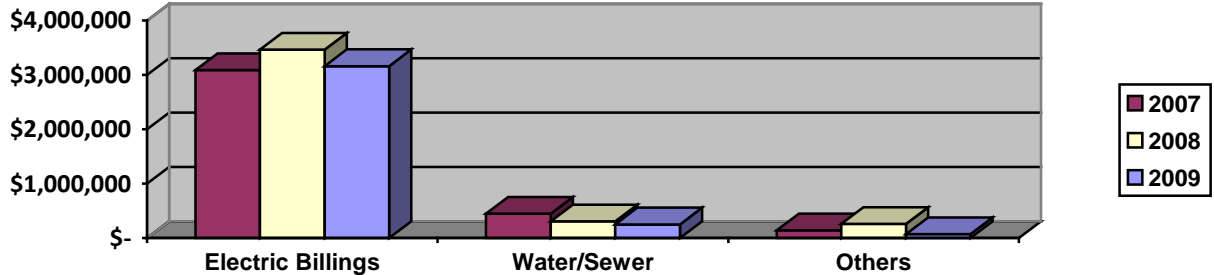
The Statement of Revenues, Expenses and Changes in Net Assets identify the various revenue and expense items that impacted on the change in net assets. As indicated above, KAJUR's total revenues decreased from \$6,665,623 in 2007 to \$6,254,169 in 2008 to \$6,216,310 in 2009. Within the operating revenues, electric billings increased from \$3,090,617 in 2007 to \$3,465,768 in 2008 but decreased to \$3,161,908 in 2009. The decrease in electric billings in 2009 is representative of the debit meter installation initiative that was completed for all residential customers in 2008. Water and sewer billings also decreased from \$445,524 in 2007 to \$306,310 in 2008 and further decreased to \$249,510 in 2009. Other billings, on the other hand, increased from \$138,390 in 2007 to \$257,881 in 2008 but dramatically decreased to \$87,481 in 2009.

The graph below shows the major components of operating revenues for 2007, 2008 and 2009.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Management's Discussion and Analysis, Continued
Year Ended September 30, 2009

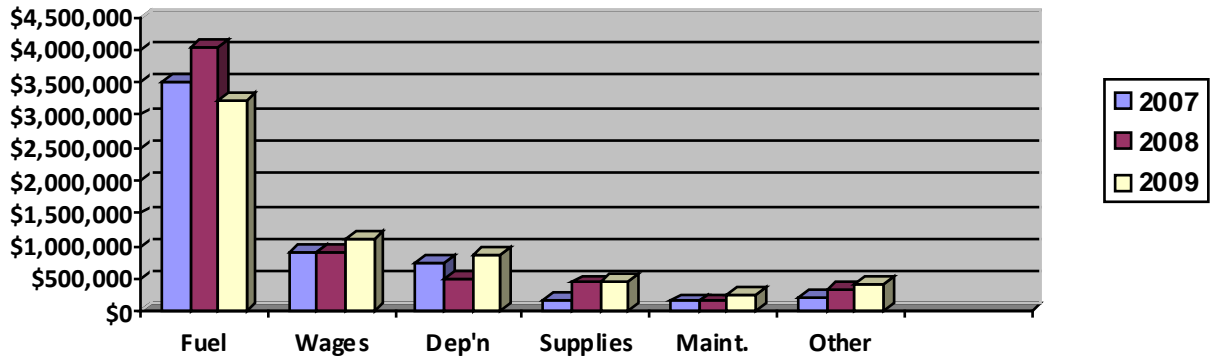
Major Income Items



Total expenses increased from \$6,549,081 in 2007 to \$6,832,359 in 2008 but decreased only slightly by \$35,814 to \$6,796,545 in 2009.

The graph below shows the major components of operating expenses for 2007, 2008 and 2009.

Major Expense Items



CAPITAL ASSETS

Net capital assets increased from \$4,690,962 in 2007 to \$5,060,129 in 2008 but decreased to \$4,241,345 in 2009. The increase amount of \$369,167 in 2007 to 2008 is the net \$1,266,128 capital asset acquisitions less depreciation of \$481,784 and the retirement of capital assets in the amount of \$415,177. The decrease amount of \$818,784 in 2008 to 2009 is the net of \$651,026 in capital asset acquisitions (and equipment in transit) less depreciation of \$860,092 and the retirement of capital assets in the amount of \$609,718.

