

MAJURO WATER AND SEWER COMPANY, INC.

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

**FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT**

YEARS ENDED SEPTEMBER 30, 2015 AND 2014

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Years Ended September 30, 2015 and 2014
Table of Contents

	<u>Page No.</u>
I. INDEPENDENT AUDITORS' REPORT	1
II. MANAGEMENT'S DISCUSSION AND ANALYSIS	3
III. FINANCIAL STATEMENTS:	
Statements of Net Position	7
Statements of Revenues, Expenses and Changes in Net Position	8
Statements of Cash Flows	9
Notes to Financial Statements	10
IV. INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS	
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	18
Schedule of Findings and Responses	20
Unresolved Prior Year Findings	23

INDEPENDENT AUDITORS' REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of Majuro Water and Sewer Company, Inc. (MWSC), a component unit of the Republic of the Marshall Islands, which comprise the statements of net position as of September 30, 2015 and 2014, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Majuro Water and Sewer Company, Inc. as of September 30, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

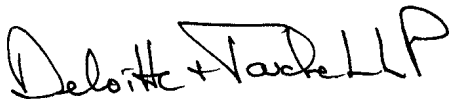
Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 7 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2016, 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* in considering MWSC's internal control over financial reporting and compliance.



November 14, 2016

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Management's Discussion and Analysis
Years Ended September 30, 2015 and 2014

FINANCIAL HIGHLIGHTS

MWSC's net position decreased by \$142,646 in 2015 compared to an increase of \$379,862 in 2014. The significant decrease was mainly due to the decrease in revenue and also a reduction in capital contributions and grants from foreign donors.

Total operating revenues decreased by \$258,505 in 2015 compared to a decrease in revenue of \$191,113 in 2014. Within the operating revenues, utility billings decreased by \$372,935 from \$1,316,865 in 2014 to \$943,930 in 2015. Hook-ups and delivery sales increased by \$111,998 from \$296,748 in 2014 to \$408,746 in 2015. The significant decrease in revenue is due to the faulty meter at Treatment Plant C to Amata Kabua International Airport (Hangar). Furthermore, there has been an additional \$310,560 allowance provided for uncollectable accounts in 2015 compared to \$467,814 in 2014.

Operating expenses decreased by \$21,765 from \$1,639,836 in 2014 to \$1,618,071 in 2015. The main contributing factor for the decrease in operating expenses is a decrease in salaries, wages and benefits of \$36,221, electricity of \$127,098, petroleum, oil and lubricants of \$1,330, insurance of \$320 and travel of \$616, offset by an increase in depreciation and amortization of \$48,629, spare parts of \$42,490, contractual services of \$25,741, office supplies of \$2,585, communications of \$642, repair and maintenance of \$6,303 and miscellaneous of \$17,431.

The Statement of Cash Flows net increase in cash was \$105,681 in 2015 compared with net decrease of \$20,801 in 2014. The operating activities of MWSC generated a net cash outflow of \$19,535 in 2015 compared to a net cash outflow of \$48,306 for 2014. The decrease in net cash flows was offset to a degree by net cash provided by capital and related financing activities which increased in 2015.

FINANCIAL ANALYSIS OF MWSC

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

A Summary of MWSC's Statements of Net Position is presented below:

	<u>2015</u>	<u>2014</u>	<u>2013</u>
Current assets	\$ 939,114	\$ 878,508	\$ 801,104
Capital and other assets	<u>1,209,568</u>	<u>1,167,321</u>	<u>462,912</u>
Total assets	<u>2,148,682</u>	<u>2,045,829</u>	<u>1,264,016</u>
Current liabilities	<u>1,978,799</u>	<u>1,733,300</u>	<u>1,331,349</u>
Net position:			
Net investment in capital assets	1,209,568	1,167,321	354,107
Restricted	310,222	177,554	226,840
Unrestricted	<u>(1,349,907)</u>	<u>(1,032,346)</u>	<u>(648,280)</u>
Total net position	\$ <u>169,883</u>	\$ <u>312,529</u>	\$ <u>(67,333)</u>

MAJURO WATER AND SEWER COMPANY, INC.

