

**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, 2011 and 2010**

## INDEPENDENT AUDITORS' REPORT

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

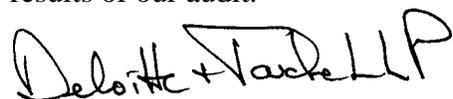
We have audited the accompanying statements of net assets of Majuro Water and Sewer Company, Inc. (MWSC), a component unit of the Republic of the Marshall Islands, as of September 30, 2011 and 2010, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years 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, 2011 and 2010, 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 July 3, 2012, 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 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.



July 3, 2012

## MAJURO WATER AND SEWER COMPANY, INC.

### Management's Discussion and Analysis Years Ended September 30, 2011 and 2010

The 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 September 30, 2011. This discussion has been prepared by management along with the financial statements and related footnote disclosure and should be read in conjunction with them. Management assumes full responsibility for the completeness and reliability of information presented in this report.

#### FINANCIAL HIGHLIGHTS

MWSC's net assets increased \$744 in 2011 compared to an increase of \$182,585 in 2010. This was due to an increase in total operating revenues of \$238,594, offset by a decrease in subsidy of \$193,668 and an increase in operating expenses of \$24,083.

An operating subsidy of \$124,431 and \$318,099 was received from the Republic of the Marshall Islands (RepMar) for fiscal years ended September 2011 and 2010, respectively. This subsidy was used to pay the electricity bills owed to Marshalls Energy Company, Inc. (MEC) and decreased by \$193,668 in 2011 compared with 2010.

Total operating revenues increased by \$238,594 (24.2%) compared to an increase in revenue of \$27,879 in 2010. Within operating revenues, utility billings increased by \$137,857 (14.8%) from \$931,635 in 2010 to \$1,069,492 in 2011. Hook ups and delivery billings decreased by \$10,895 (6.5%) from \$167,482 in 2010 to \$156,587 in 2011. The increase in revenues is also a reflection of MWSC efforts to resolve illegal water hookups and to issue customer billings as appropriate.

Operating expenses increased by \$24,083 (1.8%) from \$1,336,489 in 2010 to \$1,360,572 in 2011. The main contributing factor for the increase in operating expenses is an increase in electricity of \$28,068, spare parts of \$19,907 and contractual services of \$14,205 offset by a decrease in salaries and wages of \$47,187.

The Statement of Cash Flows net change in cash was \$1,848 and \$53,492 in 2010 and 2011, respectively. The operating activities of MWSC generated a net cash inflow of \$112,256 in 2011 compared to a net cash inflow of \$29,982 for 2010. As a result of the increase in net cash flows, MWSC's net cash used for capital and related financing activities increased in 2011 as well.

#### FINANCIAL ANALYSIS OF MWSC

The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets provide 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>2011</u>	<u>2010</u>	<u>2009</u>
Current assets	\$ 538,223	\$ 387,581	\$ 358,246
Capital assets net	<u>234,767</u>	<u>227,690</u>	<u>59,445</u>
Total Assets	<u>772,990</u>	<u>615,271</u>	<u>417,691</u>
Current liabilities	<u>437,276</u>	<u>280,301</u>	<u>265,306</u>

## MAJURO WATER AND SEWER COMPANY, INC.

### Management's Discussion and Analysis Years Ended September 30, 2011 and 2010

Net Assets:

Invested in capital assets	234,767	227,690	59,445
Unrestricted	<u>100,947</u>	<u>107,280</u>	<u>92,940</u>
Total Net Assets	\$ <u>335,714</u>	\$ <u>334,970</u>	\$ <u>152,385</u>

As indicated above, total assets increased by \$157,719 from \$615,271 in 2010 to \$772,990 in 2011. Total liabilities reflect an increase of \$156,975 from \$280,301 in 2010 to \$437,276 in 2011. Total net assets increased by \$744 from a surplus \$334,970 in 2010 to \$335,714 in 2011. There were no non-current liabilities at 30<sup>th</sup> September 2011 or 2010.