Major capital asset acquisitions include water truck in 2009 and generators in 2008.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Management's Discussion and Analysis, Continued Year Ended September 30, 2009

A summary of KAJUR's capital assets is presented below:

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Plant and machinery	\$ 5,038,589	\$ 4,859,959	\$ 4,673,318
Distribution system	2,215,325	2,215,325	1,954,079
Water system	1,181,172	1,077,072	1,031,015
Other equipment	<u>1,491,952</u>	<u>1,305,416</u>	<u>1,111,035</u>
	9,927,038	9,457,772	8,769,447
Less accumulated depreciation	<u>(5,867,453)</u>	<u>(5,007,361)</u>	<u>(4,688,203)</u>
	4,059,585	4,450,411	4,081,244
Construction work-in-progress/ equipment in transit	<u>181,760</u>	<u>609,718</u>	<u>609,718</u>
	\$ <u>4,241,345</u>	\$ <u>5,060,129</u>	\$ <u>4,690,962</u>

Please refer to note 5 to the accompanying financial statements for additional information relating to capital assets.

FUTURE OUTLOOK ON SUSTAINABILITY

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) Collection of long outstanding utility receivables, and
- c) Continuing improvements in operations.

There has been an increasing trend of operating losses in the amount of \$2,811,127 in 2007, \$3,092,740 in 2008 and \$3,147,345 in 2009. It is essential that Management continue to identify the operating loss root causes and implement a full cost recovery structure, promote system efficiencies, quantify and rectify system losses for both technical and non-technical losses and minimize its operational expenses. Until then, RepMar will be required to provide financial support to subsidize KAJUR's operation losses.

With the completion of the prepaid meter installation for all residential customers in 2008, this initiative provides a positive outlook for KAJUR financials to reduce its exposure to long outstanding utility receivables, thereby minimizing the exposure to bad debt losses and improve cash flow. In conjunction with process improvements and fostering an internal controlled environment, this provides a good starting point for KAJUR future viability.

KAJUR'S FOCUS IN THE COMING FISCAL YEAR

The following are KAJUR's goals for the coming fiscal year 2010 to include but not limited to:

- 1.) Implement an Accounts Receivable Billing System for all commercial customers. Currently, KAJUR has been utilizing excel spreadsheet to process commercial customer monthly billings for electric services. With the use of Excel Spreadsheet, there is higher risk for process gaps, billing errors and misstatements to the General Ledger and Financial Statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Management's Discussion and Analysis, Continued Year Ended September 30, 2009

- 2.) Establish charges for water and sewer customers. Since 2007, KAJUR has not been charging the customers for water and sewage usage due to unreliable system and readings to track and monitor appropriate usage. As a result, this has contributed to KAJUR's exposure to revenue losses. To mitigate the risk and establish water and sewer charges, a survey will be completed during the coming fiscal year.
- 3.) Write off approximately \$3.4M bad debt for Electric, Water and Sewer Billings. Unfortunately, the material write off amount has been identified and deemed necessary due to antiquated billing systems (i.e. Excel Spreadsheet) and economical challenges to collect monies due on past due balances. With the prepaid meter installation that was completed in fiscal year 2008, KAJUR's exposure to bad debt has been minimized for residential customers. In the meantime, KAJUR management will continue to make every effort to recover the bad debt write off.

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. Manager at P.O. Box 5819, Ebeye MH 96970.

Management's Discussion and Analysis for the year ended September 30, 2008 is set forth in the report on the audit of KAJUR's financial statements, which is dated August 24, 2009. That Discussion and Analysis explains the major factors impacting the 2008 financial statements.