Management's Discussion and Analysis
Years Ended September 30, 2015 and 2014

As indicated above, total assets increased by \$102,853 from \$2,045,829 in 2014 to \$2,148,682 in 2015.

Total liabilities reflects an increase of \$245,499 from \$1,733,300 in 2014 to \$1,978,799 in 2015. The net position decreased by \$142,646 from \$312,529 in 2014 to \$169,883 in 2015. There were no non-current liabilities at 30th September 2015 or 2014.

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

	<u>2015</u>	<u>2014</u>	<u>2013</u>
Revenues:			
Operating revenues	\$ 1,056,495	\$ 1,157,746	\$ 1,348,859
Expenses:			
Operating Expenses	1,618,071	1,639,836	1,860,629
Non-operating expenses	<u>1,487</u>	<u>616</u>	<u>2,426</u>
Total expenses	<u>1,619,558</u>	<u>1,640,452</u>	<u>1,863,056</u>
Capital contributions	<u>420,417</u>	<u>862,568</u>	<u>150,000</u>
Change in net position	\$ <u>(142,646)</u>	\$ <u>379,862</u>	\$ <u>(364,196)</u>

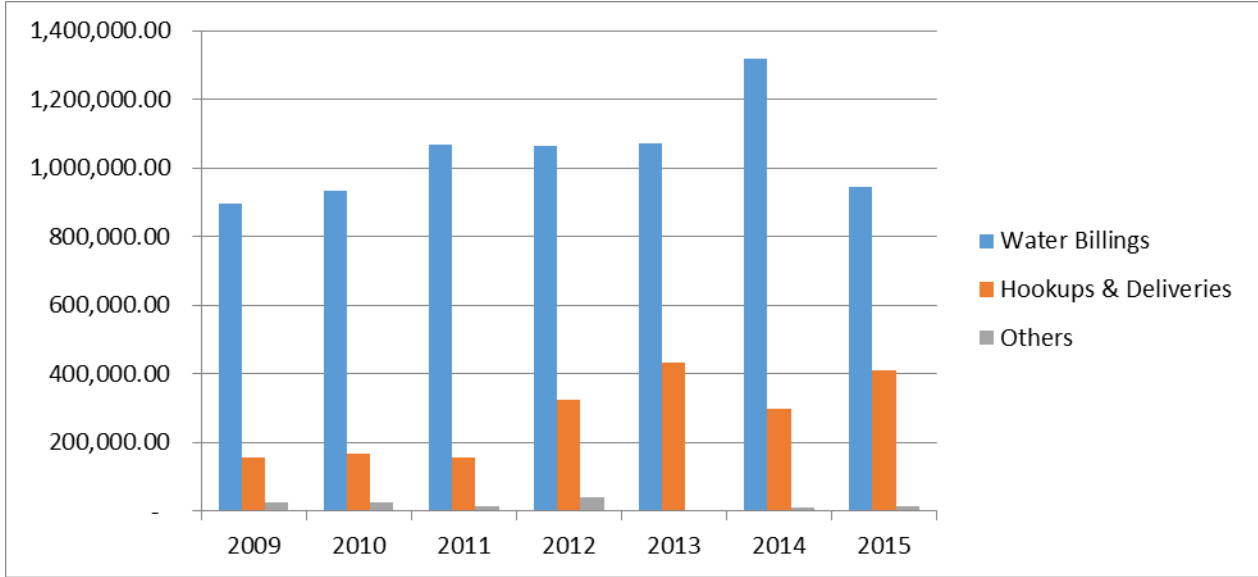
The Statement of Revenue, Expenses and Changes in Net Position identifies that various revenue and expense items that impacted the change in net position. As indicated above, MWSC's operating revenue decreased by \$101,251 from \$1,157,746 in 2014 to \$1,056,495 in 2015. The decrease in revenue for 2015 consists of a reduction in utility billings of \$372,935 offset by an increase in hook-up and delivery sales of \$111,998 and a decrease in bad debts expense of \$157,254.

