

**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, 2007 AND 2006**

## INDEPENDENT AUDITORS' REPORT

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

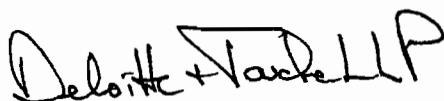
We have audited the accompanying statements of net assets of Majuro Water and Sewer Company, Inc. (MWSC), a component unit of the Republic of the Marshall Islands, as of September 30, 2007 and 2006, and the related statements of revenues, expenses and changes in net deficiency and of cash flows for the 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, 2007 and 2006, and the changes in its net deficiency 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 May 16, 2008, on our consideration of MWSC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.



May 16, 2008

## MAJURO WATER AND SEWER COMPANY, INC.

### Management's Discussion and Analysis Year Ended September 30, 2007

This section of the Majuro Water and Sewer Company, Inc. (MWSC) annual financial report presents management's discussion and analysis of MWSC's financial performance during the fiscal year ended 30<sup>th</sup> September, 2007. It is to be read in conjunction with the financial statements, which follow this section.

#### FINANCIAL HIGHLIGHTS

MWSC's net assets increased by \$87,018 in 2007 compared to a decrease of \$163,430 in 2006. Total revenue decreased by \$59,188 or 6% from \$1,069,323 in 2006 to \$1,010,135 in 2007. Within operating revenues, billings decreased from \$837,485 in 2006 to \$805,190 in 2007. Operating expenses increased slightly from \$1,191,047 in 2006 to \$1,272,521 in 2007. Most of the increase was due to the increase in electricity charges of \$69,790. Operating subsidies of \$349,404 were received from the Republic of the Marshall Islands (RepMar) for fiscal year ended September 2007, of which \$250,000 was used to pay part of the long standing debt owed to Marshalls Energy Company, Inc. for past due electricity bills. The Statement of Cash Flows reveals the operations of MWSC has generated net cash inflow of \$11,634 for 2007 compared to a net cash inflow of \$200,882 in 2006.

#### FINANCIAL ANALYSIS

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

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

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Current assets	\$ 258,927	\$ 228,294	\$ 228,621
Capital assets, net	<u>31,324</u>	<u>53,436</u>	<u>75,875</u>
Total assets	<u>290,251</u>	<u>281,730</u>	<u>304,496</u>
Current liabilities	<u>991,959</u>	<u>1,070,456</u>	<u>929,792</u>
Total liabilities	<u>991,959</u>	<u>1,070,456</u>	<u>929,792</u>
Net assets:			
Invested in capital assets	31,324	53,436	75,875
Unrestricted	<u>(733,032)</u>	<u>(842,162)</u>	<u>(701,171)</u>
Total net assets	<u>\$ (701,708)</u>	<u>\$ (788,726)</u>	<u>\$ (625,296)</u>

As indicated above, total assets increased by \$8,521 or 3% from \$281,730 in 2006 to \$290,251 in 2007. Total liabilities reflect a decrease of \$78,497 or 7% from \$1,070,456 in 2006 to \$991,959 in 2007. This is represented by a decrease in amounts owing to Social Security and RMI for withholding tax of \$127,113 or 49% to \$132,552 in 2007 compared to \$259,665 in 2006. The Social Security debt has since been fully paid off. There were no non-current liabilities at 30<sup>th</sup> September 2007.