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

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Revenues:			
Operating revenues	\$ 1,225,187	\$ 986,593	\$ 958,714
Non-operating revenues	<u>124,431</u>	<u>318,099</u>	<u>346,928</u>
Total revenues	<u>1,349,618</u>	<u>1,304,692</u>	<u>1,305,642</u>
Expenses:			
Operating expenses	1,360,572	1,336,489	1,342,178
Non-operating expenses	<u>2,699</u>	<u>7,218</u>	<u>25,410</u>
Total expenses	<u>1,363,271</u>	<u>1,343,707</u>	<u>1,367,588</u>
Capital contributions	<u>14,397</u>	<u>221,600</u>	<u>-</u>
Change in net assets	\$ <u><u>744</u></u>	\$ <u><u>182,585</u></u>	\$ <u><u>(61,946)</u></u>

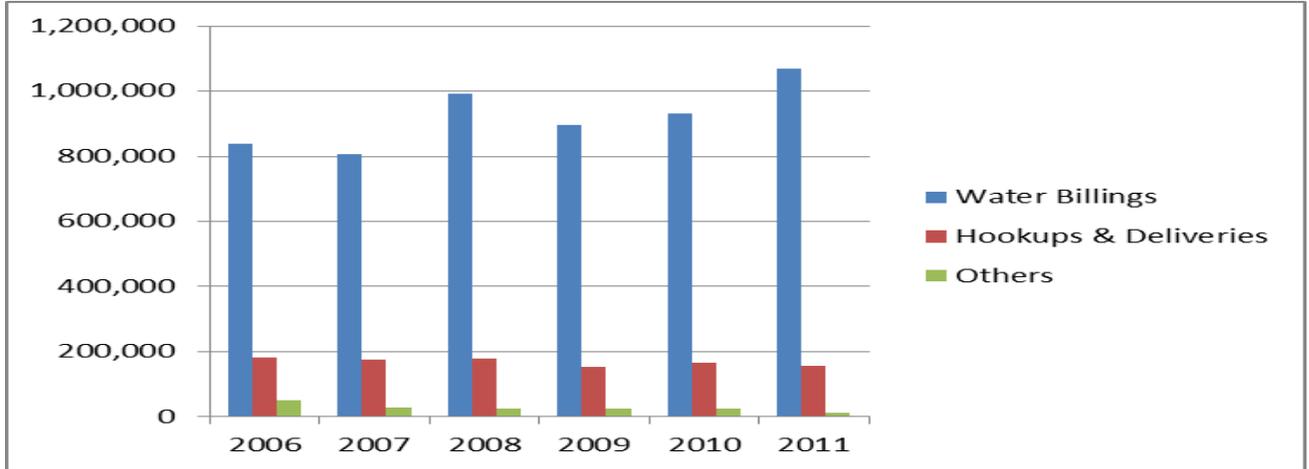
The Statement of Revenues, Expenses and Changes in Net Assets identifies the various revenue and expense items that impacted the change in net assets. As indicated above, MWSC's operating revenues increased by \$238,594 or approximately 24.2% from \$986,593 in 2010 to \$1,225,187 in 2011. The increase in operating revenues for 2011 consists of utility billings increasing by \$137,857 (14.8%) and a decrease in uncollectible accounts of \$124,246 (90.2%).

Non-operating revenues represent subsidies received from RepMar. The subsidy received in 2009 in the amount of \$346,928 was applied in its entirety to the electricity bills owed to MEC. RepMar's continued financial support to assist MWSC with the payment of the monthly electricity bills owed to MEC is represented by \$318,099 and \$124,431 received in 2010 and 2011, respectively. There was a decrease of \$193,668 in the subsidy received from RepMar from 2010 to 2011 due to the discontinuation of subsidy from RepMar.