Non-operating revenues represent operating subsidies and grants received. RepMar discontinued financial support to assist MWSC with the payment of the monthly electricity bills owed to MEC. The subsidy of \$300,000 received from RepMar in 2015 was for Capital Improvement Projects to acquire spare parts. The grant received from the Asian Development Bank (ADB) in 2015 of \$120,417 was to procure safety gears and equipments.

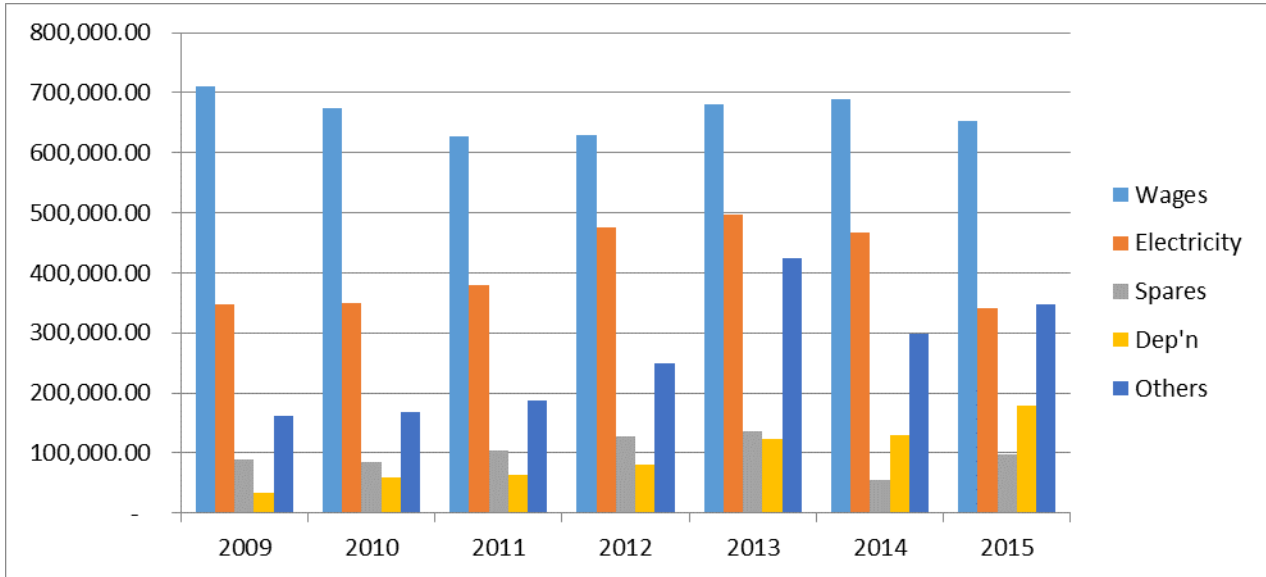
MAJURO WATER AND SEWER COMPANY, INC.

Management's Discussion and Analysis
 Years Ended September 30, 2015 and 2014

The graph below shows the major components of operating revenues for 2015 compared with the years 2009 through 2014.



Operating expenses decreased by \$21,764 to \$1,618,071 in 2015 from \$1,639,836 in 2014. The graph below shows the major components of operating expenses for 2015 compared with the years 2009 through 2014.



Management's Discussion and Analysis for the year ended September 30, 2014 is set forth in MWSC's report on the audit of financial statements, which is dated July 7, 2015. Such Management's Discussion and an Analysis explains the major factors impacting the 2014 financial statements and can be obtained from MWSC's General Manager via the contact information on page 6.

MAJURO WATER AND SEWER COMPANY, INC.

Management's Discussion and Analysis
Years Ended September 30, 2015 and 2014

CAPITAL ASSETS

Net capital assets increased by \$42,247 in 2015 as a result of the acquisition of a vehicle for a total cost of \$16,000, machinery and equipment of \$52,340, office equipment of \$31,112 and buildings and leasehold improvements of \$121,462 less total depreciation expense for the year of \$178,667.

MWSC received capital contributions of \$420,417 in 2015. The contribution of \$300,000 from RepMar was to acquire spare parts and \$120,471 from The Asian Development Bank (ADB) was to procure Safety Gears and equipments. Please refer to note 4 to the financial statements for additional information on MWSC's capital assets.