## MAJURO WATER AND SEWER COMPANY, INC.

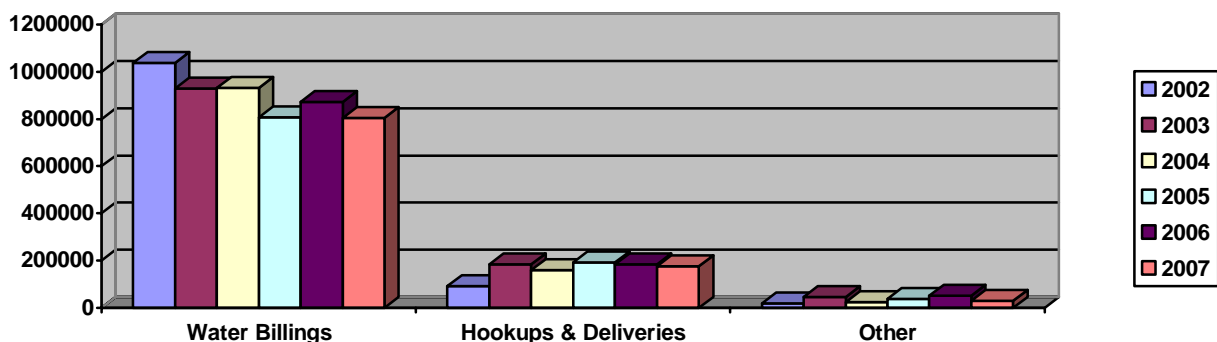
### Management's Discussion and Analysis, Continued Year Ended September 30, 2007

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

	<u>2007</u>	<u>2006</u>	<u>2005</u>
<b>Revenues:</b>			
Operating revenues	\$ 1,010,135	\$ 1,069,323	\$ 1,071,747
Non-operating revenues	<u>349,404</u>	<u>-</u>	<u>37,332</u>
<b>Total revenues</b>	<u>1,359,539</u>	<u>1,069,323</u>	<u>1,109,079</u>
<b>Expenses:</b>			
Operating expenses	1,272,521	1,191,047	1,283,449
Non-operating expenses	<u>-</u>	<u>41,706</u>	<u>-</u>
<b>Total expenses</b>	<u>1,272,521</u>	<u>1,232,753</u>	<u>1,283,449</u>
<b>Change in net assets</b>	<u>\$ 87,018</u>	<u>\$ (163,430)</u>	<u>\$ (174,370)</u>

The Statement of Revenue, Expenses and Changes in Net Assets identifies the various revenue and expense items that impacted on the change in net assets. As indicated above, MWSC's total revenues decreased by \$59,188 or 6% from \$1,069,323 in 2006 to \$1,010,135 in 2007. Utility billings decreased by \$29,918 or 4% from \$837,485 in 2006 to \$805,190 in 2007. No subsidy was received from RepMar in either 2005 or 2006. The subsidy received in 2007 was in two parts. There was a subsidy of \$250,000 received which was used to pay a portion of the long standing debt to Marshalls Energy Company, Inc., for past due electricity accounts. The remainder, \$99,404 was utilized as an operating subsidy.

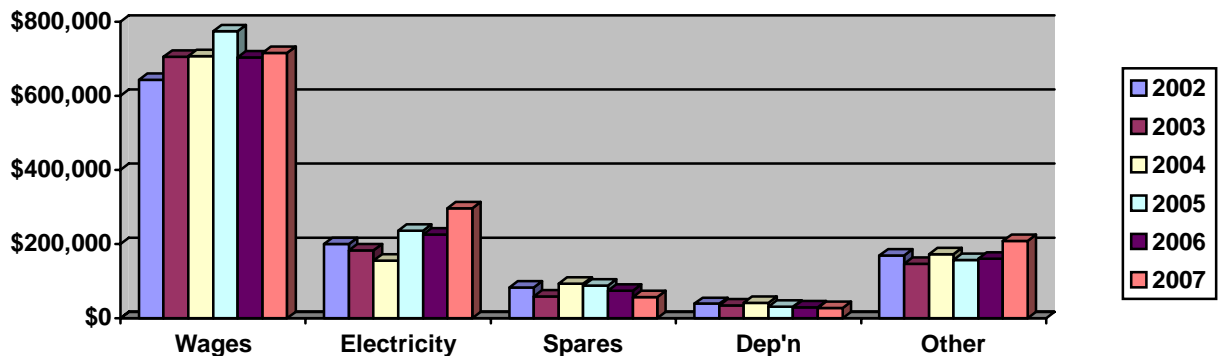
The graph below shows the major components of operating revenues for 2007 compared with the years 2002 through to 2006:



Operating expenses increased marginally by \$81,474 or 7% from \$1,191,047 in 2006 to \$1,272,521 in 2007. The operating loss increased from \$121,724 in 2006 to \$262,386 in 2007. This was largely due to the increase in electricity bills amounting to \$69,790. The graph below shows the major components of operating expenses for 2007 compared with the years 2002 through to 2006:

## MAJURO WATER AND SEWER COMPANY, INC.

### Management's Discussion and Analysis, Continued Year Ended September 30, 2007



Management's Discussion and Analysis for the year ended September 30, 2006 is set forth in the report on the audit of MWSC's financial statements, which is dated May 17, 2007. That Discussion and Analysis explains the major factors impacting the 2006 financial statements.