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. Manager at P.O. Box 5819, Ebeye MH 96970.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Statements of Net Assets
September 30, 2009 and 2008

<u>ASSETS</u>	<u>2009</u>	<u>2008</u>
Current assets:		
Cash	\$ 235,401	\$ 172,578
Receivables:		
Utility	5,311,249	4,813,862
Affiliate	-	10,398
Employees	20,511	16,180
Other	242,803	317,363
	<u>5,574,563</u>	<u>5,157,803</u>
Less allowance for doubtful accounts	(5,072,640)	(4,838,189)
Total receivables, net	<u>501,923</u>	<u>319,614</u>
Prepaid expenses	786,726	29,120
Inventories	305,648	997,656
Total current assets	<u>1,829,698</u>	<u>1,518,968</u>
Long-term prepayment	-	104,100
Capital assets, net	<u>4,241,345</u>	<u>5,060,129</u>
	<u>\$ 6,071,043</u>	<u>\$ 6,683,197</u>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Accounts payable	\$ 386,417	\$ 180,078
Current portion of social security taxes payable	96,000	142,550
Due to affiliates	189,161	446,037
Accrued liabilities	141,325	99,501
Deferred revenue	166,302	147,192
Total current liabilities	<u>979,205</u>	<u>1,015,358</u>
Accrued sick leave - long-term	55,845	52,256
Social security taxes payable, net of current portion	<u>778,586</u>	<u>777,941</u>
	<u>1,813,636</u>	<u>1,845,555</u>
Contingencies		
Net assets:		
Invested in capital assets	4,241,345	5,060,129
Unrestricted	16,062	(222,487)
Total net assets	<u>4,257,407</u>	<u>4,837,642</u>
	<u>\$ 6,071,043</u>	<u>\$ 6,683,197</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, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Operating revenues:		
Electric and service billings	\$ 3,161,908	\$ 3,465,768
Water	249,510	306,310
Other	87,481	257,881
Total operating revenues	<u>3,498,899</u>	<u>4,029,959</u>
Less provision for doubtful accounts	<u>(358,301)</u>	<u>(781,401)</u>
Total net operating revenues	<u>3,140,598</u>	<u>3,248,558</u>
Operating expenses:		
Fuel and lubricants	3,221,288	4,043,021
Salaries, wages and benefits	1,093,612	899,268
Depreciation	860,092	481,784
Supplies and materials	442,093	433,801
Operations and maintenance	239,293	145,502
Contractual services	16,447	500
Travel and transportation	216,779	159,732
Communications	14,752	15,460
Rental	-	40,607
Miscellaneous	163,936	121,623
Total operating expenses	<u>6,268,292</u>	<u>6,341,298</u>
Operating loss	<u>(3,127,694)</u>	<u>(3,092,740)</u>
Nonoperating revenues (expenses):		
Operating subsidies	-	347,900
Compact funding	3,075,712	2,487,100
Interest expense	(97,165)	(75,884)
Other income	-	170,611
Loss on write-off of fixed assets	<u>(431,088)</u>	<u>(415,177)</u>
Total nonoperating revenues, net	<u>2,547,459</u>	<u>2,514,550</u>
Capital contributions	<u>-</u>	<u>750,199</u>
Change in net assets	<u>(580,235)</u>	<u>172,009</u>
Net assets at beginning of year	<u>4,837,642</u>	<u>4,665,633</u>
Net assets at end of year	<u>\$ 4,257,407</u>	<u>\$ 4,837,642</u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Statements of Cash Flows
Years Ended September 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:		
Cash received from customers	\$ 2,981,730	\$ 3,272,225
Cash payments to suppliers for goods and services	(4,430,723)	(5,106,609)
Cash payments to employees for services	<u>(1,067,600)</u>	<u>(898,958)</u>
Net cash used for operating activities	<u>(2,516,593)</u>	<u>(2,733,342)</u>
Cash flows from noncapital financing activities:		
Promissory note repayment	(77,526)	(53,630)
Interest paid	(50,474)	(50,370)
Operating subsidies received from RepMar	<u>3,075,712</u>	<u>2,835,000</u>
Net cash provided by noncapital financing activities	<u>2,947,712</u>	<u>2,731,000</u>
Cash flows from capital and related financing activities:		
Capital contribution	-	283,780
Acquisition and construction of capital assets	<u>(368,296)</u>	<u>(565,272)</u>
Net cash used for capital and related financing activities	<u>(368,296)</u>	<u>(281,492)</u>
Net change in cash	62,823	(283,834)
Cash at beginning of year	<u>172,578</u>	<u>456,412</u>
Cash at end of year	<u>\$ 235,401</u>	<u>\$ 172,578</u>
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (3,127,694)	\$ (3,092,740)
Adjustments to reconcile loss from operations to net cash used for operating activities:		
Depreciation	860,092	481,784
Provision for doubtful accounts	358,301	781,401
(Increase) decrease in assets:		
Receivables:		
Utility	(497,387)	(658,288)
Employees	(4,331)	(3,312)
Other	(38,892)	(118,836)
Prepaid expenses	(757,606)	30,538
Inventories	692,008	(255,374)
Increase (decrease) in liabilities:		
Accounts payable	206,339	(188,515)
Social security taxes payable	(15,070)	8,995
Due to affiliates	(256,876)	266,988
Deferred revenue	19,110	18,700
Other current and accrued liabilities	<u>45,413</u>	<u>(4,683)</u>
Net cash used for operating activities	<u>\$ (2,516,593)</u>	<u>\$ (2,733,342)</u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.Statements of Cash Flows, Continued
Years Ended September 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Non-cash investing, capital, and financing activities:		
Capital contributions received from RepMar	\$ -	\$ 466,419
Prepaid expenses	-	234,437
Acquisition and construction of capital assets	-	(700,856)
	<u>\$ -</u>	<u>\$ -</u>
Capital assets	\$ 326,988	\$ 577,803
Accumulated depreciation	-	(162,626)
Prepaid expenses	104,100	-
Loss on write-off of capital assets	(431,088)	(415,177)
	<u>\$ -</u>	<u>\$ -</u>
Accrued liabilities	\$ -	\$ (170,611)
Other income	-	170,611
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2009 and 2008