FUTURE OUTLOOK ON SUSTAINABILITY

Future sustainability for MWSC will require four major changes:

1. Increase in our customer base. Currently, we have some 831 water customers and 2,383 sewer customers out of a possible 3,214. Increasing our customer base without major expansions to our capital assets will mean a significant increase in revenue without proportional increase in operating costs. Encouraging new customers will require a concerted long term community awareness and educational program to have them understand the value and benefits to connecting to our water and sewer system.
2. Renovate and repair our water, sewer and saltwater assets to improve reliability, and consequently, service to our customers. Without these improvements to standby, reliability of operations and monitoring to understand our business performance better the risks of failure of service are too high.
3. Tariff reform to recognize the cost of operating the business and to recognize inflation since the last tariff adjustment some 11 years ago.
4. Initiate survey of all service provided.

MWSC'S FOCUS IN THE COMING YEAR

MWSC's focus in the coming year will be four fold:

1. Develop a long term (20 years) strategic plan for the business, along with a 5 year development plan in compliance with the commitments of the National Strategic Plan.
2. Obtain funding to initiate replacement of the existing sewage ocean outfall.
3. Establish the most appropriate arrangements to ensure water security for Majuro and initiate plans for the required facilities to source funding for the works.
4. Renovate and repair existing water, sewer and saltwater assets, providing funding is made available.

ADDITIONAL FINANCE INFORMATION

The discussion and analysis is designed to provide 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. Manager at P.O. Box 1751 Majuro, MH 96960.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Statements of Net Position
September 30, 2015 and 2014

<u>ASSETS</u>	<u>2015</u>	<u>2014</u>
Current assets:		
Cash	\$ 255,113	\$ 149,432
Receivables:		
Utility	1,764,872	1,429,103
Affiliates	202,947	550,726
Grants	72,800	-
Other	26,913	47,218
	<u>2,067,532</u>	<u>2,027,047</u>
Less allowance for doubtful accounts	<u>(1,705,988)</u>	<u>(1,571,545)</u>
	<u>361,544</u>	<u>455,502</u>
Inventory	244,464	246,701
Prepaid expenses	<u>77,993</u>	<u>26,873</u>
Total current assets	939,114	878,508
Capital assets, net	<u>1,209,568</u>	<u>1,167,321</u>
	<u>\$ 2,148,682</u>	<u>\$ 2,045,829</u>
<u>LIABILITIES AND NET POSITION</u>		
Current liabilities:		
Accounts payable	\$ 84,559	\$ 128,019
Payable to affiliates	1,839,854	1,523,427
Other accrued liabilities	<u>54,386</u>	<u>81,854</u>
Total current liabilities	<u>1,978,799</u>	<u>1,733,300</u>
Commitment and contingency		
Net position:		
Net investment in capital assets	1,209,568	1,167,321
Restricted	310,222	177,554
Unrestricted	<u>(1,349,907)</u>	<u>(1,032,346)</u>
Total net position	<u>169,883</u>	<u>312,529</u>
	<u>\$ 2,148,682</u>	<u>\$ 2,045,829</u>

See accompanying notes to financial statements.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2015 and 2014

	2015	2014
Operating revenues:		
Utility billings	\$ 943,930	\$ 1,316,865
Hook-up and deliveries	408,746	296,748
Other	14,379	11,947
Total operating revenues	1,367,055	1,625,560
Less uncollectable accounts	(310,560)	(467,814)
Total net operating revenues	1,056,495	1,157,746
Operating expenses:		
Salaries, wages and benefits	652,266	688,487
Electricity	340,776	467,874
Depreciation and amortization	178,667	130,038
Spare parts	97,741	55,251
Contractual services	55,006	29,265
Petroleum, oil and lubricants	50,430	51,760
Insurance	40,941	41,261
Travel	40,214	40,830
Office supplies	29,082	26,497
Communications	23,108	22,466
Repairs and maintenance	20,504	14,201
Miscellaneous	89,336	71,906
Total operating expenses	1,618,071	1,639,836
Operating loss	(561,576)	(482,090)
Nonoperating expenses:		
Penalties and interest	(1,487)	(616)
Capital contributions:		
Republic of the Marshall Islands	300,000	300,000
Other grants and contributions	120,417	562,568
Total capital contributions	420,417	862,568
Change in net position	(142,646)	379,862
Net position at beginning of year	312,529	(67,333)
Net position at end of year	\$ 169,883	\$ 312,529