### CAPITAL ASSETS

Net capital assets decreased by \$22,112 in 2007 as a result of the acquisition of miscellaneous office and other equipment of \$4,935 less total depreciation for the year of \$27,047, and the retirement of old machinery and computer equipment with a total cost of \$6,201 and related accumulated depreciation of \$6,201. A summary of MWSC's capital assets is presented below:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Motor Vehicles	\$ 130,985	\$ 130,185	\$ 168,654
Machinery and Equipment	101,632	103,115	119,077
Office Equipment	42,290	42,873	55,974
Buildings and Leasehold Improvements	<u>54,317</u>	<u>54,317</u>	<u>54,317</u>
	329,224	330,490	398,022
Less Accumulated Depreciation	<u>(297,900)</u>	<u>(277,054)</u>	<u>(322,147)</u>
	<u>\$ 31,324</u>	<u>\$ 53,436</u>	<u>\$ 75,875</u>

For additional information concerning MWSC's capital assets, please refer to Note 4 to the financial statements.

### ECONOMIC FACTORS

MWSC will continue to monitor operating expenses and maintain tight fiscal constraints and control over cash and will continue to endeavor to improve collections. The ongoing viability of MWSC as a going concern will continue to be dependent upon future financial support of RepMar in the form of:

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

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

Management's Discussion and Analysis, Continued  
Year Ended September 30, 2007

**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, 2007 and 2006

<u>ASSETS</u>	<u>2007</u>	<u>2006</u>
Current assets:		
Cash	\$ 24,999	\$ 56,011
Receivables:		
Utility	1,335,450	1,366,190
Affiliates	68,612	97,300
Other	4,447	17,148
	<u>1,408,509</u>	<u>1,480,638</u>
Less allowance for doubtful accounts	<u>(1,305,018)</u>	<u>(1,427,163)</u>
	<u>103,491</u>	<u>53,475</u>
Inventory	122,204	118,808
Prepaid expenses	8,233	-
Total current assets	<u>258,927</u>	<u>228,294</u>
Capital assets, net	<u>31,324</u>	<u>53,436</u>
	<u>\$ 290,251</u>	<u>\$ 281,730</u>
<u>LIABILITIES AND NET ASSETS (DEFICIENCY)</u>		
Current liabilities:		
Accounts payable	\$ 22,615	\$ 11,430
Social security taxes payable	47,592	97,429
Withholding taxes payable	84,960	162,236
Payable to affiliates	777,334	775,220
Other accrued liabilities	59,458	24,141
Total current liabilities	<u>991,959</u>	<u>1,070,456</u>
Commitment and contingency		
Net assets (deficiency):		
Invested in capital assets	31,324	53,436
Unrestricted	<u>(733,032)</u>	<u>(842,162)</u>
Total net deficiency	<u>(701,708)</u>	<u>(788,726)</u>
	<u>\$ 290,251</u>	<u>\$ 281,730</u>

See accompanying notes to financial statements.