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

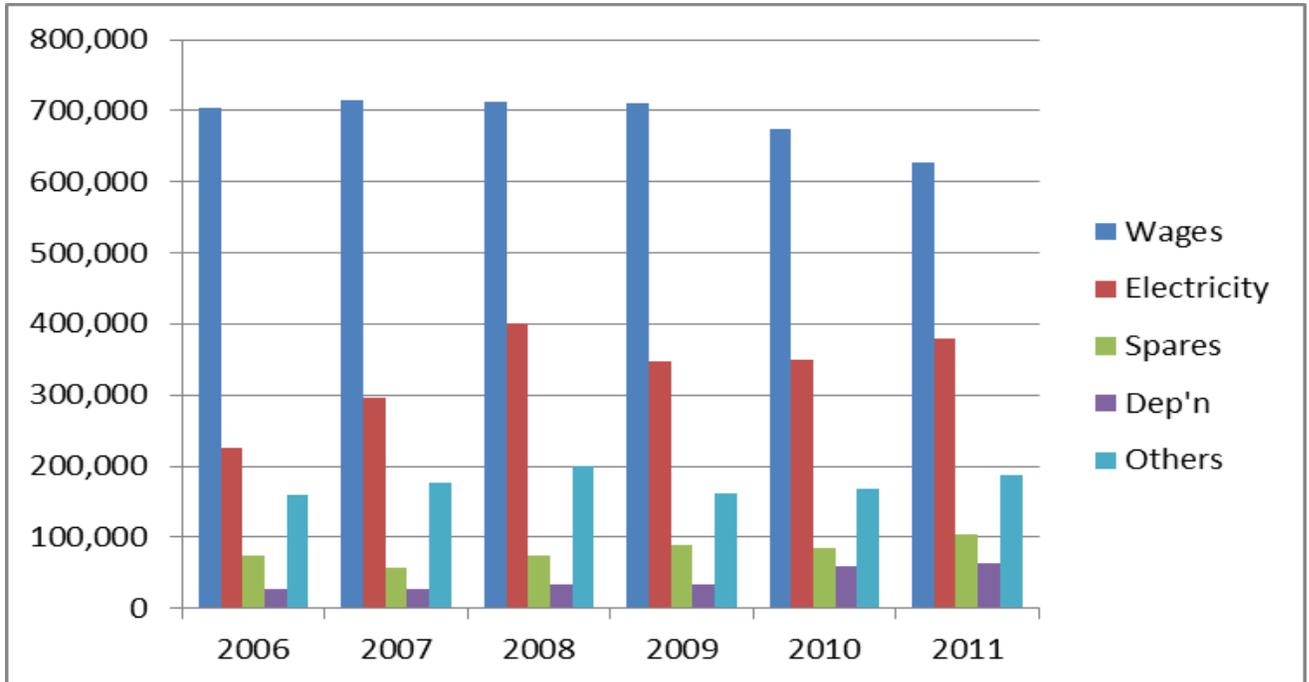
Management’s Discussion and Analysis  
 Years Ended September 30, 2011 and 2010

The graph below shows the major components of operating revenue for 2011 compared with the years 2006 through to 2010:



Operating expenses increased by \$24,083 or approximately 1.8% to \$1,360,572 in 2011 from \$1,336,489 in 2010.

The graph below shows the major components of operating expenses for 2011 compared with the years 2006 through to 2010:



Management’s Discussion and Analysis for the year ended September 30, 2010 is set forth in MWSC’s Report on the audit of financial statements, which is dated February 15, 2011. Such Management Discussion and Analysis explains the major factors impacting the 2010 financial statements and can be obtained from MWSC’s General Manager via the contact information on page 5.

## MAJURO WATER AND SEWER COMPANY, INC.

Management's Discussion and Analysis  
Years Ended September 30, 2011 and 2010

### CAPITAL ASSETS

Net capital assets increased by \$7,077 in 2011 as a result of the acquisition of a four motor vehicles for a total cost of \$52,495 and miscellaneous office, other equipment and building and leasehold improvements costing \$17,226 less total depreciation for the year of \$62,644.

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

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Motor Vehicles	\$ 193,495	\$ 141,000	\$ 141,000
Machinery and equipment	324,179	318,341	93,481
Office Equipment	36,954	33,872	31,923
Building and leasehold Improvement	<u>62,623</u>	<u>54,317</u>	<u>54,317</u>
	617,251	547,530	320,721
Less Accumulated Depreciation	<u>(382,484)</u>	<u>(319,840)</u>	<u>(261,276)</u>
	\$ <u>234,767</u>	\$ <u>227,690</u>	\$ <u>59,445</u>

Refer to note 4 to the accompanying financial statements for additional information relating to capital assets.