See accompanying notes to financial statements.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Statements of Cash Flows
Years Ended September 30, 2015 and 2014

	2015	2014
Cash flows from operating activities:		
Cash received from customers	\$ 1,223,254	\$ 1,100,583
Cash payments to suppliers for goods and services	(522,248)	(458,128)
Cash payments to employees for services	(720,541)	(690,761)
Net cash used for operating activities	(19,535)	(48,306)
Cash flows from noncapital financing activities:		
Penalties and interest paid	(1,487)	(616)
Cash flows from capital and related financing activities:		
Capital contributions received	347,617	862,568
Acquisition of capital assets	(220,914)	(834,447)
Net cash provided by capital and related financing activities	126,703	28,121
Net change in cash	105,681	(20,801)
Cash at beginning of year	149,432	170,233
Cash at end of year	\$ 255,113	\$ 149,432
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (561,576)	\$ (482,090)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation and amortization	178,667	130,038
Uncollectable accounts	310,560	467,814
(Increase) decrease in assets:		
Receivables:		
Utility	(511,886)	(244,797)
Affiliates	347,779	(261,450)
Other	20,305	(18,730)
Inventory	2,237	(32,042)
Prepaid expenses	(51,120)	(9,000)
Increase (decrease) in liabilities:		
Accounts payable	(40,468)	68,957
Payable to affiliates	354,242	335,268
Other accrued liabilities	(68,275)	(2,274)
Net cash used for operating activities	\$ (19,535)	\$ (48,306)
Summary disclosure of noncash activity:		
Capital assets	\$ -	\$ (108,805)
Prepaid expenses	-	108,805
	\$ -	\$ -

See accompanying notes to financial statements.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(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

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.

To conform to the requirements of GASB Statement 34, equity is presented in the following net position categories:

- Net investment in capital assets; capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- Restricted net position - resources in which MWSC is legally or contractually obligated to spend resources in accordance with restrictions either externally imposed by creditors, grantors, contributors, and the like, or imposed by law.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

- Unrestricted; net position that is not subject to externally imposed stipulations. Unrestricted net position 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, deferred outflows of resources, liabilities, and deferred inflows of resources 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, deferred outflows of resources, liabilities, and deferred inflows of resources associated with the operation of the fund are included in the statements of net position. Proprietary fund operating statements present increases and decreases in net position. 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.

Operating and Non-Operating Revenue and Expenses

Operating revenues and expenses generally result directly from the operation and maintenance of MWSC. Non-operating revenues and expenses result from capital and related financing activities as well as certain other non-recurring income and expense items. Other capital grants and contributions for the years ended September 30, 2015 and 2014, consist of the following:

	<u>2015</u>	<u>2014</u>
South Pacific Regional Environment Programme	\$ -	\$ 562,568
U.S. Department of the Interior	72,800	-
Asian Development Bank	40,407	-
Australian Embassy	<u>7,210</u>	<u>-</u>
	<u>\$ 120,417</u>	<u>\$ 562,568</u>

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.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

Cash, Continued

For purposes of the statements of net position and cash flows, cash is defined as cash on hand and cash held in demand accounts. As of September 30, 2015 and 2014, cash was \$255,113 and \$149,432, respectively, and the corresponding bank balances were \$276,891 and \$179,149, respectively, of which \$256,882 and \$161,657, respectively, were maintained in a financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2015 and 2014, bank deposits in the amount of \$250,000 and \$161,657, respectively, were FDIC insured. MWSC does not require collateralization of its cash deposits; therefore, deposit levels in excess of FDIC coverage are uncollateralized. Accordingly, these deposits were exposed to custodial credit risk.