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

Statements of Revenues, Expenses and Changes in Net Deficiency  
Years Ended September 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Operating revenues:		
Utility billings	\$ 805,190	\$ 837,485
Hook-up and deliveries	175,820	182,313
Other	<u>29,125</u>	<u>49,525</u>
Total operating revenues	<u>1,010,135</u>	<u>1,069,323</u>
Operating expenses:		
Salaries, wages and benefits	715,881	704,179
Electricity	295,721	225,931
Spare parts	56,272	73,295
Petroleum, oil and lubricants	52,919	43,040
Communications	30,508	19,210
Depreciation and amortization	27,047	27,828
Insurance	19,788	15,214
Contractual services	14,240	13,540
Office supplies	14,084	12,534
Repairs and maintenance	7,405	1,960
Travel	5,263	3,216
Miscellaneous	<u>33,393</u>	<u>51,100</u>
Total operating expenses	<u>1,272,521</u>	<u>1,191,047</u>
Operating loss	<u>(262,386)</u>	<u>(121,724)</u>
Nonoperating revenues (expenses):		
RepMar subsidy	349,404	-
Penalties and interest	<u>-</u>	<u>(41,706)</u>
Total nonoperating revenues (expenses), net	<u>349,404</u>	<u>(41,706)</u>
Change in net deficiency	87,018	(163,430)
Net deficiency at beginning of year	<u>(788,726)</u>	<u>(625,296)</u>
Net deficiency at end of year	<u>\$ (701,708)</u>	<u>\$ (788,726)</u>

See accompanying notes to financial statements.



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

Statements of Cash Flows  
Years Ended September 30, 2007 and 2006

	2007	2006
Cash flows from operating activities:		
Cash received from customers	\$ 960,119	\$ 1,099,583
Cash payments to suppliers for goods and services	(257,447)	(199,203)
Cash payments to employees for services	(691,038)	(699,498)
Net cash provided by operating activities	11,634	200,882
Cash flows from noncapital financing activities:		
RepMar subsidy	99,404	-
Principal payments on RepMar promissory note	(40,800)	(54,400)
Principal payments on MISSA promissory note	(30,800)	(64,207)
Penalties and interest paid	(65,515)	(38,043)
Net cash used for noncapital financing activities	(37,711)	(156,650)
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(4,935)	(4,997)
Net cash used for capital and related financing activities	(4,935)	(4,997)
Net change in cash	(31,012)	39,235
Cash at beginning of year	56,011	16,776
Cash at end of year	\$ 24,999	\$ 56,011
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (262,386)	\$ (121,724)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	27,047	27,828
Bad debts	15,235	36,093
Loss from disposal of fixed asset	-	(392)
(Increase) decrease in assets:		
Receivables:		
Utility	(106,640)	(151,409)
Affiliates	28,688	142,490
Other	12,701	3,478
Inventory	(3,396)	5,527
Prepaid expenses	(8,233)	3,383
Increase (decrease) in liabilities:		
Accounts payable	11,185	(2,954)
Social security taxes payable	10,002	8,171
Payable to affiliates	252,114	249,748
Other accrued liabilities	35,317	643
Net cash provided by operating activities	\$ 11,634	\$ 200,882
Summary of noncash financing activities:		
RepMar subsidy	\$ 250,000	\$ -
Decrease in payables to affiliates	(250,000)	-
	\$ -	\$ -

See accompanying notes to financial statements.

## MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2007 and 2006

### (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 issued Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, which was subsequently amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, and modified by GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. These statements establish financial reporting standards for governmental entities which require that management's discussion and analysis of the financial activities be included with the basic financial statements and notes and modifies certain other financial statement disclosure requirements.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2007 and 2006

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

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

- Investment in capital assets; capital assets, net of accumulated depreciation, plus construction or improvement of those assets.
- Unrestricted; net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

### Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of the fund are included in the statements of net assets. Proprietary fund operating statements present increases and decreases in net assets. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. MWSC considers utility revenues and costs that are directly related to utility operations to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

### Cash

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, 2007 and 2006, cash was \$24,999 and \$56,011, respectively, and the corresponding bank balances were \$30,813 and \$65,942, respectively, which are maintained in one financial institution subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of September 30, 2007 and 2006, bank deposits were fully FDIC insured.