(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 13, 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 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.

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

GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and modified by Statement No. 38, *Certain Financial Statement Note Disclosures*, 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.

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

- Invested 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.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

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

Custodial credit risk is the risk that in the event of a bank failure, KAJUR'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. KAJUR 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 in checking accounts. As of September 30, 2009 and 2008, the carrying amount of cash was \$235,401 and \$172,578, respectively, and the corresponding bank balances were \$255,191 and \$164,523, respectively. At September 30, 2009 and 2008, 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, 2009 and 2008. Bulk fuel inventories are held for power plant use.

Prepayments

Certain payments to vendors or persons for goods and services reflect costs applicable to future accounting periods and are recorded as prepaid expenses in the accompanying financial statements.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2009 and 2008

(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, 2009 and 2008, is \$53,035 and \$56,706, 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, 2009 and 2008, is \$111,789 and \$75,190, respectively, and is included within the statements of net assets as accrued liabilities and accrued sick leave – long-term.

New Accounting Standards

During fiscal year 2009, KAJUR implemented the following pronouncements:

- GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which establishes standards for the measurement, recognition, and display of other postemployment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers.
- GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, which provides guidance and consistency under which a governmental entity would be required to report a liability related to pollution remediation.
- GASB Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*, which 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.

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2009 and 2008

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

- GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which improves financial reporting by contributing to the GASB's efforts to codify all GAAP for state and local governments so that they derive from a single source.
- GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*, which incorporates accounting and financial reporting guidance previously only contained in the American Institute of Certified Public Accountants (AICPA) auditing literature into the GASB's accounting and financial reporting literature for state and local governments, and addresses three issues from the AICPA's literature - related party transactions, going concern considerations, and subsequent events.

The implementation of these pronouncements did not have a material effect on the accompanying financial statements.

In June 2007, GASB issued statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, which 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 KAJUR.

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which 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 KAJUR.

In December 2008, GASB issued Technical Bulletin No. 2008-1, *Determining the Annual Required Contribution Adjustment for Postemployment Benefits*, which clarifies the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, for calculating the annual required contribution (ARC) adjustment. 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.

In March 2009, GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The provisions of this statement are effective for periods beginning after June 15, 2010. 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
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(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. Loss incurred during the year as a result of these risks is not material to the financial statements.