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 and accounts that are ultimately written-off are charged against the allowance.

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 two 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

Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (deduction of net position) until then. MWSC has no items that qualify for reporting in this category.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

Deferred Inflows of Resources

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (additions to net position) until then. MWSC has no items that qualify for reporting in this category.

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 2015, MWSC implemented the following pronouncements:

- GASB *Statement No. 68, Accounting and Financial Reporting for Pensions*, which revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. The implementation of this statement did not have a material effect on the accompanying financial statements.
- GASB *Statement No. 69, Government Combinations and Disposals of Government Operations*, which improves accounting and financial reporting for state and local governments' combinations and disposals of government operations. Government combinations include mergers, acquisitions, and transfers of operations. A disposal of government operations can occur through a transfer to another government or a sale. The implementation of this statement did not have a material effect on the accompanying financial statements.
- GASB *Statement No. 71, Pension Transition for Contributions Made Subsequent to the Measurement Date - an amendment of GASB Statement No. 68*, which addresses an issue regarding application of the transition provisions of *Statement No. 68, Accounting and Financial Reporting for Pensions*. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or nonemployer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability. The implementation of this statement did not have a material effect on the accompanying financial statements.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In February 2015, GASB issued Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and financial reporting issues related to fair value measurements and requires entities to expand their fair value disclosures by determining major categories of debt and equity securities within the fair value hierarchy on the basis of the nature and risk of the investment. The provisions in Statement 72 are effective for fiscal years beginning after June 15, 2015. Management believes that the implementation of this statement only requires additional disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques and will not have a material effect on the financial statements of MWSC.

In June 2015, GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements 67 and 68 with the reporting requirements in Statement 68. The provisions in Statement No. 73 are effective for fiscal years beginning after June 15, 2015, with the exception of the provisions that address employers and governmental nonemployer contributing entities for pensions that are not within the scope of Statement 68, which are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and addresses financial reporting requirements for governments whose employees are provided with postemployment benefits other than pensions (other postemployment benefits or OPEB). The provisions in Statement No. 74 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017. 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.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In June 2015, GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which eliminates two of the four categories of authoritative GAAP that exist under the existing hierarchy prescribed by Statement 55. The two categories that will remain under the new standard are (1) GASB Statements and (2) GASB technical bulletins and implementation guides in addition to AICPA guidance that the GASB clears. The provisions in Statement No. 76 are effective for fiscal years beginning after June 15, 2015. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In August 2015, GASB issued Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements. The provisions in Statement No. 77 are effective for fiscal years beginning after December 15, 2015. 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, 2015 and 2014, respectively, 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, 2015 and 2014 was as follows:

	2015			
	<u>October 1,</u> <u>2014</u>	<u>Additions</u>	<u>Retirements</u>	<u>September 30,</u> <u>2015</u>
Vehicles	\$ 188,945	\$ 16,000	\$ -	\$ 204,945
Machinery and equipment	579,260	52,340	(21,721)	609,879
Office equipment	172,534	31,112	-	203,646
Buildings and leasehold improvements	<u>831,039</u>	<u>121,462</u>	<u>-</u>	<u>952,501</u>
	1,771,778	220,914	(21,721)	1,970,971
Less accumulated depreciation and amortization	<u>(604,457)</u>	<u>(178,667)</u>	<u>21,721</u>	<u>(761,403)</u>
	<u>\$ 1,167,321</u>	<u>\$ 42,247</u>	<u>\$ -</u>	<u>\$ 1,209,568</u>

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(4) Capital Assets, Continued

	2014			
	October 1, <u>2013</u>	<u>Additions</u>	<u>Retirements</u>	September 30, <u>2014</u>
Vehicles	\$ 164,545	\$ 24,400	\$ -	\$ 188,945
Machinery and equipment	410,158	169,102	-	579,260
Office equipment	157,836	14,698	-	172,534
Buildings and leasehold improvements	<u>95,987</u>	<u>735,052</u>	<u>-</u>	<u>831,039</u>
	828,526	943,252	-	1,771,778
Less accumulated depreciation and amortization	<u>(474,419)</u>	<u>(130,038)</u>	<u>-</u>	<u>(604,457)</u>
	<u>\$ 354,107</u>	<u>\$ 813,214</u>	<u>\$ -</u>	<u>\$ 1,167,321</u>

(5) Restricted Net Position

Restricted net position at September 30, 2015 and 2014, consists of the following:

	<u>2015</u>	<u>2014</u>
RepMar capital grants	\$ <u>310,222</u>	\$ <u>177,554</u>

(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.