### Receivables

All receivables are due from government agencies, businesses and individuals located within the Republic of the Marshall Islands and are interest free and uncollateralized. The allowance for doubtful accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectibility of these accounts and prior collection experience. The allowance is established through a provision for bad debts charged to expense.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2007 and 2006

## (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.

### New Accounting Standards

In April 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which establishes uniform financial reporting for other postemployment benefit plans by state and local governments. The provisions of this statement are effective for periods beginning after December 15, 2006. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In June 2004, GASB issued 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 post employment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In September 2006, GASB issued GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfer of Assets and Future Revenues*, which establishes criteria that governments will use to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing. The statement also includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. The provisions of this statement are effective for periods beginning after December 15, 2006. 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, 2007 and 2006

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

### New Accounting Standards, Continued

In December 2006, GASB issued 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. The provisions of this statement are effective for periods beginning after December 15, 2007. Management does not believe that the implementation of this statement will have a material effect on the financial statements of MWSC.

In May 2007, GASB issued Statement No. 50, *Pension Disclosures-an Amendment of GASB Statements No. 25 and 27*, which amends applicable note disclosure and RSI requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 27 *Accounting for Pensions by State and Local Governmental Employers*, to conform with requirements of Statements 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*. The provisions of this statement are effective for periods beginning after June 15, 2007. Management does not believe the implementation of this statement will have a material effect on the financial statements of MWSC.

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, 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 MWSC.

## (3) Risk Management

MWSC is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. MWSC has elected not to purchase commercial insurance for the risks of loss to which it is exposed. Instead, MWSC believes it is more economical to manage its risks internally. Claims expenses and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. No losses as a result of these risks have occurred in any of the past three years.

## (4) Capital Assets

Capital asset activity for the years ended September 30, 2007 and 2006, was as follows:

	2007			September 30, 2007
	October 1, 2006	Additions	Retirements	
Vehicles	\$ 130,185	\$ 800	\$ (1,483)	\$ 130,985
Machinery and equipment	103,115	-	(4,718)	101,632
Office equipment	42,873	4,135	-	42,290
Buildings and leasehold improvements	54,317	-	-	54,317
	330,490	4,935	(6,201)	329,224
Less accumulated depreciation and amortization	(277,054)	(27,047)	(6,201)	(297,900)
	\$ 53,436	\$ (22,112)	\$ -	\$ 31,324

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

Notes to Financial Statements  
September 30, 2007 and 2006

**(4) Capital Assets, Continued**

	2006			
	October 1, <u>2005</u>	<u>Additions</u>	<u>Retirements</u>	September 30, <u>2006</u>
Vehicles	\$ 168,654	\$ -	\$ (38,469)	\$ 130,185
Machinery and equipment	119,077	-	(15,962)	103,115
Office equipment	55,974	4,997	(18,098)	42,873
Buildings and leasehold improvements	<u>54,317</u>	-	-	<u>54,317</u>
	398,022	4,997	(72,529)	330,490
Less accumulated depreciation and amortization	<u>(322,147)</u>	<u>(27,828)</u>	<u>72,921</u>	<u>(277,054)</u>
	\$ <u>75,875</u>	\$ <u>(22,831)</u>	\$ <u>392</u>	\$ <u>53,436</u>

**(5) Social Security Taxes Payable**

At September 30, 2007 and 2006, MWSC was liable for taxes payable to the Marshall Islands Social Security Administration (MISSA) in the amount of \$47,592 and \$37,590, respectively. In addition, MWSC was liable for certain delinquent taxes payable. On February 7, 2003, MWSC and MISSA entered into a promissory note for the repayment of these delinquent taxes payable in the original amount of \$427,774. The terms of the agreement include monthly payments of \$10,000, inclusive of interest at 12% per annum, commencing March 30, 2003. The promissory note was paid off during fiscal year 2007. Changes in MWSC's promissory note payable to MISSA for the years ended September 30, 2007 and 2006, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Repayments</u>	<u>Ending Balance</u>
2007	\$ <u>30,800</u>	\$ <u>-</u>	\$ <u>(30,800)</u>	\$ <u>-</u>
2006	\$ <u>95,007</u>	\$ <u>-</u>	\$ <u>(64,207)</u>	\$ <u>30,800</u>