(4) Inventories

Inventories at September 30, 2009 and 2008, consist of the following:

	<u>2009</u>	<u>2008</u>
Materials and supplies	\$ 177,572	\$ 76,194
Fuel	109,053	902,439
Lubricants	<u>19,023</u>	<u>19,023</u>
	<u>\$ 305,648</u>	<u>\$ 997,656</u>

(5) Capital Assets

Capital assets activity for the years ended September 30, 2009 and 2008 is as follows:

	<u>2009</u>			<u>September 30,</u>
	<u>October 1,</u>	<u>Additions</u>	<u>Retirements</u>	<u>2009</u>
	<u>2008</u>			
Plant and machinery	\$ 4,859,959	\$ 178,630	\$ -	\$ 5,038,589
Distribution system	2,215,325	-	-	2,215,325
Water system	1,077,072	104,100	-	1,181,172
Other equipment	<u>1,305,416</u>	<u>186,536</u>	<u>-</u>	<u>1,491,952</u>
	9,457,772	469,266	-	9,927,038
Less accumulated depreciation	<u>(5,007,361)</u>	<u>(860,092)</u>	<u>-</u>	<u>(5,867,453)</u>
	4,450,411	(390,826)	-	4,059,585
Construction work-in-progress	609,718	-	(609,718)	-
Equipment in-transit	<u>-</u>	<u>181,760</u>	<u>-</u>	<u>181,760</u>
	<u>\$ 5,060,129</u>	<u>\$ (209,066)</u>	<u>\$ (609,718)</u>	<u>\$ 4,241,345</u>

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2009 and 2008

(5) Capital Assets, Continued

	2008			
	October 1, <u>2007</u>	<u>Additions</u>	<u>Retirements</u>	September 30, <u>2008</u>
Plant and machinery	\$ 4,673,318	\$ 764,444	\$ (577,803)	\$ 4,859,959
Distribution system	1,954,079	261,246	-	2,215,325
Water system	1,031,015	46,057	-	1,077,072
Other equipment	<u>1,111,035</u>	<u>194,381</u>	<u>-</u>	<u>1,305,416</u>
	8,769,447	1,266,128	(577,803)	9,457,772
Less accumulated depreciation	<u>(4,688,203)</u>	<u>(481,784)</u>	<u>162,626</u>	<u>(5,007,361)</u>
	4,081,244	784,344	(415,177)	4,450,411
Construction work-in-progress	<u>609,718</u>	<u>-</u>	<u>-</u>	<u>609,718</u>
	\$ <u>4,690,962</u>	\$ <u>784,344</u>	\$ <u>(415,177)</u>	\$ <u>5,060,129</u>

At September 30, 2009 and 2008, management of KAJUR determined that certain capital assets in the amount of \$431,088 and \$577,803, respectively, net of \$0 and \$162,626, respectively, in accumulated depreciation, no longer existed. Accordingly, these capital assets were written off resulting in a loss of \$431,088 and \$415,177, respectively, for the years ended September 30, 2009 and 2008.

(6) Social Security Taxes Payable

At September 30, 2009 and 2008, KAJUR was liable for taxes, including certain delinquent taxes, interest and penalties, payable to the Marshall Islands Social Security Administration (MISSA) in the amounts of \$874,586 and \$920,419, respectively. On October 12, 2007, KAJUR and MISSA entered into a promissory note agreement for the delinquent taxes. The terms of this agreement include monthly payments of \$8,000, interest of 12% per annum, commencing October 31, 2007. For the years ended September 30, 2009 and 2008, KAJUR incurred penalties and interest relating to these delinquent taxes of \$94,304 and \$78,622, respectively.

During the years ended September 30, 2009 and 2008, employer contributions incurred by KAJUR for MISSA taxes amounted to \$86,676 and \$79,941, respectively.

(7) Changes in Long-term Liabilities

Long-term debt activity during the years ended September 30, 2009 and 2008 were as follows:

	Balance at <u>October 1, 2008</u>	<u>Additions</u>	<u>Reductions</u>	Balance at <u>September 30, 2009</u>	Amount due <u>in One Year</u>
MISSA:					
Delinquent taxes	\$ 621,212	\$ 34,341	\$ (77,526)	\$ 578,027	\$ 48,598
Penalties and interest	<u>252,729</u>	<u>94,304</u>	<u>(50,474)</u>	<u>296,559</u>	<u>47,402</u>
Total MISSA	873,941	128,645	(128,000)	874,586	96,000
Accrued sick leave	<u>52,256</u>	<u>3,589</u>	<u>-</u>	<u>55,845</u>	<u>-</u>
Total	\$ <u>926,197</u>	\$ <u>132,234</u>	\$ <u>(128,000)</u>	\$ <u>930,431</u>	\$ <u>96,000</u>