MWSC received capital contributions from RepMar of \$300,000 for each of the years ended September 30, 2015 and 2014, of which \$240,132 and \$122,446, respectively, were spent to acquire equipment and for reconstruction of the Reservoir.

A summary of related party transactions for the years ended September 30, 2015 and 2014, and related receivable and payable balances as of September 30, 2015 and 2014, is as follows:

	2015			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 205,451	\$ 25,769	\$ 143,495	\$ -
Marshalls Energy Company, Inc.	28,036	340,776	50,592	1,831,532
Marshall Islands National Telecommunications Authority	2,220	17,996	1,332	-
Marshall Islands Social Security Administration	674	137,755	543	-
Majuro Resort, Inc.	53,664	444	4,530	1,172
Other	<u>31,904</u>	<u>345</u>	<u>2,452</u>	<u>7,150</u>
	<u>\$ 321,949</u>	<u>\$ 523,085</u>	<u>\$ 202,947</u>	<u>\$ 1,839,854</u>

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Notes to Financial Statements
September 30, 2015 and 2014

(6) Related Party Transactions, Continued

	2014			
	Revenues	Expenses	Receivables	Payables
RepMar	\$ 209,610	\$ 30,628	\$ 310,423	\$ 27,972
Marshalls Energy Company, Inc.	6,326	467,874	25,033	1,482,240
Marshall Islands National Telecommunications Authority	1,918	20,862	1,611	2,623
Marshall Islands Social Security Administration	220	72,923	581	10,592
Majuro Resort, Inc.	30,940	7,666	7,842	-
Other	<u>131,572</u>	<u>-</u>	<u>205,236</u>	<u>-</u>
	<u>\$ 380,586</u>	<u>\$ 599,593</u>	<u>\$ 550,726</u>	<u>\$ 1,523,427</u>

Receivables from and payables to affiliates are uncollateralized, are interest free and have no set repayment terms.

(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).

MWSC is currently delinquent on \$1,000,000 of payments for the franchise agreement dating back to 2003. The delinquent amount is based on a rate of \$100,000 per annum for 10 years.

During the years ended September 30, 2015 and 2014, 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 \$561,576 and \$482,090 during the years ended September 30, 2015 and 2014, 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. a related party, for electricity usage.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

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

We have audited, 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, the financial statements of Majuro Water and Sewer Company, Inc. (MWSC), which comprise the statement of net position as of September 30, 2015, and the related statements of revenues, expenses, and changes in net position and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 14, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered MWSC's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of MWSC's internal control. Accordingly, we do not express an opinion on the effectiveness of MWSC's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as item 2015-001, which we consider to be material weaknesses.

Compliance and Other Matters

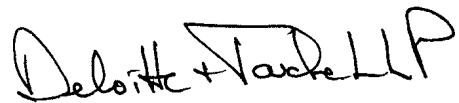
As part of obtaining reasonable assurance about whether MWSC's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as item 2015-002.

MWSC's Responses to Findings

MWSC's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. MWSC's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Deloitte + Tatchell LLP". The signature is written in a cursive, stylized font.

November 14, 2016

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Schedule of Findings and Responses
Year Ended September 30, 2015

Finding No. 2015-001

GL Account Reconciliations

Criteria: Adequate internal control policies should be adopted and established to facilitate reliable and relevant accounting records.

Condition: A Journal Voucher (JV # 150818160339 dated 07/31/15) in the amount of \$244,622 was recorded to adjust a customer account billing due to incorrect meter reading, which included correction of prior year billing, and which resulted in an unusual revenue balance. Such was corrected through a proposed audit adjustment.