### FUTURE OUTLOOK ON SUSTAINABILITY

MWSC water and sewer infrastructure is at a high risk and in a serious state of deteriorating conditions. As infrastructures continue to wear out with time, lack of funding for proper maintenance and other environmental impacts, MWSC capacity decreases and capacity needs are on the rise due to increase customer base. For more sustainability, the following will need to be addressed and incorporated into MWSC's long term strategies and goals:

1. Promote better management of water and wastewater utilities, which encompasses best practices to include asset management. MWSC needs to be able to carry out an ongoing process of oversight, evaluation, maintenance and replacement of their assets, as needed, to maximize the useful life of infrastructure.
2. Achieve full cost recovery, which will help MWSC to capture its actual cost of operating, raise revenues and also to help conserve water. Like many utility companies, MWSC is faced with the challenges of balancing its social responsibility to ensure that water is accessible and affordable to promote quality of life versus generating sufficient income to sustain its core operations. As such, MWSC may not be able to recover its full cost in its entirety and may continue to place reliance and dependency on RepMar to subsidize the deficiency.
3. Efficient water use is a critical factor especially with water shortages that the RMI may experience due to lack of capacity or seasonal droughts. Incentives and education programs will encourage more efficient use of water and to protect the water resources among the RMI community.

### 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, 2011 and 2010

<u>ASSETS</u>	<u>2011</u>	<u>2010</u>
Current assets:		
Cash	\$ 97,637	\$ 44,145
Receivables:		
Utility	1,723,724	1,732,770
Affiliates	198,355	130,744
Other	11,110	2,746
	<u>1,933,189</u>	<u>1,866,260</u>
Less allowance for doubtful accounts	<u>(1,677,978)</u>	<u>(1,664,406)</u>
	<u>255,211</u>	<u>201,854</u>
Inventory	146,694	137,089
Prepaid expenses	<u>38,681</u>	<u>4,493</u>
Total current assets	538,223	387,581
Capital assets, net	<u>234,767</u>	<u>227,690</u>
	<u>\$ 772,990</u>	<u>\$ 615,271</u>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Accounts payable	\$ 52,644	\$ 52,610
Social security taxes payable	29,374	50,061
Withholding taxes payable	14,361	36,264
Payable to affiliates	308,653	47,442
Deferred revenue	-	34,105
Other accrued liabilities	<u>32,244</u>	<u>59,819</u>
Total current liabilities	<u>437,276</u>	<u>280,301</u>
Commitment and contingency		
Net assets:		
Invested in capital assets	234,767	227,690
Unrestricted	<u>100,947</u>	<u>107,280</u>
Total net assets	<u>335,714</u>	<u>334,970</u>
	<u>\$ 772,990</u>	<u>\$ 615,271</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, 2011 and 2010

	2011	2010
Operating revenues:		
Utility billings	\$ 1,069,492	\$ 931,635
Hook-up and deliveries	156,587	167,482
Other	12,680	25,294
	1,238,759	1,124,411
Less uncollectable accounts	(13,572)	(137,818)
Total operating revenues	1,225,187	986,593
Operating expenses:		
Salaries, wages and benefits	627,710	674,897
Electricity	378,819	350,751
Spare parts	104,150	84,243
Depreciation and amortization	62,644	58,564
Petroleum, oil and lubricants	46,686	39,965
Insurance	28,896	34,007
Communications	22,181	21,898
Contractual services	20,205	6,000
Office supplies	18,818	18,897
Repairs and maintenance	9,061	5,832
Travel	4,195	34
Miscellaneous	37,207	41,401
Total operating expenses	1,360,572	1,336,489
Operating loss	(135,385)	(349,896)
Nonoperating revenues (expenses):		
RepMar subsidy	124,431	318,099
Penalties and interest	(2,699)	(7,218)
Total nonoperating revenues (expenses), net	121,732	310,881
Capital contributions	14,397	221,600
Change in net assets	744	182,585
Net assets at beginning of year	334,970	152,385
Net assets at end of year	\$ 335,714	\$ 334,970

See accompanying notes to financial statements.