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2009 and 2008

(7) Changes in Long-term Liabilities, Continued

	<u>Balance at</u> <u>October 1, 2007</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance at</u> <u>September 30, 2008</u>	<u>Amount due</u> <u>in One Year</u>
MISSA:					
Delinquent taxes	\$ 674,842	\$ -	\$ (53,630)	\$ 621,212	\$ 56,289
Penalties and interest	<u>224,477</u>	<u>78,622</u>	<u>(50,370)</u>	<u>252,729</u>	<u>39,711</u>
Total MISSA	899,319	78,622	(104,000)	873,941	96,000
Accrued sick leave	<u>45,867</u>	<u>6,389</u>	<u>-</u>	<u>52,256</u>	<u>-</u>
Total	\$ <u>945,186</u>	\$ <u>85,011</u>	\$ <u>(104,000)</u>	\$ <u>926,197</u>	\$ <u>96,000</u>

Annual repayment requirements to maturity for principal and interest are as follows:

<u>Year ending</u> <u>September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 48,598	\$ 47,402	\$ 96,000
2011	55,612	40,388	96,000
2012	48,879	47,121	96,000
2013	41,048	54,952	96,000
2014	40,003	55,997	96,000
2015 - 2019	199,905	280,096	480,000
2020 - 2023	<u>143,982</u>	<u>219,475</u>	<u>363,457</u>
	\$ <u>578,027</u>	\$ <u>745,431</u>	\$ <u>1,323,457</u>

(8) Related Party Transactions

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

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, 2009 and 2008 and the related receivable and payable balances as of September 30, 2009 and 2008, are as follows:

	<u>2009</u>		
	<u>Expenses</u>	<u>Receivable</u>	<u>Payable</u>
American Samoa Power Authority (ASPA)	\$ -	\$ -	\$ 85,459
Marshalls Energy Company, Inc.	2,394,642	-	45,595
Marshall Islands National Telecommunications Authority	14,752	86,620	-
RepMar	<u>-</u>	<u>552,114</u>	<u>58,107</u>
	\$ <u>2,409,394</u>	\$ <u>638,734</u>	\$ <u>189,161</u>

KWAJALEIN ATOLL JOINT UTILITIES RESOURCES, INC.

Notes to Financial Statements
September 30, 2009 and 2008

(8) Related Party Transactions, Continued

		<u>2008</u>	
	<u>Expenses</u>	<u>Receivable</u>	<u>Payable</u>
American Samoa Power Authority (ASPA)	\$ -	\$ -	\$ 85,459
Marshalls Energy Company, Inc.	3,671,870	-	289,743
Marshall Islands National Telecommunications Authority	15,460	-	-
RepMar	<u>20,613</u>	<u>-</u>	<u>70,835</u>
	\$ <u>3,707,943</u>	\$ <u>-</u>	\$ <u>446,037</u>

During the years ended September 30, 2009 and 2008, the operations of KAJUR were funded by appropriations from RepMar in the amounts of \$3,075,712 and \$2,835,000, respectively, of which \$0 and \$10,398 was due and receivable from RepMar at September 30, 2009 and 2008, respectively. Of these appropriations from RepMar for the years ended September 30, 2009 and 2008, \$3,075,712 and \$2,835,000, respectively, were paid directly by RepMar to vendors for the purchase of fuel and lubricants.

In addition, during the years ended September 30, 2009 and 2008, KAJUR was the recipient of capital grants from RepMar in the amounts of \$0 and \$750,199, respectively, of which \$0 and \$466,419, respectively, was paid directly by RepMar to vendors for the acquisition and construction of capital assets.

As of September 30, 2009 and 2008, KAJUR maintained demand deposit accounts with a related financial institution in the amount of \$255,191 and \$164,523, respectively.

As of September 30, 2009 and 2008, KAJUR recorded deferred revenue of \$112,800, representing unexpended capital grants.

(9) 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.

KAJUR participates in a number of federally assisted grant programs. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Cumulative questioned costs of \$1,375,456 relating to fiscal years 2004 through 2007 have been set forth in KAJUR's Single Audit Report for the year ended September 30, 2009. The ultimate disposition of these questioned costs can be determined only by final action of the respective grantor agencies. Therefore, no provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

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.