**(6) Withholding Taxes Payable**

At September 30, 2007 and 2006, MWSC was liable for delinquent withholding taxes payable to RepMar in the amount of \$78,443 and \$119,243, respectively, and related penalties and interest in the amount of \$6,517 and \$42,993, respectively. On January 30, 2006, a promissory note was refinanced whereby MWSC agreed to repay the sum of \$164,048 plus penalties and interest of \$29,336 over a period of twenty-seven months. The terms of the agreement include interest at 12% per annum commencing January 30, 2006. Changes in MWSC's promissory note payable to RepMar for the years ended September 30, 2007 and 2006, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Repayments</u>	<u>Ending Balance</u>
2007	\$ <u>119,243</u>	\$ <u>-</u>	\$ <u>(40,800)</u>	\$ <u>78,443</u>
2006	\$ <u>141,041</u>	\$ <u>32,602</u>	\$ <u>(54,400)</u>	\$ <u>119,243</u>

MWSC did not comply with the repayment terms of this promissory note. Accordingly, this payable is reflected as a current liability in the accompanying financial statements.

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2007 and 2006

## (7) Related Party Transactions

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

During the year ended September 30, 2007, MWSC received an operating subsidy from RepMar in the amount of \$349,404, of which \$250,000 was paid directly to the Marshalls Energy Company, Inc. as partial payment on outstanding electricity billings owed by MWSC.

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

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

A summary of related party transactions for the years ended September 30, 2007 and 2006, and related receivable and payable balances as of September 30, 2007 and 2006, is as follows:

	<u>2007</u>			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 76,844	\$ 2,459	\$ 22,062	\$ 84,960
Marshalls Energy Company, Inc.	6,187	295,721	17,773	775,589
Marshall Islands National Telecommunications Authority	5,428	21,263	1,569	1,745
Marshall Islands Social Security Administration	644	-	124	47,592
Majuro Resort, Inc.	31,030	-	14,933	-
Other	<u>25,987</u>	<u>12,143</u>	<u>12,151</u>	<u>-</u>
	<u>\$ 146,120</u>	<u>\$ 331,586</u>	<u>\$ 68,612</u>	<u>\$ 909,886</u>
	<u>2006</u>			
	<u>Revenues</u>	<u>Expenses</u>	<u>Receivables</u>	<u>Payables</u>
RepMar	\$ 63,592	\$ 63,204	\$ 59,063	\$ 162,236
Marshalls Energy Company, Inc.	15,895	225,931	15,418	770,960
Marshall Islands National Telecommunications Authority	9,837	10,337	792	2,270
Marshall Islands Social Security Administration	423	107,782	43	97,429
Majuro Resort, Inc.	37,601	-	9,300	-
Other	<u>62,616</u>	<u>-</u>	<u>12,684</u>	<u>1,990</u>
	<u>\$ 189,964</u>	<u>\$ 407,254</u>	<u>\$ 97,300</u>	<u>\$ 1,034,885</u>

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

# MAJURO WATER AND SEWER COMPANY, INC.

Notes to Financial Statements  
September 30, 2007 and 2006

## (8) Commitment

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

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

<u>Year ending</u> <u>September 30,</u>	
2008	\$ 266,667
2009	100,000
2010	100,000
2011	100,000
2012	100,000
2013-2016	<u>433,333</u>
	\$ <u>1,000,000</u>

During the years ended September 30, 2007 and 2006, MWSC did not record the liability per the franchise agreement due to lack of capacity to make the payments in the foreseeable future. MWSC essentially depends on financing from RepMar and MEC to be able to continue as a going concern. Thus, management will negotiate the franchise terms with RepMar. If negotiations fail, MWSC may become liable for the above amounts but management does not believe that it will possess the ability to liquidate that liability.

## (9) Going Concern

MWSC has incurred losses from operations of \$262,386 and \$121,724 during the years ended September 30, 2007 and 2006, respectively, and as of those dates, has working capital deficiencies of \$733,032 and \$842,162, respectively. Management believes that the continuation of MWSC's operations is dependent upon the future financial support of RepMar, compensation by RepMar for the cost of actual utility service provided, the collection of long outstanding utility receivables, and/or significant improvements in operations, among other matters. Additionally, in order for MWSC to continue as a going concern, it may need to delay payments to the Marshalls Energy Company, Inc. for electric usage or to delay payments to RepMar for delinquent employee withholding taxes.