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

Statements of Cash Flows  
Years Ended September 30, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Cash received from customers	\$ 1,137,725	\$ 932,260
Cash payments to suppliers for goods and services	(333,803)	(213,987)
Cash payments to employees for services	(691,666)	(688,291)
Net cash provided by operating activities	112,256	29,982
Cash flows from noncapital financing activities:		
Principal payments on RepMar promissory note	-	(12,502)
Penalties and interest paid	(3,440)	(10,423)
Net cash used for noncapital financing activities	(3,440)	(22,925)
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(55,324)	(5,209)
Net change in cash	53,492	1,848
Cash at beginning of year	44,145	42,297
Cash at end of year	\$ 97,637	\$ 44,145
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (135,385)	\$ (349,896)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	62,644	58,564
Bad debts	13,572	137,818
(Increase) decrease in assets:		
Receivables:		
Utility	9,046	(183,347)
Affiliates	(67,611)	1,282
Other	(8,364)	(276)
Inventory	(9,605)	10,912
Prepaid expenses	(34,188)	6,124
Increase (decrease) in liabilities:		
Accounts payable	34	11,660
Social security taxes payable	(20,687)	(17,879)
Withholding taxes payable	(21,162)	-
Payable to affiliates	385,642	365,541
Deferred revenue	(34,105)	(9,810)
Other accrued liabilities	(27,575)	(711)
Net cash provided by operating activities	\$ 112,256	\$ 29,982
Summary of noncash financing activities:		
RepMar subsidy and capital contribution	\$ 138,828	\$ 539,699
Decrease in payables to affiliates	(124,431)	(318,099)
Increase in capital assets due to contributed capital assets	(14,397)	(221,600)
	\$ -	\$ -

See accompanying notes to financial statements.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2011 and 2010

## (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 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 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*, establishes 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, 2011 and 2010

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

To conform to the requirements of GASB Statement 34, equity is 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 depositor 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, 2011 and 2010, cash was \$97,637 and \$44,145, respectively, and the corresponding bank balances were \$105,796 and \$38,058, respectively. Of the bank balance amounts, \$93,412 and \$32,233, respectively, were maintained in one financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance and 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.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2011 and 2010

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

### 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 the meters are read. Wastewater treatment is billed at a flat rate of \$12 per month for residential accounts and \$9 per pan for commercial and government accounts. Water delivery sales and hook-up fees are recorded when the services are provided to customers.

### New Accounting Standards

During fiscal year 2011, MWSC implemented the following pronouncements:

- GASB 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.
- GASB Statement No. 59, *Financial Instruments Omnibus*, which updates and improves existing standards regarding financial reporting of certain financial instruments and external investment pools.

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

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2011 and 2010

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

### New Accounting Standards, Continued

In December 2009, GASB issued Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, which amends Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and addresses issues related to measurement of OPEB obligations by certain employers participating in agent multiple-employer OPEB plans. The provisions of Statement 57 related to the use and reporting of the alternative measurement method are effective immediately. The provisions related to the frequency and timing of measurements are effective for actuarial valuations first used to report funded status information in OPEB plan financial statements for periods beginning after June 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In December 2010, GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In December 2010, GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*, which is designed to improve financial reporting for governmental entities by amending the requirements of Statements No. 14, *The Financial Reporting Entity*, and No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, to better meet user needs and address reporting entity issues that have come to light since those Statements were issued in 1991 and 1999, respectively. The provisions of this statement are effective for periods beginning after June 15, 2012. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In December 2010, GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is intended to enhance the usefulness of its Codification by incorporating guidance that previously could only be found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements. The provisions of this statement are effective for periods beginning after December 15, 2011. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In July 2011, GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this statement are effective for periods beginning after December 15, 2011. 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, 2011 and 2010

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

### New Accounting Standards, Continued

In July 2011, GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions* (an amendment of GASB Statement No. 53), which will improve financial reporting by state and local governments by clarifying the circumstances in which hedge accounting continues to be applied when a swap counterparty, or a swap counterparty's credit support provider, is replaced. The provisions of this statement are effective for periods beginning after June 15, 2011. 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 to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. However, as of September 30, 2011, MWSC is self-insured for any losses that could befall its buildings, equipment and inventory. 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, 2011 and 2010, was as follows:

	2011			
	October 1, 2010	Additions	Retirements	September 30, 2011
Vehicles	\$ 141,000	\$ 52,495	\$ -	\$ 193,495
Machinery and equipment	318,341	5,838	-	324,179
Office equipment	33,872	3,082	-	36,954
Buildings and leasehold improvements	<u>54,317</u>	<u>8,306</u>	<u>-</u>	<u>62,623</u>
	547,530	69,721	-	617,251
Less accumulated depreciation and amortization	<u>(319,840)</u>	<u>(62,644)</u>	<u>-</u>	<u>(382,484)</u>
	<u>\$ 227,690</u>	<u>\$ 7,077</u>	<u>\$ -</u>	<u>\$ 234,767</u>
	2010			
	October 1, 2009	Additions	Retirements	September 30, 2010
Vehicles	\$ 141,000	\$ -	\$ -	\$ 141,000
Machinery and equipment	93,481	224,860	-	318,341
Office equipment	31,923	1,949	-	33,872
Buildings and leasehold improvements	<u>54,317</u>	<u>-</u>	<u>-</u>	<u>54,317</u>
	320,721	226,809	-	547,530
Less accumulated depreciation and amortization	<u>(261,276)</u>	<u>(58,564)</u>	<u>-</u>	<u>(319,840)</u>
	<u>\$ 59,445</u>	<u>\$ 168,245</u>	<u>\$ -</u>	<u>\$ 227,690</u>

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
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### (5) Withholding Taxes Payable

At September 30, 2011 and 2010, MWSC was liable for delinquent withholding taxes payable to RepMar in the amount of \$14,361 and \$35,523, respectively, and related penalties and interest in the amount of \$0 and \$741, respectively.

### (6) Related Party Transactions

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

During the years ended September 30, 2011 and 2010, MWSC received an operating subsidy from RepMar in the amount of \$124,431 and \$318,099, respectively, which were paid directly to the Marshalls Energy Company, Inc. as payment on outstanding electricity billings owed by MWSC.

During the years ended September 30, 2011 and 2010, MWSC received capital contributions from RepMar in the amount of \$14,397 and \$221,600, respectively, through a grant received from the Pacific Islands Applied GeoScience Commission.

A summary of related party transactions for the years ended September 30, 2011 and 2010, and related receivable and payable balances as of September 30, 2011 and 2010, is as follows:

	2011			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 367,888	\$ 12,078	\$ 140,283	\$ 14,361
Marshalls Energy Company, Inc.	5,891	408,960	26,303	302,448
Marshall Islands National Telecommunications Authority	6,317	15,278	3,530	365
Marshall Islands Social Security Administration	1,192	55,260	95	29,374
Majuro Resort, Inc.	46,816	-	6,204	-
Other	<u>23,285</u>	<u>19,348</u>	<u>21,940</u>	<u>5,840</u>
	<u>\$ 451,389</u>	<u>\$ 510,924</u>	<u>\$ 198,355</u>	<u>\$ 352,388</u>
	2010			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 153,451	\$ 20,476	\$ 64,761	\$ 36,264
Marshalls Energy Company, Inc.	4,606	367,354	30,134	47,418
Marshall Islands National Telecommunications Authority	3,915	12,255	1,265	-
Marshall Islands Social Security Administration	794	60,091	130	50,061
Majuro Resort, Inc.	38,419	520	13,118	-
Other	<u>20,822</u>	<u>864</u>	<u>21,336</u>	<u>24</u>
	<u>\$ 222,007</u>	<u>\$ 461,560</u>	<u>\$ 130,744</u>	<u>\$ 133,767</u>

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

## MAJURO WATER AND SEWER COMPANY, INC.

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### (7) 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:

<u>Year ending</u> <u>September 30,</u>	
2012	\$ 666,667
2013	100,000
2014	100,000
2015	100,000
2016	<u>33,333</u>
	<u>\$ 1,000,000</u>

During the years ended September 30, 2011 and 2010, 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.

### (8) Going Concern

MWSC has incurred losses from operations of \$135,385 and \$349,896 during the years ended September 30, 2011 and 2010, 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.