Cause: The cause of the above condition is inadequate internal control policies and procedures that facilitate monitoring and review of customer billings.

Effect: The effect of the above condition is exposure to possible misstatements.

Prior Year Status: The lack of adequate internal control policies and procedures over general ledger account reconciliations was reported as a finding in the audits of MWSC for fiscal years 2013 and 2014.

Recommendation: We recommend that management adopt internal control policies and procedures requiring adequate documentation and which provides for the completeness of accounting records.

Auditee Response and Corrective Action Plan:

MWSC is in agreement with Finding No. 2015-01 and recommendation. MWSC has installed a new meter the Treatment Plant C to replace the old meter. MWSC management to implement an internal Control policy and procedure to ensure readings are verify by the Accounting Clerk or the Finance Manager.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Schedule of Findings and Responses, Continued
Year Ended September 30, 2015

Finding No. 2015-002

Local Noncompliance

RepMar's Procurement Code states the following:

- (a) Section 124 - unless otherwise authorized by law, all Government contracts shall be awarded by competitive sealed bidding.
- (b) Section 127 - procurement of goods and services not exceeding \$25,000 may be made in accordance with small purchase procedures promulgated by RepMar's Policy Office. Small purchase procedures are those relatively simple and informal methods for securing services, supplies, or other property that do not cost more than \$25,000. RepMar's Ministry of Finance has previously declared that if small purchase procedures are used, price or rate quotations shall be obtained from three qualified sources.
- (c) Section 128 - a contract may be awarded for a supply, service, or construction item without competition when it is determined in writing that there is only one source for the required supply, service, or construction item.

Condition:

- A. A disbursement of \$6,000 (Check no. 18414) did not include price quotations from three vendors to indicate that full and open competition occurred.
- B. Purchase order no. 1899 dated 09/30/15 in the amount of \$4,250 did not include price quotations from three vendors to indicate that full and open competition occurred.

Cause: The cause of the above condition is the lack of adequate internal control policies and procedures requiring documentation of procurement procedures to satisfy compliance with RepMar's Procurement Code.

Effect: The effect of the above condition is noncompliance with RepMar's Procurement Code.

Recommendation: We recommend that management establish adequate internal control policies and procedures requiring compliance with RepMar's Procurement Code.

MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)

Schedule of Findings and Responses, Continued
Year Ended September 30, 2015

Finding No. 2015-002, Continued

Local Noncompliance, Continued

Auditee Response and Corrective Action Plan:

Condition

- A. MWSC sole sourced this equipment as it is provided by the same company that provided our billing system. The check was for handhelds used by our meter readers to input meter readings and to upload the readings to our billing system. To ensure that the two components are compatible with each other, MWSC procured the handhelds from the same software company that developed our billing system. The billing software was also a finding a few years back, but due to the fact that the RMI Combined Utilities wanted a uniformed billing and accounting software we had no choice but to follow suit.

- B. The expense in question is a service charge for rewinding two of our motors. MWSC has procured 2x 30 HP motors from Dateline for our Uliga Salt Water Pump Stations. Dateline won this bid with H & D Products the other vendor that bidder but didn't complete the RFQ list. The two motors were ordered, but an oversight was made by MWSC's Operation Manager Halston deBrum in the order. Dateline submitted its submittals that detailed out the specification for the motors and other items on the list. In the submittals the motors were classed 208 volts, 3 phase & 60 hertz. After a closer look into the specifications the electrical characteristic were incorrect, the correct characteristic were: 460 volts, 3 phase & 60 hertz. The voltage were wrong, but the order has been put in. As these motors are not on the shelf equipment, they were built for order, we had no choice but to rewind them to fit the correct voltage of 460. If they were not rewind the motors would've been useless for MWSC. As Dateline were the company that provided the motors, upon winning the bid, they were the right people to do the job.

**MAJURO WATER AND SEWER COMPANY, INC.
(A COMPONENT UNIT OF THE REPUBLIC OF THE MARSHALL ISLANDS)**

Unresolved Prior Year Findings
Year Ended September 30, 2015

The status of unresolved prior year findings is disclosed within the Schedule of Findings and Responses section of this report.